ExactTarget, Inc.
Form S-1
November 23, 2011
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As filed with the Securities and Exchange Commission on November 23, 2011

Registration No. 333-

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form S-1

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

ExactTarget, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**7372**	**20-1367351**
		(I.R.S. Employer

(State or other jurisdiction of Incorporation or organization)	**(Primary Standard Industrial Classification Code Number)**	**Identification Number)**

20 North Meridian Street, Suite 200 Indianapolis, Indiana 46204 (317) 423-3928 (Address, including zip code, and telephone number,

including area code, of registrant s principal executive offices)

Scott D. Dorsey Chief Executive Officer 20 North Meridian Street, Suite 200 Indianapolis, Indiana 46204 (317) 423-3928 (Name, address, including zip code, and telephone number, including area code, of agent for service)

Copies to:

Howard B. Adler	**Steven K. Humke**	**Jeffrey D. Saper**
Anne L. Benedict	**Ice Miller LLP**	**J. Robert Suffoletta, Jr.**
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Washington, DC 20036-5306	**Indianapolis, IN 46282-0200**	**Las Cimas IV, Fifth Floor**
		Austin, TX 78746

Approximate date of commencement of proposed sale to the public: As soon as practicable after the effective date of this registration statement.

If any of the securities being registered on this Form are being offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box: ¨

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨	Accelerated filer ¨	Non-accelerated filer x (Do not check if a smaller reporting company)	Smaller reporting company ¨

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Proposed Maximum Aggregate Offering Price(1)	Amount of Registration Fee(2)
Common Stock, par value $0.001 per share	$100,000,000	$11,460

(1) Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457(o) under the Securities Act of 1933, as amended.
(2) Calculated pursuant to Rule 457(o) under the Securities Act of 1933, as amended.

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

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You should rely only on the information contained in this prospectus or contained in any free writing prospectus filed with the Securities and Exchange Commission (the SEC). Neither we nor the underwriters have authorized anyone to provide you with additional information or information different from that contained in this prospectus or in any free writing prospectus filed with the SEC. We are offering to sell, and seeking offers to buy, shares of our common stock only in jurisdictions where offers and sales are permitted. The information contained in this prospectus or a free writing prospectus is accurate only as of its date, regardless of its time of delivery, or of any sale of shares of our common stock. Our business, financial condition, results of operations and prospects may have changed since that date.

Through and including , 2012 (the 25th day after the date of this prospectus), all dealers that effect transactions in these securities, whether or not participating in this offering, may be required to deliver a prospectus. This is in addition to the dealers obligation to deliver a prospectus when acting as underwriters and with respect to their unsold allotments or subscriptions.

For investors outside the United States: Neither we nor the underwriters have done anything that would permit this offering or possession or distribution of this prospectus in any jurisdiction where action for that purpose is required, other than in the United States. You are required to inform yourselves about and to observe any restrictions relating to this offering and the distribution of this prospectus outside the United States.

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PROSPECTUS SUMMARY

The following summary highlights selected information contained elsewhere in this prospectus and does not contain all of the information that you should consider in making your investment decision. Before investing in our common stock, you should carefully read the entire prospectus, including the consolidated financial statements and the related notes included in this prospectus and the information set forth under the headings Risk Factors and Management s Discussion and Analysis of Financial Condition and Results of Operations. Unless the context requires otherwise, the words ExactTarget, we, company, us and our refer to ExactTarget, Inc. and its wholly-owned subsidiaries.

Our Business

We are a leading global provider of cross-channel, interactive marketing software-as-a-service (SaaS) solutions that empower organizations of all sizes to communicate with their customers through the interactive channels they use most email, mobile, social media and websites. Our solutions provide marketers with a broad and powerful suite of integrated applications to plan, automate, deliver and optimize data-driven interactive marketing campaigns and real-time communications to drive customer engagement, increase sales and improve their return on marketing investment.

Our suite of cross-channel, interactive marketing applications, which include email, mobile, social media and sites, is built on our highly-scalable and flexible multi-tenant SaaS platform. These channel applications are integrated with our campaign management, calendaring, real-time dashboard, integrated reporting, marketing automation and data management tools to provide marketers with a comprehensive, yet easy-to-use, solution to manage, automate and engage in real-time interactive marketing. In addition, our cloud-based platform s robust integration framework enables clients to integrate data from virtually any relevant source and leverage productized integrations with leading third-party CRM, web analytics and e-commerce providers to further enhance the relevance of their interactive communications. We also provide open application programming interfaces (APIs) and developer tools that allow third parties to embed our technology into their solutions and build applications on our platform.

Our global sales organization is focused on adding new clients and expanding relationships with existing clients. We believe our team is the largest sales organization devoted to selling interactive marketing SaaS solutions, with over 285 sales professionals located on four continents. Our field sales team sells into the large business, or enterprise market, while our inside sales team sells to small and medium-sized organizations primarily via telesales. In addition to these new business teams, we have a relationship management sales team that focuses on strengthening client relationships, driving contract renewals and selling additional applications to existing clients. We also extend our sales distribution through relationships with more than 500 marketing service providers that resell our solutions to their customers.

Our direct client base consisted of over 4,600 organizations as of September 30, 2011, ranging from enterprises to small businesses in numerous industries, including retail and e-commerce, media and entertainment, travel and hospitality, financial services and insurance, technology, daily-deal and flash-sale and marketing service providers. Among our direct clients are U.S.-based companies such as Ally Financial, Inc., Angie s List, Inc., CareerBuilder, LLC, Groupon, Inc., Microsoft Corporation, Nationwide Mutual Insurance Company, Oakley, Inc., OneAmerica Financial Partners, Inc., One King s Lane, Inc., Papa John s International, Inc., priceline.com Incorporated, The Scotts Miracle-Gro Company, Tommy Hilfiger Group, WellPoint, Inc. and Zappos.com, Inc., and companies headquartered outside the United States such as Abril Group (Brazil), Fairfax Media Limited (Australia), Icelandair

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Group (Iceland) and Telegraph Media Group Limited (United Kingdom). Several thousand additional organizations utilize our SaaS solutions through their relationships with our marketing service provider clients. Our client base is diverse, and no single client represented more than 5% of our overall revenue for each of the years ended December 31, 2008, 2009 and 2010, and the nine months ended September 30, 2011.

We provide our solutions primarily through annual and multi-year subscriptions based on volume of contracted utilization, level of functionality, number of interactive marketing channels, number of users and level of customer support. We have achieved 43 consecutive quarters of revenue growth and annual dollar-based subscription revenue renewal rates of over 100% in each of the years ended December 31, 2009 and 2010. For the years ended December 31, 2009 and 2010 and for the nine months ended September 30, 2011, our revenue was $95.4 million, $134.3 million and $148.0 million, representing period-over-period growth of 32%, 41% and 55%, respectively.

Industry Overview

Changes in media consumption, real-time engagement through social media and pervasive mobile connectivity have challenged marketers ability to deliver relevant, meaningful and timely communications. Organizations require a cross-channel view of their customers to drive real-time, relevant engagement and positive return on marketing investment.

Market Opportunity for Interactive Marketing

Consumers are increasingly using email, mobile, social media and websites to access information and interact with brands. Media consumption is shifting from offline channels to interactive channels, driving marketers to increase the percentage of advertising spending on interactive marketing. According to Forrester Research, Inc. s (Forrester) *US Interactive Marketing Forecast, 2011 To 2016*, U.S. marketers plan to increase spending on interactive channels (defined as display, search, email, mobile and social media) as a percentage of total advertising spending from 16% in 2011 to 26% in 2016, creating a projected $77 billion market in the United States by 2016, of which email, mobile and social media marketing is expected to grow from approximately $4.8 billion in 2011 to nearly $15.7 billion by 2016, representing a compound annual growth rate of 27%. We believe the addressable market outside the United States presents an even greater opportunity.

Market Challenges

Organizations often lack the technology, infrastructure and expertise needed to plan, automate, deliver and optimize data-driven, interactive marketing campaigns and real-time communications across interactive channels. Marketers considering the adoption or expansion of email and cross-channel, interactive marketing programs face many challenges, including the following:

- difficulty in integrating data to create a single, unified view of each consumer;
- complexity in effectively engaging consumers across multiple channels;
- inability of disparate point solutions to address marketers emerging needs;
- complex security and infrastructure requirements; and
- changing deliverability and regulatory standards.

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Our Solutions

Our suite of cross-channel, interactive marketing applications enables organizations to plan, automate, deliver and optimize data-driven, interactive marketing campaigns and critical, real-time communications to enhance customer engagement and improve their return on marketing investment. Key benefits of our solutions include:

Cross-channel campaign management and engagement capabilities powered by a unified view of each consumer. Our suite includes email, mobile, social media and sites applications that are integrated with campaign management, calendaring, marketing automation and data management tools to provide marketers with the ability to develop a unified view of each consumer and engage in real-time, cross-channel marketing.

Automation of marketing campaigns and real-time communications. Our solutions enable clients to automate processes required to deliver sophisticated, multi-stage marketing campaigns and personalized real-time communications such as order confirmations, e-statements, alerts, abandoned shopping cart reminders and many others.

Highly-scalable and modular SaaS architecture to meet clients evolving needs. Our SaaS technology infrastructure supports large transaction volumes and allows our clients to store large amounts of data while maintaining high application availability. Clients can easily add new channels and functionality as they expand their interactive marketing programs.

Open and flexible cloud-based platform. Our cloud-based platform s robust integration framework enables clients to integrate data from virtually any relevant source and leverage productized integrations with leading third-party applications. We also provide open APIs and developer tools that allow third parties to embed our technology into their solutions and build applications on our cloud-based platform.

Compliance with complex deliverability and regulatory standards. We solve challenging issues associated with deliverability of our clients interactive communications and enable our clients to meet legal and regulatory compliance requirements.

Our Competitive Strengths

Our vision is to inspire and enable organizations of all sizes to leverage interactive marketing technologies to achieve phenomenal business results. We have established a leadership position in interactive marketing as evidenced by our global size, scale and growth, which we believe results in several key competitive strengths including:

Leadership driven by vision and focus on innovation. Our vision, focus on innovation and significant investments have fueled our growth and enabled us to deliver interactive marketing solutions that solve marketers complex challenges. Forrester placed ExactTarget in the leader category in its *Forrester Wave: Email Marketing Service Providers, Q4 2009* report. We have extended our leadership position beyond email marketing through the integration of our social media platform, CoTweet, Inc. (CoTweet), the creation of our Social Media Lab and the launch of the Interactive Marketing Hub, our integrated, cross-channel interactive marketing solution.

Market-leading size and scale and strong business momentum. With approximately 1,100 employees located on four continents and over $40 million of expected research and development investment in 2011, we enable marketers around the globe to improve returns from their interactive marketing programs. Our substantial investments have led to strong business momentum, resulting in $148.0 million in revenue for the nine months ended September 30, 2011, an increase of 55% compared to the nine months ended September 30, 2010.

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Serving clients of all sizes, in many industries and geographies, from a single platform. Our highly-scalable SaaS architecture and modular product offerings enable us to serve large, distributed enterprises with complex interactive marketing requirements, as well as small and medium-sized organizations. Our direct client base consists of over 4,600 organizations, across numerous industries and many geographies. Several thousand additional organizations utilize our SaaS solutions through their relationships with our marketing service provider clients.

Large direct and indirect sales organization with global reach. We believe our team is the largest sales organization devoted to selling interactive marketing SaaS solutions to new and existing clients, with over 285 sales professionals located on four continents. We also extend our global sales distribution through relationships with more than 500 marketing service providers.

Corporate culture committed to client success. Named for our primary brand color, our Orange culture reflects our employees energy, passion and focus on client success. Our culture is widely regarded as one of our greatest assets and is consistently cited as a key differentiator by clients, partners, prospective clients and employees.

Our Growth Strategy

We intend to leverage our vision, our focus on innovation, the breadth of our solutions and our interactive marketing expertise to extend our market leadership and continue to fuel our growth. Key elements of our growth strategy include:

- continue to innovate and enhance our leading interactive marketing solutions;
- win new clients by expanding direct and indirect sales;
- increase revenue from our existing clients;
- continue to expand our global presence; and
- selectively pursue acquisitions.

Selected Risks Associated with Our Business

Our business is subject to numerous risks and uncertainties, including those highlighted here and described in further detail in Risk Factors immediately following this Prospectus Summary. You should carefully read Risk Factors beginning on page 9 for a detailed explanation of these risks before investing in our common stock. Some of these risks include:

- we have a recent history of losses, and we may not return to or sustain profitability in the future;
- we have experienced rapid growth in recent periods, and if we fail to manage our domestic and international growth effectively, our financial performance may be adversely affected;
- our operating results and revenue will be adversely affected if we are not able to attract new clients, retain existing clients or sell additional functionality and services to existing clients;

defects or errors in our SaaS solutions or compromises of security measures could harm our reputation, result in significant costs to us and impair our ability to sell our solutions;

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- we have been dependent on our clients use of email as a channel for interactive marketing, and any decrease in the use of email for this purpose would harm our business, prospects, operating results and financial condition;

- the market for cross-channel, interactive marketing SaaS solutions is relatively new and emerging. If the market develops more slowly or differently than we expect, our business, growth prospects and financial condition would be adversely affected;

- evolving domestic and international data privacy regulations may restrict our clients ability to solicit, collect, process, disclose and use personal information or may increase the costs of doing so, which could harm our business;

- failures of the third-party hardware, software and infrastructure on which we rely, including third-party data center hosting facilities, could impair the delivery of our solutions and adversely affect our business;

- the markets in which we participate are highly competitive, and pricing pressure or other competitive dynamics, which could include clients developing their own solutions, could adversely affect our business and operating results; and

- we rely on our management team and other key employees, and the loss of one or more key employees could harm our business.

Corporate Information

We began our operations in December 2000 as ExactTarget, LLC, an Indiana limited liability company. In July 2004, ExactTarget, LLC merged into ExactTarget, Inc., a Delaware corporation. Our principal executive offices are located at 20 North Meridian Street, Suite 200, Indianapolis, Indiana 46204. Our main telephone number is (317) 423-3928, and our website address is www.exacttarget.com. Information contained on our website is not a part of, and is not incorporated into, this prospectus.

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The Offering

Common stock offered by us	shares
Over-allotment option	shares
Common stock to be outstanding after this offering	shares, or shares if the underwriters exercise their option to purchase additional shares in full.
Use of proceeds	We intend to use the net proceeds from this offering primarily for general corporate purposes, such as expanding our sales and marketing teams, international operations, product development efforts and general and administrative functions, as well as for working capital. We may also use the net proceeds to repay our term loan and revolving line of credit or for acquisitions. See Use of Proceeds.
Exchange listing	We intend to apply for listing of our common stock on the under the symbol .

The number of shares of our common stock to be outstanding after this offering is based on 25,949,359 shares of common stock outstanding as of September 30, 2011 and excludes:

- 5,658,767 shares of common stock issuable upon the exercise of options outstanding as of September 30, 2011 granted under our 2008 equity incentive plan and 2004 stock option plan, having a weighted average exercise price of $10.31 per share;
- 2,000,000 shares of our Series D preferred stock issued in November 2011 that will automatically convert into common stock immediately prior to the completion of this offering; and
- 66,026 shares of unvested restricted common stock outstanding as of September 30, 2011.

Unless otherwise stated, information in this prospectus reflects and assumes the following:

- the filing of our amended and restated certificate of incorporation and the adoption of our amended and restated bylaws immediately prior to the completion of this offering;
- the automatic conversion of all of our outstanding preferred stock as of September 30, 2011 into an aggregate of 21,467,219 shares of our common stock immediately prior to the completion of this offering; and
- no exercise of the underwriters option to purchase additional shares.

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Summary Consolidated Financial Data

The following tables summarize the consolidated financial data for our business. You should read this summary consolidated financial data in conjunction with Selected Consolidated Financial Data, Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the related notes, all included elsewhere in this prospectus.

We derived the summary consolidated statements of operations data for the years ended December 31, 2008, 2009 and 2010 from our audited consolidated financial statements included elsewhere in this prospectus. The unaudited consolidated statements of operations data for the nine months ended September 30, 2010 and 2011, and the unaudited consolidated balance sheet data as of September 30, 2011, were derived from our unaudited consolidated financial statements included elsewhere in this prospectus. We have prepared the unaudited consolidated financial statements on the same basis as the audited consolidated financial statements and have included, in our opinion, all adjustments, consisting only of normal recurring adjustments, that we consider necessary for a fair presentation of the financial information set forth in those statements. Our historical results are not necessarily indicative of our future results, and our interim results are not necessarily indicative of the results to be expected for the full fiscal year or for any other period.

	Year Ended December 31,			Nine Months Ended September 30,	
	2008	2009	2010	2010	2011
				(unaudited)	
	(in thousands, except share and per share data)				
Consolidated Statements of Operations Data:					
Revenue	$ 72,342	$ 95,443	$ 134,267	$ 95,276	$ 147,985
Cost of revenue(1)	20,094	30,772	43,894	31,013	49,595
Gross profit	52,248	64,671	90,373	64,263	98,390
Operating expenses:					
Sales and marketing(1)	28,397	39,276	63,978	42,986	68,224
Research and development(1)	9,901	14,845	27,400	18,699	30,151
General and administrative(1)	7,436	13,397	17,159	11,979	18,082
Total operating expenses	45,734	67,518	108,537	73,664	116,457
Operating income (loss)	6,514	(2,847)	(18,164)	(9,401)	(18,067)
Other income (expense), net	34	75	(53)	30	(683)
Income (loss) before taxes	6,548	(2,772)	(18,217)	(9,371)	(18,750)
Income tax expense (benefit)	2,989	(777)	(6,127)	(3,349)	10,540
Net income (loss)	3,559	(1,995)	(12,090)	(6,022)	(29,290)
Adjustment for redemption of preferred stock		(58,601)			
Preferred stock dividend		(490)			
Net income (loss) available to common stockholders	$ 3,559	$ (61,086)	$ (12,090)	$ (6,022)	$ (29,290)
Net income (loss) per common share:					
Basic	$ 0.68	$ (11.73)	$ (3.03)	$ (1.53)	$ (6.76)
Diluted	$ 0.17	$ (11.73)	$ (3.03)	$ (1.53)	$ (6.76)
Weighted average number of common shares outstanding basic	5,234,463	5,208,696	3,989,152	3,934,577	4,332,319
Weighted average number of common shares outstanding diluted	20,359,647	5,208,696	3,989,152	3,934,577	4,332,319
Other Financial Data:					
Adjusted EBITDA(2)	$ 12,249	$ 7,723	$ (2,769)	$ 1,272	$ (892)

(1) Cost of revenue and operating expenses include the following amounts related to stock-based compensation:

	Year Ended December 31,			Nine Months Ended September 30,	
	2008	2009	2010	2010	2011
				(unaudited)	
			(in thousands)		
Cost of revenue	$ 215	$ 416	$ 664	$ 483	$ 798
Sales and marketing	320	813	1,413	852	1,644
Research and development	257	528	1,147	854	1,010
General and administrative	191	1,589	1,201	783	1,490
Total stock-based compensation	$ 983	$ 3,346	$ 4,425	$ 2,972	$ 4,942

(2) We provide Adjusted EBITDA, which is a non-GAAP financial measure, because we believe this measure provides important supplemental information regarding our operating performance and is often used by investors and analysts in their evaluation of companies such as ours. In addition, we use Adjusted EBITDA as a measurement of our operating performance because it assists us in comparing our operating performance on a consistent basis by removing the impact of certain non-cash and non-operating items. We calculate Adjusted EBITDA as net income (loss) before (1) other (income) expense, which includes interest income, interest expense and other income and expense, (2) income tax expense (benefit), (3) depreciation and amortization of property and equipment, (4) amortization of intangible assets and (5) stock-based compensation. This non-GAAP financial measure is used in addition to and in conjunction with results presented in accordance with GAAP and should not be relied upon to the exclusion of GAAP financial measures. Adjusted EBITDA reflects an additional way of viewing aspects of our operations that we believe, when viewed with our GAAP results and the accompanying reconciliations to corresponding GAAP financial measures, provides a more complete understanding of factors and trends affecting our business. The following table provides a reconciliation from net income (loss) to Adjusted EBITDA:

	Year Ended December 31,			Nine Months Ended September 30,	
	2008	2009	2010	2010	2011
				(unaudited)	
			(in thousands)		
Net income (loss)	$ 3,559	$ (1,995)	$ (12,090)	$ (6,022)	$ (29,290)
Other (income) expense, net	(34)	(75)	53	(30)	683
Income tax expense (benefit)	2,989	(777)	(6,127)	(3,349)	10,540
Depreciation and amortization of property and equipment	4,752	7,046	10,173	7,225	11,401
Amortization of intangible assets		178	797	476	832
Stock-based compensation	983	3,346	4,425	2,972	4,942
Adjusted EBITDA	$ 12,249	$ 7,723	$ (2,769)	$ 1,272	$ (892)

	As of September 30, 2011		
	Actual	Pro Forma(3)	Pro Forma As Adjusted(4)
		(unaudited)	
		(in thousands)	
Consolidated Balance Sheet Data:			
Cash and cash equivalents	$ 29,550	$	$
Working capital (deficit)	1,672		
Total assets	154,735		
Total liabilities	93,040		
Redeemable convertible preferred stock	63,000		
Total stockholders equity (deficit)	(1,305)		

(3) On a pro forma basis to give effect to the automatic conversion of all outstanding shares of our preferred stock into shares of common stock.

(4) On a pro forma as adjusted basis to give effect to (1) the issuance and sale by us of shares of common stock in this offering, and the receipt of the net proceeds from our sale of these shares at an assumed initial public offering price of $ per share, the midpoint of the range listed on the cover page of this prospectus, after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us and (2) the amendment and restatement of our certificate of incorporation in connection with this offering.

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RISK FACTORS

Investing in our common stock involves a high degree of risk. You should carefully consider the risks and uncertainties described below, together with all of the other information in this prospectus, including the financial statements and related notes, and any related free writing prospectus before deciding whether to purchase shares of our common stock. If any of the following risks are realized, in whole or in part, our business, operating results, reputation and prospects could be materially and adversely affected. In that event, the price of our common stock could decline, and you could lose part or all of your investment.

Risks Related to Our Business and Industry

We have a recent history of losses, and we may not return to or sustain profitability in the future.

We incurred net losses of $2.0 million for the year ended December 31, 2009, $12.1 million for the year ended December 31, 2010 and $29.3 million for the nine months ended September 30, 2011. We had an accumulated deficit of $140.0 million as of September 30, 2011. In recent years, we have made substantial investments in research and development, infrastructure, growing our sales team, international expansion and acquisitions to support anticipated future revenue growth. We expect to continue to make significant investments in the development and expansion of our business, which may make it difficult for us to return to profitability. In addition, as a public company, we will incur significant accounting, legal and other expenses that we did not incur as a private company. As a result of these increased expenditures, we will have to generate and sustain increased revenue relative to our costs to achieve profitability in the future. While our revenue has grown in recent periods, such revenue growth may not be indicative of our future performance, and this growth may not be sustainable. We may not be able to achieve sufficient revenue to return to profitability in future periods, and our revenue could decline or grow more slowly than we expect. We may incur significant losses in the future for a number of reasons, including due to the risks described in this prospectus.

We have experienced rapid growth in recent periods, and if we fail to manage our domestic and international growth effectively, our financial performance may be adversely affected.

We have expanded our overall business, including our revenue, team of employees, international operations and client base in recent periods. Our revenue increased from $72.3 million for the year ended December 31, 2008 to $134.3 million for the year ended December 31, 2010, and to $148.0 million for the nine months ended September 30, 2011. We increased our total number of full-time employees from 379 as of December 31, 2008 to 1,062 as of September 30, 2011. Since August 2009, we have acquired a social media marketing platform and three international reseller partners. Our historical growth rate is not necessarily indicative of the growth that we will achieve in the future. Our recent growth and anticipated future growth has placed and will continue to place strain on our team, infrastructure and operations. Our success will depend on our ability to manage this growth effectively. We intend to further expand our overall business, client base, number of employees and operations as we prepare to become a public company and continue to expand our operations internationally. Managing a large, diverse and geographically dispersed client base and workforce will require substantial management effort and significant additional investment in our team, technology and infrastructure. In order to support and sustain our growth, we will have to continue to improve our technology, our operational, financial and management controls and reporting procedures, and all of these investments will increase our costs. Furthermore, we have encountered and will continue to encounter risks and uncertainties frequently experienced by growing companies in rapidly changing industries. If our assumptions regarding these uncertainties are incorrect or change as a result of changes in the market in which we operate, if we do not address these risks successfully or if we fail to

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successfully plan for and manage our growth, our operating and financial results could differ materially from our expectations and our business and growth prospects could be adversely affected.

Our operating results and revenue will be adversely affected if we are not able to attract new clients, retain existing clients or sell additional functionality and services to existing clients.

To continue to grow our business, we must attract new clients and retain and sell additional products and services to existing clients. Many of our subscription agreements do not automatically renew at the end of their terms and some have termination clauses that could result in early termination. As the interactive marketing industry matures and as competitors introduce lower cost or differentiated competitive products or services, our ability to effectively compete with respect to pricing, technology, functionality, services and support could be impaired. In such an event, we may be unable to attract new clients or renew our agreements with existing clients on favorable or comparable terms to prior periods. In addition, we may not be able to accurately predict new subscriptions or subscription renewal rates and the impact these rates may have on our future revenue and operating results. These events and developments could have a material adverse effect on our revenue, gross margin and other operating results.

Defects or errors in our SaaS solutions could harm our reputation, result in significant costs to us and impair our ability to sell our solutions.

Our suite of cross-channel, interactive marketing SaaS solutions is inherently complex and may contain defects or errors, which may cause disruptions in availability or other performance problems that could include prolonged down-time. Any such errors, defects, disruptions in service or other performance problems, whether in connection with day-to-day operation, bug fixes, upgrades or otherwise, could be costly for us to remedy, damage our clients businesses and harm our reputation. In addition, if we have any such errors, defects, disruptions in service or other performance problems, our clients could terminate their agreements, elect not to renew their subscriptions, delay or withhold payment, or make performance claims against us. Any of these actions could result in lost business, increased insurance costs, difficulty in collecting our accounts receivable and costly litigation. Such errors, defects or other problems could also result in reduced sales or a loss of or delay in the market acceptance of our solutions.

We have been dependent on our clients use of email as a channel for interactive marketing, and any decrease in the use of email for this purpose would harm our business, prospects, operating results and financial condition.

Historically, our clients have primarily used our SaaS solutions for email-based interactive marketing to consumers who have given our clients permission to send them emails. We expect that email will continue to be the primary channel used by our clients for the foreseeable future. Should our clients lose confidence in the value or effectiveness of email marketing, or if other interactive channels are perceived to be more effective than email marketing, the demand for our solutions may decline. A number of factors could adversely affect our clients assessment of the value or effectiveness of email marketing, including continual growth in the number of emails consumers receive on a daily basis, the inability of Internet service providers (ISPs) to prevent unsolicited bulk email, or spam, from overwhelming consumers inboxes, security concerns regarding viruses, worms or similar problems affecting Internet and email utilization and increased governmental regulation or restrictive policies adopted by ISPs that make it more difficult or costly to utilize email for marketing communications.

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The market for cross-channel, interactive marketing SaaS solutions is relatively new and emerging. If the market develops more slowly or differently than we expect, our business, growth prospects and financial condition would be adversely affected.

The market for cross-channel, interactive marketing SaaS solutions, such as ours, is relatively new and may not achieve or sustain high levels of demand and market acceptance. While email has been used successfully for interactive marketing for several years, marketing via new interactive marketing channels such as mobile and social media is not as well established, and revenue from email represents a substantial majority of our total revenue. The future growth of our business depends both on the acceptance and expansion of emerging interactive marketing channels, as well as the continued use and growth of existing interactive marketing channels, including email. Even if interactive marketing through these channels becomes widely adopted, our suite of cross-channel, interactive marketing SaaS solutions may not continue to be utilized by our existing clients or we may not acquire new clients. Organizations may not make significant investments in cross-channel, interactive marketing solutions and may not purchase SaaS solutions to address their interactive marketing needs. If cross-channel, interactive marketing SaaS solutions are not widely adopted, or the market for such SaaS solutions does not develop as we expect, our business, growth prospects and financial condition would be adversely affected.

Evolving domestic and international data privacy regulations may restrict our clients ability to solicit, collect, process, disclose and use personal information or may increase the costs of doing so, which could harm our business.

Federal, state and foreign governments and supervising authorities have enacted, and may in the future enact, laws and regulations concerning the solicitation, collection, processing, disclosure or use of consumers personal information. Evolving and changing regulations regarding personal data and personal information, both within the European Union and elsewhere, especially relating to classification of IP addresses, machine identification, location data and other information, may limit or inhibit our ability to operate or expand our business. Such laws and regulations require or may require companies to implement privacy and security policies, permit consumers to access, correct or delete personal information stored or maintained by such companies, inform individuals of security incidents that affect their personal information, and, in some cases, obtain consent to use personal information for certain purposes. Other proposed legislation could, if enacted, impose additional requirements and prohibit the use of certain technologies that track individuals activities on web pages or record when individuals click on a link contained in an email message. Such laws and regulations could restrict our clients ability to collect and use email addresses, web browsing data and personal information, which may reduce demand for our solutions. Changing industry standards and industry self-regulation regarding the collection, use and disclosure of certain data may have similar effects. Existing and potential future privacy and data protection laws and increasing sensitivity of consumers to unauthorized disclosures and use of personal information may also negatively affect the public s perception of interactive marketing, including marketing practices of our clients. If our solutions are perceived to cause, or are otherwise unfavorably associated with, invasions of privacy, whether or not illegal, we or our clients may be subject to public criticism. Public concerns regarding data collection, privacy and security may also cause some consumers to be less likely to visit our clients websites or otherwise interact with our clients, which could limit the demand for our solutions and inhibit the growth of our business.

Any failure to comply with applicable privacy and data protection laws, regulations, policies and standards or any inability to adequately address privacy concerns associated with our solutions, even if unfounded, could subject us to liability, damage our reputation, impair our sales and harm our business. Furthermore, the costs to our clients of compliance with, and other burdens imposed by, such laws, regulations, policies and standards may limit adoption of and demand for our solutions.

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If our security measures are compromised or unauthorized access to client data is otherwise obtained, our solutions may be perceived as not being secure, clients may curtail or cease their use of our solutions, our reputation may be harmed and we may incur significant liabilities.

Our operations involve the storage and transmission of client and consumer data, and security incidents could result in unauthorized access to, loss of or unauthorized disclosure of this information, litigation, indemnity obligations and other possible liabilities, as well as negative publicity, which could damage our reputation, impair our sales and harm our business. Cyberattacks and other malicious Internet-based activity continue to increase, and SaaS-based platform providers of interactive marketing services have been targeted. Our security measures and the contractual restraints we maintain to prevent our clients from loading sensitive health, personal and financial information into our SaaS platform may not be sufficient to prevent the storage of such information on our systems or to prevent our systems from being compromised. We do not regularly monitor or review the content that our clients upload and store and, therefore, do not control the substance of the content within our hosted environment. If clients use our suite of cross-channel, interactive marketing SaaS solutions for the transmission or storage of personally identifiable information and our security measures are compromised as a result of third-party action, employee or client error, malfeasance, stolen or fraudulently obtained log-in credentials or otherwise, our reputation could be damaged, our business may be harmed and we could incur significant liability. We may be unable to anticipate or prevent techniques used to obtain unauthorized access or to sabotage systems because they change frequently and generally are not detected until after an incident has occurred. As we increase our client base and our brand becomes more widely known and recognized when we are a public company, we may become more of a target for third parties seeking to compromise our security systems or gain unauthorized access to our clients data. A failure or inability to meet clients expectations with respect to security and confidentiality could seriously damage our reputation and affect our ability to retain clients and attract new business.

Many governments have enacted laws requiring companies to notify individuals of data security incidents involving certain types of personal data. In addition, some of our clients contractually require notification of any data security compromise. Security compromises experienced by our competitors, by our clients or by us may lead to public disclosures, which may lead to widespread negative publicity. Any security compromise in our industry, whether actual or perceived, could harm our reputation, erode client confidence in the effectiveness of our security measures, negatively impact our ability to attract new clients, cause existing clients to elect not to renew their subscriptions or subject us to third-party lawsuits, regulatory fines or other action or liability, which could materially and adversely affect our business and operating results.

There can be no assurance that the limitations of liability in our contracts would be enforceable or adequate or would otherwise protect us from any such liabilities or damages with respect to any particular claim. We also cannot be sure that our existing general liability insurance coverage and coverage for errors or omissions will continue to be available on acceptable terms or will be available in sufficient amounts to cover one or more large claims, or that the insurer will not deny coverage as to any future claim. The successful assertion of one or more large claims against us that exceed available insurance coverage, or the occurrence of changes in our insurance policies, including premium increases or the imposition of large deductible or co-insurance requirements, could have a material adverse effect on our business, financial condition and results of operations.

We may not be able to scale our infrastructure quickly enough to meet our clients growing needs and, even if we can, our operations may be disrupted or our operating results could be harmed.

As usage of our suite of cross-channel, interactive marketing SaaS solutions grows and as clients use our solutions for more advanced interactive marketing programs, we will need to devote additional resources to improving our application architecture and our infrastructure to maintain our solutions performance. Any failure of or delays in our systems could cause service interruptions or impaired

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system performance. If sustained or repeated, these performance issues could reduce the attractiveness of our solutions to clients, result in decreased sales to new clients and lower renewal rates by existing clients, which could hurt our revenue growth and our reputation. We also may need to expand our hosting operations at a more rapid pace than we have in the past. This would involve spending substantial amounts to purchase or lease data center capacity and equipment, upgrade our technology and infrastructure and introduce new SaaS solutions. Similarly, our international expansion efforts could require us to use data centers located outside the United States. We may not be able to scale our existing systems in a manner that is satisfactory to our existing or prospective clients. In addition, any such expansion will require management time and support, could be expensive and complex, could result in inefficiencies, unsuccessful data transfers or operational failures, could reduce our margins and could adversely impact our financial results. Moreover, there are inherent risks associated with upgrading, improving and expanding our information technology systems. We cannot be sure that the improvements to our infrastructure and systems will be fully or effectively implemented on a timely basis, if at all.

Failures of the third-party hardware, software and infrastructure on which we rely, including third-party data center hosting facilities, could impair the delivery of our solutions and adversely affect our business.

We rely on hardware and infrastructure, which is purchased or leased, and software licensed from third parties, to offer our suite of cross-channel, interactive marketing SaaS solutions and related professional services. For example, we rely on bandwidth providers, ISPs, mobile providers and social networks to deliver messages to consumers on behalf of our clients. Any errors or defects in third-party hardware, software or infrastructure could result in errors, interruptions or a failure of our SaaS solutions. Furthermore, this hardware, software and infrastructure may not continue to be available on commercially reasonable terms, or at all. The loss of the right to use any of this hardware, software or infrastructure could limit access to our SaaS solutions.

We currently serve our clients from two third-party data center hosting facilities located in Indianapolis, Indiana and Las Vegas, Nevada. Although our network infrastructure is generally redundant in each of our data centers, our data storage and operational capabilities are not fully redundant across data centers. The owners and operators of these facilities do not guarantee that our clients access to our solutions will be uninterrupted, error-free or secure. We do not control the operation of these facilities, and such facilities are vulnerable to damage or interruption from a tornado, earthquake, fire, cyber-attack, terrorist attack, power loss, telecommunications failure or similar catastrophic events. They also could be subject to break-ins, computer viruses, sabotage, intentional acts of vandalism and other misconduct. The occurrence of a natural disaster or an act of terrorism, a decision to close the facilities without adequate notice or other unanticipated problems could result in lengthy interruptions in the delivery of our solutions. If for any reason our arrangement with one or more of the third-party data centers we use is terminated, we could incur additional expense in arranging for new facilities and support. In addition, the failure of the data centers to meet our capacity requirements could result in interruptions in the availability of our SaaS solutions or impair the functionality of our SaaS solutions, which could adversely affect our business.

Errors, defects, disruptions or other performance problems with the delivery of our suite of cross-channel, interactive marketing SaaS solutions may reduce our revenue, harm our reputation and brand and adversely affect our contract renewals and our ability to attract new clients. In addition, some of our client agreements require us to issue credits for downtime in excess of certain thresholds, and in some instances give our clients the ability to terminate the agreements in the event of significant amounts of downtime. Our business, growth prospects and operating results will also be harmed if our clients and potential clients are not confident that our solutions are reliable.

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During the fourth quarter of 2011, we expect to commence operations in a third data center, located in Indianapolis, Indiana. This facility, which is owned and operated by a third party, has comparable terms to our existing Indianapolis and Las Vegas, Nevada data centers. As we continue to add data centers and increase capacity in data centers to accommodate increased demand, our costs and expenses associated with these efforts may adversely affect our operating results, liquidity and financial condition.

The markets in which we participate are highly competitive, and pricing pressure or other competitive dynamics, which could include clients developing their own solutions, could adversely affect our business and operating results.

The markets for interactive marketing solutions are fragmented, highly competitive and rapidly changing. With the introduction of new technologies and potential new entrants into these markets, we expect competition to intensify in the future, which could harm our ability to increase sales and maintain our margins. We provide interactive marketing solutions to a broad array of clients, ranging from enterprises to small businesses. We have a number of competitors, including Aprimo, Inc. (which was acquired by Teradata Corporation in 2011), CheetahMail Inc. (a subsidiary of Experian Group Limited), e-Dialog Inc. (a subsidiary of eBay, Inc.), Eloqua Limited, Epsilon Data Management, LLC (a subsidiary of Alliance Data Systems Corporation), Responsys, Inc., Silverpop Systems Inc., StrongMail Systems, Inc., Unica Corporation (which was acquired by International Business Machines Corporation in 2010) and Yesmail (a division of infoGROUP Inc.). To a lesser degree, we compete with a number of email marketing providers focused on the small business market. We also face competition from social media marketing providers, such as Buddy Media, Inc. and Radian6 Technologies, Inc. (which was acquired by salesforce.com, inc. in 2011), and from mobile marketing service providers, as well as from in-house solutions that our current and prospective clients may develop.

We may also face competition from new companies entering our markets, which may include large established businesses, such as Adobe Systems Incorporated, Amazon.com, Inc., Google Inc., Oracle Corporation or salesforce.com, inc., each of which currently offers, or may in the future offer, interactive marketing or related applications such as applications for customer relationship management, analysis of Internet data and marketing automation. If these companies decide to develop, market or resell competitive interactive marketing products or services, acquire one of our competitors or form a strategic alliance with one of our competitors, our ability to compete effectively could be compromised, and our operating results could be harmed. Furthermore, we believe that our industry may experience further consolidation, which could lead to increased competition and result in pricing pressure or loss of market share, either of which could have a material adverse effect on our business, limit our growth prospects or reduce our revenue.

Our current and potential competitors may have significantly more financial, technical, marketing and other resources than we have, may be able to devote greater resources to the development, promotion, sale and support of their products and services than we can, may have more extensive customer bases and broader customer relationships than we have and may have longer operating histories and greater name recognition than we have. In some cases, these companies may choose to offer interactive marketing applications at little or no additional cost to the customer by bundling them with their existing applications. If we are unable to compete with such companies, the demand for our suite of cross-channel, interactive marketing SaaS solutions and related professional services could decline and adversely affect our business, operating results and financial condition.

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If we fail to effectively expand our sales and marketing capabilities and teams, we may not be able to increase our client base and achieve broader market acceptance of our SaaS solutions.

Increasing our client base and achieving broader market acceptance of our suite of cross-channel, interactive marketing SaaS solutions will depend on our ability to expand our sales and marketing teams and their capabilities to obtain new clients and sell additional products and services to existing clients. We believe there is significant competition for direct sales professionals with the skills and technical knowledge that we require, and we may be unable to hire or retain sufficient numbers of qualified individuals in the future. Our ability to achieve significant future revenue growth will depend on our success in recruiting, training and retaining sufficient numbers of direct sales professionals. New and planned hires require significant training and time before they become fully productive, and may not become as productive as quickly as we anticipate. Our growth prospects will be harmed if our efforts to expand, train and retain our direct sales team do not generate a corresponding significant increase in revenue.

In addition to our direct sales team, we also extend our global sales distribution through relationships with more than 500 marketing service providers. These providers do not have exclusive relationships with us, and we cannot be certain that these partners will prioritize or provide adequate resources for selling our solutions. Establishing and retaining qualified partners and training them in our solutions requires significant time and resources. If we are unable to devote sufficient time and resources to establish and train these partners, or if we are unable to maintain successful relationships with these providers, our business could be adversely affected.

Because our long-term growth strategy involves further expansion of our sales to clients outside the United States, our business will be susceptible to risks associated with international operations.

A key component of our growth strategy involves the further expansion of our operations and client base internationally. In recent years, we completed acquisitions of resellers located in the United Kingdom, Australia and Brazil. As we continue to expand the sales of our suite of cross-channel, interactive marketing SaaS solutions to clients outside the United States, our business will be increasingly susceptible to risks associated with international operations. Among the risks and challenges we believe are most likely to affect us with respect to international expansion are:

- difficulties and expenses associated with the continued adaptation of our suite of cross-channel, interactive marketing SaaS solutions for international markets, including translation into foreign languages;

- difficulties in staffing and managing foreign operations and the increased travel, real estate, infrastructure and legal compliance costs associated with international operations;

- burdens of complying with applicable laws and regulations, including regional data privacy laws and anti-bribery laws such as the Foreign Corrupt Practices Act;

- in some countries, a less-developed set of rules and infrastructure for online and mobile communications;

- our ability to secure local communications and data center services and to successfully deliver communications to international ISPs and mobile carriers;

- adverse tax burdens and foreign exchange controls that could make it difficult to repatriate earnings and cash;

- currency exchange rate fluctuations;

difficulties in enforcing contracts;

difficulties in managing a business in new markets with diverse cultures, languages, customs, legal systems, alternative dispute systems and regulatory systems;

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- trade restrictions;
- laws and business practices favoring local competitors or general preferences for local vendors;
- lesser degrees of intellectual property protection;
- political instability or terrorist activities;
- legal systems subject to undue influence or corruption; and
- business cultures in which improper sales practices may be prevalent.

We have a limited operating history outside the United States, and our ability to manage our business and conduct our operations internationally requires considerable management attention and resources and is subject to the particular challenges of supporting a rapidly growing business. In addition, we have limited experience in marketing, selling and supporting our suite of cross-channel, interactive marketing SaaS solutions and services abroad, which increases the risk that our future expansion efforts will not be successful. If we invest substantial time and resources to expand our international operations and are unable to do so successfully and in a timely manner, our business, operating results and reputation will be adversely affected. Additionally, operating in international markets requires significant management attention and financial resources. We cannot be certain that the investment and additional resources required to establish operations in other countries will result in adequate revenue and profitability levels.

Our business could be adversely affected if our clients are not satisfied with our SaaS solutions, our implementation and integration of our solutions or our professional services.

Our business depends on our ability to satisfy our clients and meet their business needs. If a client is unsatisfied with our suite of cross-channel, interactive marketing SaaS solutions and professional services, we could lose the client, incur additional costs to remedy the situation, or the profitability of our relationship with that client may be impaired. In addition, negative publicity resulting from issues related to our client relationships, regardless of accuracy, may damage our business by adversely affecting our ability to attract new clients and maintain and expand our relationships with existing clients.

In addition, supporting enterprise clients could require us to devote significant development services and support personnel, which could strain our team and infrastructure, and reduce our profit margins. If we are unable to address the needs of these clients in a timely fashion or further develop and enhance our solutions, these clients may seek to terminate their relationships with us, not renew their subscriptions, renew their subscriptions on less favorable terms or not purchase additional features or solutions. If any of these were to occur, our revenue may decline, we may not realize future growth and our operating results may be materially and adversely affected.

If we fail to respond to evolving technological requirements or to introduce adequate enhancements and new features, our SaaS solutions could become obsolete or less competitive.

To remain a leading global provider of cross-channel, interactive marketing SaaS solutions, we must continue to invest in research and development of new solutions and enhancements to our existing solutions. The process of developing new technologies, products and services is complex and expensive. Our industry is characterized by rapidly changing technologies, standards, regulations and client requirements and frequent product enhancements and introductions. The introduction of new solutions by our competitors, the market acceptance of competitive solutions based on new or alternative technologies or the emergence of new industry standards could render our solutions

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obsolete or less effective. In addition, other means of interactive marketing may be developed or adopted in the future, and our solutions may not be compatible with these new marketing channels. The success of any enhancement or new solution depends on several factors, including timely completion, adequate quality testing, introduction and market acceptance. Any new solution or feature that we develop or acquire may not be introduced in a timely or cost-effective manner, may contain defects or may not achieve the broad market acceptance necessary to generate significant revenue. If we are unable to anticipate client requirements, successfully develop or acquire new solutions or features in a timely manner or enhance our existing solutions to meet our clients requirements, our business and operating results may be adversely affected.

We may experience quarterly fluctuations in our operating results due to a number of factors, which makes our future results difficult to predict and could cause our operating results to fall below expectations or our guidance.

Our quarterly operating results have fluctuated in the past and are expected to fluctuate in the future due to a variety of factors, many of which are outside of our control. As a result, comparing our operating results on a period-to-period basis may not be meaningful. Our past results may not be indicative of our future performance. If our revenue or operating results fall below the expectations of investors or securities analysts, or below any guidance we may provide, the price of our common stock could decline.

In addition to the other risks described in this prospectus, factors that may affect our quarterly operating results include the following:

- changes in spending on interactive marketing technologies by our current or prospective clients;
- the volume of utilization above contracted levels for a particular quarter and the amount of any associated additional revenue earned;
- client renewal rates, and the pricing and volume commitments at which agreements are renewed;
- clients delaying purchasing decisions in anticipation of new products or product enhancements by us or our competitors;
- budgeting cycles of our clients;
- changes in the competitive dynamics of our industry, including consolidation among competitors or clients;
- long or delayed implementation times for new clients;
- the amount and timing of operating expenses, particularly research and development and sales and marketing expenses (including commissions and bonuses associated with performance), unforeseen product execution costs, employee benefit expenses and expenses related to the expansion of our business, operations and infrastructure;
- changes in the levels of our capital expenditures;
- the amount and timing of costs associated with recruiting, training and integrating new employees; and
- failure to successfully manage any acquisitions or the incurrence of write-downs, impairment charges or unforeseen liabilities in connection with acquisitions.

We may not be able to accurately forecast the amount and mix of future subscriptions, revenue and expenses and, as a result, our operating results may fall below our estimates or the expectations of public market analysts and investors.

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Because we recognize subscription revenue from our clients over the terms of their agreements and most of the costs associated with such agreements are incurred up front, rapid increases in new clients and expanding sales to existing clients may cause an adverse impact on our short-term operating income and cash flows and may cause our operating results to be difficult to predict.

The majority of our subscription revenue in a quarter is derived from client agreements entered into in previous quarters. Significant selling activity in a quarter may result in little incremental recognized revenue and client cash receipts during that quarter, but results in the recognition of related commissions and sales and company bonuses due to immediate expense recognition. In addition, it takes several months to ramp up a professional services consultant to full productivity and, as a result, we generally must increase our professional services capacity ahead of the recognition of associated professional services revenue, which can result in lower margins in a period of significant hiring. The timing of revenue and expense recognition and associated cash flows may result in an adverse impact on our short-term operating income and cash flows and may also make it more difficult to accurately predict current quarter operating results. The resulting variations in our operating income, earnings per share, cash flows from operating activities and other financial metrics and non-financial metrics could harm the price of our common stock if they do not meet the expectations of the public market, equity research analysts or investors.

Shifts over time in the mix of sizes or types of organizations that purchase our solutions or changes in the types of solutions purchased by our clients could negatively affect our operating results.

Our strategy is to sell our suite of cross-channel, interactive marketing SaaS solutions to organizations of all sizes. While we serve all of our clients from our single SaaS platform, our profit margins can vary depending on numerous factors, including the number of clients using our SaaS solutions, the complexity and frequency of their use, the level of utilization, the volume of messages sent, the amount of stored data and the level of professional services and support required by a client. For example, because our professional services offerings typically have a higher cost of revenue than subscriptions to our SaaS solutions, any increase in sales of professional services would likely have an adverse effect on our overall gross profit margin and operating results. Enterprise organizations generally require more professional services compared to small businesses and medium-sized companies and, as a result, the overall margin for our enterprise engagements may be lower. We supplement our internal professional services team with third parties to provide professional services, and our goal is to expand these relationships over time. If we are unable to expand our network of third-party service providers, we will likely have to expand our internal team to meet the needs of our clients, which could increase our operating costs and result in lower gross margins. If the mix of organizations that purchase our solutions changes, or the mix of solution components purchased by our clients changes, our profit margins could decrease and our operating results could be adversely affected.

As the number of enterprise clients that we serve increases, we may encounter implementation challenges, and we may have to delay revenue recognition for some complex engagements, which would harm our business and operating results.

We may face unexpected challenges with some enterprise clients or more complicated implementations of our suite of cross-channel, interactive marketing SaaS solutions with such clients. It may be difficult or expensive to implement our SaaS solutions if a client has unexpected data, hardware or software technology challenges, or complex or unanticipated business requirements. In addition, prospective enterprise clients may require acceptance testing related to implementation of our SaaS solutions. Implementation delays may also require us to delay revenue recognition until the technical or implementation requirements have been met. Any difficulties or delays in the initial

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implementation could cause clients to delay or forego future purchases of our solutions, in which case our business, operating results and financial condition would be adversely affected.

We rely on our management team and other key employees, and the loss of one or more key employees could harm our business.

Our success and future growth depend upon the continued services of our management team and other key employees, including in the areas of research and development, marketing, sales, services and general and administrative functions. From time to time, there may be changes in our management team resulting from the hiring or departure of executives, which could disrupt our business. We also are dependent on the continued service of our existing development professionals because of the complexity of our solutions. We may terminate any executive officer s employment at any time, with or without cause, and any executive officer may resign at any time, with or without cause. We do not maintain key man life insurance on any of our employees. The loss of one or more of our key employees could harm our business.

Because competition for key employees is intense, we may not be able to attract and retain the highly-skilled employees we need to support our operations and future growth.

Competition for executive officers, software developers and other key employees in our industry is intense. In particular, we compete with many other companies for software developers with high levels of experience in designing, developing and managing software, as well as for skilled sales and operations professionals, and we may not be successful in attracting and retaining the professionals we need. Job candidates and existing employees often consider the actual and potential value of the equity awards they receive as part of their overall compensation. Thus, if the perceived value or future value of our stock declines, our ability to attract and retain highly skilled employees may be adversely affected. If we fail to attract new employees or fail to retain and motivate our current employees, our business and future growth prospects could be harmed.

We derive a significant portion of our revenue from clients in the retail and e-commerce, media and entertainment, travel and hospitality, financial services and insurance, technology, daily-deal and flash-sale industries, and any downturn in these industries could harm our business.

A significant portion of our revenue is derived from clients in the retail and e-commerce, media and entertainment, travel and hospitality, financial services and insurance, technology, daily-deal and flash-sale industries. Any downturn in these industries may cause our clients to reduce their spending on interactive marketing solutions, delay or cancel interactive marketing projects or seek to terminate or renegotiate their contracts with us. Also, the increased pace of consolidation in any of these industries may result in reduced overall spending on our solutions. In particular, if our clients are acquired by entities that are not our clients, that use fewer of our solutions or that choose to discontinue, reduce or change the terms of their use of our solutions, our business and operating results could be materially and adversely affected.

Our sales cycle can be unpredictable, time-consuming and expensive, which could harm our business and operating results.

Our sales efforts involve educating prospective clients and our existing clients about the use, technical capabilities and benefits of our solutions. Some clients, particularly in the enterprise market, undertake a prolonged solution-evaluation process, which frequently involves not only our solutions but also those of our competitors. As we continue to pursue enterprise clients, we may face greater costs, longer sales cycles and less predictability in completing such sales. We may spend substantial time, effort and money on our sales efforts without any assurance that our efforts will produce any sales. It is also difficult to predict the level and timing of sales that come from our indirect sales channel of marketing service providers since these resellers do not exclusively sell our solutions. Events affecting our clients businesses may occur during the sales cycle that could affect the size or timing of a purchase, contributing to more unpredictability in our business and operating results.

Uncertain or weakened global economic conditions may adversely affect our industry, business and results of operations.

Our overall performance depends on domestic and worldwide economic conditions, which may remain challenging for the foreseeable future. Financial developments seemingly unrelated to us or to our industry may adversely affect us. The U.S. economy and other key international economies have been impacted by threatened sovereign defaults and ratings downgrades, falling demand for a variety of goods and services, restricted credit, threats to major multinational companies, poor liquidity, reduced corporate profitability, volatility in credit, equity and foreign exchange markets, bankruptcies and overall uncertainty. These conditions affect the rate of information technology spending and could adversely affect our clients ability or willingness to purchase our suite of cross-channel, interactive marketing SaaS solutions and services, delay prospective clients purchasing decisions, reduce the value or duration of their subscriptions or affect renewal rates, any of which could adversely affect our operating results. We cannot predict the timing, strength or duration of the economic recovery or any subsequent economic slowdown worldwide, in the United States, or in our industry.

Any violation of our policies or misuse of our SaaS solutions by our clients could damage our reputation and subject us to liability.

Our clients could misuse our SaaS solutions by, among other things, transmitting negative messages or website links to harmful applications, sending unsolicited commercial email, reproducing and distributing copyrighted material without permission, reporting inaccurate or fraudulent data and engaging in illegal activity. Any such use of our suite of SaaS solutions could damage our reputation and could subject us to claims for damages, copyright or trademark infringement, defamation, negligence or fraud. Moreover, our clients may use our SaaS solutions to promote their products and services in violation of federal, state and foreign laws. We rely on contractual representations made to us by our clients that their use of our SaaS solutions will comply with our policies and applicable law, including, without limitation, our Anti-Spam Policy. Although we retain the right to review customer lists and emails to verify that clients are abiding by our Anti-Spam Policy, our clients are ultimately responsible for compliance with our policies, and we do not audit our clients to confirm compliance with our policies.

We cannot predict whether the use of our SaaS solutions would expose us to liability under applicable laws or subject us to other regulatory action. Even if claims asserted against us do not result in liability, we may incur substantial costs in investigating and defending against such claims, or our reputation may be damaged. If we are found liable in connection with our clients activities, we could be required to pay fines or penalties, redesign our SaaS solutions or otherwise expend resources to remedy any damages caused by such actions and to avoid future liability.

Federal, state and foreign laws regulating email and text messaging marketing practices impose certain obligations on the senders of commercial emails and text messages, which could reduce the effectiveness of our solutions or increase our operating expenses to the extent these laws subject us to financial penalties.

The Federal Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003 (the CAN-SPAM Act) regulates commercial email messages and specifies penalties for the transmission of commercial email messages that are intended to deceive the recipient as to source or content.

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Among other things, the CAN-SPAM Act obligates each sender of commercial emails to allow recipients to opt-out of receiving future emails from the sender. In addition, the CAN-SPAM Act, regulations implemented by the Federal Communications Commission pursuant to the CAN-SPAM Act and the Telephone Consumer Protection Act (also known as the Federal Do-Not-Call law) prohibit companies from sending specified types of commercial text messages unless the recipient has opted in to the receipt of such text messages.

In addition, some states have passed laws regulating commercial email. In some cases, these laws are significantly more punitive and difficult to comply with than the CAN-SPAM Act. For example, Utah and Michigan have enacted do-not-email registries to protect minors from receiving unsolicited commercial email marketing adult content and other products that minors are prohibited from obtaining. Whether such state laws are preempted in whole or in part by the CAN-SPAM Act is uncertain. Furthermore, certain foreign jurisdictions, such as Australia, Canada and the European Union, have also enacted laws that regulate email. Some of these laws are more restrictive than U.S. laws.

As Internet commerce continues to evolve and grow, increasing regulation by federal, state or foreign governments may become more likely. Federal, state or foreign jurisdictions may in the future enact laws or regulations restricting the ability to conduct interactive marketing through mobile, social media and web channels. The cost to comply with such laws or regulations could be significant and would increase our operating expenses. We may be unable to pass along those costs to our clients in the form of increased subscription fees. If such restrictions require us to change one or more aspects of the way we operate our business, it could impair our ability to attract and retain clients or otherwise harm our business.

Noncompliance with any existing or future laws and regulations may subject us to significant financial penalties. If we are found to have violated these laws or regulations or if our clients are found to have violated these laws or regulations, we could be required to pay penalties, which would adversely affect our financial performance and harm our reputation and our business.

Regulation of the Internet and the lack of certainty regarding the application of existing laws to the Internet could substantially harm our operating results and business.

We are subject to laws and regulations applicable to doing business over the Internet. It is often not clear how existing laws governing issues such as property ownership, sales and other taxes, libel and personal privacy apply to the Internet, as these laws have in some cases failed to keep pace with technological change. Recently-enacted laws governing the Internet could also impact our business. For instance, existing and future regulations on taxing Internet use or restricting the exchange of information over the Internet could result in reduced growth or a decline in the use of the Internet and could diminish the viability of our services. Furthermore, it is possible that governments of one or more countries may censor, limit or block certain users access to websites or other social media services. Changing industry standards and industry self regulation regarding the collection, use and disclosure of certain data may have similar effects. Any such adverse legal or regulatory developments could substantially harm our operating results and our business.

If we are unable to protect our proprietary technology and intellectual property, our business could be adversely affected.

Our success is dependent upon our ability to protect our proprietary technology and intellectual property, which may require us to incur significant costs. We rely on a combination of confidentiality obligations in contracts, patents, copyrights, trademarks, service marks, trade secret laws and other contractual restrictions to establish and protect our proprietary rights. In particular, we enter into confidentiality and invention assignment agreements with all of our employees and consultants and

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enter into confidentiality agreements with the parties with whom we have business relationships in which they will have access to our confidential information. No assurance can be given that these agreements or other steps we take to protect our intellectual property will be effective in controlling access to and distribution of our solutions and our confidential and proprietary information. We will not be able to protect our intellectual property if we are unable to enforce our rights or if we do not detect unauthorized uses of our intellectual property. Despite our precautions, it may be possible for third parties to copy our solutions and use information that we regard as proprietary to create products and services that compete with ours. Third parties may also independently develop technologies that are substantially equivalent or superior to our solutions. Some license provisions protecting against unauthorized use, copying, transfer and disclosure of our solutions may be unenforceable under the laws of certain jurisdictions and foreign countries. Further, the laws of some countries do not protect proprietary rights to the same extent as the laws of the United States. To the extent we expand our international activities, our exposure to unauthorized copying and use of our solutions and proprietary information may increase.

In some cases, litigation may be necessary to enforce our intellectual property rights or to protect our trade secrets. Litigation could be costly, time consuming and distracting to management and could result in the impairment or loss of portions of our intellectual property. Furthermore, our efforts to enforce our intellectual property rights may be met with defenses, counterclaims and countersuits attacking the validity and enforceability of our intellectual property rights and exposing us to significant damages or injunctions. Our inability to protect our proprietary technology against unauthorized copying or use, as well as any costly litigation or diversion of our management s attention and resources, could delay sales or the implementation of our solutions, impair the functionality of our solutions, delay introductions of new solutions, result in our substituting less-advanced or more-costly technologies into our solutions or harm our reputation. In addition, we may be required to license additional technology from third parties to develop and market new solutions, and we cannot assure you that we could license that technology on commercially reasonable terms or at all.

We cannot be certain that any patents will be issued with respect to our current or potential patent applications.

To date, we have eight patent applications pending in one or more jurisdictions and no issued patents. We do not know whether any of our patent applications will result in the issuance of patents or whether the examination process will require us to narrow the scope of our claims. To the extent any of our applications proceed to issuance as a patent, any such future patent may be opposed, contested, circumvented, designed around by a third party or found to be invalid or unenforceable. The process of seeking patent protection can be lengthy and expensive. Some of our technology is not covered by any patent or patent application.

We have entered into a non-exclusive license that allows us to utilize methods covered by a business process patent held by a third party in providing our solutions, and our inability to maintain that license could have a material adverse effect on the functionality of our solutions, which would adversely affect our revenues and results of operations.

We have entered into a license agreement with Hula Holdings, LLC and Subscribermail, LLC (which was acquired by Harland Clarke Corp. in 2010) under which we have a non-exclusive license to use methods covered by a patent owned by Hula Holdings, LLC and licensed to Subscribermail, LLC for multi-level email methodology. The license will survive for the term of the patent, which will expire in 2021. If we were to lose the license for any reason, the functionality of our solutions may decline, which would have a material adverse effect on our revenue, financial condition and results of operations. Because the license is non-exclusive, our competitors may have access to this methodology.

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We may be sued by third parties for alleged infringement of their proprietary rights.

The software industry is characterized by the existence of a large number of patents, copyrights, trademarks, trade secrets and other intellectual property and proprietary rights. Companies in our industry are often required to defend against litigation claims based on allegations of infringement or other violations of intellectual property rights. Our technologies may not be able to withstand any third-party claims or rights against their use. As a result, our success depends upon our not infringing upon the intellectual property rights of others. Our competitors, as well as a number of other entities and individuals, may own or claim to own intellectual property relating to our industry. From time to time, we have received threatening letters or notices or may be the subject of claims that our solutions and underlying technology infringe or violate the intellectual property rights of others, and we may be found to be infringing upon such rights.

Any claims or litigation could cause us to incur significant expenses and, if successfully asserted against us, could require that we pay substantial damages or ongoing royalty payments, prevent us from offering our solutions or require that we comply with other unfavorable terms. Even if the claims do not result in litigation or are resolved in our favor, these claims, and the time and resources necessary to resolve them, could divert the resources of our management and harm our business and operating results.

Indemnity provisions in our subscription agreements potentially expose us to substantial liability for intellectual property infringement and other losses.

In our subscription agreements with our clients, we typically agree to indemnify our clients against any losses or costs incurred in connection with claims by a third party alleging that a client s use of our services infringes the intellectual property rights of the third party, unless such infringement relates to use of our services in combination with other software not provided by us, arises from modifications not authorized by us or results from continued use by the client after notification by us. Companies in the software industry, including those that provide SaaS solutions, frequently face infringement threats from non-practicing organizations (sometimes referred to as patent trolls) filing lawsuits for patent infringement. Two of our clients have notified us of claims brought against them for infringement by such a patent troll and have requested indemnification or indicated that they may seek redress from us under the indemnification provisions of our contracts with them. Other clients facing infringement claims who are accused of infringement may in the future seek indemnification from us under the terms of our contracts. If such claims are successful, or if we are required to indemnify or defend our clients from these or other claims, these matters could be disruptive to our business and management and have a material adverse effect on our business, operating results and financial condition.

We use open source software in our solutions, which may subject us to litigation or other actions that could adversely affect our business.

We use open source software in our solutions and may use more open source software in the future. In the past, companies that incorporate open source software into their products have faced claims challenging the ownership of open source software or compliance with open source license terms. Therefore, we could be subject to suits by parties claiming ownership of what we believe to be open source software or claiming noncompliance with open source licensing terms. Some open source software licenses require users who distribute open source software as part of their software to publicly disclose all or part of the source code to such software or make available any derivative works of the open source code on unfavorable terms or at no cost. If we were to use open source software subject to such licenses, we could be required to release our proprietary source code, pay damages, re-engineer our applications, discontinue sales or take other remedial action, any of which could adversely affect our business.

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Our inability to acquire and integrate other businesses, products or technologies could harm our operating results.

Since 2009, we have acquired our social media management and engagement platform and three international software reseller partners. We may in the future acquire or invest in businesses, products or technologies that we believe could complement or expand our existing solutions, expand our client base and operations worldwide, enhance our technical capabilities or otherwise offer growth or cost-saving opportunities. We have limited experience in successfully acquiring and integrating businesses, products and technologies. If we identify an appropriate acquisition candidate, we may not be successful in negotiating the terms of the acquisition, financing the acquisition or effectively integrating the acquired business, product or technology into our existing business and operations. Our due diligence may fail to identify all of the problems, liabilities or other shortcomings or challenges of an acquired business, product or technology, including issues related to intellectual property, product quality or product architecture, regulatory compliance practices, revenue recognition or other accounting practices, or employee or customer issues.

Additionally, in connection with any acquisitions we complete, we may not achieve the synergies or other benefits we expected to achieve, and we may incur write-downs, impairment charges or unforeseen liabilities that could negatively affect our operating results or financial position or could otherwise harm our business. If we finance acquisitions by issuing convertible debt or equity securities, the ownership interest of our existing stockholders may be diluted, which could adversely affect the market price of our stock. Further, contemplating or completing an acquisition and integrating an acquired business, product or technology could divert management and employee time and resources from other matters.

If we are unable to integrate our SaaS solutions with certain third-party applications, the functionality of our solutions could be adversely affected.

The functionality of our solutions depends on our ability to integrate them with third-party applications and data management systems used by our clients to obtain consumer data. In addition, we rely on access to third-party APIs to provide our social media channel offerings through social media platforms. Third-party providers of marketing applications and APIs may change the features of their applications and platforms, restrict our access to their applications and platforms or alter the terms governing use of their applications and APIs and access to those applications and platforms in a manner adverse to us. Such changes could limit our ability to integrate or could prevent us from integrating our software with these third-party applications and platforms, which could impair the functionality of our software and harm our business. Further, if we fail to integrate our software with new third-party applications and platforms that our clients use for marketing purposes, or if we fail to adapt to the data transfer requirements of such third-party applications and platforms, demand for our solutions could decrease, which would harm our business and operating results.

The market forecasts included in this prospectus may prove to be inaccurate, and even if the markets in which we compete achieve the forecasted growth, we cannot assure you that our business will grow at similar rates, or at all.

The market forecasts included in this prospectus, including the forecasts by Forrester and Gartner, Inc. (Gartner), are subject to significant uncertainty and are based on assumptions and estimates that may not prove to be accurate. This risk also applies to forecasts of anticipated spending on interactive marketing channels. Market data and forecasts relating to international spending on interactive marketing are even more limited than data for the U.S. market. If the forecasts of market growth or anticipated spending prove to be inaccurate, our business and growth prospects could be adversely affected. Even if the forecasted growth occurs, our business may not grow at a similar rate,

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or at all. Our future growth is subject to many factors, including our ability to successfully implement our business strategy, which itself is subject to many risks and uncertainties. Accordingly, the forecasts and market data in this prospectus should not be taken as indicative of our future growth.

We may not be able to utilize a significant portion of our net operating loss carry-forwards, which could adversely affect our operating results and cash flows.

As of September 30, 2011, we had $25.9 million of net operating loss carry-forwards and $4.4 million of net operating loss carry-forwards from unrecognized stock option exercise deductions. Utilization of these net operating loss carry-forwards depends on many factors, including our future income, which cannot be assured. Our loss carry-forwards begin to expire in 2029. In addition, Section 382 of the Internal Revenue Code generally imposes an annual limitation on the amount of net operating loss carry-forwards that may be used to offset taxable income when a corporation has undergone significant changes in stock ownership. Although we have undergone one or more ownership changes as a result of prior financings, we believe that any such change in ownership and the corresponding annual limitation likely will not prevent us from using our current net operating losses in any significant or material way. However, future ownership changes, including an ownership change in connection with this offering, or future regulatory changes could limit our ability to utilize our net operating loss carry-forwards. To the extent we are not be able to offset our future income against our net operating loss carry-forwards, this would adversely affect our operating results and cash flows.

Tax laws or regulations could be enacted or existing laws could be applied to us or our clients, which could increase the costs of our solutions and adversely impact our business.

The application of federal, state, local and international tax laws to services and products provided electronically is evolving. New income, sales, use or other tax laws, statutes, rules, regulations or ordinances could be enacted at any time (possibly with retroactive effect), and could be applied solely or disproportionately to services and products provided over the Internet or via email, which could discourage the use of the Internet and email as a means of commercial marketing, adversely affecting the viability of our solutions. These enactments could adversely affect our sales activity due to the inherent cost increase the taxes would represent and ultimately result in a negative impact on our operating results and cash flows.

In addition, existing tax laws, statutes, rules, regulations or ordinances could be interpreted, changed, modified or applied adversely to us (possibly with retroactive effect), which could require us or our clients to pay additional tax amounts, as well as require us or our clients to pay fines or penalties and interest for past amounts. If we are unsuccessful in collecting such taxes from our clients, we could be held liable for such costs, thereby adversely impacting our operating results and cash flows.

As a public company, our business will be subject to regulations regarding corporate governance, disclosure controls, internal control over financial reporting and other compliance areas that will increase both our costs and the risk of noncompliance with applicable laws.

After the completion of this offering, we will be subject to the reporting requirements of the Securities Exchange Act of 1934 (the Exchange Act), the Sarbanes-Oxley Act of 2002 (the Sarbanes-Oxley Act), the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 and the rules and regulations of the stock market on which our common stock is traded. Being subject to these rules and regulations will increase our legal, accounting and financial compliance costs, will make some activities more difficult, time-consuming and costly and may also place significant additional strain on our personnel, systems and resources.

The Sarbanes-Oxley Act requires, among other things, that we maintain effective disclosure controls and procedures and internal controls over financial reporting. Commencing with our fiscal year

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ending December 31, 2013, we must perform system and process evaluation and testing of our internal controls over financial reporting to allow management and our independent registered public accounting firm to report on the effectiveness of our internal controls over financial reporting in our Form 10-K filing for such year, as required by Section 404 of the Sarbanes-Oxley Act. This will require that we incur substantial accounting expense and expend significant management efforts. Prior to this offering, we have never been required to test our internal controls within a specified period, and, as a result, we may experience difficulty in meeting these reporting requirements in a timely manner, particularly if material weaknesses or significant deficiencies are found.

If we are not able to comply with the requirements of Section 404 of the Sarbanes-Oxley Act in a timely manner, the market price of our stock could decline and we could be subject to sanctions or investigations by the stock exchange on which our common stock is listed, the SEC or other regulatory authorities.

There may be limitations on the effectiveness of our controls and the failure of our control systems may materially and adversely impact us.

We do not expect that disclosure controls or internal controls over financial reporting will prevent all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system s objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, will be detected.

Implementing any required changes to our disclosure controls or internal controls may require specific compliance training of our directors, officers and employees, entail substantial costs to modify our existing accounting systems and take a significant period of time to complete. Such changes may not, however, be effective in maintaining the adequacy of our controls. Failure to develop or maintain effective controls, or any difficulties encountered in their implementation or improvement, could harm our operating results or cause us to fail to meet our reporting obligations. In the event that our disclosure controls or internal controls are perceived as inadequate or that we are unable to produce timely or accurate financial statements, investors may lose confidence in our operating results which could cause our stock price to decline.

Changes in financial accounting standards or practices may cause adverse, unexpected financial reporting fluctuations and affect our reported results of operations.

Financial accounting standards may change or their interpretation may change. A change in accounting standards or practices can have a significant effect on our reported results and may even affect our reporting of transactions completed before the change becomes effective. Changes to existing rules or the re-examining of current practices may adversely affect our reported financial results or the way we conduct our business. Accounting for revenue from sales of our solutions is particularly complex, is often the subject of intense scrutiny by the SEC, and will evolve as the Financial Accounting Standards Board (the FASB) continues to consider applicable accounting standards in this area.

We may not be able to secure sufficient additional financing on favorable terms, or at all, to meet our future capital needs.

In the future, we may require additional capital to pursue business opportunities or acquisitions or respond to challenges and unforeseen circumstances. We may also decide to engage in equity or debt financings or enter into credit facilities for other reasons. We may not be able to secure additional debt or equity financing in a timely manner, on favorable terms, or at all. Any debt financing obtained by us in the future could involve restrictive covenants relating to our capital raising activities and other financial and operational matters, which may make it more difficult for us to obtain additional capital and to pursue business opportunities, including potential acquisitions. After this offering, the holders of an aggregate of shares of our common stock outstanding as of will have rights, subject to some conditions, to require us to include their shares in registration statements that we may file for ourselves or our stockholders. If these holders exercise such registration rights and require us to include their shares in a registration statement that we propose to file, and the managing underwriter advises us that the inclusion of all shares requested by the holders would interfere with the successful marketing of the securities in such registration, the securities to be included in such registration are to be allocated to the holders first and the number of shares we propose to sell would be reduced. As a result, we may not be able to obtain adequate financing from the public offering.

Catastrophic events may disrupt our business.

We rely heavily on our network infrastructure and information technology systems for our business operations. A disruption or failure of these systems in the event of a tornado, earthquake, fire, cyber-attack, terrorist attack, power loss, telecommunications failure or other similar catastrophic event could cause system interruptions, delays in the delivery of our clients interactive marketing communications, reputational harm and loss of critical data or could prevent us from providing our interactive marketing solutions to our clients. Our system hardware is co-located in two data centers operated by third parties in Indianapolis, Indiana and Las Vegas, Nevada. A third data center in Indianapolis is planned for operation in the fourth quarter of 2011. A catastrophic event that results in the destruction or disruption of any of these data centers, or our network infrastructure or information technology systems, could affect our ability to conduct normal business operations and adversely affect our operating results.

Risks Related to this Offering and Ownership of Our Common Stock

There has been no prior market for our common stock, our stock price may be volatile or may decline regardless of our operating performance and you may not be able to resell your shares at or above the initial public offering price, if at all.

There has been no public market for our common stock prior to this offering. The initial public offering price for our common stock will be determined through negotiations between the underwriters and us and may be different from the market price of our common stock following this offering. If you purchase shares of our common stock in this offering, you may not be able to resell those shares at or above the initial public offering price, or at all. An active or liquid market in our common stock may not develop upon the closing of this offering or, if it does develop, it may not be sustainable, which could adversely affect your ability to sell your shares and could depress the market price of our common stock. The market price of our common stock may fluctuate significantly in response to numerous factors, many of which are beyond our control. In addition to the other risk factors described herein, these factors include:

- actual or anticipated fluctuations in our revenue and other operating results;

- the financial guidance we may provide to the public, any changes in such guidance, our failure to meet any such guidance or any changes in analysts recommendations;

- announcements by us or our competitors of significant technical innovations, acquisitions, strategic partnerships, joint ventures or capital commitments;

- changes in operating performance and stock market valuations of software or other technology companies, particularly companies in our industry;

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- the addition or loss of significant clients;
- fluctuations in the trading volume of our common stock or the size of our public float;
- announcements by us with regard to the effectiveness of our internal controls and our ability to accurately report our financial results;
- price and volume fluctuations in the overall stock market, including as a result of trends in the economy as a whole;
- general economic, legal, regulatory and market conditions unrelated to our performance;
- lawsuits threatened or filed against us; and
- other events or factors, including those resulting from war, incidents of terrorism or responses to these events.

If the market price of our common stock after this offering does not exceed the initial public offering price, you may not realize any return on your investment in our common stock and may lose some or all of your investment. In addition, the stock markets have experienced extreme fluctuations in price and trading volume that have caused and will likely continue to cause the stock prices of many technology companies to fluctuate in a manner unrelated or disproportionate to the operating performance of those companies. In the past, stockholders have instituted securities class action litigation following periods of declining stock prices. If we were to become involved in securities litigation, we could face substantial costs and be forced to divert resources and the attention of management from our business, which could adversely affect our business.

If securities or industry analysts do not publish research or publish inaccurate or unfavorable research about our business, our stock price and trading volume could decline.

The trading market for our common stock will depend on the research and reports that securities or industry analysts publish about us or our business. Securities analysts do not currently cover our business and may never do so. Industry analysts that currently cover us may cease to do so. If no securities analysts commence coverage of our company, or if industry analysts cease to cover our company, the trading price of our stock could decline. In the event one or more securities analysts begin to cover our company, a downgrade of our stock or the publication of inaccurate or unfavorable research about our business would likely cause our stock price to decline. If one or more of these analysts cease to cover our company or fail to publish reports about us regularly, demand for our stock could decrease, which might cause our stock price and trading volume to decline.

Sales of substantial amounts of our common stock in the public market, or the perception that they might occur, could reduce the price that our common stock might otherwise attain and may dilute your voting power and your ownership interest in us.

The price of our common stock could decline if there are substantial sales of our common stock, particularly sales by our directors, executive officers and significant stockholders, or if there is a large number of shares of our common stock available for sale. After this offering, there will be outstanding shares of our common stock, based on the number of shares outstanding as of . This includes the shares that we are selling in this offering, which may be resold in the public market immediately. The remaining outstanding shares after this offering are currently restricted as a result of market standoff agreements. In addition, certain of these shares are also subject to lock-up agreements, as more fully described in Underwriting. In each case, these shares will become sellable 180 days after the date of this prospectus, subject to extension in some circumstances. Shares held by directors, executive officers and other affiliates will be subject to volume limitations under Rule 144 under the Securities Act of 1933 (the Securities Act) and various vesting agreements in some cases.

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After this offering, the holders of an aggregate of shares of our common stock outstanding as of will have rights, subject to some conditions, to require us to file registration statements covering their shares or to include their shares in registration statements that we may file for ourselves or our stockholders. For a more detailed description of these registration rights, see Description of Capital Stock Registration Rights. All of these shares are subject to market standoff or lock-up agreements restricting their sale for 180 days after the date of this prospectus, subject to extension in some circumstances. We also intend to file registration statements covering the shares of common stock that we have issued and may issue under our employee equity incentive plans. Once these registration statements are filed, these shares will be able to be sold freely in the public market upon issuance, subject to existing market standoff or lock-up agreements. J.P. Morgan Securities LLC, Deutsche Bank Securities Inc. and Stifel, Nicolaus & Company, Incorporated acting together may, in their sole discretion, permit our officers, directors, employees and current stockholders who are subject to the contractual lock-up to sell shares prior to the expiration of the lock-up agreements. See Underwriting for more information.

We may issue shares of our common stock or securities convertible into our common stock from time to time in connection with financings, acquisitions, investments or otherwise. Any such issuance could result in ownership dilution to our existing stockholders and cause the trading price of our common stock to decline.

We have broad discretion over the use of the net proceeds from this offering and may not use them effectively.

Our management will have broad discretion to use the net proceeds of this offering for a variety of purposes, including, but not limited to, repayment of debt, general corporate purposes, working capital, sales and marketing activities, general and administrative matters, capital expenditures and potential acquisitions. We may spend or invest these proceeds in a way with which our stockholders disagree. Failure by our management to effectively use these funds could harm our business and financial condition. Until the net proceeds are used, they may be placed in investments that do not yield a favorable return to our investors, do not produce significant income or lose value.

Delaware law and our amended and restated certificate of incorporation and bylaws contain provisions that could delay or discourage takeover attempts that our stockholders may consider favorable.

Provisions in our amended and restated certificate of incorporation and amended and restated bylaws, as they will be in effect upon the closing of this offering, may have the effect of delaying or preventing a change of control or changes in our management. These provisions include the following:

- our board of directors is divided into three classes serving staggered three-year terms;
- our board of directors has the right to elect a director to fill a vacancy created by the expansion of the board of directors or due to the resignation or departure of an existing board member;
- our directors are not elected by cumulative voting; cumulative voting would allow less than a majority of stockholders to elect director candidates;
- advance notice of nominations for election to the board of directors or for proposing matters that can be acted upon at a stockholders meeting is required;
- our board of directors may alter our bylaws without obtaining stockholder approval;
- our board of directors may issue, without stockholder approval, up to shares of preferred stock with terms set by the board of directors, certain rights of which could be senior to those of our common stock;

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- stockholders do not have the right to call a special meeting of stockholders and to take action by written consent in lieu of a meeting;

- approval of at least two thirds of the shares entitled to vote at an election of directors is required to amend or repeal, or adopt any provision inconsistent with, our amended and restated bylaws or the provisions of our amended and restated certificate of incorporation regarding the election and removal of directors; and

- directors may be removed from office only for cause.

In addition, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law (the DGCL). In general, Section 203 prohibits a publicly-held Delaware corporation from engaging in a business combination with an interested stockholder for three years following the time that such stockholder becomes an interested stockholder, unless the business combination is approved in a prescribed manner. A business combination includes, among other things, a merger, asset or stock sale or other transaction resulting in a financial benefit to the interested stockholder. An interested stockholder is a person who, together with affiliates and associates, owns, or did own, within three years prior to the determination of interested stockholder status, 15% or more of a corporation s voting stock.

These provisions may prohibit large stockholders, particularly those owning 15% or more of our outstanding voting stock, from merging or combining with us. These provisions in our amended and restated certificate of incorporation and our amended and restated bylaws and the DGCL could discourage potential takeover attempts, could reduce the price that investors are willing to pay for shares of our common stock in the future and could potentially result in the market price of our common stock being lower than it otherwise would be.

Our directors, executive officers and principal stockholders will continue to have substantial control over our company after this offering and could delay or prevent a change in corporate control.

After this offering, our directors, executive officers and holders of more than 5% of our common stock, together with their affiliates, will beneficially own, in the aggregate, % of our outstanding common stock. As a result, these stockholders, acting together, would have the ability to control the outcome of matters submitted to our stockholders for approval, including the election of directors and any merger, consolidation or sale of all or substantially all of our assets. In addition, these stockholders, acting together, would have the ability to control our management and affairs. Accordingly, this concentration of ownership might harm the market price of our common stock by:

- delaying, deferring or preventing a change in control of our company;

- impeding a merger, consolidation, takeover or other business combination involving us; or

- discouraging a potential acquirer from making a tender offer or otherwise attempting to obtain control of our company.

We do not intend to pay dividends for the foreseeable future.

We have never declared or paid cash dividends on our common stock. Our existing credit facilities prohibit us from paying dividends, and any future financing agreements may also restrict our ability to pay dividends. We currently intend to retain any future earnings to finance the operation and expansion of our business, and we do not expect to declare or pay any dividends in the foreseeable future. As a result, you may only receive a return on your investment in our common stock if the market price of our common stock increases.

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If you purchase shares of our common stock in this offering, you will experience substantial and immediate dilution.

The initial public offering price of our common stock will be substantially higher than the pro forma net tangible book value per share of our outstanding common stock following this offering. Therefore, if you purchase shares of our common stock in this offering, you will experience immediate dilution of $ per share, the difference between the price per share you pay for our common stock and the pro forma net tangible book value per share as of , after giving effect to the issuance of shares of our common stock in this offering. See Dilution. This dilution is due in large part to the fact that our earlier investors paid substantially less than the initial public offering price when they purchased their shares of our capital stock.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This prospectus includes forward-looking statements. All statements contained in this prospectus are forward-looking statements, except for statements of historical fact, including statements regarding our future results of operations and financial position, and statements that address activities, events or developments that we expect, believe or anticipate will exist or may occur in the future. In some cases, forward-looking statements can be identified by various forms of words such as believe, may, might, could, will, should, seek, estimate, continue, project, intend, deliver, expect, forecast, goals, objectives, targets, plans, potential, scheduled or other similar expressions. forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategy, short-term and long-term business operations, objectives and financial needs. These forward-looking statements are subject to a number of risks, uncertainties and assumptions, including those described under Risk Factors. Moreover, we operate in a very competitive and rapidly changing environment where new risks emerge from time to time. Our management cannot predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In addition to causing our actual results to differ, such risks and factors may cause our intentions to change from those statements of intention set forth in this prospectus. Such changes in our intentions may also cause our results to differ. We may change our intentions at any time and without notice based upon changes in such factors, our assumptions or otherwise. In light of these risks, uncertainties and assumptions, the future events and trends discussed in this prospectus may not occur and actual results could differ materially and adversely from those anticipated or implied in the forward-looking statements. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements.

All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements set forth above. Given the uncertainties and risk factors that could cause our actual results to differ materially from those contained in any forward-looking statement, we caution investors not to unduly rely on our forward-looking statements. Forward-looking statements speak only as of the date they are made. We disclaim any obligation to and do not intend to update any forward-looking statements or to announce publicly the result of any revisions to any of the forward-looking statements to reflect future events or developments, except to the extent required by applicable laws. If we update one or more forward-looking statements, no inference should be drawn that we will make additional updates with respect to those or other forward-looking statements.

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INDUSTRY AND MARKET DATA

This prospectus contains estimates and information concerning our industry, including market position, market size and growth rates of the markets in which we participate, that are based on industry publications and reports, including those generated by Forrester, the Direct Marketing Association and Gartner. This information involves a number of assumptions and limitations, and you are cautioned not to give undue weight to these estimates as there is no assurance that any of them will be achieved. Although we have not independently verified the accuracy or completeness of the data contained in these industry publications and reports, based on our industry experience we believe that the publications and reports are reliable and that the conclusions contained in the publications and reports are reasonable. A variety of factors, including those described under Risk Factors, could cause results to differ materially from those expressed in these publications and reports.

The statement in this prospectus attributable to Gartner represents data published as part of a syndicated subscription service, by Gartner, and is not a representation of fact. Such statement speaks as of its original publication date (and not as of the date of this prospectus) and the opinions expressed in Gartner publications are subject to change without notice.

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USE OF PROCEEDS

We estimate that the net proceeds to us from the sale of shares of our common stock in this offering will be approximately $ million, based on an assumed initial public offering price of $ per share, the midpoint of the price range set forth on the cover page of this prospectus, and after deducting estimated underwriting discounts and commissions and estimated offering expenses payable by us. If the underwriters exercise their option to purchase additional shares in full, we estimate that our net proceeds will be approximately $ million. A $1.00 increase or decrease in the assumed initial public offering price of $ per share would increase or decrease the net proceeds to us from this offering by approximately $ million, assuming the number of shares offered by us, as indicated on the cover page of this prospectus, remains the same and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us.

The principal purposes of this offering are to create a public market for our common stock, obtain additional capital, facilitate our future access to the public equity markets, increase awareness of our company among potential clients and improve our competitive position. We intend to use the net proceeds from this offering primarily for general corporate purposes, such as expanding our sales and marketing teams, international operations, product development efforts and general and administrative functions, as well as for working capital. Additionally, we may choose to expand our business through acquisitions of or investments in other businesses, products or technologies, using cash or shares of our common stock. However, we have no commitments with respect to any such acquisitions or investments at this time. We may also use a portion of the net proceeds to repay our term loan and revolving line of credit.

Pending the use of the proceeds from this offering, we intend to invest the proceeds in short-term, interest-bearing, investment-grade instruments, certificates of deposit or direct or guaranteed obligations of the U.S. government.

DIVIDEND POLICY

We have never declared or paid cash dividends on our common stock. We currently intend to retain any future earnings for use in the operation of our business and do not intend to declare or pay any dividends in the foreseeable future. Any future determination to pay dividends on our capital stock will be at the discretion of our board of directors and will depend on our financial condition, results of operations, capital requirements and other factors that our board of directors considers relevant. Our existing credit facility currently prohibits our payment of dividends.

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CAPITALIZATION

The following table sets forth our capitalization as of September 30, 2011:

- on an actual basis;
- on a pro forma basis to give effect to the automatic conversion of all outstanding shares of our preferred stock into shares of common stock; and
- on a pro forma as adjusted basis to give effect to (1) the issuance and sale by us of shares of common stock in this offering, and the receipt of the net proceeds from our sale of these shares at an assumed initial public offering price of $ per share, the midpoint of the range listed on the cover page of this prospectus, after deducting estimated underwriting discounts and commissions and estimated offering expenses payable by us and (2) the amendment and restatement of our certificate of incorporation in connection with this offering.

You should read this table in conjunction with the section entitled Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the related notes included elsewhere in this prospectus.

	As of September 30, 2011		
	Actual	Pro Forma	Pro Forma As Adjusted
	(in thousands, except shares) (unaudited)		
Cash and cash equivalents	$ 29,550	$	$
Debt:			
Revolving line of credit	10,000		
Term loan, current and long-term portions	7,500		
Total debt	17,500		
Redeemable convertible preferred stock:			
Redeemable convertible preferred stock; at respective redemption value: 4,912,646 shares authorized and 4,912,646 shares issued and outstanding, actual; no shares authorized, issued or outstanding, pro forma and pro forma as adjusted	63,000		
Stockholders equity:			
Common stock; $0.001 par value: 35,000,000 shares authorized and 4,482,140 shares issued and outstanding, actual; shares authorized and shares issued and outstanding, pro forma; shares authorized and shares issued and outstanding, pro forma as adjusted	5		
Additional paid-in capital	14,776		
Preferred stock; at respective issuance date fair value: 16,554,573 shares authorized and 16,554,573 shares issued and outstanding, actual; no shares authorized, issued or outstanding, pro forma and pro forma as adjusted	124,921		
Accumulated other comprehensive loss	(1,014)		
Accumulated deficit	(139,993)		
Total stockholders equity (deficit)	(1,305)		
Total capitalization	$ 79,195	$	

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DILUTION

If you invest in our common stock in this offering, your interest will be diluted to the extent of the difference between the initial public offering price per share of our common stock and the pro forma as adjusted net tangible book value per share of our common stock immediately after completion of this offering. Pro forma net tangible book value dilution per share to new investors represents the difference between the initial public offering price per share of our common stock and the pro forma as adjusted net tangible book value per share of our common stock immediately after completion of this offering.

Our pro forma net tangible book value (deficit) as of September 30, 2011 before giving effect to this offering was $ million, or $ per share, based on the total number of shares of our common stock outstanding as of September 30, 2011, assuming the conversion of all outstanding shares of our preferred stock as of into shares of our common stock.

After giving effect to our sale of shares of common stock in this offering, assuming an initial public offering price of $ per share, the midpoint of the price range set forth on the cover page of this prospectus, and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us, our pro forma as adjusted net tangible book value as of September 30, 2011 would have been $ million, or $ per share. This represents an immediate increase in net tangible book value of $ per share to existing stockholders and an immediate dilution in net tangible book value of $ per share to new investors in our common stock in this offering, as illustrated in the following table:

Assumed initial public offering price per share		$
Pro forma net tangible book value (deficit) per share as of September 30, 2011, before giving effect to this offering	$	
Increase in pro forma net tangible book value (deficit) per share attributable to new investors in this offering		
Pro forma as adjusted net tangible book value per share after giving effect to this offering		
Dilution per share to new investors in this offering		

If the underwriters exercise their option to purchase additional shares of our common stock in full, the pro forma as adjusted net tangible book value per share will be $ per share, the increase in pro forma net tangible book value per share to existing stockholders will be $ per share and the dilution per share to new investors purchasing shares in this offering will be $ per share.

The following table presents, on a pro forma basis as of September 30, 2011, after giving effect to our sale of shares of common stock in this offering and the automatic conversion of all outstanding shares of preferred stock as of into shares of common stock, the differences between our existing stockholders and the new investors in this offering with respect to the number of shares of our common stock purchased from us, the total consideration paid to us and the average price paid per share:

	Shares Purchased		Total Consideration		Average Price
	Number	Percent	Amount	Percent	Per Share
Existing stockholders		%	$	%	$
New investors					
Total		100%	$	100%	

Except as otherwise indicated, the above discussion and tables assume no exercise of the underwriters option to purchase additional shares. If the underwriters exercise their option to purchase additional shares of our common stock in full, our existing stockholders will own % and our new investors will own % of the total number of shares of our common stock outstanding immediately after this offering.

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SELECTED CONSOLIDATED FINANCIAL DATA

The following selected consolidated financial data should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the related notes included elsewhere in this prospectus. The selected consolidated financial data included in this section are not intended to replace our consolidated financial statements and the related notes included elsewhere in this prospectus.

The consolidated statements of operations data for the years ended December 31, 2008, 2009 and 2010, and the consolidated balance sheet data as of December 31, 2009 and 2010, were derived from our audited consolidated financial statements that are included elsewhere in this prospectus. The consolidated statements of operations data for the years ended December 31, 2006 and 2007, and the consolidated balance sheet data as of December 31, 2006, 2007 and 2008, were derived from our audited consolidated financial statements not included in this prospectus. The unaudited consolidated statements of operations data for the nine months ended September 30, 2010 and 2011, and the unaudited consolidated balance sheet data as of September 30, 2011, were derived from our unaudited consolidated financial statements included elsewhere in this prospectus. We have prepared the unaudited consolidated financial statements on the same basis as the audited consolidated financial statements and have included, in our opinion, all adjustments, consisting only of normal recurring adjustments, that we consider necessary for a fair presentation of the financial information set forth in those statements. Our historical results are not necessarily indicative of our future results, and our interim results are not necessarily indicative of the results to be expected for the full fiscal year or for any other period.

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	Year Ended December 31, 2006	2007	2008	2009	2010	Nine Months Ended September 30, 2010 (unaudited)	2011
	(in thousands, except share and per share data)						
Consolidated Statements of Operations Data:							
Revenue	$ 31,175	$ 48,005	$ 72,342	$ 95,443	$ 134,267	$ 95,276	$ 147,985
Cost of revenue(1)	8,068	12,236	20,094	30,772	43,894	31,013	49,595
Gross profit	23,107	35,769	52,248	64,671	90,373	64,263	98,390
Operating expenses:							
Sales and marketing(1)	13,150	19,991	28,397	39,276	63,978	42,986	68,224
Research and development(1)	4,801	8,114	9,901	14,845	27,400	18,699	30,151
General and administrative(1)	2,415	3,662	7,436	13,397	17,159	11,979	18,082
Total operating expenses	20,366	31,767	45,734	67,518	108,537	73,664	116,457
Operating income (loss)	2,741	4,002	6,514	(2,847)	(18,164)	(9,401)	(18,067)
Other income (expense), net	453	151	34	75	(53)	30	(683)
Income (loss) before taxes	3,194	4,153	6,548	(2,772)	(18,217)	(9,371)	(18,750)
Income tax expense (benefit)	(3,285)	1,691	2,989	(777)	(6,127)	(3,349)	10,540
Net income (loss)	6,479	2,462	3,559	(1,995)	(12,090)	(6,022)	(29,290)
Adjustment for redemption of preferred stock	(724)	(88)		(58,601)			
Preferred stock dividend	(420)	(224)		(490)			
Net income (loss) available to common stockholders	$ 5,335	$ 2,150	$ 3,559	$ (61,086)	$ (12,090)	$ (6,022)	$ (29,290)
Net income (loss) per common share:							
Basic	$ 0.83	$ 0.42	$ 0.68	$ (11.73)	$ (3.03)	$ (1.53)	$ (6.76)
Diluted	$ 0.30	$ 0.12	$ 0.17	$ (11.73)	$ (3.03)	$ (1.53)	$ (6.76)
Weighted average number of common shares outstanding basic	6,439,581	5,163,372	5,234,463	5,208,696	3,989,152	3,934,577	4,332,319
Weighted average number of common shares outstanding diluted	19,305,431	20,169,357	20,359,647	5,208,696	3,989,152	3,934,577	4,332,319

(1) Cost of revenue and operating expenses include the following amounts related to stock-based compensation:

	Year Ended December 31, 2006	2007	2008	2009	2010	Nine Months Ended September 30, 2010 (unaudited)	2011
	(in thousands)						
Cost of revenue	$ 22	$ 57	$ 215	$ 416	$ 664	$ 483	$ 798
Sales and marketing	40	79	320	813	1,413	852	1,644
Research and development	44	149	257	528	1,147	854	1,010
General and administrative	7	64	191	1,589	1,201	783	1,490
Total stock-based compensation	$ 113	$ 349	$ 983	$ 3,346	$ 4,425	$ 2,972	$ 4,942

	As of December 31,	As of September 30,

	2006	2007	2008	2009	2010	2011 (unaudited)
			(in thousands)			
Consolidated Balance Sheet Data:						
Cash and cash equivalents	$ 4,940	$ 4,246	$ 4,968	$ 34,342	$ 22,804	$ 29,550
Working capital (deficit)	(138)	(1,233)	(2,425)	26,027	305	1,672
Total assets	22,097	32,459	43,171	94,326	122,957	154,735
Total liabilities	14,944	22,351	26,659	39,256	66,554	93,040
Redeemable convertible preferred stock	11,536	11,760	11,760	33,038	33,038	63,000
Total stockholders equity (deficit)	(4,383)	(1,652)	4,752	22,032	23,365	(1,305)

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MANAGEMENT S DISCUSSION AND ANALYSIS

OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion in conjunction with our consolidated financial statements and the related notes included elsewhere in this prospectus. In addition to historical information, this discussion contains forward-looking statements that involve risks, uncertainties and assumptions that could cause our actual results to differ materially from our expectations. Factors that could cause such differences include those described in Risk Factors and elsewhere in this prospectus. Unless otherwise indicated, all references to 2008, 2009 and 2010 mean our fiscal year ended December 31, 2008, 2009 or 2010, as applicable.

Overview

We are a leading global provider of cross-channel, interactive marketing SaaS solutions that empower organizations of all sizes to communicate with their customers through the interactive channels they use most email, mobile, social media and websites. Our solutions provide marketers with a broad and powerful suite of integrated applications to plan, automate, deliver and optimize data-driven interactive marketing campaigns and real-time communications to drive customer engagement, increase sales and improve their return on marketing investment. Our direct client base consisted of over 4,600 organizations as of September 30, 2011. Our revenue is distributed across clients ranging from enterprises to small businesses in numerous industries, including retail and e-commerce, media and entertainment, travel and hospitality, financial services and insurance, technology, daily-deal and flash-sale and marketing service providers. Our direct client base includes more than 500 marketing service providers that extend our global sales distribution by reselling our solutions to several thousand additional organizations.

We provide our solutions primarily through annual and multi-year subscriptions based on the volume of contracted utilization, level of functionality, number of interactive marketing channels, number of users and level of customer support. Clients are charged additional usage-based fees for utilization above the contracted level. Our subscription-based model and track record of long-term client relationships have allowed us to achieve annual dollar-based subscription revenue renewal rates of over 100% in 2009 and 2010 and for the nine months ended September 30, 2011 and provide us significant revenue visibility.

We believe that the demand for cross-channel, interactive marketing SaaS solutions is significant and growing, driven by organizations desire to develop a unified, cross-channel view of their customers to drive real-time, relevant engagement through email, mobile, social media and websites. We anticipate that organizations will continue to increase their use of cross-channel marketing SaaS solutions to plan, automate, deliver and optimize data-driven interactive marketing campaigns and real-time communications. We believe the market for our suite of cross-channel, interactive marketing SaaS solutions will become larger as organizations adopt cross-channel, interactive marketing. We also believe significant opportunity exists in new markets worldwide that are unserved or underserved by existing providers. We intend to increase our direct global presence in international markets to serve our multinational clients and win new clients in these markets. We also believe opportunities to acquire companies and technologies to expand the functionality of our solutions will emerge, providing access to new clients or markets, or both, although we have no agreements or understandings regarding future acquisitions at this time.

We face a number of risks in the execution of our strategy, including our potential failure to manage our domestic and international growth effectively, inability to attract new clients and retain existing clients, inability to achieve and sustain profitability and the overall impact of uncertain

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economic conditions. Due to the size and expected growth of the market opportunity, we recognize that we may face increased competition from established vendors and potential new entrants in our markets. We believe the expansion of our suite of cross-channel, interactive marketing SaaS solutions and the introduction of our Interactive Marketing Hub have been important in winning new clients and cross selling into our existing client base. While email continues to be the primary interactive marketing channel for our clients and represents a substantial majority of our total revenue, revenue from our mobile, social media and sites solutions is growing rapidly.

We were founded in December 2000, and initially focused on providing email marketing solutions to small and medium-sized clients. Since that time, we have expanded our solutions offerings to serve the enterprise market. In 2007, we broadened our product strategy to expand beyond email into emerging cross-channel, interactive marketing technologies such as mobile, landing pages and microsites. In 2010, we further expanded our cross-channel, interactive marketing capabilities with the acquisition of the enterprise social media management platform, CoTweet. Additionally, we continued to develop and improve our proprietary, cloud-based platform, expanding our integration framework to enable third-party marketing technology providers to embed our technology into their solutions and build applications on our platform. In 2011, we made our Interactive Marketing Hub generally available to clients, providing a broad and powerful suite of cross-channel, interactive marketing SaaS solutions to plan, automate, deliver and optimize data-driven, interactive marketing campaigns and real-time communications.

We have achieved 43 consecutive quarters of sequential revenue growth since our inception in December 2000. In 2008, 2009 and 2010, and for the nine months ended September 30, 2011, our revenue was $72.3 million, $95.4 million, $134.3 million and $148.0 million, respectively, representing period-over-period growth of 51%, 32%, 41% and 55%, respectively. We were profitable for the first time during the year ended December 31, 2006 and recorded operating income between 8% and 9% of revenue each year from 2006 through 2008. In 2009, we raised significant private capital and implemented a strategy focused on increased investments in sales, marketing, research and development activities and international expansion. This investment strategy has accelerated our revenue growth and has also resulted in operating losses. We have established a direct presence in international markets through acquisitions of resellers in the United Kingdom, Australia and Brazil, and subsequent investments in each of these operations. In August 2009, we acquired a reseller in the United Kingdom, allowing us to directly support clients in Europe including many of our U.S.-headquartered clients doing business in the region. In August 2010, we acquired an Australian reseller to extend our ability to support multinational clients in the Asia-Pacific region. In August 2011, we acquired a reseller in Sao Paulo, Brazil, to support clients in Latin America and to expand our sales in the region. Revenue from outside the United States as a percentage of total revenue was 5%, 6%, 8% and 12% in 2008, 2009, 2010 and for the nine months ended September 30, 2011, respectively. As a result of our increased investment strategy initiated in 2009, our cash flows from operations decreased from $12.9 million in 2008 to $6.7 million, $3.6 million and $1.8 million in 2009, 2010 and for the nine months ended September 30, 2011, respectively. We intend to continue to expand our direct and indirect sales channels, expand our global reach, extend our suite of cross-channel, interactive marketing SaaS solutions and increase revenue from new and existing clients.

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Key Metrics

We use certain key metrics to evaluate and manage our business. The following table sets forth our recurring subscription revenue, subscription revenue renewal rate and Adjusted EBITDA for the periods indicated.

	Year Ended December 31,			Nine Months Ended September 30,	
	2008	2009	2010	2010	2011
				(unaudited)	
	(in thousands, except renewal rate)				
Recurring subscription revenue(1)	$ 53,797	$ 75,231	$ 106,412	$ 76,086	$ 114,918
Subscription revenue renewal rate(2)	n/a	106%	109%	108%	110%
Adjusted EBITDA(3)	$ 12,249	$ 7,723	$ (2,769)	$ 1,272	$ (892)

(1) Recurring subscription revenue excludes revenue related to utilization above our clients contracted volume levels of $8.7 million, $7.9 million and $9.1 million in 2008, 2009 and 2010, respectively, and $6.5 million and $8.1 million for the nine months ended September 30, 2010 and 2011, respectively.
(2) Subscription revenue renewal rate calculation was not available prior to the third quarter of 2009.
(3) Adjusted EBITDA is a non-GAAP financial measure. See Prospectus Summary Summary Consolidated Financial Data for a reconciliation from net income (loss), the most directly comparable financial measure calculated and presented in accordance with GAAP, to Adjusted EBITDA.

Recurring Subscription Revenue. As a SaaS provider, we monitor recurring subscription revenue to measure our success in executing our strategy to increase the adoption of our SaaS solutions and expand our recurring revenue streams attributable to these solutions. We expect our recurring subscription revenue to remain the most significant portion of our total revenue although its percentage of total revenue may vary from period to period due to a number of factors, including the amount of revenue recognized from utilization above the contracted level and the timing of recognition of professional services revenue. We define recurring subscription revenue as the total amount of contractually-committed subscription revenue under each of our client agreements, which excludes revenue related to utilization above the contracted level.

Subscription Revenue Renewal Rate. Our ability to retain our clients and expand their use of our suite of cross-channel, interactive marketing SaaS solutions over time is an indicator of the stability of our revenue base and the long-term value of our client relationships. We assess our performance in this area using a metric we refer to as our subscription revenue renewal rate. This metric is calculated by dividing (a) total subscription revenue (including revenue related to messaging utilization above our clients contracted levels) in the current period from those clients who were clients during the prior year period, including additional sales to those clients, by (b) total subscription revenue (including revenue related to messaging utilization above our clients contracted levels) from all clients in the prior year period. This metric is calculated on a quarterly basis and, for periods longer than one quarter, we use an average of the quarterly metrics.

Adjusted EBITDA. We monitor Adjusted EBITDA because we believe this measure provides important supplemental information regarding our operating performance and is often used by investors and analysts in their evaluation of companies such as ours. In addition, we use Adjusted EBITDA as a measurement of our operating performance because it assists us in comparing our operating performance on a consistent basis by removing the impact of certain non-cash and non-operating items. We calculate Adjusted EBITDA as net income (loss) before (1) other (income) expense, which includes interest income, interest expense and other income and expense, (2) income tax expense (benefit), (3) depreciation and amortization of property and equipment, (4) amortization of intangible assets and (5) stock-based compensation. This non-GAAP financial measure is used in addition to and in conjunction with results presented in accordance with GAAP and should not be relied upon to the exclusion of GAAP financial measures. Adjusted EBITDA reflects an additional way of viewing aspects of our operations that we believe, when viewed with our GAAP results and the accompanying reconciliations to corresponding GAAP financial measures, provides a more complete understanding of factors and trends affecting our business. For a reconciliation from net income (loss) to Adjusted EBITDA, see Prospectus Summary Summary Consolidated Financial Data.

Components of Results of Operations

Revenue

We generate revenue through the sale of subscriptions to our suite of cross-channel, interactive marketing SaaS solutions and the delivery of professional services. More than 80% of our revenue in 2010 and for the nine months ended September 30, 2011 was derived from our enterprise, medium-sized and small business clients, with the balance attributable to marketing service providers that resell our solutions to thousands of their customers. We serve a wide range of clients across many industries and sizes, and our revenue is not concentrated within any single client or small group of clients. In each of 2008, 2009 and 2010 and for the nine months ended September 30, 2011, no single client represented more than 5% of our revenue, and our largest ten clients accounted for less than 20% of our revenue in the aggregate.

Clients are typically invoiced in advance on an annual, quarterly or monthly basis, with payment due upon receipt of the invoice. Invoiced amounts are reflected on the balance sheet as accounts receivable or as cash when collected and as deferred revenue until earned and recognized as revenue ratably over the performance period. Accordingly, deferred revenue represents the amount billed to clients that has not yet been earned or recognized as revenue, pursuant to agreements entered into in current and prior periods, and does not reflect that portion of a contract to be invoiced to clients on a periodic basis for which payment is not yet due. In recent periods, more of our clients have requested quarterly or monthly instead of annual billing terms. As a result, we believe that the proportion of aggregate contract value reflected on the balance sheet as deferred revenue may continue to decrease if this trend continues.

Subscription Revenue. Our subscriptions are based on volume of contracted utilization, level of functionality, number of interactive marketing channels, number of users and level of customer support. Utilization levels are based on the volume of email messages, short message service (SMS) messages, website impressions and other activities. If clients exceed the specified volume of utilization, additional fees are billed for the excess volume, generally at rates equal to or greater than the contracted minimum per-utilization fee, and are included in subscription revenue. If clients use less than the minimum contracted utilization, no rollover credit or refunds are given. Subscription agreements with our clients typically are not cancellable for a minimum period, generally one year but ranging up to three years. Our subscription revenue accounted for 86%, 87%, 86% and 83% of our total revenue in 2008, 2009 and 2010 and for the nine months ended September 30, 2011, respectively.

We recognize the aggregate minimum subscription fee ratably on a straight-line basis over the subscription term, provided that an enforceable contract has been signed by both parties, access to our SaaS solutions has been granted to the client, the fee for the subscription is fixed or determinable and collection is reasonably assured. Revenue from utilization above the contracted level is recognized in the period in which the utilization occurs. As a result of new client additions and expansion of our overall client base, we believe revenue attributable to utilization above the contracted level may continue to grow in absolute dollars.

Professional Services Revenue. Professional services revenue consists primarily of fees associated with training, implementation, integration, deliverability, campaign services and strategic consulting. Our professional services are not required for clients to utilize our suite of cross-channel,

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interactive marketing SaaS solutions. Depending upon the nature of the engagement, we may provide professional services over the term of the SaaS subscription or in connection with discrete projects. Revenue for our professional services engagements is recognized over the period of performance and is typically contracted on a fixed-fee basis.

Cost of Revenue

We allocate certain overhead expenses, such as rent, utilities, office supplies and depreciation of general office assets to cost of revenue categories based on related headcount. As a result, an overhead expense allocation is reflected in each cost of revenue category.

Cost of Subscription Revenue. Cost of subscription revenue consists primarily of wages and benefits for software operations personnel, as well as depreciation, licensing, maintenance and support for hardware and software used in production, and co-location facilities, bandwidth and infrastructure expenses. The expenses related to co-location, bandwidth and infrastructure are affected by the number of clients using our suite of cross-channel, interactive marketing SaaS solutions, the complexity and frequency of their use, the level of utilization and the amount of stored data. In addition, these expenses are affected by our requirement to maintain high application availability. Our system hardware is co-located in two third-party operated hosting facilities in Indianapolis, Indiana and Las Vegas, Nevada. During the fourth quarter of 2011, we expect to commence operations in a third data center, located in Indianapolis. We expect to make further significant capital investments in the expansion and operation of our data centers and to continue to expand our business, which will increase our cost of subscription revenue in absolute dollars.

Cost of Professional Services Revenue. Cost of professional services revenue primarily consists of wages and benefits for services personnel and related costs. Our cost of professional services revenue is significantly higher as a percentage of associated revenue than our cost of subscription revenue due to the labor costs associated with providing professional services. As it takes several months to ramp up a professional services consultant to full productivity, we generally increase our professional services capacity ahead of the recognition of associated professional services revenue, which can result in lower margins in a period of significant hiring. We expect the number of professional services personnel to increase in the future as we continue to serve more enterprise clients, resulting in higher cost of professional services revenue in absolute dollars.

Operating Expenses

We allocate certain overhead expenses, such as rent, utilities, office supplies and depreciation of general office assets to operating expense categories based on related headcount. As a result, an overhead expense allocation is reflected in each operating expense category.

Sales and Marketing. Sales and marketing expenses consist primarily of wages and benefits for sales and marketing personnel, sales commissions, travel and meeting expenses and lead-generation marketing programs. All sales and marketing costs are expensed as incurred. In particular, sales bonuses are expensed in the period of contract signing and commissions are expensed upon contract billing. Our sales and marketing expenditures have historically been highest in the last two quarters of each year, which are periods of increased sales and marketing activity. In order to continue to grow our business and increase our brand awareness, we expect to continue investing substantial resources in our sales and marketing efforts. As a result, we expect sales and marketing expenses to increase as we invest to acquire new clients and retain and grow revenue from existing clients.

Research and Development. Research and development expenses consist primarily of wages and benefits for product strategy, product architecture, product design, development and quality

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assurance personnel, and the costs of third-party development contractors. We focus our research and development efforts on usability, application performance, new features and functionality and development of emerging cross-channel marketing technologies. We expense research and development costs as incurred due to our relatively short development cycle. We expect research and development expenses to increase as we continue to enhance our product offerings.

General and Administrative. General and administrative expenses consist primarily of wages and benefits for executive, finance and accounting, legal, human resources, internal information technology support and administrative personnel. In addition, general and administrative expenses include professional services fees, bad debt expenses and other corporate expenses. We expect that general and administrative expenses will increase as we continue to add personnel to support our growth. We also anticipate that we will incur additional costs for personnel and for professional services including auditing and legal services, insurance and other corporate governance-related costs related to operating as a public company.

Provision for Income Taxes

We are subject to taxes in the United States as well as other tax jurisdictions in which we conduct business. Earnings from our non-U.S. activities are subject to local income tax and may be subject to current U.S. income tax.

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. We record a valuation allowance to reduce deferred tax assets to an amount whose realization is more likely than not.

We recognize tax benefits from uncertain tax positions when it is more likely than not that the position will be sustained upon examination, including resolutions of any related appeals or litigation processes, based on the technical merits of the position. We record interest and penalties related to unrecognized tax benefits in our provision for income taxes.

As of September 30, 2011, we recorded a full valuation allowance on our deferred tax assets. In the third quarter of 2011, we decided to explore the opportunity to launch an initial public offering and, as a result, we determined that it was no longer more likely than not that the deferred tax assets would be realized due to continued planned business investment with the proceeds of this offering. We previously overcame the negative evidence provided by our recent losses by demonstrating that we had generated income in 2006, 2007 and 2008 and using that information to show our ability to generate taxable income from existing client contracts if our planned investments were not made. In making such determination, we considered all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax planning strategies and recent financial operations.

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Adjustment for Redemption of Preferred Stock

Adjustment for redemption of preferred stock represents the impact on earnings of the redemption of a portion of our Series A and Series B preferred stock and all of our Series C preferred stock using a portion of the proceeds from the issuance of our Series D preferred stock in 2009. When preferred stock is redeemed, the excess fair value of the consideration paid to holders of preferred stock over the carrying amount of the preferred stock (excess consideration) represents a return to the preferred stockholders. Net income used in the calculation of both basic and diluted earnings per share excludes the adjustment for redemption of preferred stock. The effect of assumed conversion of preferred stock used in the calculation of diluted earnings per share excludes the impact of the redemption of those shares of our Series A, Series B and Series C preferred stock as their effect was anti-dilutive.

Results of Operations

The following tables set forth selected consolidated statements of operations data for each of the periods indicated and as a percentage of total revenue.

	Year Ended December 31,			Nine Months Ended September 30,	
	2008	**2009**	**2010**	**2010**	**2011**
				(unaudited)	
			(in thousands)		
Consolidated Statements of Operations Data:					
Revenue:					
Subscription revenue	$ 62,516	$ 83,134	$ 115,553	$ 82,565	$ 122,988
Professional services revenue	9,826	12,309	18,714	12,711	24,997
Total revenue	72,342	95,443	134,267	95,276	147,985
Cost of revenue:					
Cost of subscription revenue	12,131	18,791	25,882	18,344	28,489
Cost of professional services revenue	7,963	11,981	18,012	12,669	21,106
Total cost of revenue(1)	20,094	30,772	43,894	31,013	49,595
Gross profit	52,248	64,671	90,373	64,263	98,390
Operating expenses:					
Sales and marketing(1)	28,397	39,276	63,978	42,986	68,224
Research and development(1)	9,901	14,845	27,400	18,699	30,151
General and administrative(1)	7,436	13,397	17,159	11,979	18,082
Total operating expenses	45,734	67,518	108,537	73,664	116,457
Operating income (loss)	6,514	(2,847)	(18,164)	(9,401)	(18,067)
Other income (expense), net	34	75	(53)	30	(683)
Income (loss) before taxes	6,548	(2,772)	(18,217)	(9,371)	(18,750)
Income tax expense (benefit)	2,989	(777)	(6,127)	(3,349)	10,540
Net income (loss)	3,559	(1,995)	(12,090)	(6,022)	(29,290)
Adjustment for redemption of preferred stock		(58,601)			
Preferred stock dividend		(490)			
Net income (loss) available to common stockholders	$ 3,559	$ (61,086)	$ (12,090)	$ (6,022)	$ (29,290)

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(1) Total cost of revenue and operating expenses include the following amounts related to stock-based compensation:

	Year Ended December 31, 2008	2009	2010	Nine Months Ended September 30, 2010	2011
				(unaudited)	
			(in thousands)		
Total cost of revenue	$ 215	$ 416	$ 664	$ 483	$ 798
Sales and marketing	320	813	1,413	852	1,644
Research and development	257	528	1,147	854	1,010
General and administrative	191	1,589	1,201	783	1,490
Total stock-based compensation	$ 983	$ 3,346	$ 4,425	$ 2,972	$ 4,942

	Year Ended December 31, 2008	2009	2010	Nine Months Ended September 30, 2010	2011
				(unaudited)	
Consolidated Statements of Operations Data as a Percentage of Total Revenue(2):					
Revenue:					
Subscription revenue	86%	87%	86%	87%	83%
Professional services revenue	14	13	14	13	17
Total revenue	100	100	100	100	100
Cost of revenue:					
Cost of subscription revenue	17	20	19	19	19
Cost of professional services revenue	11	13	13	13	14
Total cost of revenue	28	32	33	33	34
Gross profit	72	68	67	67	66
Operating expenses:					
Sales and marketing	39	41	48	45	46
Research and development	14	16	20	20	20
General and administrative	10	14	13	13	12
Total operating expenses	63	71	81	77	79
Operating income (loss)	9	(3)	(14)	(10)	(12)
Other income (expense), net					(1)
Income (loss) before taxes	9	(3)	(14)	(10)	(13)
Income tax expense (benefit)	4	(1)	(5)	(4)	7
Net income (loss)	5	(2)	(9)	(6)	(20)
Adjustment for redemption of preferred stock		(61)			
Preferred stock dividend		(1)			
Net income (loss) available to common stockholders	5%	(64)%	(9)%	(6)%	(20)%

(2) Due to rounding, totals may not equal the sum of the line items in the table.

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Nine Months Ended September 30, 2010 and 2011

Revenue

	Nine Months Ended September 30,				Change	
	2010		2011			
	Amount	% of Revenue	Amount	% of Revenue	($)	(%)
	(unaudited) (in thousands, except percentages)					
Subscription revenue	$ 82,565	87%	$ 122,988	83%	$ 40,423	49%
Professional services revenue	12,711	13	24,997	17	12,286	97
Total revenue	$ 95,276	100%	$ 147,985	100%	$ 52,709	55%

The growth in subscription revenue over the period was attributable to new direct client additions, a larger base of renewal clients, increases in revenue associated with our international operations and increases in utilization above contracted levels. Subscription revenue from international clients increased by $11.7 million, from $6.5 million in the nine months ended September 30, 2010 to $18.2 million for the nine months ended September 30, 2011. The increase in international subscription revenue was attributable to increased sales and marketing investments in the United Kingdom, Australia and Brazil. Revenue from utilization above the contracted level increased by $1.5 million, or 23%, from $6.5 million for the nine months ended September 30, 2010 to $8.0 million for the nine months ended September 30, 2011.

The growth in professional services revenue over the prior year period was attributable to an increase in the number of enterprise and medium-sized clients with complex interactive marketing programs utilizing our professional services, the acceleration of new direct client additions utilizing implementation and integration services and the growth in international operations.

Cost of Revenue

	Nine Months Ended September 30,				Change	
	2010		2011			
	Amount	% of Cost of Revenue	Amount	% of Cost of Revenue	($)	(%)
	(unaudited) (in thousands, except percentages)					
Cost of subscription revenue	$ 18,344	59%	$ 28,489	57%	$ 10,145	55%
Cost of professional services revenue	12,669	41%	21,106	43%	8,437	67%
Total cost of revenue	$ 31,013	100%	$ 49,595	100%	$ 18,582	60%

The increase in cost of subscription revenue was due in part to a $2.9 million increase in employee-related costs due to the net addition of 50 employees from September 30, 2010 to September 30, 2011, primarily in our customer support and software operations team to support our larger base of clients and our international expansion. Cost of subscription revenue also increased due to a $2.7 million increase in depreciation and amortization costs related to equipment and software in our data centers, a $1.4 million increase in operating costs related to enhancing and expanding our infrastructure and a $1.1 million increase in purchases of third-party partner applications and products for resale to our clients.

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The increase in cost of professional services revenue was primarily due to a $5.0 million increase in employee-related costs due to the net addition of 75 professional services employees from September 30, 2010 to September 30, 2011. Cost of professional services revenue also increased due to a $1.6 million increase in payments to third-party professional services consultants and a $0.6 million increase related to travel and meeting expenses due to the increase in professional services personnel to support our larger base of clients and international expansion.

Gross Profit

	Nine Months Ended September 30, 2010		2011		Change	
	Amount	% of Associated Revenue	Amount	% of Associated Revenue	($)	(%)
	(unaudited) (in thousands, except percentages)					
Subscription revenue gross profit	$ 64,221	78%	$ 94,499	77%	$ 30,278	47%
Professional services revenue gross profit	42	0%	3,891	16%	3,849	NM
Total gross profit	$ 64,263	67%	$ 98,390	66%	$ 34,127	53%

Our subscription revenue gross profit increased in absolute dollars but decreased as a percentage of associated revenue. This decrease in gross profit as a percentage of associated revenue, or gross margin, was attributable to increased use of our solutions and scaling for future growth. This activity resulted in higher third-party data center costs and associated hardware and software costs, along with increased employee-related costs in our customer support and software operations team.

The increase in professional services revenue gross profit was due in part to the prospective adoption of a new accounting standard for revenue recognition of multiple deliverable arrangements, specifically related to professional services revenue and the growth in the number of clients using our professional services. Revenue from professional services is recognized using a proportional performance model based on services performed. Prior to January 1, 2011, professional services revenue was recognized ratably over the subscription term.

Sales and Marketing Expenses

	Nine Months Ended September 30, 2010	2011	Change ($)	(%)
	(unaudited) (in thousands, except percentages)			
Sales and marketing	$ 42,986	$ 68,224	$ 25,238	59%
Percentage of total revenue	45%	46%		

The increase in sales and marketing expenses was primarily due to a $9.5 million increase in employee-related costs due to the net addition of 105 sales and marketing employees from September 30, 2010 to September 30, 2011 and an $8.0 million increase in sales commissions and bonuses as a result of increased sales and performance that exceeded our sales targets. It also reflects an increase in travel and meeting expenses of $2.5 million and marketing program and event expenses of $1.6 million. Our sales and marketing headcount increased as we invested in expanding our domestic and international presence.

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Research and Development Expenses

	Nine Months Ended September 30, 2010	2011	Change ($)	(%)
	(unaudited) (in thousands, except percentages)			
Research and development	$ 18,699	$ 30,151	$ 11,452	61%
Percentage of total revenue	20%	20%		

The increase in research and development expenses was primarily due to a $5.8 million increase in third-party development contractor resources and a $3.9 million increase in employee-related costs due to a full nine months of expenses related to 2010 hires and the net addition of 21 employees from September 30, 2010 to September 30, 2011. Our research and development spending increased as we accelerated the development of our suite of cross-channel, interactive marketing SaaS solutions.

General and Administrative Expenses

	Nine Months Ended September 30, 2010	2011	Change ($)	(%)
	(unaudited) (in thousands, except percentages)			
General and administrative	$ 11,979	$ 18,082	$ 6,103	51%
Percentage of total revenue	13%	12%		

The increase in general and administrative expenses was primarily due to a $4.3 million increase in employee-related costs due to the net addition of 52 finance and accounting, legal, human resources, talent acquisition and internal information technology support personnel from September 30, 2010 to September 30, 2011 to support our growth.

Other Income (Expense), Net

	Nine Months Ended September 30, 2010	2011	Change ($)	(%)
	(unaudited) (in thousands, except percentages)			
Other income (expense), net	$ 30	$ (683)	$ (713)	NM
Percentage of total revenue	0%	(0)%		

Other income (expense) consists primarily of interest income and expense and foreign exchange gains and losses. The change in other income (expense) resulted from a $0.4 million increase in interest expense, primarily related to the full nine months of interest on borrowings under our loan and security agreement executed in November 2010. There was also an increase of $0.4 million in foreign exchange losses related to foreign currency transactions in our foreign locations.

Income Tax Expense (Benefit)

	Nine Months Ended September 30, 2010	2011	Change ($)	(%)
	(unaudited) (in thousands, except percentages)			
Income tax expense (benefit)	$ (3,349)	$ 10,540	$ 13,889	NM

Percentage of total revenue	(4)%	7%

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We had an income tax benefit of $3.3 million for the nine months ended September 30, 2010, and we incurred income tax expense of $10.5 million for the nine months ended September 30, 2011. In 2011, we determined that it was no longer more likely than not that the deferred tax assets would be realized due to continued planned business investment with the proceeds of this offering. In making such determination, we considered all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax planning strategies and recent financial results. Accordingly, we established a full valuation allowance against the net deferred tax assets.

Years Ended December 31, 2008, 2009 and 2010

Revenue

	Year Ended December 31,			Change	
	2008	2009	2010	2008 to 2009 (%)	2009 to 2010 (%)
	(in thousands, except percentages)				
Subscription revenue	$ 62,516	$ 83,134	$ 115,553	33%	39%
Professional services revenue	9,826	12,309	18,714	25%	52%
Total revenue	$ 72,342	$ 95,443	$ 134,267	32%	41%

2009 compared to 2010. The $32.4 million of growth in subscription revenue over the period was attributable to the acceleration of new direct client additions, a larger base of renewal clients, the growth in our international operations and an increase in revenue associated with utilization above contracted levels. Revenue from international clients increased by $4.6 million from $5.5 million in 2009 to $10.1 million in 2010. The increase in international subscription revenue was attributable to increased sales and marketing investments in the United Kingdom and Australia. Revenue from utilization above the contracted level increased by $1.2 million, or 15%, from $7.9 million in 2009 to $9.1 million in 2010. Revenue associated with utilization above the contracted level increased in total dollars, but decreased as a percentage of total revenue due to a larger base of renewal clients renewing at higher contracted utilization volumes.

The $6.4 million of growth in professional services revenue over the period was attributable to an increase in the number of enterprise and medium-sized clients with complex interactive marketing programs utilizing our professional services, the acceleration of new direct client additions utilizing implementation and integration services and the growth in international operations.

2008 compared to 2009. The $20.6 million of growth in subscription revenue over the period was attributable to the addition of new direct clients, a larger base of renewal clients and the growth in international operations from our acquisition and subsequent investments in the United Kingdom. Subscription revenue from international clients increased by $2.2 million, from $3.3 million in 2008 to $5.5 million in 2009. The increase in international subscription revenue was attributable to increased direct sales investments in the United Kingdom initiated in August 2009. Subscription revenue from utilization above the contracted level decreased by $0.8 million, or 9%, from $8.7 million in 2008 to $7.9 million in 2009, primarily due to an increased effort, through the formation of our relationship management team, to sell our clients additional committed volumes before their utilization exceeded the contracted volume.

The $2.5 million of growth in professional services revenue over the period was attributable to an increase in the number of enterprise and medium-sized clients with complex interactive marketing programs utilizing our professional services and the addition of new direct clients utilizing implementation and integration services.

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Cost of Revenue

	Year Ended December 31,							
	2008		2009		2010		Change	
	Amount	% of Cost of Revenue	Amount	% of Cost of Revenue	Amount	% of Cost of Revenue	2008 to 2009 (%)	2009 to 2010 (%)
	(in thousands, except percentages)							
Cost of subscription revenue	$ 12,131	60%	$ 18,791	61%	$ 25,882	59%	55%	38%
Cost of professional services revenue	7,963	40%	11,981	39%	18,012	41%	50%	50%
Total cost of revenue	$ 20,094	100%	$ 30,772	100%	$ 43,894	100%	53%	43%

2009 compared to 2010. The $7.1 million increase in cost of subscription revenue was due in part to a $2.0 million increase in employee-related costs due to the net addition of 29 employees from 2009 to 2010, primarily in our technical support team. Cost of subscription revenue also increased due to a $1.8 million increase in depreciation and amortization costs related to equipment and software in our data centers and a $1.9 million increase in operating costs related to enhancing and expanding our data centers.

The $6.0 million increase in cost of professional services revenue was primarily due to a $3.2 million increase in employee-related costs due to the net addition of 26 professional services personnel from 2009 to 2010. Cost of professional services revenue also increased due to a $1.7 million increase in payments to third-party professional services consultants.

2008 compared to 2009. The $6.7 million increase in cost of subscription revenue was due in part to a $1.9 million increase in employee-related costs due to a full year of expenses related to 2008 hires and the net addition of 13 employees from 2008 to 2009. Cost of subscription revenue also increased due to a $1.8 million increase in depreciation and amortization costs related to equipment and software in our data centers and a $1.7 million increase in operating costs related to enhancing and expanding our data centers. Cost of subscription revenue increased by a greater percentage than the percentage growth in subscription revenue as we invested in expansion of our data center infrastructure to support our growth.

The $4.0 million increase in cost of professional services revenue was primarily due to a $2.9 million increase in employee-related costs due to a full year of expenses related to 2008 hires and the net addition of 26 employees from 2008 to 2009, primarily in the professional services delivery team. Cost of professional services revenue also increased due to a $0.6 million increase in travel and meeting expenses due to the increased size of the professional services team. Cost of professional services revenue increased by a greater percentage than the percentage growth in professional services revenue as we expanded our professional services team to support our growth.

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Gross Profit

	Year Ended December 31,						Change	
	2008		2009		2010			
	Amount	% of Associated Revenue	Amount	% of Associated Revenue	Amount	% of Associated Revenue	2008 to 2009 (%)	2009 to 2010 (%)
	(in thousands, except percentages)							
Subscription revenue gross profit	$ 50,385	81%	$ 64,343	77%	$ 89,671	78%	28%	39%
Professional services revenue gross profit	1,863	19%	328	3%	702	4%	(82)%	114%
Total gross profit	$ 52,248	72%	$ 64,671	68%	$ 90,373	67%	24%	40%

2009 compared to 2010. Our subscription revenue gross profit increased in absolute dollars and as a percentage of associated revenue. This increase in gross margin was attributable to the growth of hardware and software costs at a slower rate than subscription revenue in 2010.

Professional services revenue gross profit increased in absolute dollars and as a percentage of associated revenue. This increase in gross margin was attributable to the growth of our professional services personnel costs at a slower rate than professional services revenue in 2010.

2008 compared to 2009. Our subscription revenue gross profit increased in absolute dollars but decreased as a percentage of associated revenue. The decline in gross margin in 2009 was attributable to significant capital investments in our data center infrastructure during 2008 that increased depreciation expense in 2009 at a higher rate than the increase in our subscription revenue.

Professional services revenue gross profit decreased primarily due to the significant hiring of services personnel in advance of the recognition of professional services revenue. As it takes several months to ramp up a professional services consultant to full productivity, we generally increase our professional services capacity ahead of the recognition of associated professional services revenue.

Sales and Marketing Expenses

	Year Ended December 31,			Change	
	2008	2009	2010	2008 to 2009 (%)	2009 to 2010 (%)
	(in thousands, except percentages)				
Sales and marketing	$ 28,397	$ 39,276	$ 63,978	38%	63%
Percentage of total revenue	39%	41%	48%		

2009 compared to 2010. The $24.7 million increase in sales and marketing expenses was primarily due to a $10.9 million increase in employee-related costs due to the net addition of 137 sales and marketing employees from 2009 to 2010 and a $5.9 million increase in sales commissions and bonuses as a result of increased sales and performance that exceeded our sales targets. It also reflected an increase in marketing program and event expenses of $3.5 million and an increase in travel and meeting expenses of $1.4 million. Our sales and marketing team size increased as we invested in expanding our domestic and international presence.

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2008 compared to 2009. The $10.9 million increase in sales and marketing expenses was primarily due to a $4.7 million increase in employee-related costs due to the net addition of 50 sales and marketing employees from 2008 to 2009 to expand our field sales team and to build a pre-sales consulting team to assist with technical sales, and a $1.6 million increase in sales commissions as a result of increased sales. Our sales and marketing headcount increased as we hired additional personnel to focus on adding new clients and increasing revenue from existing clients. Other factors resulting in an increase in sales and marketing expenses included an increase in marketing program and event expenses of $1.9 million and an increase in travel and meeting expenses of $0.8 million.

Research and Development Expenses

	Year Ended December 31,			Change	
	2008	2009	2010	2008 to 2009 (%)	2009 to 2010 (%)
	(in thousands, except percentages)				
Research and development	$ 9,901	$ 14,845	$ 27,400	50%	85%
Percentage of total revenue	14%	16%	20%		

2009 compared to 2010. The $12.6 million increase in research and development expenses was primarily due to an $8.1 million increase in employee-related costs due to a full year of expenses from 2009 hires and the net addition of 56 employees from 2009 to 2010, a $3.1 million increase in third-party development contractor resources and an increase in software support costs of $0.4 million. Our research and development expenses increased as we accelerated the development of our suite of cross-channel, interactive marketing SaaS solutions and initiated the integration of CoTweet.

2008 compared to 2009. The $5.0 million increase in research and development expenses was primarily due to a $2.3 million increase in employee-related costs due to the net addition of 51 employees from 2008 to 2009, an increase in software support costs of $0.9 million, and a $0.7 million increase in third-party development contractor resources. Our research and development spending increased as we expanded the development of our suite of cross-channel, interactive marketing SaaS solutions.

General and Administrative Expenses

	Year Ended December 31,			Change	
	2008	2009	2010	2008 to 2009 (%)	2009 to 2010 (%)
	(in thousands, except percentages)				
General and administrative	$ 7,436	$ 13,397	$ 17,159	80%	28%
Percentage of total revenue	10%	14%	13%		

2009 compared to 2010. The $3.8 million increase in general and administrative expenses was primarily due to a $2.6 million increase in employee-related costs due to the net addition of 24 finance and accounting, legal, human resources, talent acquisition and internal information technology support personnel from 2009 to 2010. We recognized a write off of deferred offering costs of $1.2 million in 2009 as we withdrew a registration statement that we had filed with the SEC.

2008 compared to 2009. The $6.0 million increase in general and administrative expenses was primarily due to a $3.0 million increase in employee-related costs due to the net addition of 34 finance and accounting, legal, human resources, talent acquisition and internal information technology support personnel from 2008 to 2009 and a $1.2 million write off of deferred offering costs recognized in 2009 as we withdrew a registration statement that we had filed with the SEC.

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Other Income (Expense), Net

	Year Ended December 31,			Change	
	2008	2009	2010	2008 to 2009 (%)	2009 to 2010 (%)
	(in thousands, except percentages)				
Other income (expense), net	$ 34	$ 75	$ (53)	121%	NM
Percentage of total revenue	0%	0%	(0)%		

2009 compared to 2010. Other income (expense) consists primarily of interest income and expense. Other income for 2009 was $0.08 million compared to other expense of $0.05 million for 2010. The change in other income (expense) was not significant between 2009 and 2010.

2008 compared to 2009. Other income for 2009 was $0.08 million compared to other income of $0.03 million for 2008. The change in other income (expense) was not significant between 2008 and 2009.

Income Tax Expense (Benefit)

	Year Ended December 31,			Change	
	2008	2009	2010	2008 to 2009 (%)	2009 to 2010 (%)
	(in thousands, except percentages)				
Income tax expense (benefit)	$ 2,989	$ (777)	$ (6,127)	NM	NM
Percentage of total revenue	4%	(1)%	(5)%		

2009 compared to 2010. Income tax benefit for 2010 was $6.1 million compared to an income tax benefit of $0.8 million for 2009. Income tax benefit for 2010 reflected an effective tax rate of 34% compared to an effective tax rate of 28% in 2009. The change in the effective tax rate was attributable to the change in the ratio of permanent tax differences to the income (loss) before taxes.

2008 compared to 2009. Income tax benefit for 2009 was $0.8 million compared to an income tax expense of $3.0 million for 2008. Income tax benefit for 2009 reflected an effective tax rate of 28% compared to an effective tax rate of 46% in 2008. The change in the effective tax rate was attributable to the change in the ratio of permanent tax differences to the income (loss) before taxes.

Adjustment for Redemption of Preferred Stock

2008, 2009 and 2010 comparison. Redemption of preferred stock was $58.6 million in 2009 related to the premium paid above the par value of the Series A, Series B and Series C preferred stock redeemed. No preferred stock was redeemed in either 2008 or 2010.

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Quarterly Results of Operations

The following table sets forth our unaudited consolidated statements of operations data for each of the seven consecutive quarters through and including the period ended September 30, 2011. This information was derived from our unaudited consolidated financial statements, which in the opinion of management contain all adjustments necessary for a fair presentation of such financial data in accordance with GAAP. Operating results for these periods are not necessarily indicative of the operating results for a full year. Historical results are not necessarily indicative of the results to be expected in future periods. You should read this data together with our consolidated financial statements and the related notes included elsewhere in this prospectus.

	Three Months Ended						
	Mar. 31, 2010	June 30, 2010	Sept. 30, 2010	Dec. 31, 2010	Mar. 31, 2011	June 30, 2011	Sept. 30, 2011
	(unaudited) (in thousands, except per share data)						
Consolidated Statements of Operations Data:							
Revenue:							
Subscription revenue(1)	$ 25,181	$ 27,753	$ 29,630	$ 32,989	$ 37,223	$ 40,577	$ 45,187
Professional services revenue	3,653	4,262	4,796	6,002	6,803	8,259	9,936
Total revenue	28,834	32,015	34,426	38,991	44,026	48,836	55,123
Cost of revenue:							
Cost of subscription revenue	5,869	6,163	6,312	7,538	8,676	9,325	10,487
Cost of professional services revenue	3,564	4,086	5,018	5,344	5,990	7,293	7,824
Total cost of revenue(2)	9,433	10,249	11,330	12,882	14,666	16,618	18,311
Gross profit	19,401	21,766	23,096	26,109	29,360	32,218	36,812
Operating expenses:							
Sales and marketing(2)	12,871	13,681	16,433	20,992	20,325	22,262	25,637
Research and development(2)	5,068	6,082	7,549	8,701	8,437	9,954	11,760
General and administrative(2)	3,482	3,982	4,516	5,179	5,557	5,624	6,901
Total operating expenses	21,421	23,745	28,498	34,872	34,319	37,840	44,298
Operating income (loss)	(2,020)	(1,979)	(5,402)	(8,763)	(4,959)	(5,622)	(7,486)
Other income (expense), net	19	16	(4)	(84)	(248)	(341)	(94)
Net income (loss) before taxes	(2,001)	(1,963)	(5,406)	(8,847)	(5,207)	(5,963)	(7,580)
Income tax expense (benefit)	(636)	(1,199)	(1,513)	(2,779)	(1,945)	(2,257)	14,742
Net income (loss)	$ (1,365)	$ (764)	$ (3,893)	$ (6,068)	$ (3,262)	$ (3,706)	$ (22,322)
Adjusted EBITDA(3)	$ 1,102	$ 1,590	$ (1,420)	$ (4,041)	$ 31	$ 1	$ (924)
Net income (loss) per common share:							
Basic	$ (0.36)	$ (0.19)	$ (0.96)	$ (1.46)	$ (0.76)	$ (0.86)	$ (5.09)
Diluted	$ (0.36)	$ (0.19)	$ (0.96)	$ (1.46)	$ (0.76)	$ (0.86)	$ (5.09)

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(1) Subscription revenue includes fees for utilization above the contracted level in the respective quarters as follows:

	Three Months Ended						
	Mar. 31, 2010	June 30, 2010	Sept. 30, 2010	Dec. 31, 2010	Mar. 31, 2011	June 30, 2011	Sept. 30, 2011
	(unaudited) (in thousands)						
Revenue from utilization above the contracted level	$ 2,007	$ 2,568	$ 1,904	$ 2,662	$ 3,056	$ 2,294	$ 2,720
Percentage of subscription revenue	8%	9%	6%	8%	8%	6%	6%

(2) Total cost of revenue and operating expenses include the following amounts related to stock-based compensation:

	Three Months Ended						
	Mar. 31, 2010	June 30, 2010	Sept. 30, 2010	Dec. 31, 2010	Mar. 31, 2011	June 30, 2011	Sept. 30, 2011
	(unaudited) (in thousands)						
Total cost of revenue	$ 138	$ 159	$ 186	$ 181	$ 230	$ 263	$ 305
Sales and marketing	274	339	239	561	452	548	644
Research and development	230	289	335	293	301	372	337
General and administrative	177	206	400	418	340	506	644
Total stock-based compensation	$ 819	$ 993	$ 1,160	$ 1,453	$ 1,323	$ 1,689	$ 1,930

(3) Adjusted EBITDA is a non-GAAP financial measure. See Key Metrics Adjusted EBITDA for more information. The following table provides a reconciliation from net income (loss), the most directly comparable financial measure calculated and presented in accordance with GAAP, to Adjusted EBITDA.

	Three Months Ended						
	Mar. 31, 2010	June 30, 2010	Sept. 30, 2010	Dec. 31, 2010	Mar. 31, 2011	June 30, 2011	Sept. 30, 2011
	(unaudited) (in thousands)						
Net income (loss)	$ (1,365)	$ (764)	$ (3,893)	$ (6,068)	$ (3,262)	$ (3,706)	$ (22,322)
Other (income) expense, net	(19)	(16)	4	84	248	341	94
Income tax expense (benefit)	(636)	(1,199)	(1,513)	(2,779)	(1,945)	(2,257)	14,742
Depreciation and amortization of property and equipment	2,176	2,403	2,646	2,948	3,391	3,650	4,360
Amortization of intangible assets	127	173	176	321	276	284	272
Stock-based compensation	819	993	1,160	1,453	1,323	1,689	1,930
Adjusted EBITDA	$ 1,102	$ 1,590	$ (1,420)	$ (4,041)	$ 31	$ 1	$ (924)

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	Three Months Ended						
	Mar. 31, 2010	June 30, 2010	Sept. 30, 2010	Dec. 31, 2010 (unaudited)	Mar. 31, 2011	June 30, 2011	Sept. 30, 2011
Consolidated Statements of Operations Data as a Percentage of Total Revenue(1):							
Revenue:							
Subscription revenue	87%	87%	86%	85%	85%	83%	82%
Professional services revenue	13	13	14	15	15	17	18
Total revenue	100	100	100	100	100	100	100
Cost of revenue:							
Cost of subscription revenue	20	19	18	19	20	19	19
Cost of professional services revenue	12	13	15	14	14	15	14
Total cost of revenue	33	32	33	33	33	34	33
Gross profit	67	68	67	67	67	66	67
Operating expenses:							
Sales and marketing	45	43	48	54	46	46	47
Research and development	18	19	22	22	19	20	21
General and administrative	12	12	13	13	13	12	13
Total operating expenses	74	74	83	89	78	77	80
Operating income (loss)	(7)	(6)	(16)	(22)	(11)	(12)	(14)
Other income (expense), net					(1)	(1)	
Net income (loss) before taxes	(7)	(6)	(16)	(23)	(12)	(12)	(14)
Income tax expense (benefit)	(2)	(4)	(4)	(7)	(4)	(5)	27
Net income (loss)	(5)%	(2)%	(11)%	(16)%	(7)%	(8)%	(40)%

(1) Due to rounding, totals may not equal the sum of the line items in the table.

Total revenue increased sequentially in each of the quarters presented, primarily due to the addition of new direct clients, subscription revenue renewals of existing clients in excess of 100%, increased sales of additional features and functionality to existing clients and international growth. Professional services revenue grew sequentially over the seven quarters primarily due to the increasing proportion of enterprise clients in our client base. We have historically experienced variability in our sequential quarterly subscription revenue growth, with a higher percentage of our clients entering into new subscription agreements and renewals in the fourth quarter, which has translated into a higher sequential subscription revenue growth rate in the first quarter of each year. The amount of revenue recognized from utilization above the contracted level has also varied sequentially in absolute dollars depending on the mix of clients with substantial utilization above their contracted levels each quarter.

As a result of the growth in revenue, our gross profit in absolute dollars has increased sequentially in each of the quarters presented. Gross profit as a percentage of revenue has varied sequentially due to the timing of professional services engagements and timing of costs related to our data center infrastructure expansion.

Total operating expenses generally increased over the prior year in absolute dollars in each of the quarters presented, primarily due to increased wages and benefits associated with the hiring of additional personnel in our sales and marketing, research and development and general and administrative organizations to support the growth of our business. Quarterly sales and marketing expenses can vary in absolute dollars and as a percentage of revenue due to the performance of our sales team as compared to targets and due to the timing of our annual user conferences. Also, commission and bonus expenses increased in the fourth quarter of each year presented as a result of

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a higher percentage of clients entering into new subscriptions and renewals during this quarter. Research and development expenses can vary to the extent third-party development contractor resources are utilized to support the release of new products in specific periods. General and administrative costs were flat in the three months ended June 30, 2011 compared to the three months ended March 31, 2011 due to a reversal of a contingent liability related to our acquisition of CoTweet. General and administrative costs have otherwise increased primarily due to increased headcount and outside services fees related to both the overall growth of our business and in preparation for our initial public offering.

As of September 30, 2011, we recorded a full valuation allowance on our deferred tax assets. In the third quarter of 2011, we decided to explore the opportunity to launch an initial public offering and, as a result, we determined that it was no longer more likely than not that the deferred tax assets would be realized due to continued planned business investment with the proceeds of this offering. We previously overcame the negative evidence provided by our recent tax losses by demonstrating that we had generated income in 2006, 2007 and 2008 and using that information to show our ability to generate taxable income from existing client contracts if our planned investments were not made. In making such determination, we considered all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax planning strategies and recent financial operations.

Liquidity and Capital Resources

Since our inception, we have financed our operations primarily through the proceeds from the issuance of our preferred stock, borrowings under credit facilities and cash flows from operations. At September 30, 2011, our principal sources of liquidity were cash and cash equivalents totaling $29.6 million, accounts receivable of $36.4 million and $10.0 million available to draw under our revolving bank line of credit.

In November 2010, we entered into a loan and security agreement for a $10.0 million bank term loan and a $7.0 million revolving line of credit collateralized by a blanket lien on all of our personal property, including intellectual property. Both the term loan and the revolving line bear interest at a variable rate equal to prime plus one percent. The term loan and the revolving line mature on December 1, 2013, and the term loan is payable in 36 equal installments. The loan and security agreement requires us to comply with certain covenants, including with respect to recurring revenue, capital expenditures, adjusted EBITDA, mergers and dispositions of assets, changes in business, management, ownership or business locations, liens on our assets, the incurrence of additional debt, the payment of dividends and the maintenance of bank accounts with the lender. The loan and security agreement also contains usual and customary events of default (subject to certain grace periods) upon the occurrence of certain events, such as nonpayment of amounts due under the agreement, violation of the covenants referred to above, violation of other contractual provisions, a material adverse change in our business or our insolvency. In addition, the rejection by the lender, in its reasonable discretion, of certain periodic financial and operating performance projections to be made by our board of directors pursuant to the loan and security agreement would constitute an event of default. As of December 31, 2010, we were not in compliance with the adjusted EBITDA financial covenant. In March 2011, we entered into a loan modification agreement to increase the size of the revolving line from $7.0 million to $10.0 million and for the lender to waive the covenant default. In September 2011, we entered into a loan modification agreement to increase the size of the revolving line to $20.0 million. In October 2011, we entered into a loan modification agreement to modify the terms of the capital expenditure covenant and to incorporate other changes. As of December 31, 2010 and September 30, 2011, $10.0 million and $7.5 million, respectively, were outstanding under the term loan, and no amounts and $10.0 million, respectively, were outstanding under the revolving line.

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	Year Ended December 31, 2008	2009	2010	Nine Months Ended September 30, 2011 (unaudited)
	(in thousands)			
Net cash provided by operating activities	$ 12,856	$ 6,668	$ 3,624	$ 1,840
Net cash used in investing activities	(13,300)	(14,287)	(24,561)	(30,743)
Net cash provided by financing activities	1,166	37,007	9,473	35,650

Operating Activities

The 2008 net cash inflows resulted primarily from operating income, changes in working capital accounts and the add back of non-cash charges for depreciation and stock-based compensation expense. The 2009 net cash inflows resulted primarily from changes in working capital accounts, the add back of non-cash charges for depreciation, stock-based compensation expense and the write off of capitalized deferred offering costs, which was offset by a loss from operations. The 2010 net cash inflows resulted primarily from changes in working capital accounts, the receipt of a tax refund, and the add back of non-cash charges for depreciation and stock-based compensation expense, which was offset by a loss from operations. The net cash inflows for the nine months ended September 30, 2011 were attributable to changes in working capital accounts, and the add back of non-cash charges for depreciation and stock-based compensation expense, which was offset by a loss from operations.

The changes in working capital items consisted primarily of the following (in each case reflecting amounts as of the dates indicated and amount of change from the prior period):

Accounts Receivable

	As of December 31, 2008	2009	2010	As of September 30, 2011 (unaudited)
	(in thousands, except percentages)			
Accounts receivable	$ 13,697	$ 20,567	$ 27,589	$ 36,364
Dollar change from prior period	1,708	6,870	7,022	8,775
Percentage change from prior period	14%	50%	34%	32%

The increases in accounts receivable were due to continued growth in invoiced amounts to our clients, reduced by collections on existing receivables. Clients are generally invoiced annually, quarterly or monthly over the subscription period, and payment is due upon invoicing. We generally invoice clients prior to recognizing the associated revenue in full. In 2009, accounts receivable increased at a higher rate than in prior years in part due to a larger percentage of client contracts executed and invoices generated in the last month of the fourth quarter.

Deferred Revenue

	As of December 31, 2008	2009	2010	As of September 30, 2011 (unaudited)
	(in thousands, except percentages)			
Total deferred revenue(1)	$ 17,370	$ 24,418	$ 32,966	$ 36,423
Dollar change from prior period	2,604	7,048	8,548	3,457
Percentage change from prior period	18%	41%	35%	10%

(1) Includes deferred revenue included in long-term obligations and other.

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The increases in total deferred revenue were due to continued growth in invoiced amounts under our subscription agreements, offset by the recognition of revenue. The growth in invoiced amounts was primarily due to new direct client additions, a larger base of renewal clients, increases in revenue associated with our international operations and increases in utilization above contracted levels. Deferred revenue represents the amount billed to clients that has not yet been earned or recognized as revenue, pursuant to agreements entered into in current and prior periods, and does not reflect that portion of subscriptions and professional services to be invoiced to clients on a periodic basis for which payment is not yet due. In recent periods, more of our clients have requested quarterly or monthly instead of annual billing terms. As a result, we believe that the proportion of aggregate contract value reflected on the balance sheet as deferred revenue may continue to decrease if this trend continues. This trend may slow the recognition of deferred revenue, accounts receivable and cash inflow in our financial statements.

Accrued Compensation

	As of December 31,			As of September 30,
	2008	2009	2010	2011 (unaudited)
	(in thousands, except percentages)			
Accrued compensation and related expenses	$ 4,839	$ 5,959	$ 10,143	$ 13,505
Dollar change from prior period	1,662	1,120	4,184	3,362
Percentage change from prior period	52%	23%	70%	33%

The increases in accrued compensation and related expenses were primarily due to an increase in the number and compensation of our employees and larger commissions and sales bonuses. In 2010, accrued compensation increased at a higher rate than in prior years in part due to performance that exceeded our sales targets, particularly in the fourth quarter.

Investing Activities

Net cash used in investing activities was $13.3 million, $14.3 million, $24.6 million and $30.7 million during 2008, 2009, 2010 and the nine months ended September 30, 2011, respectively. Net cash used in investing activities consisted primarily of cash paid for purchases of fixed assets to expand our data center infrastructure, computer equipment and office furniture for our employees and leasehold improvements related to additional office space. Net cash used in investing activities did not include $0.3 million, $2.3 million, $3.1 million and $2.7 million of fixed assets capitalized in 2008, 2009 and 2010 and the nine months ended September 30, 2011, respectively, as payment was made in the subsequent period. Net cash used in investing activities also included payments of $1.0 million, $5.8 million and $2.7 million in 2009 and 2010 and the nine months ended September 30, 2011, respectively, related to our acquisitions.

During the fourth quarter of 2011, we expect to commence operations in a third data center, located in Indianapolis, Indiana. This facility, which is owned and operated by a third party, has comparable terms to our existing Indianapolis and Las Vegas, Nevada data centers. We have made capital expenditures during the nine months ended September 30, 2011 and plan to make additional capital expenditures in the fourth quarter of 2011 and during 2012 in connection with this facility. We expect to make further significant capital investments in the expansion of our data center infrastructure. We also anticipate making capital investments associated with the build out and outfitting of further domestic and international sales and support offices.

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Financing Activities

Net cash provided by financing activities was $1.2 million, $37.0 million, $9.5 million and $35.7 million during 2008, 2009, 2010 and the nine months ended September 30, 2011, respectively. Net cash used in financing activities during these periods included repayments of certain borrowings pursuant to our capital leases, partially offset by proceeds from the exercise of stock options. In 2009, proceeds from the issuance of Series D, Series E and Series F preferred stock were partially offset by the repurchase of Series A, Series B and Series C preferred stock and common stock. Net cash provided by financing activities during 2010 also included $9.9 million borrowed under our credit facility.

In November 2011, we issued 2,000,000 shares of Series D preferred stock at $20.00 per share for total proceeds of $40.0 million. Such shares were sold to existing holders of Series D preferred stock and their affiliates.

Capital Resources

Since 2009, we have increased our expenditures faster than the growth in our revenue. Our future capital requirements may vary materially from those now planned and will depend on many factors, including, but not limited to:

- the development of new cross-channel, interactive marketing SaaS solutions;
- market acceptance of our solutions;
- the levels of marketing programs required to maintain and improve our competitive position in the marketplace;
- the expansion of our sales, support and marketing organizations;
- the establishment of additional offices in the United States and internationally;
- building of infrastructure necessary to support our growth;
- the response of competitors to our solutions; and
- our relationships with suppliers and clients.

Based on our current cash and accounts receivable balances, our short-term revolving line of credit and the estimated net proceeds of this offering, we believe that we will have sufficient liquidity to fund our business and meet our contractual obligations for the next twelve months. However, we may need to raise additional funds in the future in the event that we pursue acquisitions or investments in complementary businesses or technologies. If we raise additional funds through the issuance of equity or convertible securities, our stockholders may experience ownership dilution.

During the last three years, inflation and changing prices have not had a material effect on our business, and we do not expect that inflation or changing prices will materially affect our business in the next twelve months.

Off-Balance Sheet Arrangements

We do not engage in any off-balance sheet financing activities. We do not have any interest in entities referred to as variable interest entities, which include special purpose entities and other structured finance entities.

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Contractual Obligations

The following table summarizes our contractual cash obligations at September 30, 2011 and the effect such obligations are expected to have on our liquidity and cash flows in future periods:

	Payments Due by Period (in thousands)				
Contractual Obligations	**Total**	**Less than 1 Year**	**1-3 years**	**3-5 Years**	**More than 5 Years**
Notes payable(1)	$ 19,554	$ 4,247	$ 15,307	$	$
Capital leases	546	179	367		
Operating leases	25,335	3,833	7,984	7,435	6,083
Contractual commitments(2)	21,078	5,814	8,608	3,550	3,106
Total	$ 66,513	$ 14,073	$ 32,266	$ 10,985	$ 9,189

(1) Notes payable consist of our term loan and revolving line of credit.

(2) Contractual commitments primarily consist of hosting and hosting-related costs for the data center facilities that house our infrastructure and a software licensing agreement for certain software product licenses.

In the normal course of business, we indemnify third parties with whom we enter into contractual relationships, including clients, lessors, and parties to other transactions, with respect to certain matters. We have agreed, under certain conditions, to hold these third parties harmless against specified losses, such as those arising from a breach of representations or covenants, other third-party claims that our suite of cross-channel, interactive marketing SaaS solutions, when used for their intended purposes, infringe upon the intellectual property rights of such other third parties or other claims made against certain parties. It is not possible to determine the maximum potential amount of liability under these indemnification obligations due to our limited history of prior indemnification claims and the unique facts and circumstances that are likely to be involved in each particular claim. In the past we have not been required to make payments under these obligations.

Critical Accounting Policies

Our financial statements are prepared in accordance with GAAP. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, costs and expenses and related disclosures. On an ongoing basis, we evaluate our estimates and assumptions. Our actual results may differ from these estimates under different assumptions or conditions.

We believe that of our significant accounting policies, which are described in the notes to our consolidated financial statements, the following accounting policies involve the greatest degree of judgment and complexity and have the greatest potential impact on our consolidated financial statements. A critical accounting policy is one that is material to the presentation of our consolidated financial statements and requires us to make difficult, subjective or complex judgments for uncertain matters that could have a material effect on our financial condition and results of operations. Accordingly, these are the policies we believe are the most critical to aid in fully understanding and evaluating our financial condition and results of operations.

Revenue Recognition

In accordance with FASB ASC No. 605-25, we recognize revenue for subscriptions to our suite of cross-channel, interactive marketing SaaS solutions ratably over the term of the subscription agreement, which is typically one year in length but can range up to three years, commencing upon the later of the agreement start date or when there is persuasive evidence of an arrangement, and when access to our SaaS solutions has been granted to the client, the collection of the fee is reasonably

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assured and the fees to be paid by the client are fixed or determinable. Amounts that have been invoiced are recorded in accounts receivable and deferred revenue until revenue recognition criteria have been met. Our subscription agreements generally contain multiple elements including access to our SaaS solutions, contracted utilization volume and professional services. In addition, we charge fees for utilization above the contracted level which is recognized in the period in which the utilization occurs. Our subscription agreements do not provide clients the right to take possession of the software supporting the SaaS solution at any time.

We also derive revenue from professional services. Professional services revenue consists primarily of fees associated with training, implementation, integration, deliverability, campaign services and strategic consulting. Our professional services are not required for clients to utilize our SaaS solutions. Depending upon the nature of the engagement, we may provide professional services over the term of the SaaS subscription or in connection with discrete projects. Revenue from professional services is recognized using a proportional performance model based on services performed. Professional services, when sold with our subscriptions, are accounted for separately when these services have value to the client on a standalone basis.

Prospective adoption of new accounting principle. In October 2009, the FASB amended the accounting standards for multiple deliverable revenue arrangements to:

- provide updated guidance regarding how the deliverables in an arrangement should be separated and how the consideration should be allocated;

- require an entity to allocate revenue in an arrangement using its best estimate of selling price, or BESP, of deliverables if a vendor does not first have vendor-specific objective evidence, or VSOE, of selling price or does not have third-party evidence, or TPE, of selling price; and

- eliminate the use of the residual method and require an entity to allocate revenue using the relative selling price method.

We elected to adopt this accounting guidance on a prospective basis as of January 1, 2011. Our consolidated financial statements and the related notes included elsewhere in this prospectus reflect the prospective adoption of the new accounting principle. Prior to the adoption of FASB ASC No. 605-25, we were not able to establish VSOE or TPE for all undelivered elements. As a result, we typically recognized subscription and professional services revenue ratably over the contract period as a single element and allocated subscription and professional services revenue based on the contract price.

A multiple-element arrangement includes the sale of a subscription to our SaaS solutions with one or more associated professional services offerings, each of which is considered a separate unit of accounting. In determining whether professional services represent a separate unit of accounting, we consider the availability of the services from other vendors. We allocate revenue to each element in a multiple-element arrangement based upon the BESP of each deliverable.

We are not able to demonstrate VSOE or TPE of selling price with respect to sales of subscriptions to our SaaS solutions. We do not have sufficient instances of separate sales of subscriptions nor are we able to demonstrate sufficient pricing consistency with respect to such sales. We also considered that no other vendor sells similar subscriptions given the unique nature and functionality of our SaaS solutions, and therefore have determined that we are not able to establish TPE of selling price. Therefore, we have determined the BESP of subscriptions to our SaaS solution based on the following:

- the list price, which represents a component of our current go-to market strategy, as established by senior management taking into consideration factors such as the competitive and economic environment; and

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an analysis of the historical pricing with respect to both our bundled and standalone arrangements for our SaaS solutions.
We have established VSOE of selling price of professional services based on an analysis of separate sales of such professional services.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

FASB ASC No. 740 establishes financial accounting and reporting standards for the effect of income taxes. We are subject to income taxes in both the United States and numerous foreign jurisdictions. Significant judgment is required in evaluating tax positions and determining the provision for income taxes. The objectives of accounting for income taxes are to recognize the amount of taxes payable or refundable for the current year and the deferred tax liabilities and assets for the future tax consequences of events that have been recognized in an entity s financial statements or tax returns. Variations in the actual outcome of these future tax consequences could materially impact our financial position, results of operations or cash flows.

In assessing the recoverability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon generation of future taxable income during the periods in which temporary differences such as loss carry-forwards and tax credits become deductible. Management considers projected future taxable income and tax planning strategies in making this assessment and ensuring that the deferred tax asset valuation allowance is adjusted as appropriate.

Beginning with the adoption of FASB ASC No. 740 as of January 1, 2009, we recognize the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. Prior to the adoption of FASB ASC No. 740, we recognized the effect of income tax positions only if such positions were probable of being sustained.

Goodwill

Goodwill represents the excess of the aggregate purchase price paid over the fair value of the net tangible and identifiable intangible assets acquired. In accordance with FASB ASC No. 350-10, *Intangibles Goodwill and Other*, goodwill is not amortized and is tested for impairment at least annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. We have determined that we operate in one reporting unit and have selected October 31 as the date to perform our annual impairment test. In the valuation of our goodwill, we must make assumptions regarding estimated future cash flows to be derived from our reporting unit. If these estimates or their related assumptions change in the future, we may be required to record impairment for these assets. The performance of the test involves a two-step process. The first step of the impairment test involves comparing the fair value of our company to its net book value, including goodwill. If the net book value exceeds its fair value, then we perform the second step of the goodwill impairment test to determine the amount of the impairment loss. The impairment loss would be calculated by comparing the implied fair value of our company to its net book value. In calculating the implied fair value of our goodwill, the fair value of our company is allocated to all of the other assets and liabilities based on their fair values. The excess of the fair value of a company over the amount assigned to its other assets and liabilities is the implied fair value of goodwill. An impairment loss is recognized when the carrying amount of goodwill exceeds its implied fair value. The goodwill balance was $0.4 million, $15.9 million and $18.4 million as of December 31, 2009 and 2010 and September 30, 2011, respectively. No impairment of goodwill was recorded for 2008, 2009 or 2010 or for the nine months ended September 30, 2011.

Stock-Based Compensation

Effective January 1, 2006, we adopted FASB ASC No. 718-20, *Compensation Stock Compensation*, or ASC 718 which requires all share-based compensation to employees, including grants of employee stock options, to be valued at fair value on the date of grant and to be expensed over the applicable service period. We adopted this statement using the prospective transition method which does not result in restatement of our previously issued financial statements and requires only new awards or awards that are modified, repurchased or canceled after the effective date to be accounted for under the provisions of ASC 718. Prior to January 1, 2006, we accounted for stock-based compensation arrangements according to the provisions of Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees, and FASB Interpretation (FIN) No. 44*, *Accounting for Certain Transactions involving Stock Compensation an interpretation of APB Opinion No. 25* and its related interpretations. Under this method, for grants prior to January 1, 2006, no compensation expense was recognized for employee stock options granted with exercise prices greater than or equal to the fair value of the underlying common stock at date of grant. If the exercise price is less than the market value at the date of grant, the difference is recognized as deferred compensation expense, which is amortized over the vesting period. Compensation costs for the portion of awards for which the required service period has not been rendered (such as unvested options) that were outstanding as of January 1, 2006, continue to be accounted for under the provisions of APB Opinion No. 25 and were recognized as the remaining required services are rendered.

Determining the appropriate fair value model and calculating the fair value of stock-based payment awards requires the use of highly subjective assumptions, including the expected life of the stock-based payment awards and stock price volatility. We have used the Black-Scholes option-pricing model to value our option grants and determine the related compensation expense. The assumptions used in calculating the fair value of stock-based payment awards represent management s best estimates, but the estimates involve inherent uncertainties and the application of management judgment. As a result, if factors change and we use different assumptions, our stock-based compensation expense could be materially different in the future.

In 2009, 2010 and the nine months ended September 30, 2011, we used the Black-Scholes option-pricing model and the following assumptions to determine fair values of option grants and related compensation expense:

	Year Ended December 31,		Nine Months Ended September 30,
	2009	2010	2011 (unaudited)
Volatility	63.10 - 65.43%	59.07 - 62.07%	54.99 - 57.64%
Risk-free interest rate	1.76 - 2.47%	1.50 - 2.43%	1.14 - 2.12%
Expected dividend yield	0%	0%	0%
Expected option term (in years)	6.25	6.25	6.25

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We have historically been a private company and lacked company-specific historical and implied volatility information. Accordingly, we have estimated our expected volatility based on the historical volatility of our peer group consisting of publicly-held companies selected because of the similarity of their industry, business model, and financial risk profile. We intend to continue to use the same peer group to determine volatility in the future until such time that sufficient information regarding the volatility of our share price becomes available or we determine that other companies should be added or are no longer suitable.

The expected term of options has been determined utilizing the simplified method as prescribed by SAB 107, Share-Based Payment. The risk-free interest rate used for each grant is based on a U.S. Treasury instrument with a term similar to the expected term of the option. ASC 718 also requires us to estimate forfeitures at the time of grant and to revise those estimates in subsequent periods if actual forfeitures differ from those estimates. We use historical data to estimate pre-vesting option forfeitures and record stock-based compensation expense only for those awards that are expected to vest. If our actual forfeiture rate is materially different from its estimate, the stock-based compensation expense could be significantly different from what we have recorded in the current period.

We have historically granted stock options at exercise prices equivalent to the fair value of our common stock as of the date of grant as determined by our board of directors with input from management and based on a number of objective and subjective factors, including the following:

- peer group trading multiples;
- the amount of preferred stock liquidation preferences;
- our results of operations and financial condition;
- increases in the number of clients and client retention;
- improvements in our product functionality and system infrastructure;
- the illiquidity of shares of our common stock;
- our future prospects and opportunity for liquidity events such as an initial public offering and possible third-party sales; and
- prices paid for our preferred stock issued in arms-length transactions.

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The following table summarizes by grant date the number of shares subject to options granted between January 1, 2009 and September 30, 2011, the per share exercise price of the options and the per share estimated fair value of the options:

Grant Date	Number of Shares Subject to Options Granted	Per Share Exercise Price of Option(1)	Per Share Estimated Fair Value of Option(2)
		(unaudited)	
Three months ended March 31, 2009	814,500	$ 9.34	$ 4.94
Three months ended June 30, 2009	181,000	9.34	4.99
Three months ended September 30, 2009	179,500	9.34	4.95
Three months ended December 31, 2009	424,125	9.34-11.21	5.83
Three months ended March 31, 2010	366,690	11.21	5.77
Three months ended June 30, 2010	816,500	11.21	5.68
Three months ended September 30, 2010	229,850	13.60	7.70
Three months ended December 31, 2010	197,000	13.60	7.63
Three months ended March 31, 2011	650,000	15.40	8.62
Three months ended June 30, 2011	512,800	15.40	8.26
Three months ended September 30, 2011	118,150	19.17	10.34

(1) Represents the determination by our board of directors of the fair market value of our common stock on the date of grant.

(2) As described above, these values were estimated at the date of grant using the Black-Scholes option-pricing model. This model estimates the fair value by applying a series of factors including the exercise price of the option, a risk free interest rate, the expected term of the option, expected share price volatility of the underlying common stock and expected dividends on the underlying common stock. Additional information regarding our valuation of common stock and option awards is set forth in note 8 to our consolidated financial statements included elsewhere in this prospectus.

In order to determine the fair value of our common stock underlying all option grants accounted for under ASC 718 and ASC 505-50, we have also considered contemporaneous third-party valuations of our common stock that reflected the various changes in our financial performance, the value of similar publicly-held companies, publicly-reported stock transactions and other factors. Our valuation methodology has used a market approach and an income approach to estimate our aggregate enterprise value at each valuation date. The market approach estimates the fair market value of a company by applying market multiples of publicly-traded firms in similar lines of business to actual and projected results. Given the similarities between their businesses and ours, we included the following publicly-traded companies in our analysis: Responsys, Inc. (since its initial public offering), Constant Contact, Inc., salesforce.com, inc., SuccessFactors, Inc., Concur Technologies, Inc., NetSuite, Inc., The Ultimate Software Group, Inc., RightNow Technologies, Inc., Taleo Corporation and Vocus, Inc. We also utilized publicly available information to select sale transactions for privately-held and publicly-held companies comparable to us. We deemed these companies comparable due to their SaaS model and/or the nature of their business. We applied a discount for control premiums impacting prices paid in the selected comparable target company sales transactions (25% for June 2010 and 26% for June 2011).

The income approach involves applying an appropriate risk-adjusted discount rate to projected debt-free cash flows, based on forecasted revenue and costs. After considering the applicable market rate of return of 20-year U.S. Treasury bonds, we have deemed the discount rates utilized (15.0% for June 2010 and 16.0% for June 2011) to be a reasonable risk adjusted rate of return given our industry, our size and our general risk profile. The projections used were based on our expected operating performance over the five-year forecast period at the time of the valuation. We believe the assumptions underlying the estimates are reasonable as they are consistent with the plans and estimates we use to manage our business.

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Finally, the values calculated for our common stock were weighted at 50% market approach and 50% income approach for each valuation since June 2010 based on the volume of market data available for comparable companies relative to our internal five year operating performance projections. The resulting value was allocated to each class of stock in each valuation date based on application of the current-value method as described in the American Institute of Certified Public Accountants Practice Guide, Valuation of Privately-Held-Company Equity Securities Issued as Compensation (Practice Aid). As all preferred stock was in the money at each valuation date, we treated all preferred stock as if it had converted to common stock. The per share value calculated under the current-value method approximated the value calculated under the option-pricing method as described in the Practice Aid and represented the estimated fair market value of our common stock at each valuation date. As indicated below, certain of these factors or assumptions changed from period to period but the methodologies did not change.

There is inherent uncertainty in our forecasts and projections, and if we had made different assumptions and estimates than those described above, the amount of our stock-based compensation expense, net income and net income per share amounts could have been materially different. In addition, discounts to reflect the lack of a public market for our stock were estimated. We believe that we have used reasonable methodologies, approaches and assumptions consistent with the Practice Aid, in assessing the fair value of our common stock for financial reporting purposes.

As discussed more fully in note 8 to the consolidated financial statements included elsewhere in this prospectus, we granted stock options with weighted average exercise prices of $9.66, $11.52, and $15.61 per share during 2009 and 2010 and the nine months ended September 30, 2011, respectively. We determined that the fair value of our common stock increased from $9.34 per share in January 2009, to $11.21 per share in November 2009, to $13.60 per share in July 2010, to $15.40 per share in March 2011 and to $19.17 per share in July 2011. The following discussion describes the reasons for the differences between the fair value of our common stock during these periods and the midpoint of the estimated price range shown on the cover page of this prospectus of $ per share. In each determination of fair value, we assumed full conversion of our preferred stock and the exercise of all outstanding stock options.

During the three months ended March 31, 2009, we utilized a contemporaneous third-party valuation of our common stock, which reflected various changes in our financial performance, the value of similar publicly-held companies, publicly reported stock transactions and other factors. We also considered the other valuation factors described above and concluded $9.34 per share to be a reasonable estimate of fair value during this period.

During each of the three months ended June 30, 2009 and September 30, 2009, the number of our clients and our revenue continued to increase, and we increased capital investment in our business. In May 2009, we raised $70.0 million through the sale of Series D and Series E preferred stock at a price of $9.34 per share of Series D preferred stock and $10.27 per share of Series E preferred stock. In August 2009, we acquired a reseller of our SaaS solutions in the United Kingdom. With this acquisition, we enhanced our opportunity to increase market share in the European market. In September 2009, we raised $5.0 million through the sale of Series D preferred stock at a price of $9.34 per share. No dividends could be paid on the Series D preferred stock without the approval of our board of directors and a majority in interest of the holders of Series E preferred stock. In addition, (1) the Series D preferred stock has no liquidation preference, (2) the holders of the Series D preferred stock do not have the benefit of any protective provisions afforded in respect of our other then-outstanding series of preferred stock and (3) each share of Series D preferred stock would automatically convert into common stock, based on the then-effective conversion price, upon a qualified public offering. Based primarily on the terms, rights and privileges of the Series D preferred stock and the per share price of the Series D preferred stock, we determined that the fair value of our common stock remained at $9.34 per share for each of the three months ended June 30, 2009 and September 30, 2009.

During the three months ended December 31, 2009, the number of our clients and our revenue continued to increase, and we again increased the capital investment in our business. We determined that the fair value of our common stock remained at $9.34 per share for October 2009. In November 2009, we raised $70.0 million through the sale of Series D and Series F preferred stock at a price of $11.21 per share of Series D preferred stock and $12.84 per share of Series F preferred stock. At that time, our certificate of incorporation was amended to provide that no dividends could be paid on the Series D preferred stock without the approval of our board of directors and a majority in interest of the holders of the Series E preferred stock and Series F preferred stock, voting as a single class. Based primarily on the terms, rights and privileges of the Series D preferred stock and the per share price of the Series D preferred stock, we determined the fair value of our common stock to be $11.21 per share for November and December 2009.

From January 1, 2010 to June 30, 2010, our quarterly revenue performance improved compared to the corresponding quarters in 2009 through continued investment in hiring additional personnel, developing our infrastructure and releasing new SaaS solutions. In March 2010, we acquired CoTweet to extend our suite of cross-channel, interactive marketing SaaS solutions to include a social media application. In connection with that acquisition, we issued additional shares of Series D preferred stock valued at $11.21 per share. Consistent with the Practice Aid provisions, we also concluded that the price of $11.21 per share invested by third parties for our Series D preferred stock was good evidence of fair value for the three months ended March 31, 2010 and June 30, 2010. Based on the Series D preferred stock transaction, we determined the fair value of our common stock to be $11.21 per share for each of the three months ended March 31, 2010 and June 30, 2010.

From July 1, 2010 to December 31, 2010, our quarterly revenue performance improved compared to the corresponding quarters in 2009 through continued investment in hiring additional personnel, developing our infrastructure and releasing new products. In August 2010, we acquired a reseller of our SaaS solutions in Australia. With this acquisition, we enhanced our opportunity to increase market share in the Asia-Pacific market. We utilized a contemporaneous third-party valuation of our common stock to reflect various changes in our financial performance, the value of similar publicly-held companies, publicly-reported stock transactions and other factors. We had no plans for an initial public offering in the near term as we remained focused on investing and growing our company using the capital we had raised during 2009. We also considered the other valuation factors described above and concluded that $13.60 per share was a reasonable estimate of the fair value of our common stock during this period.

During each of the three months ended March 31, 2011 and June 30, 2011, the number of our clients and our revenue continued to increase, and we increased our investment in our business. In March 2011, we raised $30.0 million through the sale of Series G preferred stock at a price of $15.40 per share. Considering the capital raised in March 2011, we did not contemplate an initial public offering in the near term. Based primarily on the terms, rights and privileges and per share price of the Series G preferred stock, we determined that $15.40 per share reflected the fair value of our common stock during each of the three months ended March 31, 2011 and June 30, 2011.

During the three months ended September 30, 2011, as our financial results and market conditions continued to be favorable, our board of directors determined that we should explore the opportunity to launch an initial public offering. We initiated discussions with investment banks about a possible initial public offering. During the three months ended September 30, 2011, we engaged investment bankers, lawyers and accountants to start the process of an initial public offering and held

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our initial organizational meeting. In July 2011, we conducted a contemporaneous third-party valuation of the fair value of our common stock and, based on the results of this valuation, we granted options in August and September 2011 at a price of $19.17 per share, which we determined to be the fair market value of our common stock on such dates. In August 2011, we acquired a reseller of our SaaS solutions in Brazil. With this acquisition, we enhanced our opportunity to increase market share in South America and across the Latin American market.

There were several significant factors that impacted our July 2011 fair value determination compared to our March 2011 valuation, including:

- we updated our long-term financial projections;
- our client base and revenue increased; and
- based on publicly available information, we updated the multiples used when analyzing publicly-traded companies in similar industries and markets, and comparable sales transactions.

Based on all these factors, we also concluded that an increase in fair value of our common stock from $15.40 per share in March 2011 to $19.17 per share in July 2011 was reasonable.

In November 2011, we issued 2,000,000 shares of Series D preferred stock at $20.00 per share for total proceeds of $40.0 million. Such shares were sold to existing holders of Series D preferred stock and their affiliates.

The following table shows the intrinsic value of our outstanding vested and unvested stock options and restricted stock as of September 30, 2011, based upon the initial public offering price of $ per share, which is the midpoint of the estimated price range shown on the cover page of this prospectus.

	Number of Shares Underlying Options and Restricted Stock	Intrinsic Value (in thousands)
Total vested options outstanding	2,762,093	$
Total unvested options outstanding	2,896,674	
Total restricted stock outstanding	66,026	
Total options and restricted stock outstanding	5,724,793	$

Qualitative and Quantitative Disclosures about Market Risk

Foreign Currency Exchange Risk. Our results of operations and cash flows are subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the British Pound and Australian dollar. The volatility of exchange rates depends on many factors that we cannot forecast with reliable accuracy. We typically collect revenue and incur costs in the currency in the location in which we provide our solutions. Although we have experienced and will continue to experience fluctuations in our net income (loss) as a result of transaction gains (losses) related to transactions denominated in currencies other than the U.S. dollar, we believe that a 10% change in foreign exchange rates would not have a material impact on our results of operations. To date, we have not entered into any foreign currency hedging contracts. As our international operations grow, we will continue to reassess our approach to managing our risk relating to fluctuations in currency rates.

Interest Rate Sensitivity. Our exposure to market risk for changes in interest rates primarily relates to our investments, our revolving credit facility and our variable-rate term loan.

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The primary objective of our investment activities is to preserve principal while maximizing yields without significantly increasing risk. This objective is accomplished by making diversified investments, consisting only of investment grade securities.

Our revolving line of credit and our term loan bear interest at a variable rate of the prime rate plus one percent. Based on amounts outstanding at September 30, 2011, a 10% increase in the prime rate would not materially increase our interest expense.

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BUSINESS

Our Business

We are a leading global provider of cross-channel, interactive marketing SaaS solutions that empower organizations of all sizes to communicate with their customers through the interactive channels they use most email, mobile, social media and websites. Our solutions provide marketers with a broad and powerful suite of integrated applications to plan, automate, deliver and optimize data-driven interactive marketing campaigns and real-time communications to drive customer engagement, increase sales and improve their return on marketing investment.

Our suite of cross-channel, interactive marketing applications, which include email, mobile, social media and sites, is built on our highly-scalable and flexible multi-tenant SaaS platform. These channel applications are integrated with our campaign management, calendaring, real-time dashboard, integrated reporting, marketing automation and data management tools to provide marketers a comprehensive, yet easy-to-use, solution to manage, automate and engage in real-time interactive marketing. In addition, our cloud-based platform s robust integration framework enables clients to integrate data from virtually any relevant source and leverage productized integrations with leading third-party CRM, web analytics and e-commerce providers to further enhance the relevancy of their interactive communications. We also provide open APIs and developer tools that allow third parties to embed our technology into their solutions and build applications on our platform.

Our global sales organization is focused on adding new clients and expanding relationships with existing clients. We believe our team is the largest sales organization devoted to selling interactive marketing SaaS solutions, with over 285 sales professionals located on four continents. Our field sales team sells into the enterprise market, while our inside sales team sells to small and medium-sized organizations primarily via telesales. In addition to these new business teams, we have a relationship management sales team that focuses on strengthening client relationships, driving contract renewals and selling additional applications to existing clients. We also extend our sales distribution through relationships with more than 500 marketing service providers that resell our solutions to their customers.

Our direct client base consisted of over 4,600 organizations as of September 30, 2011, ranging from enterprises to small businesses in numerous industries, including retail and e-commerce, media and entertainment, travel and hospitality, financial services and insurance, technology, daily-deal and flash-sale and marketing service providers. Among our direct clients are U.S.-based companies such as Ally Financial, Inc., Angie s List, Inc., CareerBuilder, LLC, Groupon, Inc., Microsoft Corporation, Nationwide Mutual Insurance Company, Oakley, Inc., OneAmerica Financial Partners, Inc., One King s Lane, Inc., Papa John s International, Inc., priceline.com Incorporated, The Scotts Miracle-Gro Company, Tommy Hilfiger Group, WellPoint, Inc. and Zappos.com, Inc., and companies headquartered outside the United States such as Abril Group (Brazil), Fairfax Media Limited (Australia), Icelandair Group (Iceland) and Telegraph Media Group Limited (United Kingdom). Several thousand additional organizations utilize our SaaS solutions through their relationships with our marketing service provider clients. Our client base is diverse, and no single client represented more than 5% of our overall revenue for each of the years ended December 31, 2008, 2009 and 2010, and the nine months ended September 30, 2011.

We provide our solutions primarily through annual and multi-year subscriptions based on volume of contracted utilization, level of functionality, number of interactive marketing channels, number of users and level of customer support. We have achieved 43 consecutive quarters of revenue growth and annual dollar-based subscription revenue renewal rates of over 100% in each of the years ended December 31, 2009 and 2010. For the years ended December 31, 2009 and 2010 and for the nine months ended September 30, 2011, our revenue was $95.4 million, $134.3 million and $148.0 million, representing period-over-period growth of 32%, 41% and 55%, respectively.

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Industry Overview

Marketing has evolved significantly in recent years, driven by changes in media consumption, real-time engagement through social media and pervasive mobile connectivity through tablets and smart phones. For marketers today, delivering relevant, meaningful and timely communications is more challenging than ever, as consumers are interacting with brands offline and online through interactive channels such as email, mobile, Twitter, Facebook and websites. This new era of the hyper-connected and empowered consumer requires organizations to develop a cross-channel view of their customers to drive real-time, relevant engagement and positive return on marketing investment.

Market Opportunity for Interactive Marketing

Consumers are increasingly using email, mobile, social media and websites to access information and interact with brands. Media consumption is shifting from offline channels to interactive channels, as evidenced by Forrester s finding that in 2010, 33% of weekly media consumption among U.S. adults occurred through the Internet. This is driving marketers to increase the percentage of advertising spending on interactive marketing. According to Forrester s *US Interactive Marketing Forecast, 2011 To 2016*, U.S. marketers plan to increase spending on interactive channels (defined as display, search, email, mobile and social media) as a percentage of total advertising spending from 16% in 2011 to 26% in 2016, creating a projected $77 billion market in the United States by 2016, of which email, mobile and social media marketing is expected to grow from approximately $4.8 billion in 2011 to nearly $15.7 billion by 2016, representing a compound annual growth rate of 27%. In addition to this large U.S. market opportunity, we believe the addressable market outside the United States presents an even greater opportunity based on comparisons of population, Internet usage, mobile adoption and e-commerce spending. Key opportunities by channel include:

Email. Email remains the primary channel for interactive marketers given its compelling return on investment and ubiquity of use. According to a 2011 Direct Marketing Association report, email marketing returned an estimated $40.56 for every dollar spent on it in 2011, the highest return on investment among all marketing channels. Forrester projects the overall market for U.S. email marketing will grow from $1.5 billion in 2011 to $2.5 billion in 2016, representing a compound annual growth rate of 10%.

Mobile. According to Gartner, the installed base of mobile devices will reach 5.6 billion by 2015. Mobile marketing provides compelling benefits, such as location-based data as well as a channel for real-time engagement with customers. Given the mobile channel s ability to generate immediate response, it can be an effective way to acquire new customers and obtain permission for communication through other marketing channels. According to Forrester, U.S. mobile marketing spending is expected to grow from $1.7 billion in 2011 to $8.2 billion in 2016, representing a compound annual growth rate of 38%.

Social. The rapid emergence of social media has fundamentally changed the way consumers interact with each other and with brands. Facebook has announced it has over 800 million active users, and Twitter has announced it has over 175 million members. These leading social media networks enable marketers to interact and engage in real time with consumers. According to Forrester, U.S. social media marketing spending is expected to grow from $1.6 billion in 2011 to $5.0 billion in 2016, representing a compound annual growth rate of 26%.

Sites. Email, mobile and social media drive website traffic, which is a critical component of interactive marketing campaigns as it not only enables marketers to obtain permission for further communications, but also provides the means by which conversion occurs to generate sales. Websites provide marketers with tools such as web forms to collect customer information and online conversion tracking to create customer data-driven targeting rules to personalize landing pages and microsites.

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Market Challenges

Most organizations understand that effective email marketing and cross-channel, interactive marketing can drive customer engagement, increase sales and improve return on marketing investment. However, organizations often lack the technology, infrastructure and expertise needed to plan, automate, deliver and optimize data-driven interactive marketing campaigns and real-time communications across interactive channels. Marketers considering the adoption or expansion of email and cross-channel, interactive marketing programs face many challenges, including the following:

Difficulty in integrating data to create a single, unified view of each consumer. With the proliferation of consumer data generated by social media, web analytics and e-commerce, it is difficult for organizations to integrate these disparate data sources to create a single, unified view that reflects a collective knowledge of each consumer, including previous interactions and preferences, in order to effectively target and deliver personalized and relevant communications.

Complexity in effectively engaging consumers across multiple channels. Engaging consumers has become increasingly difficult in today s media-saturated environment, requiring marketers to provide increasingly personalized and relevant communications. Organizations require data management and interaction technologies that enable them to leverage cross-channel insights to drive relevant communications. Non-relevant content and poorly timed communications may result in interactions that fail to produce positive return on investment, tarnish brand image or alienate consumers.

Inability of disparate point solutions to address marketers emerging needs. Many solutions are designed to only address specific marketing channels or use cases. These siloed point solutions create significant cost inefficiencies and limitations in integrating data in a timely manner among solutions and interactive marketing channels. These solutions often lack the flexibility, cross-channel functionality and scalability to meet marketers evolving needs as their programs grow in scale and sophistication. This problem is exacerbated as organizations increase the number of channels they use to communicate and interact with consumers.

Complex security and infrastructure requirements. Given the critical nature of interactive communications such as fraud alerts, e-statements and time-sensitive offers, organizations require 24/7 application availability, high-volume transaction processing, sophisticated security controls and a significant amount of data storage. To meet these requirements internally, organizations must make significant investments in technical expertise, complex infrastructure, advanced security measures and data storage.

Changing deliverability and regulatory standards. To ensure marketing communications reach their intended recipients, marketers must understand and adhere to the complex and constantly-evolving permission and delivery standards of leading ISPs and telecommunication providers. In addition, organizations must maintain compliance with state, federal and international laws governing the delivery of mobile and email messages, including the U.S. CAN-SPAM Act and foreign governments privacy and permission laws and regulations.

Our Solutions

Our suite of cross-channel, interactive marketing applications enables organizations of all sizes to plan, automate, deliver and optimize data-driven interactive marketing campaigns and critical real-time communications through email, mobile, social media and websites. By integrating communications and data across multiple channels, our solutions empower our clients to create and deliver more relevant, engaging and effective customer communications, improving their return on marketing investment. Key benefits of our solutions include:

Cross-channel campaign management and engagement capabilities powered by a unified view of each consumer. Our cross-channel, interactive marketing suite includes

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email, mobile, social media and sites applications that are integrated with campaign management, calendaring, marketing automation and data management tools to provide marketers with the ability to engage in real-time, cross-channel marketing. In addition, through the integration of these applications and previously disparate data sources, our solutions enable organizations to develop a unified view of each consumer, which in turn leads to improved targeting and delivery of relevant customer communications.

Automation of marketing campaigns and real-time communications. Our solutions enable clients to automate processes required to deliver sophisticated, multi-stage marketing campaigns and personalized real-time communications such as order confirmations, e-statements, alerts, abandoned shopping cart reminders and many others. Automating these communications enables marketers to capitalize on real-time engagement and optimization rather than focusing on manual deployment of campaigns.

Highly-scalable and modular SaaS architecture to meet clients evolving needs. Our SaaS technology infrastructure supports large transaction volumes and allows our clients to store large amounts of data while maintaining high application availability and security essential for their business-critical communications. In addition, our SaaS architecture and modular product offerings enable our clients to easily add new channels and functionality and increase messaging volume as they expand their interactive marketing programs. This architecture enables us to serve organizations of all sizes from a single platform.

Open and flexible cloud-based platform. Our cloud-based platform s robust integration framework enables clients to integrate data from virtually any relevant source and leverage productized integrations with leading third-party CRM and web analytics providers such as Microsoft Dynamics CRM, salesforce.com, inc., SAP and Adobe Omniture to enhance the relevancy of interactive communications. We also provide open APIs and developer tools that allow third parties to embed our technology into their solutions and build applications on our cloud-based platform.

Compliance with complex deliverability and regulatory standards. We solve challenging issues associated with deliverability of our clients interactive communications and enable our clients to meet legal and regulatory compliance requirements through functionality embedded within our application, relationships with ISPs and telecommunications providers and our knowledge and experience regarding regulatory matters and deliverability standards.

Our Competitive Strengths

Our vision is to inspire and enable organizations of all sizes to leverage interactive marketing technologies to achieve phenomenal business results. We have established a leadership position in interactive marketing as evidenced by our global size, scale and growth, which we believe results in several key competitive strengths including:

Leadership driven by vision and focus on innovation. Our vision, focus on innovation and significant investments have fueled our growth and enabled us to deliver interactive marketing solutions that solve marketers complex challenges. Forrester placed ExactTarget in the leader category in its *Forrester Wave: Email Marketing Service Providers, Q4 2009* report. We received the highest score possible in the Wave for our product roadmap, vertical strategy, strength of management team, executive vision, customers and total employees. A 2011 update to Forrester s *Email Service Provider Wave* is currently underway. We have extended our leadership position beyond email marketing through the integration of our social media platform, CoTweet, the creation of our Social Media Lab and the launch of the Interactive Marketing Hub, our integrated, cross-channel interactive marketing solution.

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Market-leading size and scale and strong business momentum. We believe our size, scale and strong business momentum provide us with substantial competitive advantages. With approximately 1,100 employees located on four continents and over $40 million of expected research and development investment in 2011, we provide marketers around the globe with the team and technology to improve return on investment from their interactive marketing programs. Our substantial investments have led to strong business momentum, resulting in $148.0 million in revenue for the nine months ended September 30, 2011, an increase of 55% compared to the nine months ended September 30, 2010, 43 consecutive quarters of revenue growth and over 4,600 direct clients.

Serving clients of all sizes, in many industries and geographies, from a single platform. Our SaaS architecture and modular product offerings enable our clients to easily add functionality and increase messaging volume as they expand their interactive marketing programs. Our highly-scalable architecture enables us to serve large, distributed enterprises with complex interactive marketing requirements, as well as small and medium-sized organizations. As of September 30, 2011, our direct client base consisted of over 4,600 organizations in numerous industries, including retail and e-commerce, media and entertainment, travel and hospitality, financial services and insurance, technology, daily-deal and flash-sale and marketing service providers. We directly serve clients in the United States, Canada, the United Kingdom, Australia and Brazil through our sales and services operations in those countries. In addition, we are in the process of localizing our user interface to support multiple languages, thereby increasing our potential markets for expansion.

Large direct and indirect sales organization with global reach. Our global sales organization is focused on adding new clients and expanding relationships with existing clients. We believe our team is the largest sales organization devoted to selling interactive marketing SaaS solutions, with over 285 sales professionals located on four continents. Our field sales team sells into the enterprise market, while our inside sales team sells to small and medium-sized organizations primarily via telesales. In addition to these new business teams, we have a relationship management sales team that focuses on strengthening client relationships, driving contract renewals and selling additional applications to existing clients. We also extend our sales distribution through relationships with more than 500 marketing service providers that resell our solutions to several thousand additional organizations.

Corporate culture committed to client success. Named for our primary brand color, our Orange culture reflects our employees energy, passion and focus on client success and is widely regarded as one of our greatest assets. Brought to life through client interactions, employee functions and our inspiring annual user conferences, Connections and Connections UK, our culture and client commitment are consistently cited as a key differentiator by clients, partners, prospective clients and employees. The most recent company-wide survey of our employees, conducted by First Person, Inc. (formerly Benefit Associates, Inc.), found that 99.4% of employees are proud to work at our company and 98.3% would recommend our company to a friend as a good place to work. In 2011, we were named one of the nation s Best Places to Work for recent college graduates by Experience Inc. and one of Indiana s Best Places to Work for the fifth consecutive year.

Our Growth Strategy

We intend to leverage our vision, our focus on innovation, the breadth of our solutions and our extensive interactive marketing expertise to extend our market leadership and continue to fuel our growth. Key elements of our growth strategy include:

Continue to innovate and enhance our leading interactive marketing solutions. We intend to continue to make substantial investments in research and development to further

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enhance our cross-channel, interactive marketing capabilities. We expect our investments to strengthen our leadership in email marketing while continuing to expand our mobile, social media and sites applications through our Interactive Marketing Hub. We also plan to continue advancing our platform capabilities to accelerate third-party integration and application development.

Win new clients by expanding direct and indirect sales. We believe the market for interactive marketing solutions is large and underserved, and we will continue making significant investments to pursue this global market opportunity. To acquire new clients, we will continue to expand our direct sales organization of more than 285 sales professionals and our indirect distribution channels of more than 500 marketing service providers. As we expand, we will continue to employ a disciplined and analytical sales strategy tailored for each market and industry.

Increase revenue from our existing clients. With more than 4,600 clients in many markets and industries, we believe we have a significant opportunity to sell additional applications to our clients and expand their use of emerging interactive channels such as mobile and social media. Our team of relationship managers focuses on strengthening client relationships, driving contract renewals and selling additional applications to our existing clients. This focus has led to the achievement of annual dollar-based subscription revenue renewal rates of over 100% in each of the years ended December 31, 2009 and 2010.

Continue to expand our global presence. We believe there is substantial opportunity to expand our business globally as adoption of interactive marketing increases. Our strategic focus on global expansion has increased our non-U.S. revenue from approximately 6% of our revenue for the year ended December 31, 2009, to approximately 8% for the year ended December 31, 2010 and 12% for the nine months ended September 30, 2011. We directly serve clients in Canada, the United Kingdom, Australia and Brazil through our sales and services operations in those countries. As part of our strategy to expand into new global markets, we are in the process of localizing our user interface to support multiple languages.

Selectively pursue acquisitions. We have successfully extended our business through acquisitions, both in terms of product functionality through our acquisition of CoTweet, and geographic presence through the acquisitions of our resellers in the United Kingdom, Australia and Brazil. These acquisitions have strengthened our market leadership while providing modest incremental revenue. We will continue to selectively explore acquisition opportunities of companies and technologies to expand the functionality of our solutions, provide access to new clients or markets, or both.

Our Products

Our suite of cross-channel, interactive marketing applications, which include email, mobile, social media and sites, is built on our highly-scalable and flexible multi-tenant SaaS platform. These applications are integrated via our Interactive Marketing Hub, which provides campaign management, calendaring, real-time dashboards and integrated reporting, as well as marketing automation and data management applications to provide marketers a comprehensive solution to manage, automate and engage in real-time interactive marketing. In addition, our cloud-based platform s robust integration framework enables clients to integrate data from virtually any relevant source and leverage productized integrations with leading third-party CRM, web analytics and e-commerce providers to further enhance the relevancy of interactive communications. We also provide open APIs and developer tools that allow third parties to embed our technology into their solutions and build applications on our platform.

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The following diagram illustrates our platform and suite of cross-channel, interactive marketing applications.

Interactive Marketing Hub

The Interactive Marketing Hub provides marketers with a comprehensive solution to engage in real-time, cross-channel marketing. The Interactive Marketing Hub integrates our email, mobile, social media and sites Channel Applications with powerful data management and marketing automation Hub Applications. Built on our cloud-based FUEL platform, these applications integrate seamlessly with Hub Tools which include a unified calendar, campaigns, real-time dashboards and integrated reporting.

Channel Applications

Channel Applications provide powerful, easy-to-use, interactive marketing engagement solutions to plan, automate, deliver and optimize messages across email, mobile, social media and sites. Channel Applications can be purchased individually or as a suite, and are seamlessly integrated with the Interactive Marketing Hub s cross-channel campaign management, calendaring, real-time dashboard and integrated reporting tools. Each Channel Application is described below.

Email. Our email marketing solutions enable organizations of all sizes to power data-driven email marketing campaigns and real-time communications to drive customer engagement, increase sales and improve their return on marketing investments. Our multiple product editions and modular approach allow our clients to easily add functionality and increase messaging volume as they expand their interactive marketing programs. Each edition is briefly described below:

Core Edition is designed for small and medium-sized organizations as well as departments within enterprises and provides comprehensive, yet easy-to-use, functionality that includes content management tools, segmentation tools and reporting, such as opens, clicks, bounces and other performance metrics.

Advanced Edition is tailored to meet the needs of sophisticated email marketers. In addition to the capabilities included in the Core Edition, the Advanced Edition includes more sophisticated features such as content syndication, dynamic content, relational data, advanced marketing automation, real-time triggered and transactional communications for e-statements, alerts and order confirmations and advanced real-time reporting. The Advanced Edition also provides full access to our FUEL platform s open integration framework and developer tools that facilitates integration with other business systems and applications.

Enterprise Edition is built for large, distributed enterprises that need centralized control and compliance for email marketing communications. In addition to the capabilities included in the Advanced Edition, the Enterprise Edition includes enhanced international sending, advanced role and permission administration, content locking and sharing, and enterprise analytics and reporting. The Enterprise Edition can also include our simplified Xpress Sending interface that enables non-technical users within distributed marketing organizations to create and send emails using pre-approved content via defined templates.

Mobile. Our mobile applications enable marketers to create, automate, deliver and optimize the performance of personalized inbound and outbound SMS mobile messages and support messaging in more than 80 countries worldwide. Through these applications, clients can easily create polls, quizzes, surveys, contests, mobile tickets, coupon redemption, SMS alerts and mobile opt-in for email campaigns. Our mobile capabilities also include tools to optimize email and sites programs for rendering on mobile devices, and we also provide mobile access to our real-time integrated reporting.

Social. Our social media applications provide comprehensive solutions to manage engagement on social networks such as Twitter and Facebook and integrate social data and interactions into cross-channel campaigns. Each application is briefly described below:

SocialEngage (powered by CoTweet) provides a comprehensive social media management application that enables teams to manage multiple social media accounts with administrator-defined user permissions and roles. The application supports real-time social media engagement and enables multiple users to create follow-up tasks and real-time alerts, view individual-level engagement history and consumer profiles including social influence scores, and schedule and automate future posts that can be associated with any campaign defined in the Interactive Marketing Hub.

SocialPages provides an easy-to-use drag and drop interface that allows marketers to easily create, publish and manage branded Facebook pages and tabs that display dynamic content and incorporate engaging features such as forms, YouTube videos, Flickr galleries and the Facebook Like button. The application supports gated content, which allows marketers to display content based on whether a visitor has previously liked the brand.

Sites. Our sites application provides a flexible solution to create, manage, host and integrate data-driven landing pages and other types of microsites into cross-channel marketing campaigns. Our sites application provides an intuitive editor to create custom landing pages with pre-built content options such as forms and consumer subscription centers and also provides full HTML control for more advanced users. Landing pages support dynamic content, enabling marketers to optimize offers and increase engagement by displaying unique content based on a consumer s previous interactions or preferences.

Hub Applications

Hub Applications provide premium capabilities for advanced cross-channel marketing automation, data management, customer data segmentation and analysis. Hub Applications enhance the value our clients can achieve from our Channel Applications, and seamlessly integrate with our Interactive Marketing Hub s cross-channel campaign management, calendaring, real-time dashboard and integrated reporting tools. Each Hub Application is described below.

Audience Builder provides an intuitive drag-and-drop interface that enables marketers to explore multiple data scenarios through real-time filtering and segmentation to create highly-refined target audiences in real time for any campaign or automated messaging series.

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Automation Studio provides an intuitive drag and drop interface to plan, create and execute complex, multi-stage, recurring cross-channel campaigns based on consumer behavior, time or custom attributes. Automated communications can be triggered by events such as product purchases, online registrations or website browsing behavior.

Hub Tools

Our Hub Tools enable integrated planning, cross-channel campaign management and real-time reporting. Each Hub Tool is described below:

Calendar provides a single view of planned and completed campaigns, events and interactions across email, mobile, Facebook, Twitter and websites.

Campaigns enables marketers to easily define interactive marketing campaigns and associated content and interactions across email, mobile, Facebook, Twitter and websites.

Pulse provides real-time dashboards that display information such as the number of Facebook fans, Twitter followers, email subscribers and current status of automated programs and engagement metrics such as opens, clicks and conversions.

Integrated Reporting provides contextual and comprehensive reporting throughout our Interactive Marketing Hub.

FUEL Platform

Our applications are built and delivered on our highly-scalable and flexible, cloud-based FUEL platform. FUEL provides an open integration framework, enabling clients and third-party application providers to integrate data from systems such as CRM, web analytics, and e-commerce through our partner ecosystem of productized integrations with leading providers such as Microsoft Dynamics CRM, salesforce.com, inc., SAP, and Adobe Omniture. Clients and third-party application providers can leverage our APIs and developer tools to embed our technology into their solutions and build applications on our platform. Key features of our cloud-based FUEL platform are described below:

Common Data Model creates a unified, cross-channel view of each consumer by aggregating online behavioral data, channel engagement history, communication preferences and other online or offline data.

Security provides a single sign-on environment for all Interactive Marketing Hub applications secured by multiple technologies, including but not limited to two-factor authentication, IP whitelisting and IP blocking, and enables real-time monitoring and alerting of system activity.

Developer Tools provide a comprehensive library of user interface controls and APIs that enable developers to quickly build applications with a common look and feel on our cloud-based platform.

Integration Framework provides a comprehensive suite of integration capabilities that include our open APIs, CRM and Web analytics integrations, Embedded/Xpress Marketing and HubExchange. Our Embedded/Xpress Marketing solution enables independent software vendors and developers to embed the functionality of our email and mobile applications directly into their technology offerings. Our HubExchange enables marketing technology providers to develop and sell applications built on our platform while leveraging single sign-on and seamless integration into calendaring and campaign management.

Customer Support

All of our solutions include access to our exclusive, client-only social network, 3sixty. This online community currently enables more than 25,000 users to form groups, access on-demand tutorials, whitepapers and case studies, post questions, provide product feedback and access key subscription

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and account information. In addition, included in standard subscriptions to our solutions, all clients have access to our technical support, which is available 24 hours a day, 365 days a year by phone or email. Clients with complex and advanced technical needs may also upgrade their subscriptions to include our Premium or Platinum support offerings, which provide direct access to highly-technical support personnel.

Our Services

We complement our suite of cross-channel, interactive marketing SaaS solutions with a broad array of professional services designed to drive marketing success for our clients. Our experienced global team of professional consultants helps clients accelerate the implementation and execution of their cross-channel marketing efforts, increase their revenue from interactive channels and improve their return on marketing investment. Our collaborative and full-service offerings include:

- ***Training.*** We offer a variety of methods of introduction to our products, including self-help resources, web-based and on-site training, enterprise workshops and train the trainer programs.

- ***Implementation***. Clients who purchase implementation services are assigned an implementation consultant who works closely with them to accomplish the successful adoption and deployment of our solutions.

- ***Integration.*** Through our platform s integration framework, our applications can be integrated with CRM, web analytics, e-commerce and other proprietary business systems. Our integration consultants help clients define their integration needs and design solutions to meet business objectives.

- ***Deliverability.*** Our team of experts helps optimize the delivery of clients email and mobile messages to their customers. Our proprietary inbox technology, expert consultation and substantial industry and ISP relationships help clients maximize deliverability rates.

- ***Campaign Services.*** Our team of designers, developers and creative experts support the full campaign development lifecycle through creating, testing and optimizing cross-channel campaigns that increase consumer engagement and deliver business results.

- ***Strategic Consulting.*** With our dedicated team of marketing strategists, we provide consulting and program management to help clients define, develop and implement interactive communication strategies. These consulting services are designed to meet the needs of complex organizations with multiple brands, business units and geographies.

Our Clients

Our clients range from enterprises to small businesses in numerous industries, including retail and e-commerce, media and entertainment, travel and hospitality, financial services and insurance, technology, daily-deal and flash-sale and marketing service providers. As of September 30, 2011, we served more than 4,600 direct clients, which included approximately 500 marketing service providers that resell our solutions to several thousand additional organizations.

Our direct clients include U.S.-based companies such as Ally Financial, Inc., Angie s List, Inc., CareerBuilder, LLC, Groupon, Inc., Microsoft Corporation, Nationwide Mutual Insurance Company, Oakley, Inc., OneAmerica Financial Partners, Inc., One King s Lane, Inc., Papa John s International, Inc., priceline.com Incorporated, The Scotts Miracle-Gro Company, Tommy Hilfiger Group, WellPoint, Inc. and Zappos.com, Inc., and companies headquartered outside the United States such as Abril Group (Brazil), Fairfax Media Limited (Australia), Icelandair Group (Iceland) and Telegraph Media Group Limited (United Kingdom).

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Our client base is diverse, and no single client represented more than 5% of our overall revenue for each of the years ended December 31, 2008, 2009 and 2010, and the nine months ended September 30, 2011. Our top ten clients accounted for less than 20% of our revenue for the same periods.

Sales and Marketing

Our global sales team is focused on adding new clients and expanding relationships with existing clients. We believe our team is the largest sales organization devoted to selling interactive marketing SaaS solutions, with over 285 sales professionals located on four continents. Our field sales team sells into the enterprise market, while our inside sales team sells to small and medium-sized organizations primarily via telesales. We utilize a disciplined sales process to monitor and evaluate our sales activity from lead identification and evaluation, to sales contacts, opportunity valuation and closing. Field and inside sales professionals are supported by our sales operations team, consisting of solution consultants and business analysts. In addition to these new business teams, we have a relationship management sales team that focuses on strengthening client relationships, driving contract renewals and selling additional applications. We also extend our sales distribution through relationships with more than 500 marketing service providers that resell our solutions to several thousand additional organizations.

Our global marketing team complements our sales organization through lead generation, brand building, analyst relations and industry research. Our primary marketing programs include email, mobile and social media marketing, search engine optimization, online advertising, tradeshows, partner marketing events, public relations and field marketing. Our marketing team also conducts primary research that serves as the foundation for industry thought leadership and our demand-generation activities. This research identifies emerging trends in consumer behavior and marketers adoption of interactive marketing across email, mobile, Facebook and Twitter. Most recently, our multi-part research series *Subscribers*, *Fans, and Followers* has provided thousands of marketers with new consumer insights and best practices for implementing effective cross-channel, interactive marketing. Our marketing team directly supports our large and distributed sales organization through collaborative initiatives, including the creative development and execution of sales proposals, personalized prospecting campaigns, managing large prospective client pursuits and key renewals, creating targeted regional field marketing events and hosting our annual Connections client conferences in the United States and the United Kingdom, which are attended by thousands of marketers from around the world.

Research and Development

Our vision and focus on innovation have fueled our growth and enabled us to deliver interactive marketing SaaS solutions designed to solve marketers complex challenges. We allocate a substantial portion of our operating expenses to developing new capabilities and enhancing existing solutions, conducting software and quality assurance testing and improving our platform and suite of interactive marketing applications to meet our clients evolving interactive marketing needs. Our technical staff monitors and tests our software regularly, and we maintain a disciplined release process to enhance our existing suite of applications and to introduce new capabilities without interrupting service delivery. As of September 30, 2011, we had 190 employees dedicated to research and development, including developers in our Social Media Lab. We supplement our research and development efforts with contractors. We invested $30.2 million in research and development during the nine months ended September 30, 2011, and research and development expenses totaled $27.4 million, $14.8 million and $9.9 million for the years ended December 31, 2010, 2009 and 2008, respectively.

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Our Technology

Our suite of cross-channel, interactive marketing applications is built on our highly-scalable and flexible, multi-tenant SaaS architecture, which enables us to serve all of our clients from a single codebase. Because each new client is provisioned within this existing infrastructure, we believe we can efficiently scale our solutions as our business grows. Scalability is achieved through application partitioning that allows for horizontal scaling across multiple parts of our platform. Each application partition can be scaled independently of other application partitions. Examples of partitions include our user interface, API, message building, message transferring, analytics and tracking, database management, image management and reporting. Through cloud-enabling technologies, such as server virtualization and storage networking, new capacity can be provided as it is needed within an application partition, which allows for effective management to meet high transaction volumes.

Our applications are written in C#, Java and JavaScript, and we use commercially-available hardware and a combination of proprietary and commercially-available software, including Microsoft SQL Server, Hadoop, Redis, Microsoft Windows and Linux. We own substantially all of the hardware deployed in support of our software. Our system hardware is co-located in two third-party operated hosting facilities in Indianapolis, Indiana and Las Vegas, Nevada. During the fourth quarter of 2011, we expect to commence operations in a third data center, located in Indianapolis. This facility, which is owned and operated by a third party, has comparable terms to our existing Indianapolis and Las Vegas data centers. These facilities provide around-the-clock security personnel, video surveillance and biometric access screening, and are serviced by onsite electrical generators and fire detection and suppression systems. Our network infrastructure is fully redundant within each of our data centers, including network teaming to provide network redundancy that includes multiple upstream Internet connections.

We continuously monitor the performance and availability of our software applications. We have a highly-available, scalable infrastructure that utilizes load-balanced web server pools, redundant interconnected network switches and firewalls, intrusion detection and fault-tolerant storage devices. Production data is backed up on a daily basis and stored in multiple locations to help ensure transactional integrity and restoration capability. Application monitoring includes automated tools that help ensure our software is operating within appropriate performance benchmarks. In addition, our system engineers proactively monitor the status and effectiveness of our applications as well as manage message delivery into domains such as AOL, Yahoo, MSN and Google. We use third-party firms to perform security audits that test our applications and infrastructure security.

Our Competition

The markets for interactive marketing solutions are fragmented, highly competitive and rapidly changing. We provide our solutions to a broad array of clients, ranging from enterprises to small businesses, while our competitors generally focus on either the small business market or the enterprise market. Our competitors include Aprimo, Inc. (which was acquired by Teradata Corporation in 2011), CheetahMail Inc. (a subsidiary of Experian Group Limited), e-Dialog Inc. (a subsidiary of eBay Inc.), Eloqua Limited, Epsilon Data Management, LLC (a subsidiary of Alliance Data Systems Corporation), Responsys, Inc., Silverpop Systems Inc., StrongMail Systems, Inc., Unica Corporation (which was acquired by International Business Machines Corporation in 2010) and Yesmail (a division of infoGROUP Inc.). To a lesser degree, we compete with a number of email marketing providers focused on the small business market. We also face competition from social media marketing providers, such as Buddy Media, Inc. and Radian6 Technologies, Inc. (which was acquired by salesforce.com, inc. in 2011), and from mobile marketing service providers, as well as from in-house solutions that our current and prospective clients may develop.

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We believe the principal competitive factors in our market include:

- product features, effectiveness, interoperability and reliability;
- breadth and expertise of sales organization;
- ability to integrate across interactive marketing channels;
- platform scalability;
- pace of innovation and product roadmap;
- domain expertise in interactive marketing;
- strength of professional services organization;
- price of products and services;
- integration with third-party applications and data sources;
- return on investment;
- ease of use; and
- size and financial stability of operations.

We believe we currently compete effectively with respect to each of the factors identified above.

Our Culture

Named for our primary brand color, our Orange culture reflects our employees energy, passion and focus on client success and is widely regarded as one of our greatest assets. Brought to life through client interactions, employee functions and our inspiring annual user conferences, Connections and Connections UK, our culture and client commitment are consistently cited as key differentiators by clients, partners, prospective clients and employees. The most recent company-wide survey of our employees, conducted by First Person, Inc. (formerly Benefit Associates, Inc.), found that 99.4% of employees are proud to work at our company and 98.3% would recommend our company to a friend as a good place to work. In 2011, we were named one of the nation s Best Places to Work for recent college graduates by Experience Inc. and one of Indiana s Best Places to Work for the fifth consecutive year.

Presented daily with the opportunity to market to the best marketers in the world, our team is passionate about our brand, what it stands for and the unique opportunity we have to make a difference for our clients. Our Orange culture is visible across our organization and highlighted through a host of initiatives and programs including:

- our Core Values Recognition Program, which encourages any employee to recommend broader recognition of another team member for going above and beyond the call of duty;

- our employee-led committees of ExactImpact, ExactGreen, ExactFun and ExactWellness, which create opportunities for employees to come together around important causes to make a difference at work and in local communities;

- our high-energy work environments located in architecturally significant buildings on four continents, which feature modern design and team-based work stations that fuel collaboration and innovation;

- our employee volunteer program, which allows employees to spend up to eight hours annually to volunteer for philanthropic efforts during work hours;

- our Catapult recent college graduate recruiting program, which helps us attract promising graduates from leading universities; this award-winning program helps us develop the next generation of company leaders by providing a rotational experience to new graduates, enabling them to learn many facets of our business;

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- our commitment to open and transparent employee communications, as highlighted by our employee suggestion box that provides employees an opportunity to anonymously submit candid feedback directly to the CEO and our weekly email from the CEO to all employees highlighting company performance and accomplishments and company and industry insights; and

- our ExactTarget Foundation, which is in the process of being established and will be funded primarily through employee and third-party contributions, to help combat childhood hunger, advance education and accelerate entrepreneurship.

Government Regulation

Email/Communications

Our clients use our suite of cross-channel, interactive marketing SaaS solutions to plan, automate, deliver and optimize data-driven interactive marketing campaigns and real-time communications to drive customer engagement, increase sales and improve their return on marketing investment. These communications are governed by a variety of U.S. federal, state, and foreign laws and regulations. With respect to email campaigns, for example, in the United States, the CAN-SPAM Act establishes certain requirements for the distribution of commercial email messages and provides for penalties for transmission of commercial email messages that are intended to deceive the recipient as to source or content or that do not give opt-out control to the recipient. The U.S. Federal Trade Commission is primarily responsible for enforcing the CAN-SPAM Act, and the Department of Justice, certain other federal agencies, state attorneys general and ISPs also have authority to enforce certain of its provisions.

The CAN-SPAM Act s provisions include:

- prohibiting false or misleading email header information;

- prohibiting the use of deceptive subject lines;

- requiring that all commercial email must contain a valid opt-out mechanism that gives recipients the opportunity to opt-out of receiving future commercial email messages from the sender for at least 30 days after the initial email is sent;

- requiring opt-out requests to be honored within ten business days;

- requiring that the sender must include a valid physical postal address in the email message; and

- requiring that commercial email sent to recipients that have not given prior affirmative consent to receipt of the message (that is, an opt-in) must provide a clear notice that it is an advertisement.

The CAN-SPAM Act preempts, or blocks, most state laws that expressly regulate the use of email to send commercial messages, except with respect to laws that prohibit falsity or deception in any portion of a commercial email message or information attached thereto, fraud and computer crime. The scope of these exceptions is not settled, and many states have adopted laws regulating commercial email practices that typically provide a private right of action and specify damages and other penalties in addition to those imposed by the CAN-SPAM Act, which in some cases may be substantial. Violations of the CAN-SPAM Act s provisions can result in criminal and civil penalties, including statutory penalties that can be based in part upon the number of emails sent, with enhanced penalties for commercial email senders who harvest email addresses, use dictionary attack patterns to generate email addresses or relay emails through a network without permission.

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With respect to text messaging campaigns, for example, the CAN-SPAM Act and regulations implemented by the U.S. Federal Communications Commission pursuant to the CAN-SPAM Act, and the Telephone Consumer Protection Act, also known as the Federal Do-Not-Call law, among other requirements, prohibit companies from sending specified types of commercial text messages unless the recipient has given his or her prior express consent.

Moreover, some foreign jurisdictions, such as Australia, Canada and the European Union, have enacted laws that regulate sending email, some of which are more restrictive than U.S. laws. For example, some foreign laws prohibit sending unsolicited email unless the recipient has provided the sender advance consent to receipt of such email, or in other words has opted-in to receiving it.

Additionally, our clients collect and use personal information about consumers to conduct their marketing programs, which subjects them to federal, state and foreign privacy laws that regulate the use, collection and disclosure of consumers personal information. In European Union member states and certain other countries outside the United States, data protection is more highly regulated and rigidly enforced. Noncompliance with these laws and regulations carries significant financial penalties.

We are strong advocates of permission-based email marketing. We use the phrase permission-based email marketing to refer to the practice of sending email to our clients customers only if such customers have affirmatively opted-in to receive any, or a specific type, of email from our client, through our system. Our standard terms and conditions require our clients to comply with all applicable laws, including, among others, the CAN-SPAM Act and other privacy regulations around the globe. If our clients marketing campaigns are alleged to violate applicable laws and we are deemed to be responsible for such violations, or if we were deemed to be directly subject to and in violation of these requirements, it is possible that we could be exposed to liability. To help manage this risk we require compliance certifications from our clients, include indemnity provisions in our standard agreements and take other steps to help our clients stay in compliance with the CAN-SPAM Act and other applicable laws.

We have taken additional steps to facilitate our clients compliance with the CAN-SPAM Act through the adoption of our Anti-Spam Policy which provides that our clients:

- use our software only to send emails to customers and prospects that have directly consented (opted-in) to receiving their email;
- will not use our system to send unsolicited email;
- will provide us with the source of the email addresses, the method used to capture the data, and verification of the consent to receive emails from such client for any list of email addresses used in our system;
- will not use rented or purchased lists, email append lists or any other list that contains email addresses captured using any other method than opt-in; and
- will not use opt-out lists in our system.

Our clients make representations to us regarding compliance with our Anti-Spam Policy. In addition, we retain the right to review customer lists and emails to verify that clients are abiding by our Anti-Spam Policy. However, our clients are ultimately responsible for compliance with our policies, and we do not audit our clients for compliance with our policies.

Privacy/Data Security

We are subject to a number of federal, state and foreign laws and regulations regarding data governance and the privacy and protection of member data that affect companies conducting business on the Internet. In the area of information security and data protection, many governments have

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passed laws requiring notification to users when there is a security incident that results in unauthorized disclosure of their sensitive personal data, such as the 2002 amendment to California s Information Practices Act, or requiring the adoption of minimum information security standards to protect data as it is in transit. The costs of compliance with these laws are expected to increase in the future as a result of changes in interpretation and continued data incidents that lead to additional legislation and regulation. Furthermore, any failure on our part to comply with these laws may subject us to significant liabilities and may result in fines to our clients and us.

Intellectual Property

Our intellectual property is an essential element of our business. We rely on a combination of patent, trademark, copyright and trade secret laws in the United States and other jurisdictions as well as confidentiality procedures and contractual provisions to protect our proprietary technology and our brand.

We have eight patent applications pending in one or more jurisdictions and no issued patents. Members of our software application development management regularly meet to identify new ideas that potentially warrant patent protection. Ideas are submitted to an internal patent committee in the form of an invention disclosure. The patent committee determines whether to proceed with filing a patent application and the jurisdictions in which to file. The jurisdiction decision is made by balancing the cost of pursuing patent protection with the importance of the subject matter of each patent application in a given jurisdiction.

Our U.S. registered trademarks include: EXACTTARGET®, Deliverability REPORT CARD®, REPORT BUILDER®, SUBSCRIBERS RULE!® and ET@®. We have several other trademark applications pending. We focus our trademark efforts in the United States, and when justified by cost and strategic importance, we file corresponding foreign trademark applications in certain jurisdictions such as the European Union, Australia, New Zealand, Singapore, Brazil and the People s Republic of China. Our trademark strategy is designed to provide a balance between the need for coverage in our strategic markets and the need to maintain costs at a reasonable level.

We also enter into confidentiality and proprietary rights agreements with our employees, consultants and other third parties and control access to software, documentation and other proprietary information.

In our subscription agreements with our clients, we typically agree to indemnify our clients against any losses or costs incurred in connection with claims by a third party alleging that a client s use of our services infringes the intellectual property rights of the third party, unless such infringement relates to use of our services in combination with other software not provided by us, arises from modifications not authorized by us or results from continued use by the client after notification by us. Companies in the software industry, including those that provide SaaS, frequently face infringement threats from non-practicing organizations filing lawsuits for patent infringement.

As part of our strategy regarding product development and intellectual property, we have faced and will likely continue to face, direct and indirect accusations of infringement from third parties. We investigate each accusation or claim carefully and respond or defend against the allegations as each situation warrants with the goal of minimizing expenses and disruptions to our business and the business of our clients.

We have in the past and may in the future license third-party intellectual property, software products, and other technology to be incorporated into some elements of our services. In this regard, in 2006, we entered into a non-exclusive patent license agreement with Subscribermail, LLC and Hula

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Holdings, LLC (which was acquired by Harland Clark Corp. in 2010). Under the agreement, we have been granted a license to use the multi-level email methodology covered by a patent owned by Hula Holdings, LLC and licensed to Subscribermail, LLC. The duration of our license is equal to the remaining term of the patent, which expires in 2021.

Employees

As of September 30, 2011, we employed a total of 1,062 employees worldwide, a majority of whom are located in the United States. These employees included 401 in sales and marketing, 190 in research, development and technology, 324 in professional services and customer support and 147 in general and administrative positions. The employees of our Brazilian subsidiary are represented by a local labor union, as is customary in Brazil. None of our other employees are represented by any labor union, and we have never experienced a work stoppage. We believe we have good relations with our employees.

Facilities

Our corporate headquarters, including our principal administrative, marketing, technical support and research and development departments, are located in Indianapolis, Indiana, where we lease approximately 66,536 square feet under an agreement that expires in 2016, approximately 48,890 square feet under an agreement that expires in 2018, and approximately 48,167 square feet under an agreement that expires in 2021. Our system hardware is co-located in two third-party operated hosting facilities in Indianapolis, Indiana and Las Vegas, Nevada. During the fourth quarter of 2011, we expect to commence operations in a third data center, located in Indianapolis. This facility, which is owned and operated by a third party, has comparable terms to our existing Indianapolis and Las Vegas data centers. We also maintain smaller leased regional offices in San Francisco, California, Bellevue, Washington, New York, New York, the United Kingdom, Australia and Brazil. We do not own any real property. We believe that our current facilities are suitable and adequate to meet our current needs, and that suitable additional or substitute space will be available as needed to accommodate expansion of our operations.

Legal Proceedings

We are not currently, nor have we been in the past, subject to any material legal proceedings. From time to time, however, we may become involved in various legal proceedings in the ordinary course of our business, and may be subject to third-party infringement claims. These claims, even those that lack merit, could result in the expenditure of significant financial and managerial resources.

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MANAGEMENT

Executive Officers and Directors

The following table provides information regarding our executive officers and directors as of September 30, 2011:

Name	Age	Position(s)
Scott D. Dorsey	44	Chief Executive Officer, Director and Chairman
Steven A. Collins	46	Chief Financial Officer
Traci M. Dolan	54	Chief Administrative Officer and Secretary
Andrew J. Kofoid	46	Executive Vice President, Global Sales
Timothy B. Kopp	38	Chief Marketing Officer
Scott S. McCorkle	45	Chief Operating Officer
Peter D. McCormick	43	General Manager, ExactTarget Global
Michael M. Brown(1)	39	Director
Matthew W. Ferguson(2)(3)	44	Director
Timothy I. Maudlin(1)(3)(4)	60	Director
Scott M. Maxwell(1)(3)	49	Director
Rory T. O Driscoll(2)	47	Director
David L. Yuan(2)	36	Director

(1) Member of the Audit Committee
(2) Member of the Compensation Committee
(3) This individual has agreed to become a member of the Nominating and Corporate Governance Committee effective upon the closing of this offering
(4) Lead Independent Director

Scott D. Dorsey co-founded ExactTarget in December 2000 and has served as our Chief Executive Officer and a member of our board of directors since that time. He has been the Chairman of our board of directors since May 2010. Prior to co-founding ExactTarget, Mr. Dorsey held a variety of sales and marketing leadership roles with Steelcase, Inc. and Divine, Inc. Mr. Dorsey holds a B.S. in Marketing from Indiana University and an M.B.A. from the Kellogg Graduate School of Management at Northwestern University. While at the Kellogg Graduate School, Mr. Dorsey majored in Entrepreneurship and E-Commerce & Technology. As our Chief Executive Officer and co-founder, Mr. Dorsey has developed intimate knowledge of our business and operations, and we believe Mr. Dorsey provides a valuable perspective as Chairman of our board of directors. Further, we believe that Mr. Dorsey s experiences with our company since its inception will be advantageous as we become a newly-public company.

Steven A. Collins has served as our Chief Financial Officer since June 2011. Prior to joining us, Mr. Collins served as Senior Vice President and Chief Financial Officer of NAVTEQ Corporation, a digital mapping provider. Mr. Collins was with NAVTEQ from 2003 to 2011 and led a team of over 150 finance professionals with responsibility for Finance, Accounting, Tax, Treasury, Sourcing, Travel and Facilities. Before joining NAVTEQ, Mr. Collins served as a Partner at Grace Venture Partners, a venture capital firm that he co-founded, from 2000 to 2003. From 1991 through 2000, Mr. Collins held a variety of financial leadership positions with The Walt Disney Company. Mr. Collins holds a B.S. in Industrial Engineering from Iowa State University and an M.B.A. with concentrations in Finance and Strategy from the Wharton School of the University of Pennsylvania.

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Traci M. Dolan has served as our Chief Administrative Officer since July 2011 and as our Secretary since January 2007. Ms. Dolan served as our Chief Financial Officer from February 2004 to June 2011, as our Vice President of Finance and Administration from October 2004 to August 2007, and as our Executive Vice President of Finance and Administration from August 2007 to July 2011. From March 2000 to December 2003, Ms. Dolan served as Chief Financial Officer, Vice President of Finance and Administration, Secretary and Treasurer of Made2Manage Systems, Inc., a publicly-traded software company. Ms. Dolan previously held financial management and operational positions with Macmillan Publishing, where she was Vice President of Finance and Operations, and with Coopers & Lybrand, where she was an audit manager. Ms. Dolan holds a B.S. in Accounting from Indiana University.

Andrew J. Kofoid has served as our Executive Vice President, Global Sales since May 2010. Prior to joining us, Mr. Kofoid was Vice President of Sales at Dassault Systèmes S.A., a global enterprise product lifecycle management software provider. From 2002 to 2010, Mr. Kofoid served in various U.S.- and European-based sales positions, ranging from Regional Sales Director to Vice President of Sales where he managed over 200 sales and services team members. Before joining Dassault Systèmes, Mr. Kofoid served in sales and sales management positions at Oracle Corporation and IBM. Mr. Kofoid graduated from Purdue University with a B.S. in Electrical Engineering and holds an M.B.A. from the Kellogg Graduate School of Management at Northwestern University.

Timothy B. Kopp has served as our Chief Marketing Officer since December 2007. From December 2006 to December 2007, Mr. Kopp was the Chief Marketing Officer for WebTrends Inc., a provider of unified mobile, social and web analytics and engagement, where he led the company s global marketing strategy and managed a team of more than 35 associates worldwide and an annual budget of approximately $10 million. Before joining WebTrends, Mr. Kopp was Vice President, Worldwide Interactive Marketing for The Coca Cola Company from October 2005 to February 2007. At Coca-Cola, Mr. Kopp managed a global team of more than 50 marketing professionals and a global budget in excess of $50 million. Mr. Kopp was also one of the founding members of Procter and Gamble s Interactive Marketing program where he was employed from January 1998 to October 2005. Mr. Kopp holds a B.B.A. in Finance and Accounting from the University of Cincinnati and an M.B.A. from the University of Dayton.

Scott S. McCorkle has served as our Chief Operating Officer since December 2008. Previously, Mr. McCorkle served as our Vice President, Technology and Product from August 2005 to July 2007 and as our Executive Vice President, Technology and Product from August 2007 to December 2008. Prior to joining ExactTarget, Mr. McCorkle co-founded Mezzia, Inc., a company that provided on-demand software to manage the planning, budgeting, and execution of capital spending and project-based initiatives. Mr. McCorkle was with Mezzia from December 1999 to July 2005, first as its Vice President of Product and then as its President. Mr. McCorkle previously held senior management positions with IBM s customer management group and Software Artistry, a company acquired by IBM. Mr. McCorkle holds a B.S. in Computer Science from Ball State University and an M.B.A. from Indiana University.

Peter D. McCormick co-founded ExactTarget in December 2000 and has served as our General Manager, ExactTarget Global since August 2009. From July 2007 to August 2009, Mr. McCormick served as our Executive Vice President, Partnerships, and from June 2006 to July 2007 as our Executive Vice President, Client Services. Mr. McCormick held executive positions at ExactTarget with responsibility for services, product development and marketing from inception through June of 2006. Prior to co-founding ExactTarget, Mr. McCormick held sales and channel development leadership positions with Divine, Inc., Target, Inc., and Steelcase, Inc. Mr. McCormick holds a B.S. in finance from the University of Minnesota and an M.B.A. from the Carlson Graduate School of Management at the University of Minnesota.

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Michael M. Brown has served as a member of our board of directors since May 2009. Since 2007, Mr. Brown has been a General Partner of Battery Ventures, a private equity and venture capital firm focused on technology companies, which he initially joined in 1998. He currently serves on the boards of several privately-held companies, including Digby Technology, Bluestem Brands and TradeKing Group, Inc. Mr. Brown was previously a member of the High Technology Group at Goldman, Sachs & Co., from 1996 to 1998 and worked as a Financial Analyst within Goldman s Financial Institutions Group between 1994 and 1996. Mr. Brown graduated magna cum laude from Georgetown University with a dual B.S. in Finance and International Business. Mr. Brown provides the board with extensive experience advising high-growth technology companies and in financial and accounting matters.

Matthew W. Ferguson has served as a member of our board of directors since January 2008. Mr. Ferguson has been the President and Chief Executive Officer of CareerBuilder, LLC, a human capital solutions company, since 2003, and previously served as its Chief Operating Officer. Mr. Ferguson also previously served as Senior Vice President of Business Development for Headhunter.net, which was acquired by CareerBuilder, LLC. Mr. Ferguson also held a position developing strategic partnerships for Digitalwork.com, started two entrepreneurial ventures, and was an attorney at Baker & McKenzie LLP. Mr. Ferguson holds a B.A. from Indiana University, an M.B.A. from the University of Chicago and a J.D. from Northwestern University. Based on his current role with CareerBuilder, LLC, Mr. Ferguson provides the board with extensive experience in leading high-growth entrepreneurial ventures.

Timothy I. Maudlin has served as a member of our board of directors since May 2008 and as our lead independent director since May 2010. Since 2007, Mr. Maudlin has served as the lead independent director on the board of directors for Web.com Group, having previously served as a director since February 2002. Mr. Maudlin also serves as a director of Newegg, Inc., one of the largest online-only retailers in the United States, and is the Chairperson of its audit and governance committees and a member of its compensation committee. Mr. Maudlin served as a managing partner of Medical Innovation Partners, a venture capital firm from 1989 through 2007 and as President of its management company since 1985. Mr. Maudlin has served as a director of Sucampo Pharmaceuticals, Inc., a NASDAQ-listed pharmaceutical company since September 2006, and he is currently the Chairman of its audit committee and its nominating and corporate governance committee, and a member of the compensation committee. Mr. Maudlin is a certified public accountant and holds a B.A. from St. Olaf College and an M.M. from the Kellogg Graduate School of Management at Northwestern University. Mr. Maudlin provides the board with extensive experience in accounting, finance, public company governance and advising high-growth companies.

Scott M. Maxwell has served as a member of our board of directors since July 2004. Mr. Maxwell has been the Senior Managing Director of OpenView Venture Partners, a venture capital fund with a focus on software, the Internet and technology-enabled companies that he founded, since 2006. Prior to founding OpenView Venture Partners, Mr. Maxwell served Insight Venture Partners as Chief Operating Officer from 2000 to 2001 and as a Partner and Managing Director from 2000 to 2006. Prior to 2000, Mr. Maxwell had been a Partner and Managing Director, Corporate Development at Putnam Investments, a Senior Vice President, Chief Financial Officer of the Global Equity Division and a member of the Global Equities Executive Committee at Lehman Brothers and a management consultant at McKinsey & Company. Mr. Maxwell has a B.S. and a Master of Science in Mechanical Engineering from University of California, Davis. Mr. Maxwell also graduated from the Massachusetts Institute of Technology, with a Ph.D. in Mechanical Engineering, and an M.B.A. from the Massachusetts Institute of Technology Sloan School of Management. Mr. Maxwell provides the board with the benefit of his extensive experience in the technology industry and capital markets including his focus on financial management and operations.

Rory T. O Driscoll has served as a member of our board of directors since May 2009. Mr. O Driscoll has been a Managing Director at Scale Venture Partners, a venture capital firm focused on information technology companies, and its predecessor funds, since 1994. He currently serves on the boards of several privately-held companies, including Arena Solutions, Inc., Axcient, Inc., Box.net, Inc., DocuSign, Inc., Hubspan, Inc., Livescribe, Inc. and Vantage Media, LLC. Prior to joining Scale Venture Partners, Mr. O Driscoll was founder and Chief Executive Officer of Mercia Ltd., a manufacturing company in the United Kingdom. Mr. O Driscoll holds a B.Sc. from the London School of Economics. Mr. O Driscoll provides the board with the benefit of his expertise in advising high-growth technology companies, including his directorships at several publicly-held companies in the digital marketing arena, including Omniture, Inc., which was subsequently acquired by Adobe Systems Incorporated, and NetGenesis Corporation, which was subsequently acquired by SPSS Inc.

David L. Yuan has served as a member of our board of directors since November 2009. Mr. Yuan has been a General Partner at Technology Crossover Ventures, a private equity and venture capital firm, since 2005. He currently serves on the boards of several privately-held companies, including Merkle, Inc. Prior to joining Technology Crossover Ventures, Mr. Yuan managed investments at J.P. Morgan Partners and was also one of the first employees at 1stUp, an ISP, which was later sold to CMGi. Mr. Yuan began his career as a management consultant with Bain & Company. Mr. Yuan graduated from Harvard University with an A.B. in Economics, and holds an M.B.A. from the Stanford Graduate School of Business. Mr. Yuan provides the board with the benefit of his extensive experience in the technology industry and capital markets, including his directorships at several technology companies.

Board Composition

We currently have seven directors, each of whom was elected as a director under our certificate of incorporation and the board composition provisions of our fourth amended and restated stockholders agreement (the stockholders agreement) by and among us and certain holders of our preferred and common stock as follows:

- Mr. Yuan was elected as the designee of stockholders who hold a majority of the outstanding shares of our Series F preferred stock;

- Messrs. Brown and O Driscoll were elected as the designees of stockholders who hold a majority of the outstanding shares of our Series E preferred stock;

- Messrs. Dorsey and Maxwell were elected as the designees of stockholders who hold a majority of the outstanding shares of our common stock; and

- Messrs. Ferguson and Maudlin were elected as the designees of stockholders who hold a majority of the outstanding shares of our common stock and preferred stock.

The voting provisions of our stockholders agreement by which the directors were elected will terminate upon the closing of this offering, and there will be no contractual obligations regarding the election of our directors after the closing of this offering. Our current directors will continue to serve as directors until their resignations or until their successors are duly elected by the holders of our common stock.

Classified Board

Our amended and restated certificate of incorporation and amended and restated bylaws that will be in effect at the closing of this offering will provide for a classified board of directors consisting of three classes of directors, each serving staggered three-year terms. Our directors will be divided among the three classes as follows:

- Class I directors will be Messrs. Brown and Maxwell, whose initial term will expire at the first annual meeting of stockholders following the closing of this offering;

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Class II directors will be Messrs. Yuan and Ferguson, whose initial term will expire at the second annual meeting of stockholders following the closing of this offering; and

Class III directors will be Messrs. Dorsey, Maudlin and O Driscoll, whose initial term will expire at the third annual meeting of stockholders following the closing of this offering.

Directors for a particular class will be elected for three-year terms at the annual meeting of stockholders in the year in which their term expires. As a result, only one class of directors will be elected at each annual meeting of our stockholders, with the other classes continuing for the remainder of their respective three-year terms. Each director s term continues until the election and qualification of his successor, or his earlier death, resignation or removal.

Director Independence

Under the listing requirements and rules of the , independent directors must comprise a majority of a listed company s board of directors within a specified period. Our board of directors has undertaken a review of its composition, the composition of its committees and the independence of each director. Based upon information requested from and provided by each director concerning his background, employment and affiliations, including family relationships, our board of directors has determined that each of Messrs. Brown, Ferguson, Maudlin, Maxwell, O Driscoll and Yuan is independent under the rules of the . In making this determination, our board of directors assessed the current and prior relationships that each non-employee director has with us and all other relevant facts and circumstances, including the beneficial ownership of our capital stock by each non-employee director. Based on these assessments, for each director deemed to be independent, our board of directors made a determination that, because of the nature of the director s relationships and/or the amounts involved, the director had no relationships with our company or our management that, in the judgment of the board, would impair the director s independence. For those directors that have relationships with our significant stockholders, consistent with the rules of , our board of directors does not believe that ownership of our company s stock, or a relationship with a stockholder, by itself, prevents a director from being independent.

The independence determinations of the board of directors included reviewing the following transactions. Our board specifically considered that: (1) Mr. Brown is a General Partner of Battery Ventures, affiliates of which will own approximately % of our common stock after the closing of this offering; (2) Mr. O Driscoll is a Managing Director at Scale Venture Partners, which (together with its affiliates) will own approximately % of our common stock after the closing of this offering; and (3) Mr. Yuan is a General Partner of Technology Crossover Ventures, which (together with its affiliated entities) will own approximately % of our common stock after the closing of this offering. Our board of directors also considered Mr. Ferguson s relationship with CareerBuilder, LLC, where he serves as President and Chief Executive Officer. CareerBuilder, LLC has been one of our clients for several years. We have provided services to CareerBuilder, LLC in the ordinary course, and the amounts involved are not significant to us or CareerBuilder, LLC. During each of 2008, 2009 and 2010, the aggregate amount of payments that we received from CareerBuilder, LLC was less than $0.8 million and represented less than 2% of both our, and CareerBuilder, LLC s, consolidated gross annual revenues. Mr. Ferguson does not have any financial or other interest in our relationship with CareerBuilder, LLC and does not personally benefit from this relationship.

Our board of directors also specifically considered that Mr. Maudlin serves as a non-employee director of Web.com Group, Inc., which has been one of our clients for several years. Our board of directors believes that a relationship between our company and an entity where a director s only relationship is serving on the entity s board is not material and does not impact the director s independence.

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Board Committees

Audit Committee

Our Audit Committee is currently composed of Messrs. Maudlin, Maxwell and Brown, each of whom is a non-employee, independent member of our board of directors. Mr. Maudlin is the Chairman of the Audit Committee and our Audit Committee financial expert, as currently defined under SEC rules. Each member of the Audit Committee meets the requirements for financial literacy under the applicable rules of the . In November 2011, our board of directors determined that Messrs. Maudlin and Maxwell meet the additional, heightened independence criteria applicable to directors serving on the Audit Committee under SEC and rules. Upon the closing of this offering, the composition of our Audit Committee will comply with all applicable requirements of the SEC and the listing requirements of . A majority of our Audit Committee members meet the additional, heightened independence criteria applicable to directors serving on the Audit Committee under SEC and rules, and after the phase in period under the applicable requirements of the SEC and the listing requirements of , upon which we intend to rely, all members of our Audit Committee will meet such additional, heightened independence criteria. The Audit Committee operates under a written charter that satisfies the applicable standards of the SEC and the listing requirements of , and oversees our corporate accounting and financial reporting process. The Audit Committee s responsibilities include, but are not limited to:

- appointing, compensating, retaining and overseeing our independent registered public accounting firm;
- reviewing the qualifications, performance and independence of the independent registered public accounting firm at least annually;
- consulting with the independent registered public accounting firm to assure the rotation of the lead audit partner and the audit partner responsible for reviewing the audit every five years;
- approving in advance the engagement of the independent registered public accounting firm for all audit services and permissible non-audit services, subject to any permissible pre-approval procedures;
- establishing policies for our hiring of employees or former employees of the independent registered public accounting firm who participated in the audit of our company;
- reviewing and discussing with management and the independent registered public accounting firm our annual and quarterly financial statements and related disclosures;
- resolving any disagreements between the independent registered public accounting firm and management regarding financial reporting;
- meeting with and having required discussions with the independent registered public accounting firm;
- overseeing the preparation of the report required by the rules of the SEC to be included in our annual proxy statement;

- overseeing our internal audit function; and

- reviewing and approving any related-party transactions in accordance with our related-party transactions policy, as in effect from time to time.

Compensation Committee

The current members of our Compensation Committee are Messrs. Ferguson, O Driscoll and Yuan, each of whom is a non-employee, independent member of our board of directors. Mr. O Driscoll is the Chairman of the Compensation Committee. The Compensation Committee operates under a

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written charter that satisfies the applicable standards of the SEC and the . The Compensation Committee s responsibilities include, but are not limited to:

- reviewing and approving goals and objectives relevant to the compensation of our Chairman of the board and/or Chief Executive Officer;
- annually evaluating the performance of our Chairman of the board and/or Chief Executive Officer in light of such compensation goals and objectives and determining the compensation of our Chairman of the board and/or Chief Executive Officer;
- annually reviewing and approving the compensation of our other executive officers;
- overseeing and administering our compensation plans and making recommendations to the board with respect to new plans or amendments to existing plans;
- overseeing the preparation of the Compensation Committee report required by the rules of the SEC to be included in our annual proxy statement; and
- approving and amending the compensation of our directors.

Nominating and Corporate Governance Committee

Our Nominating and Corporate Governance Committee will consist of Messrs. Maudlin, Maxwell and Ferguson, each of whom is a non-employee, independent member of our board of directors. Mr. Maudlin will be the Chairman of the Nominating and Corporate Governance Committee. The Nominating and Corporate Governance Committee will operate under a written charter that satisfies the applicable standards of the SEC and the . The Nominating and Corporate Governance Committee s responsibilities will include, but will not be limited to:

- developing and recommending to the board criteria for board membership;
- establishing procedures for identifying and evaluating director candidates;
- identifying individuals qualified to become board members;
- recommending qualified candidates for election to the board and the board s committees;
- developing and recommending to the board corporate governance guidelines;
- overseeing the self-evaluation of the board and the board s committees; and

developing and recommending to the board procedures for stockholders to send communications to the board.

Compensation Committee Interlocks and Insider Participation

None of the members of our Compensation Committee is, or has at any time during the past year been, an officer or employee of ExactTarget. None of our executive officers currently serves, or in the past year has served, as a member of the board of directors or compensation committee of any other entity that has one or more executive officers serving on our board of directors or Compensation Committee.

Leadership Structure and Risk Oversight

Our board of directors believes that it should maintain flexibility to select a chairman and determine board leadership structure from time to time. Our board of directors does not have a policy on whether the role of the chairman and chief executive officer should be separate and believes that it is currently in the best interest of the company and its stockholders for Mr. Dorsey to serve in both roles, in light of his knowledge of our company and its industry. This also enables Mr. Dorsey to act as the key link between the board of directors and other members of management. His ability to speak as Chairman of the board and Chief Executive Officer also provides strong unified leadership for our company.

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To help assure effective independent oversight, our board of directors appointed Mr. Maudlin to serve as our lead independent director. In this role, Mr. Maudlin will, among other responsibilities, preside over regularly scheduled meetings at which only our independent directors are present, serve as a liaison between the Chairman of the Board and the independent directors, assist the board in helping to assure effective corporate governance and perform such additional duties as our board of directors may otherwise determine and delegate.

Our board of directors oversees the management of risks inherent in the operation of our business and the implementation of our business strategies. Our board of directors performs this oversight role by using several different levels of review. In connection with its reviews of the operations and corporate functions of our company, our board of directors addresses the primary risks associated with those operations and corporate functions. In addition, our board of directors reviews the risks associated with our company s business strategies periodically throughout the year as part of its consideration of undertaking any such business strategies.

Each of our board committees also oversees the management of our company s risk that falls within the committees areas of responsibility. In performing this function, each committee has full access to management, as well as the ability to engage advisors. Our chief financial officer reports to the Audit Committee and is responsible for identifying, evaluating and implementing risk management controls and methodologies to address any identified risks. In connection with its risk management role, our Audit Committee meets privately with representatives from our independent registered public accounting firm and our Chief Financial Officer. The Audit Committee oversees the operation of our risk management program, including the identification of the primary risks associated with our business and periodic updates to such risks, and reports to our board of directors regarding these activities.

Code of Business Conduct and Ethics

We have adopted a code of business conduct and ethics that applies to all of our employees, officers and directors, including those officers responsible for financial reporting. Upon the closing of this offering, the full text of our code of business conduct and ethics will be posted on the investor relations section of our website. The inclusion of our website address in this prospectus does not include or incorporate by reference the information on our website into this prospectus. We intend to disclose future amendments to certain provisions of our code of business conduct and ethics, or waivers of these provisions, on our website and/or in public filings.

2010 Non-Employee Director Compensation

The compensation of our non-employee directors, other than our non-employee directors that are affiliated with our venture capital investors, for fiscal 2010 is set forth in the table below.

Name	Fees Earned or Paid in Cash	Stock Awards(1)	Total
Timothy I. Maudlin(2)	$ 35,000	$ 80,000	$ 115,000
Matthew W. Ferguson(3)	22,500	80,000	102,500
Scott M. Maxwell(4)	23,750	80,000	103,750

(1) The amounts in this column represent the aggregate grant date fair value of restricted stock units granted to our non-employee directors during fiscal 2010 computed in accordance with FASB ASC Topic 718. As of the last day of our fiscal year, each of our non-employee directors held 7,136 unvested restricted stock units.
(2) During fiscal 2010, Mr. Maudlin was the Lead Director and served as the Chair of the Audit Committee.
(3) During fiscal 2010, Mr. Ferguson served as a member of the Compensation Committee.
(4) During fiscal 2010, Mr. Maxwell served as a member of the Audit Committee.

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Directors who are also employees or officers, as well as directors who are affiliated with our venture capital investors do not receive any additional compensation for their service on the board. All directors, however, are reimbursed for their out-of-pocket expenses incurred in connection with their duties as directors. The non-employee director compensation program from fiscal 2010 provided for the following:

Type of Fee/Grant	Dollar Value
Annual Retainer Fee	$ 10,000
Lead Director Fee	5,000
Audit Committee Chair Fee	10,000
Audit Committee Member Fee	3,750
Compensation Committee Chair Fee	5,000
Compensation Committee Member Fee	2,500
Per Meeting Fee (there were eight meetings during 2010)	1,250
Annual Restricted Stock Unit Grant	80,000

As reflected in the table above, on May 27, 2010, each non-employee director received an annual equity award of restricted stock units with a value of approximately $80,000 pursuant to our Independent Directors Restricted Stock Plan and ExactTarget, Inc. 2008 Equity Incentive Plan. The number of units subject to such award was determined by dividing $80,000 by the fair market value of our common stock on such date. The restricted stock unit awards vested on January 1, 2011.

On March 11, 2011, the Compensation Committee approved for fiscal 2011 the following increases to board compensation: the Lead Director will receive $10,000 in cash annually (an increase of $5,000) and additional restricted stock units with a value of approximately $10,000.

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EXECUTIVE COMPENSATION

Compensation Discussion and Analysis

This section explains how our executive compensation programs are designed and operate with respect to our named executive officers listed in the Summary Compensation Table below. Our named executive officers in 2010 were: Scott D. Dorsey, Chief Executive Officer; Traci M. Dolan, Chief Financial Officer; Scott S. McCorkle, Chief Operating Officer; Andrew J. Kofoid, Executive Vice President, Global Sales; and Timothy B. Kopp, Chief Marketing Officer. This compensation discussion and analysis should be read together with the compensation tables and related disclosures set forth below. After the end of the 2010 fiscal year, in June 2011, Steven A. Collins was appointed our Chief Financial Officer and Ms. Dolan became our Chief Administrative Officer.

General Overview and Objectives of our Executive Compensation Programs

The principal objectives of our executive compensation programs are the following:

- To attract and retain talented and experienced executives;
- To incentivize our executives to manage our business to meet our short-term and long-term business goals;
- To reward clear, easily measured performance goals that closely align our executive officers incentives with the long-term interests of stockholders; and
- To ensure that our total compensation is fair, reasonable and competitive.

Our compensation programs are designed to be flexible and complementary and to collectively serve the principles and objectives described above. Compensation for our named executive officers consists of the elements identified in the following table.

Compensation Element	Objective
Base salary	To recognize ongoing performance of job responsibilities
Performance-based cash compensation	To emphasize overall corporate objectives and provide additional reward opportunities for our named executive officers based on corporate performance
Long-term equity incentive compensation	To reward increases in stockholder value and to emphasize and reinforce named executive officer alignment with stockholder interests
Severance and change of control benefits	To provide income protection in the event of involuntary loss of employment and to focus named executive officers on stockholder interests when considering strategic alternatives
401(k) savings plan	To provide retirement savings in a tax-efficient manner
Health and welfare benefits	To provide a basic level of protection from health, dental, life and disability risks

Each of the elements of our executive compensation program is discussed in more detail below. We have not adopted any formal or informal policies or guidelines for allocating compensation between long-term and short-term compensation, between cash and non-cash compensation or among different forms of cash and non-cash compensation.

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Determining Executive Compensation

With respect to our named executive officers other than himself, Mr. Dorsey, our Chief Executive Officer, has historically reviewed the performance of each named executive officer, and based on this review and the factors described below, made recommendations to the Compensation Committee of the board of directors with respect to the total compensation package for such named executive officer. The Compensation Committee makes the final determination with regard to the total compensation package for our named executive officers, including our Chief Executive Officer.

In determining base salary and target performance-based cash compensation, the Compensation Committee used the named executive officers current level of compensation as the starting point. In making adjustments to those levels, the Compensation Committee and our Chief Executive Officer review market data taken from the anonymous technology compensation survey published by Culpepper and Associates, Inc. and publicly-available information regarding compensation paid to executive officers by members of a peer group composed of publicly-traded companies in our industry. The Culpepper report used for our 2010 compensation decisions sorted the results based on geography (the Midwest, excluding Chicago and Minneapolis), size of the company (using only those companies with annual revenue between $100 million and $250 million) and sector (software).

For compensation decisions for 2010, the companies in our peer group, which are reviewed by the Compensation Committee on an annual basis, were Constant Contact, Inc., Interactive Intelligence Group, Inc. and Vocus, Inc. The companies were selected because they are in the software and service industry and are of comparable size to us when comparing annual revenue and number of employees. The revenue for 2010 for the peer group companies ranged from $97 million to $174 million (compared to our revenue of $134 million). We do not target compensation levels for our named executive officers to a specific percentile within either the survey or peer group data, but instead use this information as a check to ensure that the salaries and performance-based cash compensation opportunities of our named executive officers are within a reasonable range (generally approximating the mid-point for comparable executives) compared to the data.

In making decisions regarding long-term equity incentive compensation awards, we have relied on the general industry experience of our Compensation Committee members and a review of the overall stock ownership percentage held by the individual executives and what portion of outstanding equity awards was unvested at the time of the review.

We have not historically targeted a specific mix between fixed and variable compensation, cash and equity incentive awards or long-term and short-term compensation. Our mix of compensation elements has been designed to reward recent results and motivate long-term performance through a combination of short-term cash and long-term equity incentive awards.

In September 2011, in anticipation of becoming a public company, the Compensation Committee engaged Compensia, Inc., an independent compensation consultant, to review our compensation program for our named executive officers, which review may result in future changes to one or more elements of our compensation program for the named executive officers.

Elements of Compensation

Base Salaries. In general, base salaries for our named executive officers are initially established through arm s-length negotiation at the time the individual is hired, taking into account the market data described above and internal pay equity considerations (that is, that differences in relative job responsibilities result in appropriate differences in compensation), as well as the individual s qualifications and experience. Base salaries of our named executive officers are reviewed annually by

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the Compensation Committee. Adjustments to base salaries are based on individual performance, as well as the market data described above and internal pay equity considerations. We do not assign a specific weight to any single factor in making these decisions. Based on these factors, in 2010 the base salaries for our named executive officers were increased from 2009 base salaries as follows:

Named Executive Officer	Base Salary Increase
Scott D. Dorsey	$ 25,000
Traci M. Dolan	20,000
Scott S. McCorkle	25,000
Andrew J. Kofoid	n/a
Timothy B. Kopp	25,000

Performance-Based Cash Compensation. Our named executive officers participate in our performance-based cash bonus program, which provides for an opportunity to earn quarterly and annual cash bonuses upon achievement of performance objectives approved by the Compensation Committee. This program was established to further align named executive officer compensation with corporate business objectives.

Target Bonuses. As with base salaries, the target incentive compensation opportunities for our named executive officers are initially established through arm s-length negotiations at the time the individual is hired, taking into account the market data described above and internal pay equity considerations, as well as the individual s qualifications and experience. Along with base salaries, incentive compensation targets are reviewed annually by the Compensation Committee. Adjustments to incentive compensation targets are based on individual performance, as well as the market data described above and internal pay equity considerations. We do not assign a specific weight to any single factor in making these decisions. For 2010, the incentive compensation targets for our named executive officers were as follows:

Named Executive Officer	Target Quarterly Bonus	Target Annual Bonus	Total Target Bonus for 2010
Scott D. Dorsey	$ 40,000	$ 40,000	$ 200,000
Traci M. Dolan	20,000	20,000	100,000
Scott S. McCorkle	30,000	30,000	150,000
Andrew J. Kofoid(1)	45,000	75,000	210,000
Timothy B. Kopp	25,000	25,000	125,000

(1) Mr. Kofoid commenced employment with us in May of 2010 and was entitled to a guaranteed bonus of at least $45,000 for the second quarter.

Bonus Determinations. Under our performance-based cash bonus program, each year (generally during the first quarter) the Compensation Committee establishes financial performance objectives, and, in the case of the annual bonuses for the named executive officers other than Mr. Dorsey and Mr. Kofoid, individual strategic objectives, which serve as the basis for determining the amount of quarterly and annual bonuses to be paid under the program (after 2010, annual bonuses for all of the named executive officers are expected to be based only on financial performance objectives). For 2010, the Compensation Committee established financial performance objectives tied to total bookings and adjusted operating income for quarterly bonuses and to new bookings and adjusted operating income for annual bonuses. The Compensation Committee determines threshold and target levels for each of these goals in consultation with management and taking into account our performance for the immediately preceding year. The adjusted operating income threshold operates as a pass or fail measure; we must achieve our threshold level in order for the executives to become eligible for a bonus for the applicable quarter or annual period. Additionally, there is a target level of adjusted operating income, and anything above the threshold but below the target would result in 50% of the target bonus becoming eligible for payout, subject to performance against the total bookings or new bookings objective, as applicable. If the adjusted operating income target is achieved, then the total bookings or new bookings objective determines the level of the bonus payout, with respect to the financial performance objectives. We must achieve at least 90% of the target level of the total bookings or new bookings objective, as applicable, for bonuses to be paid under the program for the corresponding period; performance at the 90% level would result in bonus payouts to the named executive officers at no more than 50% of the named executive officers individual target bonus opportunity for the period. The bonus payout increases 5% for every 1% increase in total bookings or new bookings, as applicable, over 90% of the target level. For the second and fourth quarters of 2010, the previously established bonus targets were updated to include the effects of acquisitions made during the first and third quarters. As a result, bonus targets for new and total bookings were increased and adjusted operating income thresholds were reduced. The revisions to the targets were consistent with the board of directors-approved financial plans of the new entities.

For purposes of the bonus program, we define bookings as the annual contract value, incremental messaging fees, and additional commitments by existing clients. New bookings means bookings with organizations that have not been a client during the preceding twelve months and includes all bookings for the first twelve months that they are a client. Total bookings means all bookings from new and existing clients. For multi-year contracts, bookings are limited to bookings attributable to the first twelve months of the contract term. For purposes of the bonus program, adjusted operating income is defined as operating income, adjusted to exclude the impact of stock-based compensation and amortization of intangibles.

For each of the named executive officers other than Mr. Dorsey and Mr. Kofoid, 50% of the annual bonus can be earned relative to the performance against the financial performance objectives and 50% of the annual bonus can be earned relative to performance against individual strategic objectives. Mr. Dorsey and Mr. Kofoid did not have individual strategic objectives as part of their bonus determination because their individual objectives were deemed to be delivering both new and existing bookings targets. Ms. Dolan s two individual objectives were tied to days sales outstanding goals (relating to the collection of receivables) and revenue forecasting accuracy. Mr. Kopp s individual objectives were linked to attendance and cost management of our Connections annual user conferences and new bookings goals. Mr. McCorkle s individual objectives were tied to infrastructure capital spending at or below plan and cost of revenue at or below plan. All three of these named executive officers met their strategic financial objectives for 2010.

Our performance in 2010 relative to our targets, and the resulting bonus payouts, are reflected in the table below:

2010 Period	**Total Bookings Actual** *(as a % of target)*	**New Bookings Actual** *(as a % of target)*	**Adjusted Operating Income Target** *(pass/fail)*	**Individual Strategic Objectives**	**Total Bonus Actual** *(as a % of target)*
First Quarter	103%	n/a	pass	n/a	115%
Second Quarter	102	n/a	pass	n/a	110
Third Quarter	110	n/a	pass	n/a	150
Fourth Quarter	116	n/a	(2)	n/a	180
Full Year	n/a	102%	pass	satisfied	(1)

(1) Mr. Dorsey is only subject to the financial strategic objectives (one half Total Bookings and one half New Bookings) and thus earned 125% of his targeted annual bonus. Mr. Kofoid is only subject to the financial strategic objectives (one third Total Bookings and two thirds New Bookings) and thus earned 130% of his targeted annual bonus. Ms. Dolan, Mr. McCorkle and Mr. Kopp each earned 110% of 50% (or 55%) of their annual bonuses that were subject to the financial strategic objectives and 100% of 50% (or 50%) of their annual bonuses that were subject to the individual strategic objectives.

(2) The fourth quarter operating income target was not met due to significant over-performance in new and total bookings resulting in sales commissions and bonuses in excess of planned levels. As a result of the significant over-performance in bookings, the Compensation Committee used its discretion and approved the full amount of the bonuses.

Long-Term Equity Incentive Compensation. Our named executive officers are eligible to receive long-term equity-based incentive awards, which are intended to align the interests of our named executive officers with the interests of our stockholders and to emphasize and reinforce our focus on team success. Historically, our long-term equity-based incentive compensation awards have been made solely in the form of nonqualified stock options subject to vesting based on continued employment. We believe that stock options are an effective tool for meeting our compensation goal of increasing long-term stockholder value by tying the value of the stock options to our future performance. Because employees are able to profit from stock options only if our stock price increases relative to the stock option s exercise price, we believe stock options provide meaningful incentives to employees to achieve increases in the value of our stock over time.

All stock option awards are approved by the Compensation Committee. Each named executive officer received an initial grant of stock options in connection with the commencement of his employment. Our named executive officers and other employees are also eligible to receive additional grants from time to time. We do not have a set program for the award of equity grants; however, each of our named executive officers received additional option grants in 2009 and 2010 (other than Mr. Kofoid, who joined the company in 2010).

The exercise price of each stock option grant is the fair market value of our common stock on the grant date. Stock option awards to our named executive officers typically vest over a four-year period as follows: 25% of the award vests on the first anniversary of the date of grant; and the remainder of the award vests in equal monthly installments over the 36 months thereafter. We believe this vesting schedule appropriately encourages long-term employment with our company, while allowing our executives to realize compensation in line with the value they create for our stockholders.

Based on the factors described above, in 2010, the Compensation Committee granted stock options to the named executive officers as set forth below in the table entitled Grants of Plan-Based Awards for Year 2010.

Severance and Change in Control Arrangements. Pursuant to employment agreements entered with each of our named executive officers, each of our named executive officers is eligible for severance pay equal to six months (twelve months for Mr. Dorsey) of base salary if the executive s employment is terminated by us other than due to death, disability or termination for unacceptable performance or if the executive resigns for adequate reason. Subsequent to 2010, COBRA benefits were added to severance pay over the severance period. We provide these benefits to promote retention and ease the consequences to the executive of an unexpected termination of employment.

The employment agreements with each of our named executive officers also provide for enhanced severance benefits in the event the executive is terminated by us without cause or resigns for good reason, in each case, upon or within twelve months following a change in control. These benefits consist of severance pay equal to the sum of twelve months (18 months for Mr. Dorsey) of base salary and 50% of the executive s bonus for the calendar year immediately preceding the year in which the termination date occurs. Subsequent to 2010, COBRA benefits were added to severance pay over the severance period. Further, pursuant to the named executive officers outstanding stock option agreements, upon a change in control, each executive would be entitled to accelerated vesting of the portion of the executive s then-outstanding stock options that would have become vested in the following twelve months (24 months for the options granted to Mr. Dorsey and Ms. Dolan in 2004 and

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2009). These arrangements are intended to preserve morale and productivity and encourage executive retention in the face of the disruptive impact of a change in control and to allow our named executive officers to focus on the value of strategic alternatives to stockholders without concern for the impact on their continued employment, as each of their positions is at heightened risk of turnover in the event of a change in control.

Please refer to the discussion below under Potential Payments upon Termination or Change in Control for a more detailed discussion of our severance and change of control arrangements.

Employee Benefits. Our named executive officers are eligible for the same benefits available to our full-time employees generally. These include participation in a tax-qualified 401(k) plan and group life, health, dental and disability insurance plans. The type and extent of benefits offered are intended to be competitive within our industry.

Other Compensation Practices and Policies

Perquisites and Personal Benefits. Our named executive officers are eligible to participate in the same benefits as those offered to all full time employees, and we do not have any programs for providing material personal benefits or executive perquisites to our named executive officers.

Stock Ownership Guidelines. There currently are no equity ownership requirements or guidelines that any of our named executive officers or other employees must meet or maintain.

Policy Regarding the Timing of Equity Awards. As a privately-owned company, there has been no market for our common stock. Accordingly, in 2010, we had no program, plan or practice pertaining to the timing of stock option grants to executive officers coinciding with the release of material non-public information. We do not have any plans to implement such a program, plan or practice after becoming a public company.

Policy Regarding Restatements. We do not currently have a formal policy requiring a fixed course of action with respect to compensation adjustments following later restatements of financial results. Under those circumstances, the Compensation Committee would evaluate whether compensation adjustments were appropriate based upon the facts and circumstances surrounding the restatement.

Tax Deductibility. The Compensation Committee has not previously considered the potential future effects of Section 162(m) of the Code on the compensation paid to our named executive officers. Section 162(m) places a limit of $1 million on the amount of compensation that a publicly-held corporation may deduct in any one year with respect to its chief executive officer and each of the next three most highly compensated executive officers (other than its chief financial officer). In general, certain qualifying performance-based compensation is not subject to this deduction limit. As we are not currently publicly traded, the Compensation Committee has not previously taken the deductibility limit imposed by Section 162(m) into consideration in making compensation decisions. We expect that following this offering, the Compensation Committee will adopt a policy that, where reasonably practicable, we will seek to qualify the variable compensation paid to our named executive officers for an exemption from the deductibility limitations of Section 162(m). However, we may authorize compensation payments that do not comply with the exemptions in Section 162(m) when we believe that such payments are appropriate to attract and retain executive talent.

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Tabular Disclosure Regarding Executive Compensation

The following tables provide information regarding the compensation awarded to or earned during our fiscal year ended December 31, 2010 by our Chief Executive Officer, Chief Financial Officer and our three other most highly compensated executive officers (collectively referred to herein as the named executive officers).

Summary Compensation Table for Year Ended December 31, 2010

Name and Principal Position	Year	Salary	Option Awards(1)	Non-Equity Incentive Plan Compensation(2)	All Other Compensation(3)	Total
Scott D. Dorsey *Chief Executive Officer*	2010	$ 375,000	$ 567,510	$ 272,000	$ 1,171	$ 1,215,681
Traci M. Dolan *Chief Financial Officer*	2010	265,000	198,629	132,000	1,171	596,800
Scott S. McCorkle *Chief Operating Officer*	2010	300,000	425,633	198,000	171	923,804
Andrew J. Kofoid(4) *Executive Vice President of Global Sales*	2010	142,506	1,135,020	291,000	796	1,569,322
Timothy B. Kopp *Chief Marketing Officer*	2010	250,000	283,755	165,000	1,171	699,926

(1) The amounts in this column represent the aggregate grant date fair value of option awards granted to the named executive officer in the applicable fiscal year computed in accordance with FASB ASC Topic 718. See note 8 of the notes to our consolidated financial statements included elsewhere in this prospectus for a discussion of the assumptions made by our company in determining the grant date fair value of option awards.

(2) The amounts included in the Non-Equity Incentive Plan Compensation column reflect cash bonuses (quarterly and annual) paid pursuant to our performance-based cash bonus program for 2010, as described in Performance-based Cash Compensation above. For more information, see Grants of Plan-Based Awards for Year 2010 below.

(3) These amounts consist solely of matching contributions under our 401(k) plan and life insurance premiums paid by us.

(4) Mr. Kofoid commenced employment with us in May 2010. His option award represents an initial grant upon hire.

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Grants of Plan-Based Awards for Year 2010

Name	Grant Date	Estimated Future Payouts Under Non-Equity Incentive Plan Awards(1) Threshold	Target	Maximum	All Other Stock Awards: Number of Securities Underlying Options(2)	Exercise or Base Price of Options Awards, per share	Grant Date Fair Value of Stock and Option Awards(3)
Scott D. Dorsey	2/25/2010	$ 100,000	$ 200,000	n/a			
	5/27/2010				100,000	$ 11.21	$ 567,510
Traci M. Dolan	2/25/2010	45,000	100,000	n/a			
	5/27/2010				35,000	11.21	198,629
Scott S. McCorkle	2/25/2010	67,500	150,000	n/a			
	5/27/2010				75,000	11.21	425,633
Andrew J. Kofoid(4)	4/20/2010	127,500	210,000	n/a			
	5/27/2010				200,000	11.21	1,135,020
Timothy B. Kopp	2/25/2010	56,250	125,000	n/a			
	5/27/2010				50,000	11.21	283,755

(1) Amounts reported represent the potential performance-based incentive cash payments each executive could have earned pursuant to the performance-based cash bonus program for 2010 (including quarterly and annual bonuses), as described in Performance-based Cash Compensation above. At the time of grant, the incentive payments could have ranged from the threshold amounts to an uncapped maximum. The actual amounts earned for 2010 are set forth in the Non-Equity Incentive Plan Compensation column in the Summary Compensation Table above.

(2) Reflects shares of common stock underlying option awards granted in 2010 under the ExactTarget, Inc. 2008 Equity Incentive Plan. The options vest over a four-year period as follows: 25% of the award vests on the first anniversary of the date of grant; and the remainder of the award vests in equal monthly installments over the 36 months thereafter.

(3) The grant date fair value of option awards is determined in accordance with FASB ASC Topic 718. See note 8 of the notes to our consolidated financial statements included elsewhere in this prospectus for a discussion of the assumptions made by our company in determining the grant date fair value of option awards. These amounts do not correspond to the actual value that will be recognized by the named executive officers.

(4) Mr. Kofoid commenced employment with us in May 2010. The option award above represents an initial grant upon hire.

Outstanding Equity Awards at Year-End 2010

Name	Option Awards(5) Number of Securities Underlying Unexercised Options Exercisable	Number of Securities Underlying Unexercised Options Unexercisable	Option Exercise Price	Option Expiration Date
Scott D. Dorsey	95,833	104,167	$ 9.34	1/25/2019
	0	100,000	11.21	5/26/2020
Traci M. Dolan	120,000	0	1.00	10/25/2014
	23,958	26,042	9.34	1/25/2019
	0	35,000	11.21	5/26/2020
Scott S. McCorkle	116,694	0	2.50	8/30/2015

	87,500	12,500	5.52	6/20/2017
	14,583	10,417	10.76	8/25/2018
	47,916	52,084	9.34	1/25/2019
	0	75,000	11.21	5/26/2020
Andrew J. Kofoid	0	200,000	11.21	5/26/2020
Timothy B. Kopp	58,750	25,000	6.72	12/11/2017
	23,958	26,042	9.34	1/25/2019
	0	50,000	11.21	5/26/2020

(5) These stock options have a ten-year term and become vested over a four-year period following the grant date, with 25% of the award becoming vested on the first anniversary of the date of grant, and the remainder of the award becoming vested in equal monthly installments over the 36 months thereafter.

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Potential Payments upon Termination or Change in Control

The table below reflects the amount of compensation that would become payable to each of our named executive officers under existing plans and arrangements if the named executive officer s employment had terminated on December 31, 2010, given the named executive officer s compensation and service levels as of such date. These benefits are in addition to benefits available prior to the occurrence of any termination of employment, including benefits generally available to salaried employees, such as distributions under our 401(k) plan. In addition, in connection with any actual termination of employment, we may determine to enter into an agreement or to establish an arrangement providing additional benefits or amounts, or altering the terms of benefits described below, as we determine appropriate. The actual amounts that would be paid upon a named executive officer s termination of employment can be determined only at the time of such executive s separation from us. Due to the number of factors that affect the nature and amount of any benefits provided upon the events discussed below, any actual amounts paid or distributed may be higher or lower than reported below.

As discussed above in Compensation Discussion and Analysis, pursuant to employment agreements entered with each of our named executive officers, each of our named executive officers is eligible for severance pay equal to six months (twelve months for Mr. Dorsey) of base salary if the executive s employment is terminated by us other than due to death, disability or termination for unacceptable performance or if the executive resigns for adequate reason.

The employment agreements with each of our named executive officers also provide for enhanced severance benefits in the event the executive is terminated by us without cause (and not due to death or disability) or resigns for good reason, in each case, upon or within twelve months following a change in control. These benefits consist of severance pay equal to the sum of twelve months (18 months for Mr. Dorsey) of base salary and 50% of the executive s bonus for the calendar year immediately preceding the year in which the termination date occurs. Subsequent to 2010, COBRA benefits were added to severance pay over the severance period.

Further, pursuant to the named executive officers outstanding stock option agreements, upon a change in control, each executive would be entitled to accelerated vesting of the portion of the executive s then outstanding stock options that would have become vested in the following twelve months (24 months for options granted to Mr. Dorsey and Ms. Dolan in 2004 and 2009).

For purposes of the employment and stock option agreements with our named executive officers, adequate reason, cause, change in control, good reason and unacceptable performance are generally defined as follows:

Adequate reason means our (i) material breach of the employment agreement, (ii) material reduction of the executive s base (or in the case of Mr. Kofoid, variable) compensation, or (iii) requirement that the executive perform the principal duties of employment at a location more than 40 miles from our headquarters (or in the case of Mr. Kofoid, from a location other than Chicago, Illinois).

Cause means the executive s (i) act or omission constituting fraud, (ii) commission (or in the case of Mr. Kopp, conviction of or entry of a plea of nolo contendere with respect to) of a felony, (iii) intentional disclosure of confidential information or (iv) material neglect of duty or serious misconduct (or in the case of Mr. Kopp, intentional gross misconduct), in each case that is materially injurious to us (and, in the case of Mr. Kopp, that has caused substantial injury to us).

Change in control means (i) our consummation of a merger, consolidation, reorganization or similar business transaction, unless immediately after such transaction, more than 50% of the

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outstanding voting power of the surviving or resulting entity is held by persons who were stockholders of the company immediately before the transaction or (ii) our consummation of a sale of all or substantially all of our assets.

Good reason means our (i) material breach of the employment agreement, (ii) material reduction of the executive s base (and in the case of Mr. Kofoid, variable) compensation (or in the case of Mr. Kopp, any decrease in base salary or material decrease in overall compensation and benefits), (iii) requirement that the executive perform the principle duties of employment at a location that is more than 40 miles from the location at which the executive was required to perform such duties immediately before the change in control (or in the case of Mr. Kofoid, from a location other than Chicago, Illinois), (iv) material diminution of the executive s authority, duties or responsibilities, (v) other than for Mr. Kopp, material diminution in the budget over which the executive retains authority or (vi) other than for Mr. Kopp, material diminution in the authority, duties or responsibilities of the supervisor to whom the executive is required to report.

Unacceptable performance means the executive s (i) act or omission constituting cause, (ii) willful and material failure to perform the duties of the executive s employment, (iii) willful and material violation of our code of ethics or written harassment policies or (iv) intentional breach of a material term or condition of the executive s employment agreement.

Name and Termination Event	Cash Severance	Option Acceleration(1)	Total
Scott D. Dorsey			
Involuntary termination	$ 375,000	n/a	$ 375,000
Involuntary termination following change in control	644,765	$ 595,291	1,240,056
Change in control	n/a	595,291	595,291
Traci M. Dolan			
Involuntary termination	132,500	n/a	132,500
Involuntary termination following change in control	306,113	144,838	450,951
Change in control	n/a	144,838	144,838
Scott S. McCorkle			
Involuntary termination	150,000	n/a	150,000
Involuntary termination following change in control	364,475	307,406	671,881
Change in control	n/a	307,406	307,406
Andrew J. Kofoid			
Involuntary termination	117,500	n/a	117,500
Involuntary termination following change in control	235,000	189,207	424,207
Change in control	n/a	189,207	189,207
Timothy B. Kopp			
Involuntary termination	125,000	n/a	125,000
Involuntary termination following change in control	294,258	280,019	574,277
Change in control	n/a	280,019	280,019

(1) These amounts are calculated based on the number of shares of company common stock that would have been subject to acceleration multiplied by the difference between the fair value of our common stock on December 31, 2010 of $13.60 per share and the exercise price of the stock option.

Stock Incentive Plans

ExactTarget, Inc. 2004 Stock Option Plan, as Amended

Our 2004 Stock Option Plan, as amended, which we refer to as the 2004 Plan, was approved by our stockholders and board of directors. Since the approval of the 2008 Plan (described below), no future issuances were permitted under the 2004 Plan; however, forfeitures from the 2004 Plan are added to the pool of shares available for issuance under the 2008 Plan.

The 2004 Plan provides for the grant of incentive stock options and nonstatutory stock options. Our employees, officers and directors, and any subsidiary corporation s employees, officers and directors, are eligible to receive awards under the 2004 Plan; however, incentive stock options may only be granted to our employees or any subsidiary corporation s employees.

In accordance with the terms of the 2004 Plan, our board of directors, or our Compensation Committee, administers the 2004 Plan. Subject to any limitations in the 2004 Plan, the administrator has the power to determine the terms of the awards, including the employees and directors who will receive awards, the exercise price, the number of shares subject to each award, the vesting schedule and exercisability of awards and the form of consideration payable upon exercise.

Most stock options granted under the 2004 Plan vest over a four year period with 25% vested after one year and thereafter at the rate of 1/48 per month. In the event of a change in control (as defined in individual option agreements), additional options may vest equal in most cases to an additional twelve months of vesting (that is, an additional 12/48 of the options shall be deemed to have vested).

With respect to all incentive stock options granted under the 2004 Plan, the exercise price must at least be equal to the fair market value of our common stock on the date of grant. The term of an option may not exceed ten years, except that with respect to any participant who owns 10% of the voting power of all classes of our outstanding stock as of the grant date, the term must not exceed five years and the exercise price must equal at least 110% of the fair market value of our common stock on the grant date. The administrator determines the terms of all other options.

After termination of an employee or director, he or she may exercise his or her options for the period of time stated in the option agreement unless such termination is for cause (as defined in the 2004 Plan), in which case all of the outstanding stock options as of the date of termination shall be forfeited immediately. If termination is due to disability, death or retirement, the options will remain exercisable for no less than three months. In all other cases, other than a termination for cause, the options will generally remain exercisable for at least one month. However, an option may not be exercised later than the expiration of its term.

Unless otherwise determined by the administrator, the 2004 Plan generally does not allow for the sale or transfer of option awards under the 2004 Plan other than by will or the laws of descent and distribution, and option awards may be exercised during the lifetime of the participant only by such participant.

Our board of directors has the authority to amend, alter, suspend or terminate the 2004 Plan provided such action does not impair the rights of any participant, with respect to previously-issued options, without the written consent of such participant.

Our 2004 Plan provides that in the event of the proposed dissolution or liquidation of the company, or in the event of a proposed sale of substantially all of the assets of the company, each stock option shall terminate as of a date fixed by the board of directors, provided that no fewer than 30 days written notice of the date so fixed shall be given to each holder of stock options and each

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holder of stock options shall have the right during the period of 30 days preceding such termination to exercise his or her stock options as to all or any part of the shares of common stock covered thereby.

ExactTarget, Inc. 2008 Equity Incentive Plan, as Amended

Our 2008 Equity Incentive Plan, as amended to date, which we refer to as the 2008 Plan, became effective on February 1, 2008 and was approved by our board of directors on January 23, 2008 and by our stockholders on March 28, 2008. As of September 30, 2011, the aggregate number of shares of our common stock with respect to which awards may be granted under the 2008 Plan was 4,647,339 shares, plus

- any shares of our common stock covered by a stock option under the 2004 Plan that are forfeited or remain unpurchased or undistributed upon termination or expiration of the stock option under the 2004 Plan; plus

- any shares of our common stock exchanged by a participant as full or partial payment to us of the exercise price of an award under the 2008 Plan or a stock option under the 2004 Plan.

The 2008 Plan was amended in November 2011 to increase the number of shares available for grant under the plan by an additional 3,926,283 shares. The number of shares reserved for issuance under our 2008 Plan will increase automatically on the first day of January of each of the years 2013 through 2017 by a number of shares equal to the lesser of (i) 5% of the total number of our shares outstanding as of the immediately preceding December 31, or (ii) such maximum amount, if any, determined by our board of directors.

The maximum number of shares subject to all awards granted in any calendar year to a participant is limited to 200,000.

The 2008 Plan provides for the grant of incentive stock options, nonstatutory stock options, stock appreciation rights and restricted stock. Our employees and directors, and any subsidiary corporation s employees and directors, are eligible to receive awards under the 2008 Plan. However, incentive stock options may only be granted to our employees or any subsidiary corporation s employees.

In accordance with the terms of the 2008 Plan, our board of directors, or our Compensation Committee, administers the 2008 Plan, however, the Compensation Committee may delegate to our Chief Executive Officer all or part of its authority and duties with respect to the granting of options to certain individuals. Subject to any limitations in the 2008 Plan, the Compensation Committee has the power to determine the terms of the awards, including the employees and directors who will receive awards, the exercise price of options, the fair market value of the shares subject to each award, the number of shares subject to each award, the vesting schedule and exercisability of awards and the form of consideration payable upon exercise or purchase, as applicable.

With respect to all stock options granted under the 2008 Plan, the exercise price must at least be equal to the fair market value of our common stock on the date of grant. The term of an option may not exceed 10 years, except that with respect to any participant who owns 10% or more of the voting power of all classes of our outstanding stock as of the grant date, the term must not exceed five years and the exercise price must equal at least 110% of the fair market value on the grant date. The Compensation Committee determines the terms of all other options.

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The Compensation Committee has the authority to establish the effect of a separation from service on the rights and benefits under any award; however, a director s separation from service will not accelerate or otherwise increase the number of shares subject to an award unless the Compensation Committee expressly determines that it will. Participants may exercise awards after a separation from service only in accordance with the terms of the award agreement and, unless otherwise expressly provided by the Compensation Committee, only with respect to the number of shares as to which the award could have been exercised on the date of the separation from service.

Unless otherwise provided by law or the applicable award agreement, the 2008 Plan generally does not allow for the sale or transfer of awards under the 2008 Plan or exercise of awards by any person other than the participant. However, the 2008 Plan permits transfers to the company, designation of beneficiaries and transfers or exercises by beneficiaries in the event of the participant s death, transfers by will or the laws of descent and distribution or transfers or exercises by an authorized legal representative on behalf of a participant who has suffered a disability.

The Compensation Committee has the authority to amend the 2008 Plan without the written consent of the affected participant if the amendment does not materially adversely affect any then-outstanding award. Stockholder approval is required only to the extent required under applicable law or if the board of directors determines that it is necessary or advisable.

Our 2008 Plan provides that, upon the occurrence of any of the events described below, the 2008 Plan and each outstanding award will terminate, subject to any provision made by the Compensation Committee for the continuation of awards. If awards are to terminate, each participant will have the right, by giving notice at least ten days before the effective date of the event in question, to exercise all or any part of an unexpired award to the extent then exercisable. Events triggering termination of the 2008 Plan and each award granted under the plan include the following:

- dissolution, liquidation or sale of all or substantially all of the business, properties and assets of the company,
- any reorganization, merger, consolidation, sale or exchange of securities in which the company does not survive,
- any sale, reorganization, merger, consolidation or exchange of securities in which the company survives and any of the company s stockholders have the opportunity to receive cash, securities of another entity or other property in exchange for their shares of the company s common stock, or
- any acquisition by any person or group of beneficial ownership of more than 50% of our outstanding shares.

The Compensation Committee has the authority to accelerate the vesting and exercisability of all or any portion of any award at any time in its sole discretion, regardless of any provision in the relevant award agreement. The Compensation Committee may determine the terms and conditions of any acceleration so long as the terms and conditions do not materially adversely affect the rights of any participant without the consent of the participant. The Compensation Committee may rescind the effect of any acceleration if it was done in anticipation of an event and the Compensation Committee or the board of directors later determines that the event will not occur.

As of September 30, 2011, there were options to purchase 5,658,767 shares of common stock outstanding at a weighted average exercise price of $10.31 per share, and there were 66,026 shares of unvested restricted common stock outstanding.

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CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Other than the executive officer and director compensation arrangements discussed above under Management and Executive Compensation, and the arrangements described below, there have been no transactions since January 1, 2008 in which we have been a participant, where the amount involved in the transaction exceeded or will exceed $120,000 and in which any of our directors, executive officers or holders of more than 5% of our capital stock, or any immediate family member of, or person sharing the household with, any of these individuals, had or will have a direct or indirect material interest.

Fourth Amended and Restated Stockholders Agreement

We have entered into a fourth amended and restated stockholders agreement (the stockholders agreement) with certain holders of our preferred stock and common stock, including certain holders of more than 5% of our capital stock and entities affiliated with certain of our directors. Entities affiliated with Technology Crossover Ventures, Battery Ventures, Scale Venture Partners, Greenspring Associates and SAP Ventures are parties to the stockholders agreement. The election of the members of our board of directors is governed by certain provisions contained in the stockholders agreement. The holders of a majority of our Series F preferred stock, voting as a separate class, have designated David L. Yuan for election to our board of directors. The holders of a majority of our Series E preferred stock, voting as a separate class, have designated Michael M. Brown and Rory T. O Driscoll for election to our board of directors. The holders of a majority of our common stock, voting as a separate class, have designated Scott D. Dorsey and Scott M. Maxwell for election to our board of directors. The holders of a majority of our common stock and preferred stock, voting together as a class on an as-converted basis, have designated Timothy I. Maudlin and Matthew W. Ferguson for election to our board of directors. In addition, the stockholders agreement, among other things:

- obligates us to deliver periodic financial statements to certain stockholders who are parties to the stockholders agreement, including entities affiliated with Technology Crossover Ventures, Battery Ventures, Scale Venture Partners, Greenspring Associates and SAP Ventures;

- grants a right of first offer with respect to sales of our shares by us, subject to specified exclusions, to certain stockholders, including entities affiliated with Technology Crossover Ventures, Battery Ventures, Scale Venture Partners, Greenspring Associates and SAP Ventures;

- grants Greenspring Associates the right to have one non-voting observer participate in certain meetings of the board of directors;

- grants us certain rights of first refusal with respect to proposed transfers of our securities by certain stockholders; and

- grants our investors certain rights of first refusal and co-sale rights with respect to proposed transfers of our securities by certain stockholders.

The stockholders agreement will terminate upon the closing of this offering. This is not a complete description of the stockholders agreement and is qualified by the full text of the stockholders agreement filed as an exhibit to the registration statement of which this prospectus is a part.

Fourth Amended and Restated Registration Rights Agreement

We have entered into a fourth amended and restated registration rights agreement dated March 28, 2011 (the registration rights agreement). The registration rights agreement gives holders of our preferred stock, including certain holders of more than 5% of our capital stock and entities affiliated with certain of our directors, certain registration rights, including the right to demand that we file a registration statement and the right to request that their shares be covered by a registration statement that we are otherwise filing. Entities affiliated with Technology Crossover Ventures, Battery Ventures,

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Scale Venture Partners, Greenspring Associates and SAP Ventures are parties to the registration rights agreement. For a more detailed description of these registration rights, see Description of Capital Stock Registration Rights.

May 2009 Preferred Stock Transaction

In May 2009, we sold an aggregate of 5,353,316 shares of our Series D preferred stock at a purchase price per share of $9.34, for an aggregate purchase price of $50.0 million, and we sold an aggregate of 1,947,419 shares of our Series E preferred stock at a purchase price per share of $10.27, for an aggregate purchase price of $20.0 million. The following table summarizes purchases of our Series D and Series E preferred stock by entities affiliated with members of our board of directors and persons who hold more than 5% of our outstanding capital stock:

Name of Stockholder	Shares of Series D Preferred Stock	Shares of Series E Preferred Stock	Total Purchase Price
Entities affiliated with Battery Ventures(1)	2,982,562	1,084,990	$ 38,999,976
Scale Venture Partners(2)	1,147,139	417,304	14,999,990
Entities affiliated with Greenspring Associates(3)	1,223,615	445,125	15,999,997

(1) Affiliates of Battery Ventures that purchased shares in the transaction described above and whose shares are aggregated for purposes of reporting share ownership information are Battery Ventures VIII, L.P. and Battery Ventures VIII Side Fund, L.P. Mr. Brown, a member of our board of directors, is a general partner at Battery Ventures. Entities affiliated with Battery Ventures are holders of more than 5% of a class of our voting securities.

(2) Mr. O Driscoll, a member of our board of directors, is a managing director at Scale Venture Partners. Scale Venture Partners is the holder of more than 5% of a class of our voting securities.

(3) Affiliates of Greenspring Associates that purchased shares in the transaction described above and whose shares are aggregated for purposes of reporting share ownership information are Greenspring Global Partners III, L.P., Greenspring Global Partners III-A, L.P., Greenspring Global Partners III-B, L.P., Greenspring Global Partners IV-A, L.P., Greenspring Global Partners IV-B, L.P., Greenspring Global Partners IV-C, L.P. and Greenspring Crossover Ventures I, L.P. Entities affiliated with Greenspring Associates are holders of more than 5% of a class of our voting securities.

With the proceeds from the sale of our Series D preferred stock, in May 2009 we repurchased shares of our common stock, Series A preferred stock, Series B preferred stock, Series C preferred stock and Series D preferred stock from several of our stockholders. Messrs. Dorsey, McCorkle and McCormick and Ms. Dolan participated in these share repurchases and received $3.5 million, $0.6 million, $1.7 million and $0.5 million, respectively.

November 2009 Preferred Stock Transaction

In November 2009, we sold an aggregate of 5,352,364 shares of our Series D preferred stock at a purchase price per share of $11.21, for an aggregate purchase price of $60.0 million, and we sold an aggregate of 778,968 shares of our Series F preferred stock at a purchase price per share of $12.8375, for an aggregate purchase price of $10.0 million. The following table summarizes purchases of our Series D and Series F preferred stock by entities affiliated with members of our board of directors and persons who hold more than 5% of our outstanding capital stock:

Name of Stockholder	Shares of Series D Preferred Stock	Shares of Series F Preferred Stock	Total Purchase Price
Entities affiliated with Technology Crossover Ventures(4)	5,352,364	778,968	$ 70,000,002

(4) Affiliates of Technology Crossover Ventures that purchased shares in the transaction described above and whose shares are aggregated for purposes of reporting share ownership information are TCV VII, L.P., TCV VII (A), L.P. and TCV Member Fund, L.P. Mr. Yuan, a member of our board of directors, is a general partner at Technology Crossover Ventures. Entities affiliated with Technology Crossover Ventures are holders of more than 5% of a class of our voting securities.

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On December 31, 2009, entities affiliated with Technology Crossover Ventures exchanged $3.1 million of our Series D preferred stock (272,791 shares of our Series D preferred stock) for $3.1 million of our Series F preferred stock (238,207 shares of our Series F preferred stock).

With the proceeds from the sale of our Series D preferred stock, in December 2009 we repurchased shares of our common stock, Series A preferred stock, Series B preferred stock and Series C preferred stock from several of our stockholders. Messrs. Dorsey, McCorkle and McCormick and Ms. Dolan participated in these share repurchases and received $2.5 million, $0.5 million, $1.2 million and $0.3 million, respectively.

March 2011 Preferred Stock Transaction

In March 2011, we sold an aggregate of 1,948,052 shares of our Series G preferred stock at a purchase price per share of $15.40, for an aggregate purchase price of $30.0 million. The following table summarizes purchases of our Series G preferred stock by entities affiliated with members of our board of directors and persons who hold more than 5% of our outstanding capital stock:

Name of Stockholder	Shares of Series G Preferred Stock	Total Purchase Price
Entities affiliated with Battery Ventures(1)	451,554	$ 6,953,931
Scale Venture Partners(2)	176,738	2,721,765
Entities affiliated with Greenspring Associates(3)	473,999	7,299,584
Entities affiliated with Technology Crossover Ventures(4)	777,941	11,980,290

(1) Affiliates of Battery Ventures that purchased shares in the transaction described above and whose shares are aggregated for purposes of reporting share ownership information are Battery Ventures VIII, L.P. and Battery Ventures VIII Side Fund, L.P. Mr. Brown, a member of our board of directors, is a general partner at Battery Ventures. Entities affiliated with Battery Ventures are holders of more than 5% of a class of our voting securities.

(2) Mr. O Driscoll, a member of our board of directors, is a managing director at Scale Venture Partners. Scale Venture Partners is the holder of more than 5% of a class of our voting securities.

(3) Affiliates of Greenspring Associates that purchased shares in the transaction described above and whose shares are aggregated for purposes of reporting share ownership information are Greenspring Global Partners I, L.P., Greenspring Global Partners II, L.P., Greenspring Global Partners II-A, L.P., Greenspring Global Partners II-B, L.P., Greenspring Global Partners III, L.P., Greenspring Global Partners III-A, L.P., Greenspring Global Partners III-B, L.P., Greenspring Global Partners IV-A, L.P., Greenspring Global Partners IV-B, L.P., Greenspring Global Partners IV-C, L.P. and Greenspring Crossover Ventures I, L.P. Entities affiliated with Greenspring Associates are holders of more than 5% of a class of our voting securities.

(4) Affiliates of Technology Crossover Ventures that purchased shares in the transaction described above and whose shares are aggregated for purposes of reporting share ownership information are TCV VII, L.P., TCV VII (A), L.P. and TCV Member Fund, L.P. Mr. Yuan, a member of our board of directors, is a general partner at Technology Crossover Ventures. Entities affiliated with Technology Crossover Ventures are holders of more than 5% of a class of our voting securities.

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November 2011 Preferred Stock Transaction

In November 2011, we sold an aggregate of 2,000,000 shares of our Series D preferred stock at a purchase price per share of $20.00, for an aggregate purchase price of $40.0 million. These shares were sold to a total of 18 accredited investors all of which were existing holders of Series D preferred stock or their affiliates. The following table summarizes purchases of our Series D preferred stock by entities affiliated with members of our board of directors and persons who hold more than 5% of our outstanding capital stock:

Name of Stockholder	Shares of Series D Preferred Stock	Total Purchase Price
Entities affiliated with Battery Ventures(1)	375,000	$ 7,500,000
Scale Venture Partners(2)	225,000	4,500,000
Entities affiliated with Greenspring Associates(3)	775,000	15,500,000
Entities affiliated with Technology Crossover Ventures(4)	300,000	6,000,000

(1) Affiliates of Battery Ventures that purchased shares in the transaction described above and whose shares are aggregated for purposes of reporting share ownership information are Battery Ventures VIII, L.P. and Battery Ventures VIII Side Fund, L.P. Mr. Brown, a member of our board of directors, is a general partner at Battery Ventures. Entities affiliated with Battery Ventures are holders of more than 5% of a class of our voting securities.

(2) Mr. O Driscoll, a member of our board of directors, is a managing director at Scale Venture Partners. Scale Venture Partners is the holder of more than 5% of a class of our voting securities.

(3) Affiliates of Greenspring Associates that purchased shares in the transaction described above and whose shares are aggregated for purposes of reporting share ownership information are Greenspring Global Partners I, L.P., Greenspring Global Partners II, L.P., Greenspring Global Partners II-A, L.P., Greenspring Global Partners II-B, L.P., Greenspring Global Partners IV-A, L.P., Greenspring Global Partners IV-B, L.P., Greenspring Global Partners IV-C, L.P., Greenspring Crossover Ventures I, L.P., Greenspring Global Partners V-A, L.P., Greenspring Global Partners V-C, L.P. and Greenspring Growth Equity II, L.P. Entities affiliated with Greenspring Associates are holders of more than 5% of a class of our voting securities.

(4) Affiliates of Technology Crossover Ventures that purchased shares in the transaction described above and whose shares are aggregated for purposes of reporting share ownership information are TCV VII, L.P., TCV VII (A), L.P. and TCV Member Fund, L.P. Mr. Yuan, a member of our board of directors, is a general partner at Technology Crossover Ventures. Entities affiliated with Technology Crossover Ventures are holders of more than 5% of a class of our voting securities.

All of the outstanding shares of our preferred stock will automatically convert into shares of our common stock immediately prior to the completion of this offering.

Indemnification Agreements

We have entered into indemnification agreements with our directors and certain executive officers. These agreements confirm our obligations to indemnify the directors and officers to the fullest extent authorized by the DGCL. The agreements also provide that we will advance, if requested by an indemnified person, any and all expenses incurred in connection with a proceeding, subject to reimbursement by the indemnified person should a final judicial determination be made that indemnification is not available under applicable law. We agree that our obligations under the agreements will continue after the indemnified party is no longer serving our company with respect to claims based on the indemnified party s service at our company. The description above is only a summary and is qualified in its entirety by reference to the form of the indemnification agreement filed as an exhibit to the registration statement of which this prospectus forms a part.

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Review, Approval or Ratification of Transactions with Related Parties

We have a written policy that our executive officers, directors, director nominees, stockholders who own more than 5% of our voting securities, and any immediate family members and certain related persons of the foregoing persons (each a Related Party) are not permitted to enter into a transaction with us, regardless of the dollar amount involved, without the prior consent of our Audit Committee or the Chairman of our Audit Committee. If a member of the Audit Committee is a party to such transaction, he or she may not participate in the review of such transaction. Any request for us to enter into a related party transaction must first be presented to our General Counsel, who will determine whether a transaction is a related party transaction and, if so, will submit the related party transaction to the Audit Committee or its Chairman for review and approval. All Related Parties are required to notify the General Counsel of any possible related party transaction. In approving or rejecting the proposed transaction, our Audit Committee or its Chairman must consider all of the facts and circumstances it deems appropriate, including but not limited to the benefits to us, the terms of the transaction, the terms available to third parties or to employees generally, the availability of other sources for comparable services or products, and, if applicable, the impact on a director s independence. Our Audit Committee or its Chairman may approve only those agreements that are in, or are not inconsistent with, our best interests, as our Audit Committee or its Chairman determines in good faith.

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PRINCIPAL STOCKHOLDERS

The following table sets forth certain information with respect to the beneficial ownership of our common stock as of November 18, 2011 and as adjusted to reflect the sale of common stock offered by us in this offering, for:

- each stockholder known by us to be the beneficial owner of more than 5% of our outstanding shares of common stock;
- each of our directors;
- each of our named executive officers; and
- all of our directors and executive officers as a group.

We have determined beneficial ownership in accordance with the rules of the SEC. Except as indicated by the footnotes below, we believe, based on the information furnished to us, that the persons and entities named in the table below have sole voting and investment power with respect to all shares of our common stock that they beneficially own, subject to applicable community property laws.

Applicable percentage ownership is based on 27,983,654 shares of common stock outstanding as of November 18, 2011, assuming conversion of all outstanding shares of preferred stock into 23,467,219 shares of common stock, which includes 2,000,000 shares of our Series D preferred stock issued in November 2011. For purposes of the table below, we have assumed that shares of common stock will be sold in this offering. In computing the number of shares of common stock beneficially owned by a person or entity and the percentage ownership of that person or entity, we deemed to be outstanding all shares of common stock subject to options or other convertible securities held by that person or entity that are currently exercisable or exercisable within 60 days of November 18, 2011. We did not deem these shares outstanding, however, for the purpose of computing the percentage ownership of any other person. Unless otherwise indicated, the address of each beneficial owner listed in the table below is c/o ExactTarget, Inc., 20 North Meridian Street, Suite 200, Indianapolis, Indiana 46204.

	Shares Beneficially Owned Prior to this Offering		Shares Beneficially Owned After this Offering	
Name of Beneficial Owner	**Number**	**Percentage**	**Number**	**Percentage**
5% Stockholders:				
Entities affiliated with Technology Crossover Ventures(1)	7,218,594	25.8%		
Entities affiliated with Greenspring Associates(2)	4,990,506	17.8		
Entities affiliated with Battery Ventures(3)	4,904,106	17.5		
Scale Venture Partners III, L.P.(4)	1,997,687	7.1		
Directors and Named Executive Officers:				
Michael M. Brown(5)	4,904,106	17.5		
Matthew W. Ferguson(6)	25,330	*		
Timothy I. Maudlin(7)	32,980	*		
Scott M. Maxwell(8)	32,330	*		
Rory T. O Driscoll(9)	1,997,687	7.1		
David L. Yuan(10)	7,218,594	25.8		
Scott D. Dorsey(11)	1,091,666	3.9		
Steven A. Collins		*		
Traci M. Dolan(12)	172,499	*		
Scott S. McCorkle(13)	345,122	1.2		
Timothy B. Kopp(14)	143,124	*		
Andrew J. Kofoid(15)	79,166	*		
All executive officers and directors as a group (13 persons)	16,072,291	57.3		

* Represents beneficial ownership of less than 1% of the outstanding common stock.

(1) Includes 4,722,558 shares owned by TCV VII, L.P., 2,452,536 shares owned by TCV VII (A), L.P. and 43,500 shares owned by TCV Member Fund, L.P. Technology Crossover Management VII, L.P. is the direct general partner of TCV VII, L.P. and TCV VII (A), L.P. Technology Crossover Management VII, Ltd. is the direct general partner of Technology Crossover Management VII, L.P., the ultimate general partner of TCV II, L.P. and TCV VII (A), L.P., and a general partner of TCV Member Fund, L.P. David L. Yuan, one of our directors, is a Class A Director of Technology Crossover Management VII, Ltd. and, together with nine other individual Class A Directors of Technology Crossover Management VII, Ltd., shares voting and dispositive power with respect to the shares beneficially owned by TCV VII, L.P., TCV VII (A), L.P. and TCV Member Fund, L.P. Technology Crossover Management VII, Ltd., Technology Crossover Management VII, L.P., and the Class A Directors of Technology Crossover Management VII, Ltd. disclaim beneficial ownership of any shares held by TCV VII, L.P., TCV VII (A), L.P. and TCV Member Fund, L.P., except to the extent of their respective pecuniary interests. The address for these entities is c/o Technology Crossover Ventures, 528 Ramona Street, Palo Alto, California 94301.

(2) Includes 89,936 shares owned by Greenspring Global Partners I, L.P., 861,848 shares owned by Greenspring Global Partners II, L.P., 21,222 shares owned by Greenspring Global Partners II-A, L.P., 205,155 shares owned by Greenspring Global Partners II-B, L.P., 555,577 shares owned by Greenspring Global Partners III, L.P., 254,813 shares owned by Greenspring Global Partners III-A, L.P., 803,799 shares owned by Greenspring Global Partners III-B, L.P., 109,488 shares owned by Greenspring Global Partners IV-A, L.P., 919,987 shares owned by Greenspring Global Partners IV-B, L.P., 325,882 shares owned by Greenspring Global Partners IV-C, L.P., 197,195 shares owned by Greenspring Global Partners V-A, L.P., 52,805 shares owned by Greenspring Global Partner V-C, L.P., 125,000 shares owned by Greenspring Growth Equity II, L.P., and 467,799 shares owned by Greenspring Crossover Ventures I, L.P. Greenspring Associates, Inc. is the general partner of Greenspring Global Partners I, L.P. Greenspring Associates, Inc. is the general partner of Greenspring General Partners II, L.P. and Greenspring General Partner II, L.P. is the general partner of Greenspring Global Partners II, L.P., Greenspring Global Partners II-A, L.P. and Greenspring Global Partners II-B, L.P. Greenspring GP III, LLC is the general partner of Greenspring General Partner III, L.P. and Greenspring General Partner III, L.P. is the general partner of Greenspring Global Partners III, L.P., Greenspring Global Partners III-A, L.P. and Greenspring Global Partners III-B, L.P. Greenspring GP IV, LLC is the general partner of Greenspring General Partner IV, L.P. and Greenspring General Partner IV, L.P. is the general partner of Greenspring Global Partners IV-A, L.P., Greenspring Global Partners IV-B, L.P. and Greenspring Global Partners IV-C, L.P. Greenspring GP V, LLC is the general partner of Greenspring General Partner V, L.P. and Greenspring General Partner V, L.P. is the general partner of Greenspring Global Partners V-A, L.P. and Greenspring Global Partners V-C, L.P. Greenspring FF-GP II, LLC is the general partner of Greenspring FF-GP II, L.P. and Greenspring FF-GP II, L.P. is the general partner of Greenspring Growth Equity II, L.P. Greenspring Crossover I GP, LLC is the general partner of Greenspring Crossover I GP, L.P. and Greenspring Crossover I GP, L.P. is the general partner of Greenspring Crossover Ventures I, L.P. James Lim and Ashton Newhall are the managing members of Greenspring GP III, LLC, Greenspring GP IV, LLC, Greenspring GP V, LLC, Greenspring FF-GP II, LLC, Greenspring Crossover I GP, LLC and Greenspring Associates, Inc. and share such management powers. Greenspring GP III, LLC, Greenspring GP IV, LLC, Greenspring GP V, LLC, Greenspring FF-GP II, LLC, Greenspring Crossover I GP, LLC and Greenspring Associates, Inc. have the sole voting and investment power over the shares owned by each Greenspring Associates affiliate noted above, although each of them disclaims beneficial ownership of such shares, except to the extent of his pecuniary interest therein. The address of the entities affiliated with Greenspring Associates is 100 Painters Mill Road, Suite 700, Owings Mills, Maryland 21117.

(3) Includes 2,447,053 shares owned by Battery Ventures VIII, L.P., 2,447,053 shares owned by Battery Ventures VIII Side Fund, L.P. and 10,000 shares owned by Battery Management Company, LLC. Battery Partners VIII, LLC is the sole general partner of Battery Ventures VIII, L.P. and Battery Ventures VIII Side Fund, LLC is the sole general partner of Battery Ventures VIII Side Fund, L.P. Michael Brown, one of our directors, Neeraj Agrawal, Thomas J. Crotty, Sunil Dhaliwal, Richard D. Frisbie, Kenneth P. Lawler, Roger H. Lee, R. David Tabors and Scott R. Tobin are the managing members of Battery Partners VIII, LLC and Battery Ventures VIII Side Fund, LLC and may be deemed to have shared voting and dispositive power over the shares held by Battery Ventures VIII, L.P. and Battery Ventures VIII Side Fund, L.P. Each of Messrs. Brown, Agrawal, Crotty, Dhaliwal, Frisbie, Lawler, Lee, Tabors and Tobin disclaims beneficial ownership of such shares except to the extent of his pecuniary interest therein. Mr. Thomas J. Crotty has sole voting and dispositive power over the shares held by Battery Management Company, LLC. Mr. Crotty disclaims beneficial ownership of such shares except to the extent of his pecuniary interest therein. The address of the funds affiliated with Battery Ventures is 930 Winter Street, Suite 2500, Waltham, Massachusetts 02451.

(4) Rory T. O Driscoll, one of our directors, Kate Mitchell, Sharon Wienbar, Robert Theis and Stacey Bishop are the managing members of Scale Venture Management III, LLC, the ultimate general partner of Scale Venture Partners III, L.P., and share voting and investment authority over the shares held by Scale Venture Partners III, L.P. The managing members disclaim beneficial ownership of such shares except to the extent of any pecuniary interest therein. The address for Scale Venture Partners III, L.P. is 950 Tower Lane, Suite 700, Foster City, California 94404.

(5) Consists of the shares listed in footnote (3) above, which are held by the entities affiliated with Battery Ventures. Mr. Brown, one of our directors, is a managing member of the general partners of Battery Ventures VIII, L.P. and Battery Ventures VIII Side Fund, L.P. and therefore may be deemed to share voting and dispositive power over the shares held by these entities.

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(6) Consists of 25,330 shares of restricted stock, of which 20,136 shares are vested and 5,194 shares are unvested as of November 18, 2011.

(7) Consists of 32,980 shares of restricted stock, of which 27,136 shares are vested and 5,844 shares are unvested as of November 18, 2011.

(8) Consists of 32,330 shares of restricted stock, of which 27,136 shares are vested and 5,194 shares are unvested as of November 18, 2011.

(9) Consists of the shares listed in footnote (4) above, which are held by Scale Venture Partners III, L.P. Mr. O Driscoll, one of our directors, is a managing member of the general partners of Scale Venture Partners III, L.P. and shares voting and investment authority over the shares held by Scale Venture Partners III, L.P. but disclaims beneficial ownership of these shares, except to the extent of his pecuniary interest therein.

(10) Consists of the shares listed in footnote (1) above, which are held by the entities affiliated with Technology Crossover Ventures. Mr. Yuan, one of our directors, is a Class A Director of the general partner of the TCV funds and shares voting and dispositive power with respect to the shares beneficially owned by the TCV funds but disclaims beneficial ownership of these shares, except to the extent of his pecuniary interest therein.

(11) Consists of (i) 900,000 shares and (ii) 191,666 shares issuable pursuant to stock options exercisable within 60 days of November 18, 2011.

(12) Consists of 172,499 shares issuable pursuant to stock options exercisable within 60 days of November 18, 2011.

(13) Consists of (i) 304 shares and (ii) 344,818 shares issuable pursuant to stock options exercisable within 60 days of November 18, 2011.

(14) Consists of 143,124 shares issuable pursuant to stock options exercisable within 60 days of November 18, 2011.

(15) Consists of 79,166 shares issuable pursuant to stock options exercisable within 60 days of November 18, 2011.

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DESCRIPTION OF CAPITAL STOCK

General

Upon the closing of this offering, our amended and restated certificate of incorporation will authorize us to issue up to shares of common stock, par value $0.001 per share, and shares of preferred stock, par value $0.001 per share, all of which preferred stock will be undesignated.

As of September 30, 2011, there were:

- 4,482,140 shares of our common stock outstanding held by approximately 147 stockholders;
- 25,949,359 shares of our common stock outstanding after giving effect to the automatic conversion of all of our outstanding preferred stock into common stock immediately prior to the completion of this offering. This excludes 2,000,000 shares of our Series D preferred stock issued in November 2011 that will also automatically convert into common stock immediately prior to the completion of this offering; and
- 5,658,767 shares of our common stock issuable upon exercise of outstanding stock options.

The following descriptions of our capital stock and provisions of our amended and restated certificate of incorporation and amended and restated bylaws are summaries and are qualified by reference to applicable law and to the amended and restated certificate of incorporation and the amended and restated bylaws that will be in effect upon the closing of this offering. Copies of these documents will be filed with the SEC as exhibits to the registration statement of which this prospectus forms a part. The descriptions of the common stock and preferred stock reflect changes to our capital structure that will occur upon the closing of this offering.

Common Stock

Dividend Rights

Subject to the rights, if any, of the holders of any outstanding series of our preferred stock, holders of our common stock will be entitled to receive dividends out of any of our funds legally available when, as and if declared by our board of directors. We have never declared or paid cash dividends on any of our common stock and currently do not anticipate paying any cash dividends after the offering or in the foreseeable future.

Voting Rights

Each holder of our common stock is entitled to one vote per share on all matters on which stockholders are generally entitled to vote. Our amended and restated certificate of incorporation does not provide for cumulative voting in the election of directors.

Liquidation

If we liquidate, dissolve or wind up our affairs, holders of our common stock are entitled to share proportionately in our assets available for distribution to stockholders, subject to the rights, if any, of the holders of any outstanding series of our preferred stock.

Other Rights

All of our outstanding shares of common stock are fully paid and nonassessable, and the shares of common stock we will issue in connection with this offering also will be fully paid and nonassessable. The holders of our common stock have no preemptive rights and no rights to convert their common stock into any other securities, and our common stock is not subject to any redemption or sinking fund provisions.

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Preferred Stock

Under our amended and restated certificate of incorporation and subject to the limitations prescribed by law, our board of directors may issue our preferred stock in one or more series, and may establish from time to time the number of shares to be included in such series and may fix the designation, powers, privileges, preferences and relative participating, optional or other rights, if any, of the shares of each such series and any qualifications, limitations or restrictions thereof. See Anti-Takeover Effects Provisions. Our preferred stock will, if issued, be fully paid and nonassessable. When and if we issue preferred stock, we will establish the applicable preemptive rights, dividend rights, voting rights, conversion privileges, redemption rights, sinking fund rights, rights upon voluntary or involuntary liquidation, dissolution or winding up and any other relative rights, preferences and limitations for the particular preferred stock series.

Options

As of September 30, 2011, options to purchase 5,658,767 shares of our common stock were outstanding.

Restricted Stock

As of September 30, 2011, 66,026 shares of unvested restricted common stock were outstanding.

Registration Rights

After the closing of this offering, holders of shares of our common stock will be entitled to certain rights with respect to the registration of their shares under the Securities Act. These registration rights are contained in the registration rights agreement. In connection with this offering, each stockholder that has registration rights agreed not to sell or otherwise dispose of any securities without the prior written consent of the underwriters for a period of 180 days after the date of this prospectus, subject to a possible extension of up to 34 additional days beyond the end of such 180-day period. For more information regarding such restrictions, see Underwriting. The following description of the terms of these registration rights is intended as a summary only and is qualified in its entirety by reference to the registration rights agreement filed as an exhibit to the registration statement of which this prospectus is part.

Demand Registration Rights

After the closing of this offering, the stockholders that are parties to the registration rights agreement will be entitled to certain demand registration rights. At any time beginning 180 days after the closing of this offering, the holders of at least 50% of these shares then outstanding may, on not more than two occasions, demand that we register the offer and sale of all or a portion of their shares. We may delay the filing of a registration statement for up to 120 days once in any 18-month period if our board of directors determines in good faith that such registration would be seriously detrimental to us.

Piggyback Registration Rights

After the closing of this offering, if we propose to register the offer and sale of any of our securities under the Securities Act, either for our own account or for the account of other security holders, the stockholders that are parties to the registration rights agreement will be entitled to certain piggyback registration rights. These rights will allow the holders to include their shares in such registration, subject to certain marketing and other limitations. As a result, whenever we propose to file a registration statement under the Securities Act, other than with respect to a demand registration or a

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registration statement on Form S-4 or Form S-8, the holders of these shares are entitled to notice of the registration and have the right to include their shares in the registration, subject to limitations that the underwriters may impose on the number of shares included in the registration. If the managing underwriter of an underwritten public offering advises us that the inclusion of all shares requested by the holders of these shares would interfere with the successful marketing of our securities in such registration, then the securities to be included in such registration are to be allocated as follows: first, to the holders of these shares in the order set forth in the registration rights agreement; second, to us; and third, to any others requesting registration of any of our securities.

Form S-3 Registration Rights

After the closing of this offering, the stockholders that are parties to the registration rights agreement may make a written request that we register the offer and sale of their shares on Form S-3 if we are eligible to file a registration statement on Form S-3 so long as the request covers at least that number of shares with an anticipated aggregate offering price of $1 million. These stockholders may make an unlimited number of requests for registration on Form S-3; however, we will not be required to effect more than two such registrations in any twelve-month period.

Registration Expenses

We will pay all expenses incurred in connection with each of the registrations described above, except for underwriting discounts, selling commissions and allowances.

Expiration of Registration Rights

The registration rights described above will survive this offering and will expire upon the earlier of (i) five years following the closing of this offering and (ii) with respect to any particular stockholder, such time following the closing of this offering at which such stockholder can sell all of such stockholder s shares subject to the registration rights agreement in compliance with Rule 144(b)(1)(i) of the Securities Act or at which such stockholder holds 1% or less of our common stock and all of such stockholder s shares (together with shares held by any affiliate of the stockholder with whom such stockholder must aggregate its sales) could be sold in any three-month period without registration in compliance with Rule 144 of the Securities Act.

Anti-Takeover Effects Provisions

Our amended and restated certificate of incorporation, our amended and restated bylaws and the DGCL contain provisions that could make acquisition of our company by means of a tender offer, a proxy contest or otherwise more difficult. These provisions are expected to discourage certain types of coercive takeover practices and takeover bids that our board of directors may consider inadequate and to encourage persons seeking to acquire control of us to first negotiate with our board of directors. We believe that the benefits of increased protection of our ability to negotiate with the proponent of an unfriendly or unsolicited proposal to acquire or restructure us outweigh the disadvantages of discouraging takeover or acquisition proposals because, among other things, negotiation of these proposals could result in an improvement of their terms. The description set forth below is only a summary and is qualified in its entirety by reference to our amended and restated certificate of incorporation and amended and restated bylaws, filed as exhibits to the registration statement of which this prospectus is part.

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Classified Board of Directors

Our amended and restated certificate of incorporation provides for a classified board of directors consisting of three classes of directors. Directors of each class are chosen for three-year terms upon the expiration of their current terms, and each year our stockholders will elect one class of our directors. The directors designated as Class I directors will have terms expiring at the first annual meeting of stockholders following the closing of this offering, the directors designated as Class II directors will have terms expiring at the second annual meeting of stockholders following the closing of this offering, and the directors designated as Class III directors will have terms expiring at the third annual meeting of stockholders following the closing of this offering.

We believe that a classified board structure facilitates continuity and stability of leadership and policy by helping ensure that, at any given time, a majority of our directors will have prior experience as directors of our company and will be familiar with our business and operations. In our view, this will permit more effective long-term planning and help create long-term value for our stockholders. The classified board structure, however, could prevent a party who acquires control of a majority of our outstanding voting stock from obtaining control of our board of directors until the second annual stockholders meeting following the date that party obtains control of a majority of our voting stock. The classified board structure may discourage a third party from initiating a proxy contest, making a tender offer or otherwise attempting to obtain control of us, as the structure makes it more difficult for a stockholder to replace a majority of our directors.

Number of Directors; Filling Vacancies; Removal

Our amended and restated certificate of incorporation and amended and restated bylaws provide that our business and affairs will be managed by our board of directors. Our amended and restated certificate of incorporation and amended and restated bylaws provide that our board of directors will consist of such number of directors as is determined by a resolution adopted by the majority of directors then in office. In addition, our amended and restated certificate of incorporation and amended and restated bylaws provide that any board vacancy, including a vacancy resulting from an increase in the number of directors, may be filled solely by the affirmative vote of a majority of the remaining directors then in office and entitled to vote, even though the number of remaining directors may be less than a quorum of the board of directors. Our amended and restated certificate of incorporation and amended and restated bylaws also provide that any director, or the entire board of directors, may be removed from office at any time, for cause, only by the affirmative vote of the holders of at least 66 2/3% of the total voting power of the outstanding shares of our capital stock entitled to vote generally in the election of directors, voting as a single class. These provisions will prevent stockholders from removing incumbent directors without cause and filling the resulting vacancies with their own nominees.

Notwithstanding the foregoing, our amended and restated certificate of incorporation and amended and restated bylaws provide that whenever the holders of any class or series of our preferred stock have the right to elect additional directors under specified circumstances, the election, removal, term of office, filling of vacancies and other features of such directorships will be governed by the terms of the applicable certificate of designation.

Special Meetings

Our amended and restated certificate of incorporation and amended and restated bylaws provide that, subject to the rights of any class or series of our preferred stock, special meetings of the stockholders may only be called by the board of directors or the Chairman of the board of directors or the Chief Executive Officer with the concurrence of a majority of the entire board of directors. These provisions make it more difficult for stockholders to take action opposed by our board of directors.

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No Stockholder Action by Written Consent

Our amended and restated certificate of incorporation and amended and restated bylaws require that all actions to be taken by stockholders must be taken at a duly called annual or special meeting, and stockholders are not permitted to act by written consent. These provisions make it more difficult for stockholders to take action opposed by our board of directors.

Amendments to Our Amended and Restated Certificate of Incorporation and Amended and Restated Bylaws

Our amended and restated certificate of incorporation provides that, notwithstanding any other provision of our amended and restated certificate of incorporation, the affirmative vote of the holders of at least 66 2/3% of the total voting power of the outstanding shares of our capital stock entitled to vote generally in the election of directors, voting as a single class, will be required to: (1) amend or repeal, or adopt any provision inconsistent with, the provisions in our amended and restated certificate of incorporation relating to the number, classification, term and election of directors, the removal of directors, stockholder action by written consent, stockholders ability to call special meetings and requirements for amendment of our certificate of incorporation and bylaws; and (2) amend or repeal, or adopt any provision inconsistent with, any provision of our amended and restated bylaws. These provisions will make it more difficult for stockholders to make changes to our amended and restated certificate of incorporation and amended and restated bylaws that are opposed by our board of directors.

Advance Notice Provisions for Stockholder Nominations and Stockholder Proposals

Our amended and restated bylaws establish an advance notice procedure for stockholders to make nominations of candidates for election to our board of directors or to bring other business before an annual stockholders meeting (the Notice Procedures). Subject to the terms of any class or series of our preferred stock, our Notice Procedures provide that nominations for election to our board of directors or the proposal of business other than such nominations may be made (1) pursuant to our notice of meeting, (2) by or at the direction of our board of directors or (3) by any stockholder of record (a Record Stockholder) who has complied with the Notice Procedures at the time such stockholder delivers the notice required by the Notice Procedures. Under the Notice Procedures, a Record Stockholder s director nomination will not be timely unless such Record Stockholder delivers written notice to our corporate secretary of such Record Stockholder s nomination or intent to nominate at our principal executive offices not later than close of business on the 90th day nor earlier than the close of business on the 120th day before the one-year anniversary of the prior year s annual meeting; provided that if the annual meeting is convened more than 30 days before or delayed by more than 70 days after the one-year anniversary of the prior year s annual meeting, or if directors are being nominated at a special meeting, notice will be timely if delivered not earlier than the close of business on the 120th day prior to such meeting and not later than the close of business on the 90th day prior to such meeting or the tenth day following the date on which we first make a public announcement of such meeting. These provisions do not apply if a stockholder has notified us of his or her intention to present a stockholder proposal at an annual or special stockholders meeting pursuant to and in compliance with Rule 14a-8 under the Exchange Act, and we have included such proposal in our proxy materials.

Under the Notice Procedures, a stockholder s notice proposing to nominate a person for election as a director or to bring other business before an annual stockholders meeting must contain certain information, as set forth in our amended and restated bylaws. Only persons nominated in accordance with the Notice Procedures will be eligible to serve as directors and only such business that has been brought before the meeting in accordance with these Notice Procedures will be conducted at an annual stockholders meeting.

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By requiring advance notice of nominations by stockholders, the Notice Procedures will afford our board of directors an opportunity to consider the qualifications of the proposed nominees and, to the extent deemed necessary or desirable by our board of directors, to inform stockholders about such qualifications. By requiring advance notice of other proposed business, the Notice Procedures will also provide an orderly procedure for conducting annual meetings of stockholders and, to the extent deemed necessary or desirable by our board of directors, will provide our board of directors with an opportunity to inform stockholders of any business proposed for such meetings and make recommendations on action to be taken on such business, so that stockholders can better decide whether to attend the meeting or to grant a proxy for the disposition of any such business.

Contests for the election of directors or the consideration of stockholder proposals will be precluded if the proper procedures are not followed. Third parties may therefore be discouraged from conducting a solicitation of proxies to elect their own slate of directors or to approve their own proposals.

Our Preferred Stock

Our amended and restated certificate of incorporation authorizes our board of directors to provide for series of our preferred stock and, for each such series, to fix the number of shares and designation, and any voting powers, preferences and relative, participating, optional or other special rights and qualifications and restrictions of such preferences and rights.

We believe that the ability of our board of directors to issue preferred stock will provide us with flexibility in structuring possible future financings and acquisitions, and in meeting other corporate needs that might arise. The authorized shares of our preferred stock, as well as shares of common stock, will be available for issuance without further stockholder action, unless applicable law or applicable stock exchange or automated stock quotation system rules require such action.

Although our board of directors has no present intention of doing so, it could issue a series of our preferred stock that could, depending on the terms of such series, impede the completion of a merger, tender offer or other takeover attempt. Our board of directors will base any determination on issuing such shares on its judgment as to the best interests of the company and our stockholders. Our board of directors, in so acting, could issue preferred stock that has terms that could discourage an acquisition attempt through which an acquiror may be able to change the composition of our board of directors, even if a majority of our stockholders believes such a transaction is in the stockholders best interests and even if stockholders might receive a premium over the then-current market price for their stock.

Section 203 of the Delaware General Corporation Law

Section 203 of the DGCL provides that, subject to certain specified exceptions, a corporation will not engage in any business combination with any interested stockholder for a three-year period following the time that such stockholder becomes an interested stockholder unless (1) before that time, the board of directors of the corporation approved either the business combination or the transaction which resulted in the stockholder becoming an interested stockholder, (2) upon consummation of the transaction which resulted in the stockholder becoming an interested stockholder, the interested stockholder owned at least 85% of the voting stock of the corporation outstanding at the time the transaction commenced (excluding certain shares) or (3) on or after such time, both the board of directors of the corporation and at least 66 2/3% of the outstanding voting stock which is not owned by the interested stockholder, at an annual or special meeting of the stockholders and not by written consent, approves the business combination. Section 203 of the DGCL generally defines an interested stockholder to include (x) any person that owns 15% or more of the outstanding voting

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stock of the corporation, or is an affiliate or associate of the corporation and owned 15% or more of the outstanding voting stock of the corporation at any time within three years immediately prior to the relevant date and (y) the affiliates and associates of any such person.
Section 203 of the DGCL generally defines a business combination to include (1) mergers and sales or other dispositions of 10% or more of the corporation s assets with or to an interested stockholder, (2) certain transactions resulting in the issuance or transfer to the interested stockholder of any stock of the corporation or its subsidiaries, (3) certain transactions which would increase the proportionate share of the stock of the corporation or its subsidiaries owned by the interested stockholder and (4) receipt by the interested stockholder of the benefit (except proportionately as a stockholder) of any loans, advances, guarantees, pledges, or other financial benefits.

Under certain circumstances, Section 203 of the DGCL makes it more difficult for a person who would be an interested stockholder to effect various business combinations with a corporation for a three-year period, although the certificate of incorporation or stockholder-adopted bylaws may exclude a corporation from the restrictions imposed under Section 203. Neither our amended and restated certificate of incorporation nor our amended and restated bylaws exclude our company from the restrictions imposed under Section 203 of the DGCL. We anticipate that Section 203 may encourage companies interested in acquiring us to negotiate in advance with our board of directors since the stockholder approval requirement would not be applicable if our board of directors approves, prior to the time the stockholder becomes an interested stockholder, either the business combination or the transaction which results in the stockholder becoming an interested stockholder.

Listing

We intend to apply for listing of our common stock on the under the symbol .

Transfer Agent and Registrar

The transfer agent and registrar for our common stock is .

Liability and Indemnification of Directors and Officers

Elimination of Liability of Directors

Our amended and restated certificate of incorporation provides that, to the fullest extent permitted by the DGCL, no director will be personally liable to us or to our stockholders for monetary damages for breach of fiduciary duty as a director. Notwithstanding this provision, pursuant to Section 102(b)(7) of the DGCL a director can be held liable (1) for any breach of the director s duty of loyalty to the company or our stockholders, (2) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (3) under Section 174 of the DGCL (which concerns unlawful payments of dividends, stock purchases or redemptions) or (4) for any transaction from which the director derives an improper personal benefit.

While our amended and restated certificate of incorporation provides directors with protection from awards for monetary damages for breaches of their duty of care, it does not eliminate this duty. Accordingly, our amended and restated certificate of incorporation will have no effect on the availability of equitable remedies such as an injunction or rescission based on a director s breach of his or her duty of care. The provisions of our amended and restated certificate of incorporation described above apply to an officer of our company only if he or she is a director of our company and is acting in his or her capacity as director, and do not apply to officers of our company who are not directors.

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Indemnification of Directors, Officers and Employees

Our amended and restated bylaws require us to indemnify any person who was or is a party or is threatened to be made a party to, or was otherwise involved in, a legal proceeding by reason of the fact that he or she is or was a director or an officer of our company or, while a director, officer or employee of our company, is or was serving at our request as a director, officer, employee, agent or trustee of another corporation or of a partnership, joint venture, trust or other enterprise, including service with respect to an employee benefit plan, to the fullest extent authorized by the DGCL, as it exists or may be amended, against all expense, liability and loss (including attorneys fees, judgments, fines, ERISA excise taxes or penalties and amounts paid in settlement by or on behalf of such person) actually and reasonably incurred in connection with such service. We are authorized under our amended and restated bylaws to carry directors and officers insurance protecting us, any director, officer, employee or agent of ours or another corporation, partnership, joint venture, trust or other enterprise, against any expense, liability or loss, whether or not we would have the power to indemnify the person under the DGCL. We may, to the extent authorized from time to time, indemnify any of our agents to the fullest extent permitted with respect to directors, officers and employees in our amended and restated bylaws.

The limitation of liability and indemnification provisions in our amended and restated certificate of incorporation and amended and restated bylaws may discourage stockholders from bringing a lawsuit against our directors for breach of fiduciary duty. These provisions also may reduce the likelihood of derivative litigation against our directors and officers, even though such an action, if successful, might otherwise benefit us and our stockholders. In addition, your investment in our common stock may be adversely affected to the extent we pay the costs of settlement and damage awards under these indemnification provisions.

By its terms, the indemnification provided for in our amended and restated bylaws is not exclusive of any other rights that the indemnified party may be or become entitled to under any law, agreement, vote of stockholders or directors, provisions of our amended and restated certificate of incorporation or amended and restated bylaws or otherwise. Any amendment, alteration or repeal of our amended and restated bylaws indemnification provisions is, by the terms of our amended and restated bylaws, prospective only and will not adversely affect the rights of any indemnitee in effect at the time of any act or omission occurring prior to such amendment, alteration or repeal.

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SHARES ELIGIBLE FOR FUTURE SALE

Immediately prior to this offering, there was no public market for our common stock. Future sales of significant amounts of our common stock, including shares issued upon exercise of outstanding options or in the public market after this offering, or the anticipation of those sales, could adversely affect public market prices prevailing from time to time and could impair our ability to raise capital through sales of our equity securities. We intend to apply for listing of our common stock on the under the symbol . We cannot provide any assurances that an active public market for our common stock will develop or be substantial in the future.

Upon completion of this offering, we will have outstanding shares of common stock, assuming no exercise of the underwriters over-allotment option and no exercise of outstanding options. Of these shares, the shares of common stock to be sold in this offering will be freely tradable without restriction or further registration under the Securities Act, except for any shares purchased by our affiliates, as that term is defined in Rule 144 under the Securities Act. All remaining shares of common stock held by existing stockholders will be restricted securities as that term is defined in Rule 144 under the Securities Act. Substantially all of these restricted securities will be subject to the lock-up agreements described below. After the expiration of the lock-up agreements, these restricted securities may be sold in the public market only if registered or if they qualify for an exemption from registration under Rule 144 or 701 under the Securities Act.

Rule 144

In general, under Rule 144 as currently in effect, once we have been a reporting company subject to the reporting requirements of Section 13 or Section 15(d) of the Exchange Act for 90 days, an affiliate who has beneficially owned restricted shares of our common stock for at least six months would be entitled to sell within any three-month period a number of shares that does not exceed the greater of either of the following:

- 1% of the number of shares of common stock then outstanding, which will equal approximately shares immediately after this offering; or

- the average weekly reported volume of trading of our common stock during the four calendar weeks preceding the filing of a notice on Form 144 with respect to the sale.

However, the holding period is one year until we have been a reporting company for at least 90 days. In addition, any sales by affiliates under Rule 144 are also limited by manner-of-sale provisions and notice requirements and the availability of current public information about us.

The volume limitation, manner of sale and notice provisions described above will not apply to sales by non-affiliates. For purposes of Rule 144, a non-affiliate is any person or entity who is not our affiliate at the time of sale and has not been our affiliate during the preceding three months. Once we have been a reporting company for 90 days, a non-affiliate who has beneficially owned restricted shares of our common stock for six months may rely on Rule 144 provided that certain public information regarding us is available. The holding period is one year until we have been a reporting company for at least 90 days. However, a non-affiliate who has beneficially owned the restricted shares proposed to be sold for at least one year will not be subject to any restrictions under Rule 144 regardless of how long we have been a reporting company.

We are unable to estimate the number of shares that will be sold under Rule 144 since this will depend on the market price for our common stock, the personal circumstances of the stockholder and other factors.

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Rule 701

In general, under Rule 701 of the Securities Act, any of our employees, consultants or advisors who purchased shares from us in connection with a qualified compensatory stock plan or other written agreement is eligible to resell those shares 90 days after the effective date of this offering in reliance on Rule 144, but without compliance with the various restrictions, including the holding period, contained in Rule 144. Subject to the 180-day lock-up period described below, approximately shares of our common stock will be eligible for sale in accordance with Rule 701.

Lock-up Agreements

We, our officers, directors and substantially all of our stockholders, who, as of the date hereof, hold an aggregate of approximately shares of our common stock on an as-converted basis, have agreed, subject to limited exceptions, not to offer, pledge, sell, contract to sell, sell any option or contract to purchase, purchase any option or contract to sell, grant any option, right or warrant to purchase, or otherwise transfer or dispose of, directly or indirectly, any shares of common stock beneficially owned (as such term is used in Rule 13d-3 of the Exchange Act) or any other securities so owned convertible into or exercisable or exchangeable for common stock for a period of 180 days after the date of this prospectus, without the prior written consent of J.P. Morgan Securities LLC, Deutsche Bank Securities Inc. and Stifel, Nicolaus & Company, Incorporated, on behalf of the underwriters. These lock-up restrictions also prohibit these persons and entities from entering into any swap or other arrangement that transfers to another, in whole or in part, any of the economic consequences of ownership of any shares of common stock or any securities convertible into or exercisable or exchangeable for shares of common stock for the same 180 day period without the prior written consent of J.P. Morgan Securities LLC, Deutsche Bank Securities Inc. and Stifel, Nicolaus & Company, Incorporated, on behalf of the underwriters. Notwithstanding the foregoing, if (1) during the last 17 days of the 180-day restricted period, we issue an earnings release or material news or a material event relating to our company occurs; or (2) prior to the expiration of the 180-day restricted period, we announce that we will release earnings results during the 16-day period beginning on the last day of the 180-day period, the restrictions described above shall continue to apply until the expiration of the 18-day period beginning on the issuance of the earnings release or the occurrence of the material news or material event.

Stock Plans

As of September 30, 2011, there were outstanding options to purchase 5,658,767 shares of common stock, of which options to purchase 2,762,093 shares of common stock were exercisable as of September 30, 2011. There were also 66,026 shares of unvested restricted stock outstanding as of September 30, 2011. We intend to file registration statements on Form S-8 under the Securities Act covering all of the shares of common stock subject to outstanding options and options and other awards issuable pursuant to our equity plans. The filing will take place after the date of this prospectus and such filing will permit the resale of any such shares owned by non-affiliates in the public market without restriction under the Securities Act (but subject to the provisions of the lock-up agreement described above during the 180-day lock-up period).

Registration Rights

Upon the completion of this offering, holders of at least shares of our common stock will be eligible to exercise certain registration rights. These shares will become freely tradable upon the effectiveness of any registration statement covering such shares. See Description of Capital Stock Registration Rights.

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MATERIAL U.S. FEDERAL INCOME TAX CONSEQUENCES

The following discussion describes certain material U.S. federal income tax consequences associated with the purchase, ownership and disposition of shares of our common stock. This discussion deals only with shares of our common stock held as capital assets within the meaning of Section 1221 of the Internal Revenue Code of 1986, as amended (the Code) (generally, property held for investment). This discussion does not address special situations, including, without limitation, those of:

- brokers or dealers in securities;
- banks or other financial institutions;
- regulated investment companies;
- real estate investment trusts;
- insurance companies;
- tax-exempt entities;
- persons holding common stock as a part of a hedging, integrated, conversion or constructive sale transaction or a straddle;
- traders in securities that elect to use a mark-to-market method of accounting for their securities holdings;
- persons liable for alternative minimum tax;
- U.S. Holders (as defined below) whose functional currency is not the U.S. dollar;
- entities or arrangements treated as partnerships for U.S. federal income tax purposes or investors in such entities;
- persons who acquired our common stock through the exercise of employee stock options or otherwise as compensation for services;
- U.S. expatriates;
- controlled foreign corporations;

- passive foreign investment companies; and

- persons deemed to sell our common stock under the constructive sale provisions of the Code.

This discussion does not address all aspects of U.S. federal income taxation and does not deal with all tax consequences that may be relevant to holders in light of their personal circumstances. Furthermore, this discussion is based upon the provisions of the Code, the existing and proposed U.S. Treasury regulations promulgated thereunder and administrative and judicial interpretations thereof, all as of the date hereof, and such authorities may be repealed, revoked, modified or subject to differing interpretations, possibly with retroactive effect, so as to result in U.S. federal income tax consequences different from those discussed below. This discussion does not address any state, local or foreign tax consequences, or any U.S. federal tax consequences other than U.S. federal income tax consequences.

If a partnership or other entity or arrangement treated as a partnership for U.S. federal income tax purposes holds our common stock, the tax treatment of a partner will generally depend upon the status of the partner and the activities of the partnership. Partners in a partnership purchasing our common stock, are urged to consult their own tax advisors.

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THIS SUMMARY IS FOR GENERAL INFORMATION ONLY AND IS NOT INTENDED TO CONSTITUTE A COMPLETE DESCRIPTION OF ALL TAX CONSEQUENCES RELATING TO THE PURCHASE, OWNERSHIP AND DISPOSITION OF OUR COMMON STOCK. PROSPECTIVE HOLDERS OF OUR COMMON STOCK ARE URGED TO CONSULT WITH THEIR OWN TAX ADVISORS REGARDING THE TAX CONSEQUENCES TO THEM (INCLUDING THE APPLICATION AND EFFECT OF ANY STATE, LOCAL, AND FOREIGN INCOME AND OTHER TAX LAWS) OF THE PURCHASE, OWNERSHIP AND DISPOSITION OF OUR COMMON STOCK.

Consequences to U.S. Holders

The following is a summary of the U.S. federal income tax consequences that will apply to a U.S. Holder of shares of our common stock. A U.S. Holder of shares of our common stock means a beneficial owner of shares of common stock that is for U.S. federal income tax purposes:

- an individual citizen or resident of the United States;
- a corporation (or other entity taxable as a corporation) created or organized in the United States or under the laws of the United States or any state thereof or the District of Columbia;
- an estate the income of which is subject to U.S. federal income taxation regardless of its source; or
- a trust if it is subject to the primary supervision of a court within the United States and one or more U.S. persons have the authority to control all substantial decisions of the trust or has a valid election in effect under applicable U.S. Treasury regulations to be treated as a U.S. person.

Dividends

If a U.S. Holder receives a distribution in respect of shares of our common stock, it generally will be treated as a dividend to the extent that it is paid from current or accumulated earnings and profits. A distribution that exceeds current and accumulated earnings and profits will be treated as a nontaxable return of capital reducing a U.S. Holder s tax basis in the common stock and any remaining excess will be treated as capital gain.

Under current legislation, dividend income may be taxed to an individual U.S. Holder at rates applicable to long-term capital gains, provided that a minimum holding period and other limitations and requirements are satisfied. The legislation providing for this long-term capital gains rate treatment is scheduled to expire on December 31, 2012, at which time, unless such legislation is extended, dividends received by an individual U.S. Holder will generally be taxed at ordinary income rates. Any dividends that we pay to a U.S. Holder that is a U.S. corporation will qualify for a deduction allowed to U.S. corporations in respect of dividends received from other U.S. corporations equal to a portion of any dividends received, subject to generally applicable limitations on that deduction. In general, a dividend distribution to a corporate U.S. Holder may qualify for the 70% dividends-received deduction if the U.S. Holder owns less than 20% of the voting power and value of our stock. U.S. Holders should consult their own tax advisors regarding the holding period and other requirements that must be satisfied in order to qualify for the reduced tax rate on dividends and the dividends-received deduction.

Sale, Exchange, or Other Disposition of Common Stock

A U.S. Holder will generally recognize capital gain or loss on the sale, exchange or other disposition of our common stock. The amount of gain or loss will equal the difference between the amount realized on the sale and the tax basis of such U.S. Holder in the disposed of common stock. The amount realized will include the amount of any cash and the fair market value of any other property received in exchange for the stock. The gain or loss recognized on a sale will be long-term capital gain or loss if the common stock had been held for more than one year. Long-term capital gains of non-corporate U.S. Holders are generally taxed at lower rates than those applicable to ordinary income. The deductibility of capital losses is subject to certain limitations.

Medicare Contribution Tax

For taxable years beginning after December 31, 2012, U.S. Holders who are individuals, estates or certain trusts are required to pay a 3.8% tax on the lesser of (1) the U.S. person s net investment income for the relevant taxable year and (2) the excess of the U.S. person s modified gross income for the taxable year over a certain threshold (which in the case of individuals will be between $125,000 and $250,000 depending on the individual s circumstances). Net investment income generally includes, among other things, dividends and capital gains from the sale or other disposition of stock, unless such dividend income or gains are derived in the ordinary course of the conduct of a trade or business (other than a trade or business that consists of certain passive or trading activities). A U.S. Holder that is an individual, estate or trust should consult its tax advisor regarding the applicability of the Medicare tax to its income and gains in respect of its investment in our common stock.

Information Reporting and Backup Withholding

Under certain circumstances, U.S. Treasury regulations require information reporting and backup withholding on certain payments on common stock or on the sale thereof. When required, we will report to the Internal Revenue Service and to each U.S. Holder the amounts paid on or with respect to our common stock and the U.S. federal withholding tax, if any, withheld from such payments. A U.S. Holder will be subject to backup withholding on the dividends paid on the common stock and proceeds from the sale of the common stock at the applicable rate (which is currently 28%) if the U.S. Holder (a) fails to provide us or our paying agent with a correct taxpayer identification number or certification of exempt status (such as a certification of corporate status), (b) has been notified by the Internal Revenue Service that it is subject to backup withholding as a result of the failure to properly report payments of interest or dividends, or (c) in certain circumstances, has failed to certify under penalty of perjury that it is not subject to backup withholding. A U.S. Holder may be eligible for an exemption from backup withholding by providing a properly completed Internal Revenue Service Form W-9 to us or our paying agent.

Backup withholding does not represent an additional U.S. federal income tax. Any amounts withheld from a payment to a U.S. Holder under the backup withholding rules will be allowed as a credit against such holder s U.S. federal income tax liability and may entitle the holder to a refund, provided that the required information or returns are timely furnished by the holder to the Internal Revenue Service.

Consequences to Non-U.S. Holders

The following is a summary of the U.S. federal income tax consequences that will apply to a Non-U.S. Holder of shares of our common stock. A Non-U.S. Holder is a beneficial owner of common stock (other than an entity or arrangement treated as a partnership for U.S. federal income tax purposes) that is not a U.S. Holder.

Dividends

Dividends paid to a Non-U.S. Holder, if any, generally will be subject to withholding of U.S. federal income tax at a 30% rate or such lower rate as may be specified by an applicable income tax treaty. A Non-U.S. Holder wishing to claim the benefits of an applicable income tax treaty for dividends will be required to complete Internal Revenue Service Form W-8BEN (or other applicable forms) and certify under penalties of perjury that such Non-U.S. Holder is not a U.S. person and is entitled to the benefits of the applicable income tax treaty. Special certifications and other requirements may apply to certain Non-U.S. Holders that are entities rather than individuals.

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Dividends paid to a Non-U.S. Holder that are effectively connected with such Non-U.S. Holder s conduct of a trade or business within the United States or, if certain treaties apply, are attributable to a U.S. permanent establishment, are not subject to the withholding tax but instead are subject to U.S. federal income tax rates in the same manner as a U.S. Holder. Special certification and disclosure requirements, including the completion of Internal Revenue Service Form W-8ECI (or any successor form), must be satisfied for effectively connected dividends to be exempt from withholding. In addition, a non-U.S. Holder that is a foreign corporation may be subject to an additional branch profits tax at a 30% rate or such lower rate as may be specified by an applicable income tax treaty on any effectively connected dividends received by such non-U.S. Holder.

If a Non-U.S. Holder is eligible for a reduced rate of U.S. withholding tax pursuant to an income tax treaty, such Non-U.S. Holder may obtain a refund of any excess amounts withheld by filing an appropriate claim for refund with the Internal Revenue Service.

Sale, Exchange or Other Disposition of Common Stock

A Non-U.S. Holder generally will not be subject to U.S. federal income tax with respect to gain recognized on a sale, exchange or other disposition of shares of our common stock unless:

- the gain is effectively connected with such Non-U.S. Holder s conduct of a trade or business in the United States, or, if certain income tax treaties apply, is attributable to a U.S. permanent establishment;
- an individual Non-U.S. Holder holds shares of our common stock as a capital asset, is present in the United States for 183 days or more in the taxable year of the sale, exchange or other disposition, and certain other conditions are met; or
- our common stock constitutes a U.S. real property interest by reason of our status as a U.S. real property holding corporation for U.S. federal income tax purposes at any time within the shorter of the five-year period preceding the disposition or such Non-U.S. Holder s holding period of our common stock.

We believe that we are not currently and will not become a U.S. real property holding corporation. However, because the determination of whether we are a U.S. real property holding corporation depends on the fair market value of our U.S. real property assets relative to the fair market value of our other business assets, there can be no assurance that we will not become a U.S. real property holding corporation in the future. Even if we become a U.S. real property holding corporation, however, as long as our common stock is regularly traded on an established securities market, such common stock will be treated as an interest in a U.S. real property holding corporation only if a Non-U.S. Holder actually or constructively holds more than 5% of our regularly traded common stock at any time during the applicable period as specified in the Code.

An individual Non-U.S. Holder described in the first bullet above will be subject to tax on the net gain derived from the sale under regular graduated U.S. federal income tax rates in the same manner as if such Non-U.S. Holder were a U.S. Holder.

A foreign corporation Non-U.S. Holder described in the first bullet above will be subject to tax on the net gain under regular graduated U.S. federal income tax rates in the same manner as a U.S. Holder and, in addition, may be subject to the branch profits tax at a rate of 30% or at such lower rate as may be specified by an applicable income tax treaty.

A Non-U.S. Holder described in the second bullet above will be subject to a flat 30% tax on the gain derived from the sale, exchange or other disposition, which may be offset by U.S. source capital losses (even though such Non-U.S. Holder is not considered a resident of the United States). A Non-U.S. Holder that is an individual and eligible for the benefits of a tax treaty between the United

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States and such Non-U.S. Holder s country of residence will be subject to U.S. federal income tax on the disposition of shares of our common stock in the manner specified by the treaty and generally will only be subject to such tax if the gain on such disposition is attributable to a permanent establishment maintained by the Non-U.S. Holder in the United States and the Non-U.S. Holder claims the benefit of the treaty by properly submitting an IRS Form W-8BEN (or suitable successor or substitute form).

Information Reporting and Backup Withholding

In general, we must report annually to the Internal Revenue Service and to each Non-U.S. Holder the amount of dividends paid to such holder and the U.S. federal withholding tax withheld with respect to those dividends, regardless of whether withholding is reduced or eliminated by an applicable income tax treaty. Copies of this information reporting may also be made available under the provisions of a specific tax treaty or agreement with the tax authorities in the country in which the Non-U.S. Holder resides or is established.

U.S. backup withholding tax (currently at a rate of 28%) is imposed on certain dividend payments to Non-U.S. Holders that fail to furnish the information required under the U.S. information reporting requirements. Dividends on common stock paid to a Non-U.S. Holder will generally be exempt from backup withholding, provided the Non-U.S. Holder meets applicable certification requirements, including providing a correct and properly executed Internal Revenue Service Form W-8BEN, or otherwise establishes an exemption.

Information reporting and, depending on the circumstances, backup withholding will apply to the proceeds of a sale of our common stock within the United States or conducted through certain U.S.-related financial intermediaries, unless the beneficial owner certifies under penalty of perjury that it is a Non-U.S. Holder (and the payor does not have actual knowledge or reason to know that the beneficial owner is a U.S. person as defined under the Code), or such owner otherwise establishes an exemption.

Backup withholding does not represent an additional U.S. federal income tax. Any amounts withheld from a payment to a Non-U.S. Holder under the backup withholding rules will be allowed as a credit against such holder s U.S. federal income tax liability and may entitle the holder to a refund, provided that the required information or returns are timely furnished by the holder to the Internal Revenue Service.

Foreign Account Legislation

Recent legislation, which will be phased in beginning on January 1, 2014, generally will impose a withholding tax of 30% on any dividends on our common stock paid to a foreign financial institution, unless such institution enters into an agreement with the U.S. government to, among other things, collect and provide to the U.S. tax authorities substantial information regarding U.S. account holders of such institution (which includes certain equity and debt holders of such institution, as well as certain account holders that are foreign entities with U.S. owners). The legislation will also generally impose a withholding tax of 30% on any dividends on our common stock paid to a non-financial foreign entity unless such entity provides the withholding agent with either certification that such entity does not have any substantial U.S. owners or identification of the direct and indirect substantial U.S. owners of the entity. Finally, withholding of 30% also generally will apply to the gross proceeds of a disposition of our common stock paid to a foreign financial institution or to a non-financial foreign entity unless the reporting and certification requirements described above have been met. Under certain circumstances, a Non-U.S. Holder of our common stock may be eligible for refunds or credits of such taxes. Investors are encouraged to consult with their tax advisors regarding the possible implications of this legislation on their investment in our common stock.

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UNDERWRITING

We are offering the shares of common stock described in this prospectus through a number of underwriters. J.P. Morgan Securities LLC, Deutsche Bank Securities Inc. and Stifel, Nicolaus & Company, Incorporated are acting as representatives of the underwriters. We have entered into an underwriting agreement with the underwriters. Subject to the terms and conditions of the underwriting agreement, we have agreed to sell to the underwriters, and each underwriter has severally agreed to purchase, at the public offering price less the underwriting discounts and commissions set forth on the cover page of this prospectus, the number of shares of common stock listed next to its name in the following table:

Name	Number of Shares
J.P. Morgan Securities LLC	
Deutsche Bank Securities Inc.	
Stifel, Nicolaus & Company, Incorporated	
RBC Capital Markets, LLC	
Pacific Crest Securities, Inc.	
Canaccord Genuity Inc.	
Raymond James & Associates, Inc.	
Total	

The underwriters are committed to purchase all the shares of common stock offered by us if they purchase any shares. The underwriting agreement also provides that if an underwriter defaults, the purchase commitments of non-defaulting underwriters may be increased or the offering may be terminated.

The underwriters propose to offer the shares of common stock directly to the public at the initial public offering price set forth on the cover page of this prospectus and to certain dealers at that price less a concession not in excess of $ per share. After the initial public offering of the shares, the offering price and other selling terms may be changed by the underwriters. Sales of shares made outside the United States may be made by affiliates of the underwriters. The representatives have advised us that the underwriters do not intend to confirm discretionary sales in excess of % of the shares of common stock offered in this offering.

The underwriters have an option to purchase up to additional shares of common stock from us to cover sales of shares by the underwriters that exceed the number of shares specified in the table above. The underwriters have 30 days from the date of this prospectus to exercise this over-allotment option. If any shares are purchased with this over-allotment option, the underwriters will purchase shares in approximately the same proportion as shown in the table above. If any additional shares of common stock are purchased, the underwriters will offer the additional shares on the same terms as those on which the shares are being offered.

The underwriting discounts and commissions are equal to the public offering price per share of common stock less the amount paid by the underwriters to us per share of common stock. The underwriting discounts and commissions are $ per share. The following table shows the per share and total underwriting discounts and commissions payable by us to the underwriters in connection with this offering assuming both no exercise and full exercise of the underwriters option to purchase additional shares.

		Total	
	Per share	No exercise	Full exercise
Public offering price			
Underwriting discounts and commissions			
Proceeds, before expenses, to us			

We estimate that the total expenses of this offering, including registration, filing and listing fees, printing fees and legal and accounting expenses, but excluding the underwriting discounts and commissions, will be approximately $.

A prospectus in electronic format may be made available on the websites maintained by one or more underwriters, or selling group members, if any, participating in the offering. The underwriters may agree to allocate a number of shares to underwriters and selling group members for sale to their online brokerage account holders. Internet distributions will be allocated by the representatives to underwriters and selling group members that may make Internet distributions on the same basis as other allocations.

We, all of our directors and officers and the holders of shares of our common stock, on an as-converted basis, have agreed that, subject to certain exceptions, without the prior written consent of J.P. Morgan Securities LLC, Deutsche Bank Securities Inc. and Stifel, Nicolaus & Company, Incorporated on behalf of the underwriters, we and they will not, for a period of 180 days after the date of this prospectus:

- offer, pledge, sell, contract to sell, sell any option or contract to purchase, purchase any option or contract to sell, grant any option, right or warrant to purchase, or otherwise transfer or dispose of, directly or indirectly, any shares of common stock or any securities convertible into or exercisable or exchangeable for common stock, or publicly disclose the intention to make any offer, sale, pledge or disposition;

- enter into any swap or other agreement that transfers, in whole or in part, any of the economic consequences of ownership of common stock or any security convertible into or exercisable or exchangeable for common stock; or

- make any demand for or exercise any right with respect to the registration of any shares of common stock or any security convertible into or exercisable or exchangeable for common stock;

with respect to the first and second bullets above, whether any such transaction is to be settled by delivery of common stock or such other securities, in cash or otherwise.

The 180-day restricted period described in the preceding paragraph will be extended if:

- during the last 17 days of the 180-day restricted period, we issue an earnings release or material news or a material event relating to us occurs; or

- prior to the expiration of the 180-day restricted period, we announce that we will release earnings results during the 16-day period beginning on the last day of the 180-day restricted period;

in which case the restrictions described in the preceding paragraph will continue to apply until the expiration of the 18-day period beginning on the issuance of the earnings release or the occurrence of the material news or material event.

We have agreed to indemnify the underwriters against certain liabilities, including liabilities under the Securities Act.

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We intend to apply for listing of our common stock on the under the symbol .

In connection with this offering, the underwriters may engage in stabilizing transactions, which involves making bids for, or purchasing and selling shares of, common stock in the open market for the purpose of preventing or retarding a decline in the market price of the common stock while this offering is in progress. These stabilizing transactions may include making short sales of the common stock, which involves the sale by the underwriters of a greater number of shares of common stock than they are required to purchase in this offering, and purchasing shares of common stock on the open market to cover positions created by short sales. Short sales may be covered shorts, which are short positions in an amount not greater than the underwriters over-allotment option referred to above, or may be naked shorts, which are short positions in excess of that amount. The underwriters may close out any covered short position either by exercising their over-allotment option, in whole or in part, or by purchasing shares in the open market. In making this determination, the underwriters will consider, among other things, the price of shares available for purchase in the open market compared to the price at which the underwriters may purchase shares through the over-allotment option. A naked short position is more likely to be created if the underwriters are concerned that there may be downward pressure on the price of the common stock in the open market that could adversely affect investors who purchase in this offering. To the extent that the underwriters create a naked short position, they will purchase shares in the open market to cover the position.

The underwriters have advised us that, pursuant to Regulation M of the Securities Act, they may also engage in other activities that stabilize, maintain or otherwise affect the price of the common stock, including the imposition of penalty bids. This means that if the representatives of the underwriters purchase common stock in the open market in stabilizing transactions or to cover short sales, the representatives can require the underwriters that sold those shares as part of this offering to repay the underwriting discount received by them.

These activities may have the effect of raising or maintaining the market price of the common stock or preventing or retarding a decline in the market price of the common stock, and, as a result, the price of the common stock may be higher than the price that otherwise might exist in the open market. If the underwriters commence these activities, they may discontinue them at any time. The underwriters may carry out these transactions on the , in the over-the-counter market or otherwise.

Prior to this offering, there has been no public market for our common stock. The initial public offering price has been determined by negotiations among us and the representatives of the underwriters. In determining the initial public offering price, we and the representatives of the underwriters considered a number of factors including:

- the information set forth in this prospectus and otherwise available to the representatives;
- our prospects and the history and prospects for the industry in which we compete;
- an assessment of our management;
- our prospects for future earnings;
- the general condition of the securities markets at the time of this offering;
- the recent market prices of, and demand for, publicly traded common stock of generally comparable companies; and
- other factors deemed relevant by the underwriters and us.

Neither we nor the underwriters can assure investors that an active trading market will develop for our common stock, or that the shares will trade in the public market at or above the initial public offering price.

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Other than in the United States, no action has been taken by us or the underwriters that would permit a public offering of the shares of common stock offered by this prospectus in any jurisdiction where action for that purpose is required. The shares of common stock offered by this prospectus may not be offered or sold, directly or indirectly, nor may this prospectus or any other offering material or advertisements in connection with the offer and sale of any such shares of common stock be distributed or published in any jurisdiction, except under circumstances that will result in compliance with the applicable rules and regulations of that jurisdiction. Persons into whose possession this prospectus comes are advised to inform themselves about and to observe any restrictions relating to the offering and the distribution of this prospectus. This prospectus does not constitute an offer to sell or a solicitation of an offer to buy any shares of common stock offered by this prospectus in any jurisdiction in which such an offer or a solicitation is unlawful.

United Kingdom

This document is only being distributed to and is only directed at (i) persons who are outside the United Kingdom, or (ii) investment professionals falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, or the Order, or (iii) high net worth entities, and other persons to whom it may lawfully be communicated, falling within Article 49(2)(a) to (d) of the Order, all such persons together being referred to as relevant persons. The shares of common stock are only available to, and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such shares of common stock will be engaged in only with, relevant persons. Any person who is not a relevant person should not act or rely on this document or any of its contents.

European Economic Area

In relation to each Member State of the European Economic Area that has implemented the Prospectus Directive, each, a Relevant Member State, from and including the date on which the European Union Prospectus Directive, or the EU Prospectus Directive, is implemented in that Relevant Member State, or the Relevant Implementation Date, the Registrant may not make an offer of shares of common stock described in this prospectus to the public in that Relevant Member State prior to the publication of a prospectus in relation to the shares that has been approved by the competent authority in that Relevant Member State or, where appropriate, approved in another Relevant Member State and notified to the competent authority in that Relevant Member State, all in accordance with the EU Prospectus Directive, except that the Registrant may, with effect from and including the Relevant Implementation Date, make an offer of shares to the public in that Relevant Member State at any time:

- to legal entities that are authorized or regulated to operate in the financial markets or, if not so authorized or regulated, whose corporate purpose is solely to invest in securities;

- to any legal entity that has two or more of (1) an average of at least 250 employees during the last financial year; (2) a total balance sheet of more than 43,000,000; and (3) an annual net turnover of more than 50,000,000, as shown in its last annual or consolidated accounts;

- to fewer than 100 natural or legal persons (other than qualified investors as defined in the EU Prospectus Directive) subject to obtaining the prior consent of the book-running managers for any such offer; or

- in any other circumstances that do not require the publication by the Registrant of a prospectus pursuant to Article 3 of the Prospectus Directive.

For the purposes of this provision, the expression an offer of securities to the public in relation to any securities in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and the securities to be offered so as to enable an investor to decide to purchase or subscribe for the securities, as the same may be varied in that

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Member State by any measure implementing the EU Prospectus Directive in that Member State and the expression EU Prospectus Directive means Directive 2003/71/EC and includes any relevant implementing measure in each Relevant Member State.

Hong Kong

The shares may not be offered or sold by means of any document other than (i) in circumstances that do not constitute an offer to the public within the meaning of the Companies Ordinance (Cap.32, Laws of Hong Kong), or (ii) to professional investors within the meaning of the Securities and Futures Ordinance (Cap.571, Laws of Hong Kong) and any rules made thereunder, or (iii) in other circumstances that do not result in the document being a prospectus within the meaning of the Companies Ordinance (Cap.32, Laws of Hong Kong), and no advertisement, invitation or document relating to the shares may be issued or may be in the possession of any person for the purpose of issue (in each case whether in Hong Kong or elsewhere), that is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted under the laws of Hong Kong) other than with respect to shares that are or are intended to be disposed of only to persons outside Hong Kong or only to professional investors within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder.

Singapore

This prospectus has not been registered as a prospectus with the Monetary Authority of Singapore. Accordingly, this prospectus and any other document or material in connection with the offer or sale, or invitation for subscription or purchase, of the shares may not be circulated or distributed, nor may the shares be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore other than (i) to an institutional investor under Section 274 of the Securities and Futures Act, Chapter 289 of Singapore, or the SFA, (ii) to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions, specified in Section 275 of the SFA or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA.

Where the shares are subscribed or purchased under Section 275 by a relevant person that is: (a) a corporation (which is not an accredited investor) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or (b) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and where each beneficiary of which is an accredited investor, shares, debentures and units of shares and debentures of that corporation or the beneficiaries rights and interest in that corporation or trust shall not be transferable for six months after that corporation or that trust has acquired the shares under Section 275 except: (1) to an institutional investor under Section 274 of the SFA or to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions, specified in Section 275 of the SFA; (2) where no consideration is given for the transfer; or (3) by operation of law.

Switzerland

This document, as well as any other material relating to the shares of our common stock, which are the subject of the offering contemplated by this prospectus, does not constitute an issue prospectus pursuant to Article 652a of the Swiss Code of Obligations. The shares will not be listed on the SIX Swiss Exchange and, therefore, the documents relating to the shares, including, but not limited to, this document, do not claim to comply with the disclosure standards of the listing rules of the SIX Swiss Exchange and corresponding prospectus schemes annexed to the listing rules of the SIX Swiss Exchange.

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The shares are being offered in Switzerland by way of a private placement, i.e., to a small number of selected investors only, without any public offer and only to investors who do not purchase the shares with the intention to distribute them to the public. The investors will be individually approached by us from time to time.

Certain of the underwriters and their affiliates have provided in the past to us and our affiliates and may provide from time to time in the future certain commercial banking, financial advisory, investment banking and other services for us and such affiliates in the ordinary course of their business, for which they have received or will receive customary fees and commissions. In addition, from time to time, certain of the underwriters and their affiliates may effect transactions for their own account or the account of customers, and hold on behalf of themselves or their customers, long or short positions in our debt or equity securities or loans, and may do so in the future.

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LEGAL MATTERS

The validity of the shares of common stock offered hereby will be passed upon for us by Ice Miller LLP. Certain others matters will be passed upon for us by Gibson, Dunn & Crutcher LLP. Wilson Sonsini Goodrich & Rosati, Professional Corporation, is acting as counsel to the underwriters.

EXPERTS

The consolidated financial statements of ExactTarget, Inc. as of December 31, 2009 and 2010, and for each of the years in the three-year period ended December 31, 2010, have been included herein in reliance upon the reports of KPMG LLP, independent registered public accounting firm, appearing elsewhere herein and upon the authority of said firm as experts in accounting and auditing.

WHERE YOU CAN FIND MORE INFORMATION

We have filed with the SEC a registration statement on Form S-1 under the Securities Act with respect to the common stock we propose to sell in this offering. This prospectus, which constitutes part of the registration statement, does not contain all of the information set forth in the registration statement. For further information about us and the common stock that we propose to sell in this offering, we refer you to the registration statement and the exhibits and schedules filed as a part of the registration statement. Statements contained in this prospectus as to the contents of any contract or other document filed as an exhibit to the registration statement are not necessarily complete. If a contract or document has been filed as an exhibit to the registration statement, we refer you to the copy of the contract or document that has been filed as an exhibit to the registration statement. When we complete this offering, we will also be required to file annual, quarterly and special reports, proxy statements and other information with the SEC.

You can read our SEC filings, including the registration statement, over the Internet at the SEC s website at www.sec.gov. You may also read and copy any document we filed with the SEC at its public reference facility at 100 F Street, N.E., Washington, D.C. 20549. You may also obtain copies of the documents at prescribed rates by writing to the Public Reference Section of the SEC at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference facilities.

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EXACTTARGET, INC.

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Independent Auditors Report

The Board of Directors and Stockholders

ExactTarget, Inc.:

We have audited the consolidated balance sheets of ExactTarget, Inc. and Subsidiaries (the Company) as of December 31, 2009 and 2010, and the related consolidated statements of operations, redeemable convertible preferred stock and stockholders equity (deficit), and cash flows for each of the years in the three-year period ended December 31, 2010. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of ExactTarget, Inc. as of December 31, 2009 and 2010, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2010, in conformity with U.S. generally accepted accounting principles.

/s/ KPMG LLP

Indianapolis, Indiana

April 28, 2011

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EXACTTARGET, INC.

Consolidated Balance Sheets

December 31, 2009 and 2010 and September 30, 2011

(In thousands, except share data)

	As of December 31, 2009	As of December 31, 2010	As of September 30, 2011 (unaudited)
Assets			
Current Assets:			
Cash and cash equivalents	$ 34,342	$ 22,804	$ 29,550
Accounts receivable, net	20,567	27,589	36,364
Prepaid expenses	4,204	4,367	7,527
Deferred income taxes	438	968	
Income tax receivable	2,943	319	232
Other current assets	513	918	2,251
Total current assets	63,007	56,965	75,924
Property and equipment, net	26,824	37,199	55,851
Goodwill	438	15,868	18,438
Intangible assets, net of accumulated amortization	866	2,562	3,595
Deferred income taxes	3,150	9,572	
Other assets	41	791	927
Total assets	$ 94,326	$ 122,957	$ 154,735
Liabilities and Stockholders Equity			
Current Liabilities:			
Accounts payable	$ 4,288	$ 2,858	$ 8,383
Accrued liabilities	2,498	8,199	12,066
Accrued compensation and related expenses	5,959	10,143	13,505
Current portion of long-term obligations and other	400	3,860	5,049
Deferred revenue	23,835	31,600	35,249
Total current liabilities	36,980	56,660	74,252
Long-term obligations and other	866	1,703	2,443
Long-term portion of accrued straight-line rent	1,410	1,524	2,178
Long-term portion of debt		6,667	14,167
Total liabilities	39,256	66,554	93,040
Redeemable convertible preferred stock:			
Series E, Series F and Series G redeemable convertible preferred stock, at respective redemption value. Authorized 4,912,646 shares at September 30, 2011, issued and outstanding 2,964,594, 2,964,594 and 4,912,646 shares at December 31, 2009, December 31, 2010 and September 30, 2011, respectively	33,038	33,038	63,000
Stockholders equity:			
	4	4	5

Common stock, $.001 par value. Authorized 35,000,000 shares at September 30, 2011; issued and outstanding 3,785,748, 4,230,244 and 4,482,140 shares at December 31, 2009, December 31, 2010 and September 30, 2011, respectively			
Additional paid in capital		9,246	14,77>
Change in unrealized gain/loss on securities	89	(1,193)	106
Cumulative effect of accounting change			292
Change in net gain/loss on cash-flow hedging instruments	(124)	105	(173)
Change in foreign currency translation adjustments	29	(107)	59
Change in minimum pension liability	560	(140)	(105)
Total other comprehensive income (loss)	554	(1,335)	179
SFAS 158 adjustment	(466)		
Balance at end of year	178	90	1,425
Total stockholders equity	**$ 18,876**	**$ 15,325**	**$ 14,238**
Outstanding Shares (in thousands)			
Balance at beginning of year	302,152	294,208	283,380
Issuance of common stock in underwritten offerings			6,703
Issuance of shares from equity unit contracts	17,856		
Issuance of shares under incentive and stock compensation plans	3,358	7,988	4,157
Return of shares to treasury stock under incentive and stock compensation plans	(51)	(44)	(32)
Balance at end of year	323,315	302,152	294,208

Consolidated Statements of Comprehensive Income

	For the years ended December 31,		
(In millions)	**2006**	**2005**	**2004**
Comprehensive Income			
Net income	$2,745	$ 2,274	$2,115
Other Comprehensive Income (Loss), Net of Tax			
Change in unrealized gain/loss on securities			
Change in unrealized gain/loss on securities	89	(1,193)	106
Cumulative effect of accounting change			292
Change in net gain/loss on cash-flow hedging instruments	(124)	105	(173)
Change in foreign currency translation adjustments	29	(107)	59
Change in minimum pension liability adjustment	560	(140)	(105)
Total other comprehensive income (loss)	554	(1,335)	179
Total comprehensive income	**$3,299**	**$ 939**	**$2,294**

See Notes to Consolidated Financial Statements.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
Consolidated Statements of Cash Flows

(In millions)	For the years ended December 31, 2006	2005	2004
Operating Activities			
Net income	$ 2,745	$ 2,274	$ 2,115
Adjustments to reconcile net income to net cash provided by operating activities			
Amortization of deferred policy acquisition costs and present value of future profits	3,558	3,169	2,843
Additions to deferred policy acquisition costs and present value of future profits	(4,092)	(4,131)	(3,914)
Change in:			
Reserve for future policy benefits, unpaid losses and loss adjustment expenses and unearned premiums	975	2,163	877
Reinsurance recoverables	1,071	(361)	128
Receivables	(34)	(682)	(395)
Payables and accruals	(287)	(267)	(11)
Accrued and deferred income taxes	657	168	529
Net realized capital (gains) losses	251	(17)	(291)
Net increase in equity securities, held for trading	(5,609)	(12,872)	(7,409)
Net receipts from investment contracts credited to policyholder accounts associated with equity securities, held for trading	5,594	13,087	7,909
Depreciation and amortization	606	561	274
Cumulative effect of accounting change, net of tax			23
Other, net	203	640	(44)
Net cash provided by operating activities	**5,638**	**3,732**	**2,634**
Investing Activities			
Proceeds from the sale/maturity/prepayment of:			
Fixed maturities, available-for-sale	35,432	36,895	34,981
Equity securities, available-for-sale	514	105	127
Mortgage loans	392	511	292
Partnerships	154	226	249
Payments for the purchase of:			
Fixed maturities, available-for-sale	(40,368)	(40,580)	(36,527)
Equity securities, available-for-sale	(924)	(598)	(278)
Mortgage loans	(1,974)	(1,068)	(636)
Partnerships	(809)	(439)	(483)
Change in policy loans, net	(36)	646	(149)
Change in payables for collateral under securities lending, net	970	(367)	(36)
Change in all other securities, net	(454)	12	297
Purchase price adjustment of business acquired		8	(58)
Sale of subsidiary, net of cash transferred	(112)		
Additions to property and equipment, net	(195)	(211)	(180)

Net cash used for investing activities	**(7,410)**	**(4,860)**	**(2,401)**
Financing Activities			
Deposits and other additions to investment and universal life-type contracts	27,450	25,780	27,877
Withdrawals and other deductions from investment and universal life-type contracts	(27,096)	(25,099)	(22,178)
Transfers from (to) separate accounts related to investment and universal life-type contracts	1,189	706	(4,737)
Issuance of shares from equity unit contracts	1,020		
Issuance of common stock in underwritten offering			411
Issuance of long-term debt	990		197
Repayment/maturity of long-term debt	(1,415)	(250)	(450)
Change in short-term debt	(173)	100	(477)
Proceeds from issuance of consumer notes	258		
Proceeds from issuances of shares under incentive and stock compensation plans, net	147	390	161
Excess tax benefits on stock-based compensation	10		
Return of shares under incentive and stock compensation plans	(5)	(2)	(2)
Dividends paid	(460)	(345)	(325)
Net cash provided by financing activities	**1,915**	**1,280**	**477**
Foreign exchange rate effect on cash	8	(27)	(24)
Net increase in cash	151	125	686
Cash beginning of year	1,273	1,148	462
Cash end of year	**$ 1,424**	**$ 1,273**	**$ 1,148**
Supplemental Disclosure of Cash Flow Information:			
Net Cash Paid During the Year for:			
Income taxes	$ 179	$ 447	$ 32
Interest	$ 274	$ 248	$ 246

See Notes to Consolidated Financial Statements.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollar amounts in millions, except for per share data, unless otherwise stated)

1. Basis of Presentation and Accounting Policies

Basis of Presentation

The Hartford Financial Services Group, Inc. is a financial holding company for a group of subsidiaries that provide investment products and life and property and casualty insurance to both individual and business customers in the United States and internationally (collectively, The Hartford or the Company).

The consolidated financial statements have been prepared on the basis of accounting principles generally accepted in the United States of America, which differ materially from the accounting practices prescribed by various insurance regulatory authorities.

Consolidation

The consolidated financial statements include the accounts of The Hartford Financial Services Group, Inc., companies in which the Company directly or indirectly has a controlling financial interest and those variable interest entities in which the Company is the primary beneficiary. The Company determines if it is the primary beneficiary using both qualitative and quantitative analyses. Entities in which The Hartford does not have a controlling financial interest but in which the Company has significant influence over the operating and financing decisions are reported using the equity method. All material intercompany transactions and balances between The Hartford and its subsidiaries and affiliates have been eliminated. For further discussions on variable interest entities see Note 4.

Use of Estimates

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The most significant estimates include those used in determining property and casualty reserves for unpaid losses and loss adjustment expenses, net of reinsurance; Life deferred policy acquisition costs and present value of future profits associated with variable annuity and other universal life-type contracts; the evaluation of other-than-temporary impairments on investments in available-for-sale securities; the valuation of guaranteed minimum withdrawal benefit derivatives; pension and other postretirement benefit obligations; and contingencies relating to corporate litigation and regulatory matters.

Reclassifications

Certain reclassifications have been made to prior year financial information to conform to the current year presentation.

Adoption of New Accounting Standards

Employers Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R)

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R) (SFAS 158). This statement requires an entity to: (a) recognize an asset for the funded status, measured as the difference between the fair value of plan assets and the benefit obligation, of defined benefit postretirement plans that are overfunded and a liability for plans that are underfunded, measured as of the employer s fiscal year end; and (b) recognize changes in the funded status of defined benefit postretirement plans, other than for the net periodic benefit cost included in net income, in accumulated other comprehensive income. For pension plans, the funded status must be based on the projected benefit obligation which includes an assumption for future salary increases. The provisions of FASB Statement No. 87, Employers Accounting for Pensions (SFAS 87) and FASB Statement No. 106, Employers Accounting for Postretirement Benefits Other Than Pensions in measuring plan assets and benefit obligations and in determining the amount of net periodic benefit cost continue to apply upon initial and subsequent application of SFAS 158. SFAS 158 is effective for public entities with years ending after December 15, 2006, with certain exceptions not applicable to The Hartford, through an adjustment to the ending balance of accumulated other comprehensive income, net of tax. As of December 31, 2006, the effect of adopting SFAS 158 was a decrease of $717 in the net defined benefit postretirement plan asset and a corresponding after-tax decrease of $466 in the accumulated other comprehensive income component of equity. Because the Company recorded a decrease of $560, net of tax, in its additional minimum liability adjustment related to its pension plans, the balance sheet change was an increase of $145 in the net defined benefit postretirement plan asset and a corresponding after-tax increase of $94 in the accumulated other comprehensive income component of equity. Note 17 provides further details about the adoption of SFAS 158.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements

In September 2006, the Securities and Exchange Commission (SEC) staff issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements (SAB 108). SAB 108 provides guidance for how errors should be evaluated to assess materiality from a quantitative perspective. SAB 108 permits companies to initially apply its provisions by either restating prior financial statements or recording the cumulative effect of initially applying the approach as adjustments to the carrying values of assets and liabilities as of January 1, 2006 with an offsetting adjustment to retained earnings. The Company adopted SAB 108 on December 31, 2006. The adoption had no effect on the Company s consolidated financial condition or results of operations.

Share-Based Payment

In December 2004, the FASB issued Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment (SFAS 123(R)), which replaced SFAS No. 123, Accounting for Stock-Based Compensation (SFAS 123) and superseded the American Institute of Certified Public Accountants (AICPA) Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees . SFAS 123(R) requires companies to recognize compensation costs for share-based payments to employees based on the grant-date fair value of the award. In January 2003, the Company began expensing all stock-based compensation awards granted or modified after January 1, 2003 under the fair value recognition provisions of SFAS 123 and therefore the adoption of SFAS 123(R) did not have a material effect on the Company s financial position or results of operations and is not expected to have a material effect on future operations. The Company adopted SFAS 123(R) effective January 1, 2006 using the modified prospective method and therefore prior period amounts have not been restated. The Company recognized an immaterial effect of adoption as of January 1, 2006 to reverse expense previously recognized on awards expected to be forfeited, as required under SFAS 123(R). The under-mentioned related FASB Staff Positions (FSPs) have been issued to amend specific provisions of SFAS 123(R) as follows:

In November 2005, the FASB issued FASB Staff Position No. 123(R)-3, Transition Election Related to Accounting for the Tax Effects of Share-Based Payment Awards (FSP 123(R)-3), which provides a practical transition election related to accounting for the tax effects of share-based payment awards to employees. FSP 123(R)-3 addresses an alternative method for calculating the pool of excess tax benefits available to absorb tax deficiencies (APIC pool) recognized subsequent to the adoption of SFAS 123(R). The Company is required to make a one time election to utilize either the method stated in FSP 123(R)-3 or the method stated in SFAS 123(R) for computing the APIC pool related to employee compensation. The Company did not adopt the APIC pool computation method outlined in FSP 123(R)-3, and has elected to compute its APIC pool related to employee compensation by using the method described in SFAS 123(R) and the guidance related to reporting cash flows described in SFAS 123(R). Therefore, FSP 123(R)-3 did not have an effect on the Company s consolidated financial condition or results of operations.

In February 2006, the FASB issued FASB Staff Position No. 123(R)-4, Classification of Options and Similar Instruments Issued as Employee Compensation That Allow for Cash Settlement upon the Occurrence of a Contingent Event (FSP 123(R)-4), which amends certain provisions of SFAS 123(R) which require that options and similar instruments be classified as liabilities if the entity can be required under any circumstances to settle the option or similar instrument by transferring cash or other assets. FSP 123(R)-4 provides that a cash settlement feature that can be exercised only upon the occurrence of a contingent event that is outside the employee s control does not meet the conditions stipulated in SFAS 123(R) until it becomes probable that the event will occur. FSP 123(R)-4 shall be applied no later than the second quarter of 2006. The Company s Stock Plan does not allow for cash settlement on options or similar instruments awarded to employees in the event of a change in control. Therefore, FSP 123(R)-4 did not have an effect on the Company s consolidated financial condition or results of operations.

In October 2006, the FASB issued FASB Staff Position No. 123(R)-6, Technical Correction of FASB Statement No. 123(R) (FSP 123(R)-6). FSP 123(R)-6 specifically amends SFAS 123(R) to (a) exempt nonpublic entities from the aggregate intrinsic value disclosure requirement; (b) revise the computation of the minimum compensation cost that must be recognized to comply with SFAS 123(R); (c) indicate that at the date the illustrative awards were no longer probable of vesting, any previously recognized compensation cost should have been reversed; and (d) amend the definition of short-term inducement to exclude an offer to settle an award. The adoption of FSP 123(R)-6 in the fourth quarter of 2006 did not have an effect on the Company s consolidated financial condition or results of operations.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments

In November 2005, the FASB released FASB Staff Position Nos. FAS 115-1 and FAS 124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments (FSP 115-1), which effectively replaces Emerging Issues Task Force Issue No. 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments (EITF 03-1). FSP 115-1 contains a three-step model for evaluating impairments and carries forward the disclosure requirements in EITF Issue No. 03-1 pertaining to securities in an unrealized loss position. Under the model, any security in an unrealized loss position is considered impaired; an evaluation is made to determine whether the impairment is other-than-temporary; and, if an impairment is considered other-than-temporary, a realized loss is recognized to write the security s cost or amortized cost basis down to fair value. FSP 115-1 references existing other-than-temporary impairment guidance for determining when an impairment is other-than-temporary and clarifies that subsequent to the recognition of an other-than-temporary impairment loss for debt securities, an investor shall account for the security using the constant effective yield method. FSP 115-1 is effective for reporting periods beginning after December 15, 2005, with earlier application permitted. The Company adopted FSP 115-1 upon issuance. The adoption did not have a material effect on the Company s consolidated financial condition or results of operations.

Certain Nontraditional Long-Duration Contracts and Separate Accounts

In July 2003, the AICPA issued Statement of Position (SOP) 03-1, Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts (SOP 03-1). SOP 03-1 addresses a wide variety of topics, some of which have a significant impact on the Company. The major provisions of SOP 03-1 require:

- Recognizing expenses for a variety of contracts and contract features, including guaranteed minimum death benefits (GMDB), certain death benefits on universal-life type contracts and annuitization options, on an accrual basis versus the previous method of recognition upon payment;
- Reporting and measuring assets and liabilities of certain separate account products as general account assets and liabilities when specified criteria are not met;
- Reporting and measuring the Company s interest in its separate accounts as general account assets based on the insurer s proportionate beneficial interest in the separate account s underlying assets; and
- Capitalizing sales inducements that meet specified criteria and amortizing such amounts over the life of the contracts using the same methodology as used for amortizing deferred acquisition costs (DAC).

SOP 03-1 was effective for financial statements for fiscal years beginning after December 15, 2003. At the date of initial application, January 1, 2004, the cumulative effect of the adoption of SOP 03-1 on net income and other comprehensive income was comprised of the following individual impacts shown net of income tax benefit of $12:

Components of Cumulative Effect of Adoption	**Net Income**	**Other Comprehensive Income**
Establishing GMDB and other benefit reserves for annuity contracts	$ (54)	$
Reclassifying certain separate accounts to general account	30	294
Other	1	(2)
Total cumulative effect of adoption	**$ (23)**	**$ 292**

Future Adoption of New Accounting Standards

Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, Including an amendment of FASB Statement No. 115 (SFAS 159). The objective of SFAS 159 is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported net income caused by measuring related assets and liabilities differently. This statement permits entities to choose, at specified election dates, to measure eligible items at fair value (i.e., the fair value option). Items eligible for the fair value option include certain recognized financial assets and liabilities, rights and obligations under certain insurance contracts that are not financial instruments, host financial instruments resulting from the separation of an embedded nonfinancial derivative instrument from a nonfinancial hybrid instrument, and certain commitments. Business entities shall report unrealized gains and losses on items for which the fair value option has been elected in net income. The fair value option: (a) may be applied instrument by instrument, with certain exceptions; (b) is irrevocable (unless a new election date occurs); and (c) is applied only to entire instruments and not to portions of instruments. SFAS 159 is effective as of the beginning of an entity s first fiscal year that begins after November 15, 2007, although early adoption is permitted under certain conditions. Companies shall report the effect of the first remeasurement to fair value as a cumulative-effect adjustment to the opening balance of retained

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

earnings. The Company expects to adopt SFAS 159 on January 1, 2008, but has not yet determined the items to which the Company may apply the fair value option and the impact on the Company s consolidated financial statements.

Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS 157). This statement defines fair value, establishes a framework for measuring fair value under accounting principles generally accepted in the United States, and enhances disclosures about fair value measurements. The definition focuses on the price that would be received to sell the asset or paid to transfer the liability (an exit price), not the price that would be paid to acquire the asset or received to assume the liability (an entry price). SFAS 157 provides guidance on how to measure fair value when required under existing accounting standards. The statement establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels (Level 1, 2 and 3). Level 1 inputs are observable inputs that reflect quoted prices for identical assets or liabilities in active markets that the Company has the ability to access at the measurement date. Level 2 inputs are observable inputs, other than quoted prices included in Level 1, for the asset or liability or prices for similar assets and liabilities. Level 3 inputs are unobservable inputs reflecting the reporting entity s estimates of the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk). Quantitative and qualitative disclosures will focus on the inputs used to measure fair value for both recurring and non-recurring fair value measurements and the effects of the measurements in the financial statements. SFAS 157 is effective for fiscal years beginning after November 15, 2007, with earlier application encouraged only in the initial quarter of an entity s fiscal year. The Company will adopt SFAS 157 on January 1, 2008, but has not yet quantified the impact. However, the Company has certain significant product riders, including GMWB, that are recorded using fair value. Under SFAS 157, fair value for GMWB will use significant Level 3 inputs including risk margins. The Company s account value associated with GMWB is $48.3 billion as of December 31, 2006. As a result, the one time realized capital loss that could be recorded upon the adoption of SFAS 157 could materially reduce the Company s 2008 net income. Realized gains and losses that will be recorded in future years are also likely to be more volatile than amounts recorded in prior years. In addition, adoption of SFAS 157 will result in a future reduction in variable annuity fee income as fees attributed to the embedded derivative will increase consistent with incorporating additional risk margins and other indicia of exit value in the valuation of the embedded derivative.

Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109

The FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109 (FIN 48), dated June 2006. The interpretation requires public companies to recognize the tax benefits of uncertain tax positions only where the position is more likely than not to be sustained assuming examination by tax authorities. The amount recognized would be the amount that represents the largest amount of tax benefit that is greater than 50% likely of being ultimately realized. A liability would be recognized for any benefit claimed, or expected to be claimed, in a tax return in excess of the benefit recorded in the financial statements, along with any interest and penalty (if applicable) on the excess. FIN 48 will require a tabular reconciliation of the change in the aggregate unrecognized tax benefits claimed, or expected to be claimed, in tax returns and disclosure relating to accrued interest and penalties for unrecognized tax benefits. Disclosures will also be required for those uncertain tax positions where it is reasonably possible that the estimate of the tax benefit will change significantly in the next 12 months. FIN 48 is effective for fiscal years beginning after December 15, 2006. Upon adoption, as of the first quarter of 2007, FIN 48 will not have a material effect on the Company s consolidated financial condition or results of operations.

Accounting for Certain Hybrid Financial Instruments an amendment of FASB Statements No. 133 and 140

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments an amendment of FASB Statements No. 133 and 140 (SFAS 155). This statement amends SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities (SFAS 133), and SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities and resolves issues addressed in SFAS 133

Implementation Issue No. D1, Application of Statement 133 to Beneficial Interest in Securitized Financial Assets . This Statement: (a) permits fair value remeasurement for any hybrid financial instrument (asset or liability) that contains an embedded derivative that otherwise would require bifurcation; (b) clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS 133; (c) establishes a requirement to evaluate beneficial interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation; (d) clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives; and, (e) eliminates restrictions on a qualifying special-purpose entity s ability to hold passive derivative financial instruments that pertain to beneficial interests that are or contain a derivative financial instrument. The standard also requires presentation within the financial statements that identifies those hybrid financial instruments for which the fair value election has been applied and information on the income statement impact of the changes in fair value of those instruments. The Company is required to apply SFAS 155 to all financial instruments acquired, issued or subject to a remeasurement event beginning January 1, 2007. SFAS 155 did not have an effect on the Company s consolidated financial condition and results of operations upon adoption at January 1, 2007. However, the standard could affect the future income recognition for securitized

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

financial assets or issued liabilities because there may be more embedded derivatives identified with changes in fair value recognized in net income.

Accounting by Insurance Enterprises for Deferred Acquisition Costs (DAC) in Connection with Modifications or Exchanges of Insurance Contracts

In September 2005, the AICPA issued Statement of Position 05-1, Accounting by Insurance Enterprises for Deferred Acquisition Costs (DAC) in Connection with Modifications or Exchanges of Insurance Contracts , (SOP 05-1). SOP 05-1 provides guidance on accounting by insurance enterprises for DAC on internal replacements of insurance and investment contracts. An internal replacement is a modification in product benefits, features, rights or coverages that occurs by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. Modifications that result in a replacement contract that is substantially changed from the replaced contract should be accounted for as an extinguishment of the replaced contract. Unamortized DAC, unearned revenue liabilities and deferred sales inducements from the replaced contract must be written-off. Modifications that result in a contract that is substantially unchanged from the replaced contract should be accounted for as a continuation of the replaced contract. SOP 05-1 is effective for internal replacements occurring in fiscal years beginning after December 15, 2006, with earlier adoption encouraged. Initial application of SOP 05-1 should be as of the beginning of the entity s fiscal year. The Company will adopt SOP 05-1 on January 1, 2007. The Company expects the cumulative effect upon adoption of SOP 05-1 to be $50 to $65, after-tax, which will be recorded as a reduction in retained earnings as of January 1, 2007.

Investments

The Hartford s investments in fixed maturities, which include bonds, redeemable preferred stock and commercial paper; and certain equity securities, which include common and non-redeemable preferred stocks, are classified as available-for-sale and accordingly, are carried at fair value with the after-tax difference from cost or amortized cost, as adjusted for the effect of deducting the life and pension policyholders share of the immediate participation guaranteed contracts; and certain life and annuity deferred policy acquisition costs and reserve adjustments, reflected in stockholders equity as a component of accumulated other comprehensive income (AOCI). The equity investments associated with the variable annuity products offered in Japan are recorded at fair value and are classified as trading with changes in fair value recorded in net investment income. Policy loans are carried at outstanding balance. Mortgage loans on real estate are recorded at the outstanding principal balance adjusted for amortization of premiums or discounts and net of valuation allowances, if any. Other investments primarily consist of derivatives, and limited partnership interests and proportionate share limited liability companies (collectively limited partnerships). Limited partnerships are accounted for under the equity method and accordingly the Company s share of earnings are included in net investment income. Derivatives are carried at fair value.

Valuation of Fixed Maturities

The fair value for fixed maturity securities is largely determined by one of three primary pricing methods: independent third party pricing service market quotations, independent broker quotations or pricing matrices, which use market data provided by external sources. With the exception of short-term securities for which amortized cost is predominantly used to approximate fair value, security pricing is applied using a hierarchy or waterfall approach whereby prices are first sought from independent pricing services with the remaining unpriced securities submitted to brokers for prices or lastly priced via a pricing matrix.

Prices from independent pricing services are often unavailable for securities that are rarely traded or are traded only in privately negotiated transactions. As a result, certain of the Company s asset-backed (ABS) and commercial mortgage-backed securities (CMBS) are priced via broker quotations. A pricing matrix is used to price securities for which the Company is unable to obtain either a price from an independent third party service or an independent broker quotation. The pricing matrix begins with current determine the market price for the security. The credit spreads, as assigned by a nationally recognized rating agency, incorporate the issuer s credit rating and a risk premium, if warranted, due to the issuer s industry and the security s time to maturity. The issuer-specific yield adjustments, which can be positive or negative, are updated twice annually, as of June 30 and December 31, by an independent third party source and are intended to adjust security prices for issuer-specific factors. The matrix-priced securities at December 31, 2006 and 2005, primarily consisted of non-144A private placements and have an average duration of 5.1 and 5.0 years, respectively.

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

The following table presents the fair value of fixed maturity securities by pricing source as of December 31, 2006 and 2005.

	2006		2005	
	Fair Value	Percentage of Total Fair Value	Fair Value	Percentage of Total Fair Value
Priced via independent market quotations	$69,023	85.5%	$65,986	86.3%
Priced via broker quotations	4,309	5.3%	2,728	3.6%
Priced via matrices	5,605	6.9%	5,452	7.1%
Priced via other methods	137	0.2%	211	0.3%
Short-term investments [1]	1,681	2.1%	2,063	2.7%
Total	**$80,755**	**100.0%**	**$76,440**	**100.0%**

[1] Short-term investments are primarily valued at amortized cost, which approximates fair value.

The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between knowledgeable, unrelated willing parties. As such, the estimated fair value of a financial instrument may differ significantly from the amount that could be realized if the security was sold immediately.

Other-Than-Temporary Impairments on Available-for-Sale Securities

One of the significant estimates inherent in the valuation of investments is the evaluation of investments for other-than-temporary impairments. The evaluation of impairments is a quantitative and qualitative process, which is subject to risks and uncertainties and is intended to determine whether declines in the fair value of investments should be recognized in current period earnings. The risks and uncertainties include changes in general economic conditions, the issuer s financial condition or near term recovery prospects and the effects of changes in interest rates. The Company s accounting policy requires that a decline in the value of a security below its cost or amortized cost basis be assessed to determine if the decline is other-than-temporary. If the security is deemed to be other-than-temporarily impaired, a charge is recorded in net realized capital losses equal to the difference between the fair value and cost or amortized cost basis of the security. In addition, for securities expected to be sold, an other-than-temporary impairment charge is recognized if the Company does not expect the fair value of a security to recover to cost or amortized cost prior to the expected date of sale. The fair value of the other-than-temporarily impaired investment becomes its new cost basis. The Company has a security monitoring process overseen by a committee of investment and accounting professionals that identifies securities that, due to certain characteristics, as described below, are subjected to an enhanced analysis on a quarterly basis.

Securities not subject to EITF Issue No. 99-20, Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests That Continued to Be Held by a Transferor in Securitized Financial Assets (non-EITF Issue No. 99-20 securities) that are in an unrealized loss position, are reviewed at least quarterly to determine if an other-than-temporary impairment is present based on certain quantitative and qualitative factors. The primary factors considered in evaluating whether a decline in value for non-EITF Issue No. 99-20 securities is other-than-temporary include: (a) the length of time and the extent to which the fair value has been less than cost or amortized cost, (b) the financial condition, credit rating and near-term prospects of the issuer, (c) whether the debtor is current on contractually obligated interest and principal payments and (d) the intent and ability of the Company to retain the investment for a period of time sufficient to allow for recovery.

Each quarter, during this analysis, the Company asserts its intent and ability to retain until recovery those securities judged to be temporarily impaired. Once identified, these securities are systematically restricted from trading unless approved by the committee. The committee will only authorize the sale of these securities based on predefined criteria that relate to events that could not have been foreseen. Examples of the criteria include, but are not limited to, the deterioration in the issuer s creditworthiness, a change in regulatory requirements or a major business combination or major disposition.

For certain securitized financial assets with contractual cash flows including ABS, EITF Issue No. 99-20 requires the Company to periodically update its best estimate of cash flows over the life of the security. If the fair value of a securitized financial asset is less than its cost or amortized cost and there has been a decrease in the present value of the estimated cash flows since the last revised estimate, considering both timing and amount, an other-than-temporary impairment charge is recognized. The Company also considers its intent and ability to retain a temporarily impaired security until recovery. Estimating future cash flows is a quantitative and qualitative process that incorporates information received from third party sources along with certain internal assumptions and judgments regarding the future performance of the underlying collateral. In addition, projections of expected future cash flows may change based upon new information regarding the performance of the underlying collateral.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

Mortgage Loan Impairments

Mortgage loans on real estate are considered to be impaired when management estimates that, based upon current information and events, it is probable that the Company will be unable to collect amounts due according to the contractual terms of the loan agreement. For mortgage loans that are determined to be impaired, a valuation allowance is established for the difference between the carrying amount and the Company s share of either (a) the present value of the expected future cash flows discounted at the loan s original effective interest rate, (b) the loan s observable market price or (c) the fair value of the collateral. Changes in valuation allowances are recorded in net realized capital gains and losses.

Net Realized Capital Gains and Losses

Net realized capital gains and losses from investment sales, after deducting the life and pension policyholders share for certain products, are reported as a component of revenues and are determined on a specific identification basis. Net realized capital gains and losses also result from fair value changes in derivatives contracts (both free-standing and embedded) that do not qualify, or are not designated, as a hedge for accounting purposes, and the change in value of derivatives in certain fair-value hedge relationships. Impairments are recognized as net realized capital losses when investment losses in value are deemed other-than-temporary. Foreign currency transaction remeasurements are also included in net realized capital gains and losses. Net realized capital gains and losses on security transactions associated with the Company s immediate participation guaranteed contracts are recorded and offset by amounts owed to policyholders and were less than $1 for the years ended December 31, 2006 and 2005, and 2004. Under the terms of the contracts, the net realized capital gains and losses will be credited to policyholders in future years as they are entitled to receive them.

Net Investment Income

Interest income from fixed maturities and mortgage loans on real estate is recognized when earned on the constant effective yield method based on estimated principal repayments, if applicable. The calculation of amortization of premium and accretion of discount for fixed maturities also takes into consideration call and maturity dates that produce the lowest yield. For high credit quality securitized financial assets subject to prepayment risk, yields are recalculated and adjusted periodically to reflect historical and/or estimated future principal repayments using the retrospective method. For non-highly rated securitized financial assets any yield adjustments are made using the prospective method. Prepayment fees on fixed maturities and mortgage loans are recorded in net investment income when earned. For limited partnerships, the equity method of accounting is used to recognize the Company s share of earnings. For fixed maturities that have had an other-than-temporary impairment loss, the Company amortizes the new cost basis to par or to estimated future value over the remaining life of the security based on future estimated cash flows.

Net investment income on equity securities held for trading includes dividend income and the changes in market value of the securities associated with the variable annuity products sold in Japan. The returns on these policyholder-directed investments inure to the benefit of the variable annuity policyholders but the underlying funds do not meet the criteria for separate account reporting as provided in SOP 03-1. Accordingly, these assets are reflected in the Company s general account and the returns credited to the policyholders are reflected in interest credited, a component of benefits, losses and loss adjustment expenses.

Derivative Instruments

Overview

The Company utilizes a variety of derivative instruments, including swaps, caps, floors, forwards, futures and options through one of four Company-approved objectives: to hedge risk arising from interest rate, equity market, price or currency exchange rate risk or volatility; to manage liquidity; to control transaction costs; or to enter into replication transactions. For a further discussion of derivative instruments, see the Derivative Instruments section of Note 4.

The Company s derivative transactions are used in strategies permitted under the derivative use plans required by the State of Connecticut, the State of Illinois and the State of New York insurance departments.

Accounting and Financial Statement Presentation of Derivative Instruments and Hedging Activities

Derivatives are recognized on the balance sheet at fair value. As of December 31, 2006 and 2005, approximately 84% and 81% of derivatives, respectively, based upon notional values, were priced via valuation models which utilize market data, while the remaining 16% and 19% of derivatives, respectively, were priced via broker quotations. These percentages exclude the guaranteed minimum withdrawal benefit (GMWB) rider and the associated reinsurance contracts, which are discussed below. The derivative

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

contracts are reported as assets or liabilities in other investments and other liabilities, respectively, in the consolidated balance sheets, excluding embedded derivatives and GMWB reinsurance contracts. Embedded derivatives are recorded in the consolidated balance sheets with the associated host instrument. GMWB reinsurance contract amounts are recorded in reinsurance recoverables in the consolidated balance sheets.

On the date the derivative contract is entered into, the Company designates the derivative as (1) a hedge of the fair value of a recognized asset or liability (fair-value hedge), (2) a hedge of the variability in cash flows of a forecasted transaction or of amounts to be received or paid related to a recognized asset or liability (cash-flow hedge), (3) a foreign-currency fair value or cash-flow hedge (foreign-currency hedge), (4) a hedge of a net investment in a foreign operation (net investment hedge) or (5) held for other investment and risk management purposes, which primarily involve managing asset or liability related risks which do not qualify for hedge accounting.

Fair-Value Hedges

Changes in the fair value of a derivative that is designated and qualifies as a fair-value hedge, along with the changes in the fair value of the hedged asset or liability that is attributable to the hedged risk, are recorded in current period earnings with any differences between the net change in fair value of the derivative and the hedged item representing the hedge ineffectiveness. Periodic cash flows and accruals of income/expense (periodic derivative net coupon settlements) are recorded in the line item of the consolidated statements of operations in which the cash flows of the hedged item are recorded.

Cash-Flow Hedges

Changes in the fair value of a derivative that is designated and qualifies as a cash-flow hedge are recorded in AOCI and are reclassified into earnings when the variability of the cash flow of the hedged item impacts earnings. Gains and losses on derivative contracts that are reclassified from AOCI to current period earnings are included in the line item in the consolidated statements of operations in which the cash flows of the hedged item are recorded. Any hedge ineffectiveness is recorded immediately in current period earnings as net realized capital gains and losses. Periodic derivative net coupon settlements are recorded in the line item of the consolidated statements of operations in which the cash flows of the hedged item are recorded.

Foreign-Currency Hedges

Changes in the fair value of derivatives that are designated and qualify as foreign-currency hedges are recorded in either current period earnings or AOCI, depending on whether the hedged transaction is a fair-value hedge or a cash-flow hedge, respectively. Any hedge ineffectiveness is recorded immediately in current period earnings as net realized capital gains and losses. Periodic derivative net coupon settlements are recorded in the line item of the consolidated statements of operations in which the cash flows of the hedged item are recorded.

Net Investment in a Foreign Operation Hedges

Changes in fair value of a derivative used as a hedge of a net investment in a foreign operation, to the extent effective as a hedge, are recorded in the foreign currency translation adjustments account within AOCI. Cumulative changes in fair value recorded in AOCI are reclassified into earnings upon the sale or complete, or substantially complete, liquidation of the foreign entity. Any hedge ineffectiveness is recorded immediately in current period earnings as net realized capital gains and losses. Periodic derivative net coupon settlements are recorded in the line item of the consolidated statements of operations in which the cash flows of the hedged item are recorded.

Other Investment and Risk Management Activities

The Company s other investment and risk management activities primarily relate to strategies used to reduce economic risk or replicate permitted investments and do not receive hedge accounting treatment. Changes in the fair value, including periodic derivative net coupon settlements, of derivative instruments held for other investment and risk management purposes are reported in current period earnings as net realized capital gains and losses.

Hedge Documentation and Effectiveness Testing

To qualify for hedge accounting treatment, a derivative must be highly effective in mitigating the designated changes in value or cash flow of the hedged item. At hedge inception, the Company formally documents all relationships between hedging instruments and hedged items, as well as its risk-management objective and strategy for undertaking each hedge transaction. The documentation process includes linking derivatives that are designated as fair-value, cash-flow, foreign-currency or net investment hedges to specific assets or liabilities on the balance sheet or to specific forecasted transactions and defining the effectiveness and ineffectiveness testing methods to be used. The Company also formally assesses, both at the hedge s inception and ongoing on a quarterly basis,

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

whether the derivatives that are used in hedging transactions have been and are expected to continue to be highly effective in offsetting changes in fair values or cash flows of hedged items. Hedge effectiveness is assessed using qualitative and quantitative methods. Qualitative methods may include comparison of critical terms of the derivative to the hedged item. Quantitative methods include regression or other statistical analysis of changes in fair value or cash flows associated with the hedge relationship. Hedge ineffectiveness of the hedge relationships are measured each reporting period using the Change in Variable Cash Flows Method , the Change in Fair Value Method , the Hypothetical Derivative Method , or the Dollar Offset Method .

Discontinuance of Hedge Accounting

The Company discontinues hedge accounting prospectively when (1) it is determined that the derivative is no longer highly effective in offsetting changes in the fair value or cash flows of a hedged item; (2) the derivative is dedesignated as a hedging instrument; or (3) the derivative expires or is sold, terminated or exercised.

When hedge accounting is discontinued because it is determined that the derivative no longer qualifies as an effective fair-value hedge, the derivative continues to be carried at fair value on the balance sheet with changes in its fair value recognized in current period earnings.

When hedge accounting is discontinued because the Company becomes aware that it is not probable that the forecasted transaction will occur, the derivative continues to be carried on the balance sheet at its fair value, and gains and losses that were accumulated in AOCI are recognized immediately in earnings.

In other situations in which hedge accounting is discontinued on a cash-flow hedge, including those where the derivative is sold, terminated or exercised, amounts previously deferred in AOCI are reclassified into earnings when earnings are impacted by the variability of the cash flow of the hedged item.

Embedded Derivatives

The Company purchases and issues financial instruments and products that contain embedded derivative instruments. When it is determined that (1) the embedded derivative possesses economic characteristics that are not clearly and closely related to the economic characteristics of the host contract, and (2) a separate instrument with the same terms would qualify as a derivative instrument, the embedded derivative is bifurcated from the host for measurement purposes. The embedded derivative, which is reported with the host instrument in the consolidated balance sheets, is carried at fair value with changes in fair value reported in net realized capital gains and losses.

Credit Risk

The Company s derivative counterparty exposure policy establishes market-based credit limits, favors long-term financial stability and creditworthiness and typically requires credit enhancement/credit risk reducing agreements. Credit risk is measured as the amount owed to the Company based on current market conditions and potential payment obligations between the Company and its counterparties. Credit exposures are generally quantified daily, netted by counterparty for each legal entity of the Company, and collateral is pledged to and held by, or on behalf of, the Company to the extent the current value of derivatives exceeds the exposure policy thresholds which do not exceed $10. The Company also minimizes the credit risk in derivative instruments by entering into transactions with high quality counterparties rated A1/A or better, which are monitored by the Company s internal compliance unit and reviewed frequently by senior management. In addition, the compliance unit monitors counterparty credit exposure on a monthly basis to ensure compliance with Company policies and statutory limitations. The Company also maintains a policy of requiring that derivative contracts, other than exchange traded contracts, currency forward contracts, and certain embedded derivatives, be governed by an International Swaps and Derivatives Association Master Agreement which is structured by legal entity and by counterparty and permits right of offset. To date, the Company has not incurred any losses on derivative instruments due to counterparty nonperformance.

Product Derivatives and Risk Management

The Company offers certain variable annuity products with a guaranteed minimum withdrawal benefit (GMWB) rider. The GMWB represents an embedded derivative in the variable annuity contracts that is required to be reported separately from the host variable annuity contract. It is carried at fair value and reported in other policyholder funds.

The fair value of the GMWB obligation is calculated based on actuarial and capital market assumptions related to the projected cash flows, including benefits and related contract charges, over the lives of the contracts, incorporating expectations concerning policyholder behavior. Because of the dynamic and complex nature of these cash flows, best estimate assumptions and stochastic techniques under a variety of market return scenarios are used. Estimating these cash flows involves numerous estimates and subjective judgments including those regarding expected market rates of return, market volatility, correlations of market returns and discount rates. At each valuation date,

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

the Company assumes expected returns based on risk-free rates as represented by the current LIBOR forward curve rates; market volatility assumptions for each underlying index based on a blend of observed market implied volatility data and annualized standard deviations of monthly returns using the most recent 20 years of observed market performance; correlations of market returns across underlying indices based on actual observed market returns and relationships over the ten years preceding the valuation date; and current risk-free spot rates as represented by the current LIBOR spot curve to determine the present value of expected future cash flows produced in the stochastic projection process.

In valuing the embedded derivative, the Company attributes to the derivative a portion of the fees collected from the contract holder equal to the present value of future GMWB claims (the Attributed Fees). All changes in the fair value of the embedded derivative are recorded in net realized capital gains and losses. The excess of fees collected from the contract holder for the GMWB over the Attributed Fees are associated with the host variable annuity contract recorded in fee income. Upon adoption of SFAS 157, the Company will revise many of the assumptions used to value GMWB.

For contracts issued prior to July 2003, the Company has a reinsurance arrangement in place to transfer its risk of loss due to GMWB. This arrangement is recognized as a derivative and carried at fair value in reinsurance recoverables. Changes in the fair value of the reinsurance agreement is recorded in net realized capital gains and losses. As of July 2003, the Company had substantially exhausted all of its reinsurance capacity, with respect to contracts issued after July 2003, and began hedging its exposure to the GMWB rider using a sophisticated program involving interest rate futures, Standard and Poor s (S&P) 500 and NASDAQ index put options and futures contracts and Europe, Australasia and Far East (EAFE) Index swaps to hedge GMWB exposure to international equity markets. For the years ended December 31, 2006, 2005 and 2004, net realized capital gains and losses included the change in market value of the embedded derivative related to the GMWB liability, the derivative reinsurance arrangement and the related derivative contracts that were purchased as economic hedges, the net effect of which was a $26 loss, $46 loss and $8 gain, before deferred policy acquisition costs and tax effects, respectively.

A contract is in the money if the contract holder s GRB is greater than the account value. For contracts that were in the money , the Company s exposure as of December 31, 2006, was $8. However, the only ways the contract holder can monetize the excess of the GRB over the account value of the contract is upon death or if their account value is reduced to zero through a combination of a series of withdrawals that do not exceed a specific percentage of the premiums paid per year and market declines. If the account value is reduced to zero, the contract holder will receive a period certain annuity equal to the remaining GRB. As the amount of the excess of the GRB over the account value can fluctuate with equity market returns on a daily basis the ultimate amount to be paid by the Company, if any, is uncertain and could be significantly more or less than $8.

Separate Accounts

The Company maintains separate account assets and liabilities, which are reported at fair value. Separate accounts include contracts, wherein the policyholder assumes the investment risk. Separate account assets are segregated from other investments and investment income and gains and losses accrue directly to the policyholder.

Deferred Policy Acquisition Costs and Present Value of Future Profits

Life Life policy acquisition costs include commissions and certain other expenses that vary with and are primarily associated with acquiring business. Present value of future profits (PVFP) is an intangible asset recorded upon applying purchase accounting in an acquisition of a life insurance company. Deferred policy acquisition costs and the present value of future profits intangible asset are amortized in the same way. Both are amortized over the estimated life of the contracts acquired. Within the following discussion, deferred policy acquisition costs and the present value of future profits intangible asset will be referred to as DAC . At December 31, 2006 and December 31, 2005, the carrying value of the Company s Life DAC asset was $9.1 billion and $8.6 billion, respectively. Of those amounts, $4.4 billion and $4.5 billion related to individual variable annuities sold in the U.S., $1.4 billion and $1.2 billion related to individual variable annuities sold in Japan and $2.1 billion and $1.9 billion related to universal life-type contracts sold by Individual Life.

The Company amortizes DAC related to investment contracts and universal life-type contracts (including individual variable annuities) using the retrospective deposit method. Under the retrospective deposit method, acquisition costs are amortized in proportion to the present value of estimated gross profits (EGPs). EGPs are also used to amortize other assets and liabilities on the Company s balance sheet, such as sales inducement assets and unearned revenue reserves. Components of EGPs are used to determine reserves for guaranteed minimum death and income benefits. For most contracts, the Company evaluates EGPs over a 20 year horizon as estimated profits emerging subsequent to year 20 are immaterial. The Company uses other measures for amortizing DAC, such as gross costs (net of reinsurance), as a replacement for EGPs when EGPs are expected to be negative for multiple years of the contract s life. The Company also adjusts the DAC balance, through other comprehensive income, by an amount that represents the amortization of DAC that would have been required as a charge or credit to operations had unrealized gains and losses

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

on investments been realized. Actual gross profits, in a given reporting period, that vary from management s initial estimates result in increases or decreases in the rate of amortization, commonly referred to as a true-up , which are recorded in the current period. The true-up recorded for the years ended December 31, 2006, 2005 and 2004 was an increase to amortization of $41, $18 and $16, respectively.

Each year, the Company develops future EGPs for the products sold during that year. The EGPs for products sold in a particular year are aggregated into cohorts. Future gross profits are projected for the estimated lives of the contracts, and are, to a large extent, a function of future account value projections for individual variable annuity products and to a lesser extent for variable universal life products. The projection of future account values requires the use of certain assumptions. The assumptions considered to be important in the projection of future account value, and hence the EGPs, include separate account fund performance, which is impacted by separate account fund mix, less fees assessed against the contract holder s account balance, surrender and lapse rates, interest margin, and mortality. The assumptions are developed as part of an annual process and are dependent upon the Company s current best estimates of future events. The Company s current aggregate separate account return assumption is approximately 8.0% (after fund fees, but before mortality and expense charges) for U.S. products and 5.0% (after fund fees, but before mortality and expense charges) in aggregate for all Japanese products, but varies from product to product. The overall actual return generated by the separate account is dependent on several factors, including the relative mix of the underlying sub-accounts among bond funds and equity funds as well as equity sector weightings. The Company s overall U.S. separate account fund performance has been reasonably correlated to the overall performance of the S&P 500 Index (which closed at 1,418 on December 29, 2006), although no assurance can be provided that this correlation will continue in the future.

Estimating future gross profits is a complex process requiring considerable judgment and the forecasting of events well into the future. Estimating future gross profits is important not only for determining the amortization of DAC but also in the accounting and valuation of sales inducement assets, unearned revenue reserves and guaranteed minimum death and income benefit reserves. The estimation process, the underlying assumptions and the resulting EGPs, are evaluated regularly.

During the fourth quarter of 2006, the Company refined its estimation process for DAC amortization and completed a comprehensive study of assumptions. The Company plans to complete a comprehensive assumption study and refine its estimate of future gross profits in the third quarter of 2007 and at least annually thereafter.

Upon completion of an assumption study, the Company revises its assumptions to reflect its current best estimate, thereby changing its estimate of projected account values and the related EGPs in the DAC, sales inducement and unearned revenue reserve amortization models as well as the guaranteed minimum death and income benefit reserving models. The cumulative balance of DAC as well as sales inducement assets, unearned revenue reserves and guaranteed minimum death and income benefit reserves are adjusted with an offsetting benefit or charge to income to reflect such changes in the period of the revision, a process known as unlocking . An unlock that results in an after-tax benefit generally occurs as a result of actual experience or future expectations being favorable compared to previous estimates of account value growth and EGPs. An unlock that results in an after-tax charge generally occurs as a result of actual experience or future expectations being unfavorable compared to previous estimates of account value growth and EGPs.

In addition to when a comprehensive assumption study is completed, revisions to best estimate assumptions used to estimate future gross profits are necessary when the EGPs in the Company s models fall outside of a reasonable range of EGPs. The Company performs a quantitative process each quarter to determine the reasonable range of EGPs. This process involves the use of internally developed models, which run a large number of stochastically determined scenarios of separate account fund performance. Incorporated in each scenario are assumptions with respect to lapse rates, mortality, and expenses, based on the Company s most recent assumption study. These scenarios are run for individual variable annuity business in the U.S. and independently for individual variable annuity business in Japan and are used to calculate statistically significant ranges of reasonable EGPs. The statistical ranges produced from the stochastic scenarios are compared to the present value of EGPs used in the Company s models. If EGPs used in the Company s models fall outside of the statistical ranges of reasonable EGPs, an unlock would be necessary. A similar approach is used for variable universal life business.

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

Unlock Results

As described above, during the fourth quarter of 2006, the Company completed a comprehensive study of assumptions underlying EGPs, resulting in an unlock . The study covered all assumptions, including mortality, lapses, expenses and separate account returns, in substantially all product lines. The new best estimate assumptions were applied to the current in-force to project future gross profits. The impact on the Company s assets and liabilities as a result of the unlock during the fourth quarter was as follows:

Segment After-tax (charge) benefit	DAC and PVFP	Unearned Revenue Reserves	Death and Income Benefit Reserves [1]	Sales Inducement Assets	Total
Retail Products Group	$ (70)	$ 5	$ (10)	$ 3	$(72)
Retirement Plans	20				20
Individual Life	(49)	31			(18)
International Japan Annuity	26		27		53
Life Other	(46)				(46)
Corporate	(13)				(13)
Total	**$(132)**	**$36**	**$ 17**	**$ 3**	**$(76)**

[1] As a result of the unlock, death benefit reserves, in the Retail Products Group, increased $294, offset by an increase of $279 in reinsurance recoverables.

An unlock only revises EGPs to reflect current best estimate assumptions. The Company must also test the aggregate recoverability of the DAC asset by comparing the amounts deferred to the present value of total EGPs. In addition, the Company routinely stress tests its DAC asset for recoverability against severe declines in its separate account assets, which could occur if the equity markets experienced a significant sell-off, as the majority of policyholders funds in the separate accounts is invested in the equity market. As of December 31, 2006, the Company believed U.S. individual and Japan individual variable annuity separate account assets could fall, through a combination of negative market returns, lapses and mortality, by at least 53% and 70%, respectively, before portions of its DAC asset would be unrecoverable.

Property & Casualty The Property & Casualty operations also incur costs, including commissions, premium taxes and certain underwriting and policy issuance costs, that vary with and are related primarily to the acquisition of property and casualty insurance business. These costs are deferred and amortized ratably over the period the related premiums are earned. Deferred acquisition costs are reviewed to determine if they are recoverable from future income, and if not, are charged to expense. Anticipated investment income is considered in the determination of the recoverability of deferred policy acquisition costs. For the years ended December 31, 2006, 2005 and 2004, no material amounts of deferred policy acquisition costs were charged to expense based on the determination of recoverability.

Reserve for Future Policy Benefits and Unpaid Losses and Loss Adjustment Expenses

Life Liabilities for the Company s group life and disability contracts as well its individual term life insurance policies include amounts for unpaid losses and future policy benefits. Liabilities for unpaid losses include estimates of amounts to fully settle known reported claims as well as claims related to insured events that the Company estimates have been incurred but have not yet been reported. Liabilities for future policy benefits are calculated by the net level premium method using interest, withdrawal and mortality assumptions appropriate at the time the policies were issued. The methods used in determining the liability for unpaid losses and future policy benefits are standard actuarial methods recognized by the American Academy of Actuaries. For the tabular reserves, discount rates are based on the Company s earned investment yield and the morbidity/mortality tables used are standard industry tables modified to reflect the Company s actual experience when appropriate. In particular, for the Company s group disability known claim reserves, the morbidity table for the early durations of claim is based exclusively on the Company s experience, incorporating factors such as gender, elimination period and diagnosis. These reserves are computed such that they are expected to meet the Company s future policy obligations. Future policy benefits are computed at amounts that, with additions from estimated premiums to be received and with interest on such reserves compounded annually at certain assumed rates, are expected to be sufficient to meet the Company s policy obligations at their maturities or in the event of an insured s death. Changes in or deviations from the assumptions used for mortality, morbidity, expected future premiums and interest can significantly affect the Company s reserve levels and related future operations and, as such, provisions for adverse deviation are built into the long-tailed liability assumptions. Certain contracts classified as universal life-type may also include additional death or other insurance benefit features, such as guaranteed minimum death or income benefits offered with variable annuity contracts or no lapse guarantees offered with universal life insurance contracts. An additional liability is established for these benefits by estimating the expected present value of the

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1. Basis of Presentation and Accounting Policies (continued)

benefits in excess of the projected account value in proportion to the present value of total expected assessments. Excess benefits is accrued as a liability as actual assessments are recorded. Determination of the expected value of excess benefits and assessments are based on a range of scenarios and assumptions including those related to market rates of return and volatility, contract surrender rates and mortality experience. Revisions to assumptions are made consistent with the Company s process for a DAC unlock. See Life Deferred Policy Acquisition Costs and Present value of Future Benefits in the Note.

Property & Casualty The Hartford establishes property and casualty reserves to provide for the estimated costs of paying claims under insurance policies written by the Company. These reserves include estimates for both claims that have been reported and those that have been incurred but not reported, and include estimates of all losses and loss adjustment expenses associated with processing and settling these claims. Estimating the ultimate cost of future losses and loss adjustment expenses is an uncertain and complex process. This estimation process is based significantly on the assumption that past developments are an appropriate predictor of future events, and involves a variety of actuarial techniques that analyze experience, trends and other relevant factors. The uncertainties involved with the reserving process have become increasingly difficult due to a number of complex factors including social and economic trends and changes in the concepts of legal liability and damage awards. Accordingly, final claim settlements may vary from the present estimates, particularly when those payments may not occur until well into the future.

The Hartford regularly reviews the adequacy of its estimated losses and loss adjustment expense reserves by line of business within the various operating segments. Adjustments to previously established reserves are reflected in the operating results of the period in which the adjustment is determined to be necessary. Such adjustments could possibly be significant, reflecting any variety of new and adverse or favorable trends.

Most of the Company s property and casualty reserves are not discounted. However, certain liabilities for unpaid claims for permanently disabled claimants have been discounted to present value using an average interest rate of 5.6% in 2006 and 2005, respectively. As of December 31, 2006 and 2005, such discounted reserves totaled $707 and $680, respectively (net of discounts of $510, and $505, respectively). In addition, certain structured settlement contracts, that fund loss run-offs for unrelated parties having payment patterns that are fixed and determinable, have been discounted to present value using an average interest rate of 5.5%. At December 31, 2006 and 2005, such discounted reserves totaled $273 and $264, respectively (net of discounts of $95 and $103, respectively). Accretion of these discounts did not have a material effect on net income during 2006 or 2005.

Other Policyholder Funds and Benefits Payable

The Company has classified its fixed and variable annuities, 401(k), certain governmental annuities, private placement life insurance (PPLI), variable universal life insurance, universal life insurance and interest sensitive whole life insurance as universal life-type contracts. The liability for universal life-type contracts is equal to the balance that accrues to the benefit of the policyholders as of the financial statement date (commonly referred to as the account value), including credited interest, amounts that have been assessed to compensate the Company for services to be performed over future periods, and any amounts previously assessed against policyholders that are refundable on termination of the contract.

The Company has classified its institutional and governmental products, without life contingencies, including funding agreements, certain structured settlements and guaranteed investment contracts, as investment contracts. The liability for investment contracts is equal to the balance that accrues to the benefit of the contract holder as of the financial statement date, which includes the accumulation of deposits plus credited interest, less withdrawals and amounts assessed through the financial statement date. Contract holder funds include funding agreements held by Variable Interest Entities issuing medium-term notes.

Revenue Recognition

Life For investment and universal life-type contracts, the amounts collected from policyholders are considered deposits and are not included in revenue. Fee income for universal life-type contracts consists of policy charges for policy administration, cost of insurance charges and surrender charges assessed against policyholders account balances and are recognized in the period in which services are provided. For the Company s traditional life and group disability products premiums are recognized as revenue when due from policyholders.

Property & Casualty Property and casualty insurance premiums are earned on a pro rata basis over the lives of the policies and include accruals for ultimate premium revenue anticipated under auditable and retrospectively rated policies. Unearned premiums represent the premiums applicable to the unexpired terms of policies in force. An estimated allowance for doubtful accounts is recorded on the basis of periodic evaluations of balances due from insurers, management s experience and current economic conditions. The allowance for doubtful accounts included in premiums receivable and agents balances in the consolidated balance sheets was \$114 and \$120 as of December 31, 2006 and 2005, respectively. Other revenue consists primarily of revenues associated with the Company s servicing businesses.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

Foreign Currency Translation

Foreign currency translation gains and losses are reflected in stockholders equity as a component of accumulated other comprehensive income. The Company s foreign subsidiaries balance sheet accounts are translated at the exchange rates in effect at each year end and income statement accounts are translated at the average rates of exchange prevailing during the year. The national currencies of the international operations are generally their functional currencies.

Dividends to Policyholders

Policyholder dividends are paid to certain life and property and casualty policies, which are referred to as participating policies. Such dividends are accrued using an estimate of the amount to be paid based on underlying contractual obligations under policies and applicable state laws.

Life Participating life insurance in force accounted for 3%, 3% and 5% as of December 31, 2006, 2005 and 2004, respectively, of total life insurance in force. Dividends to policyholders were $22, $37 and $29 for the years ended December 31, 2006, 2005 and 2004, respectively. There were no additional amounts of income allocated to participating policyholders. If limitations exist on the amount of net income from participating life insurance contracts that may be distributed to stockholders, the policyholder s share of net income on those contracts that cannot be distributed is excluded from stockholders equity by a charge to operations and a credit to a liability.

Property & Casualty Net written premiums for participating property and casualty insurance policies represented 8%, 10% and 8% of total net written premiums for the years ended December 31, 2006, 2005 and 2004, respectively. Dividends to policyholders were $6, $11 and $12 for the years ended December 31, 2006, 2005 and 2004, respectively.

Mutual Funds

The Company maintains a retail mutual fund operation, whereby the Company, through wholly-owned subsidiaries, provides investment management and administrative services to The Hartford Mutual Funds, Inc. and The Hartford Mutual Funds II, Inc (The Hartford mutual funds), families of 52 mutual funds and 1 closed end fund. The Company charges fees to the shareholders of the mutual funds, which are recorded as revenue by the Company. Investors can purchase shares in the mutual funds, all of which are registered with the Securities and Exchange Commission (SEC), in accordance with the Investment Company Act of 1940.

The mutual funds are owned by the shareholders of those funds and not by the Company. As such, the mutual fund assets and liabilities and related investment returns are not reflected in the Company s consolidated financial statements since they are not assets, liabilities and operations of the Company.

Reinsurance

Through both facultative and treaty reinsurance agreements, the Company cedes a share of the risks it has underwritten to other insurance companies. Assumed reinsurance refers to the Company s acceptance of certain insurance risks that other insurance companies have underwritten.

Reinsurance accounting is followed for ceded and assumed transactions when the risk transfer provisions of SFAS 113, Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts, have been met. To meet risk transfer requirements, a reinsurance contract must include insurance risk, consisting of both underwriting and timing risk, and a reasonable possibility of a significant loss to the reinsurer.

Earned premiums and incurred losses and loss adjustment expenses reflect the net effects of ceded and assumed reinsurance transactions. Included in other assets are prepaid reinsurance premiums, which represent the portion of premiums ceded to reinsurers applicable to the unexpired terms of the reinsurance contracts. Reinsurance recoverables include balances due from reinsurance companies for paid and unpaid losses and loss adjustment expenses and are presented net of an allowance for uncollectible reinsurance. The allowance for uncollectible reinsurance was $412 and $413 as of December 31, 2006 and 2005, respectively.

Income Taxes

The Company recognizes taxes payable or refundable for the current year and deferred taxes for the tax consequences of differences between the financial reporting and tax basis of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years the temporary differences are expected to reverse.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

1. Basis of Presentation and Accounting Policies (continued)

Property and Equipment

Property and equipment is carried at cost net, of accumulated depreciation. Depreciation is based on the estimated useful lives of the various classes of property and equipment and is determined principally on the straight-line method. Accumulated depreciation was $1.2 billion as of December 31, 2006 and 2005, respectively. Depreciation expense was $193, $206 and $156 for the years ended December 31, 2006, 2005 and 2004, respectively.

2. Earnings per Share

Earnings per share amounts have been computed in accordance with the provisions of SFAS No. 128, Earnings per Share . The following tables present a reconciliation of net income and shares used in calculating basic earnings per share to those used in calculating diluted earnings per share.

(In millions, except for per share data)

2006	**Net Income**	**Shares**	**Per Share Amount**
Basic Earnings per Share			
Net income available to common shareholders	$2,745	308.8	$ 8.89
Diluted Earnings per Share			
Stock compensation plans		3.0	
Equity Units		4.1	
Net income available to common shareholders plus assumed conversions	$2,745	315.9	$ 8.69
2005			
Basic Earnings per share			
Net income available to common shareholders	$2,274	298.0	$ 7.63
Diluted Earnings per Share			
Stock compensation plans		3.3	
Equity Units		4.3	
Net income available to common shareholders plus assumed conversions	$2,274	305.6	$ 7.44
2004			
Basic Earnings per Share			
Net income available to common shareholders	$2,115	292.3	$ 7.24
Diluted Earnings per Share			
Stock compensation plans		2.8	
Equity Units		1.9	

Net income available to common shareholders plus assumed conversions	$2,115	297.0	$ 7.12

Basic earnings per share is computed based on the weighted average number of shares outstanding during the year. Diluted earnings per share include the dilutive effect of stock compensation plans and the Company s equity units, if any, using the treasury stock method. Under the treasury stock method for stock compensation plans, shares are assumed to be issued and then reduced for the number of shares repurchaseable with theoretical proceeds at the average market price for the period. Contingently issuable shares are included for the number of shares issuable assuming the end of the reporting period was the end of the contingency period, if dilutive.

Theoretical proceeds include option exercise price payments, unamortized stock compensation expense and tax benefits realized in excess of the tax benefit recognized in net income. The difference between the number of shares assumed issued and number of shares purchased represents the dilutive shares. Under the treasury stock method for the equity units, the number of shares of common stock used in calculating diluted earnings per share is increased by the excess, if any, of the number of shares issuable upon settlement of the purchase contracts, over the number of shares that could be purchased by The Hartford in the market using the proceeds received upon settlement. The number of issuable shares is based on the average market price for the last 20 trading days of the period. The number of shares purchased is based on the average market price during the entire period.

Upon exercise of outstanding options or vesting of other stock compensation plan awards, the additional shares issued and outstanding are included in the calculation of the Company s weighted average shares from the date of exercise or vesting. Similarly, upon settlement of the purchase contracts associated with the Company s equity units, the associated common shares are added to the Company s issued and outstanding shares. During the 20 trading day period ending on the third trading day prior to August 16, 2006, The Hartford s common stock price exceeded $56.875 per share. As a result, on August 16, 2006, the 7% equity unit purchase

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

2. Earnings per Share (continued)

contracts issued in 2003 were settled, resulting in the issuance of approximately 12.1 million common shares that were added to the Company s issued and outstanding shares and were included in the calculation of the Company s weighted average shares for the period the shares were outstanding. Additionally, in connection with the settlement on November 16, 2006 of the 6% equity units issued in 2002, The Hartford s common stock price exceeded $57.645 per share during the 20 trading day period ending on the third trading day period prior to November 16, 2006, resulting in the issuance of approximately 5.7 million common shares that were added to the Company s issued and outstanding shares and were included in the calculation of the Company s weighted average shares for the period the shares were outstanding. For further discussion of the Company s equity units offerings, see Note 14.

3. Segment Information

The Hartford is organized into two major operations: Life and Property & Casualty, each containing reporting segments. Within the Life and Property & Casualty operations, The Hartford conducts business principally in ten operating segments. Additionally, Corporate primarily includes the Company s debt financing and related interest expense, as well as certain capital raising activities and purchase accounting adjustments.

Life

Life s business is conducted by Hartford Life, Inc. (Hartford Life or Life), an indirect subsidiary of The Hartford, headquartered in Simsbury, Connecticut, and is a leading financial services and insurance organization. Life includes six reportable operating segments: Retail Products Group (Retail), Retirement Plans, Institutional Solutions Group (Institutional), Individual Life, Group Benefits and International.

Retail offers individual variable and fixed market value adjusted (MVA) annuities, retail mutual funds, 529 college savings plans, Canadian and offshore investment products.

Retirement Plans provides products and services to corporations pursuant to Section 401(k) and products and services to municipalities and not-for-profit organizations under Section 457 and 403(b) of the IRS code. Retirement also offers mutual funds to institutional investors.

Institutional primarily offers institutional liability products, including stable value products, structured settlements and institutional annuities (primarily terminal funding cases), as well as variable Private Placement Life Insurance (PPLI) owned by corporations and high net worth individuals. Within stable value, Institutional has an investor note program that offers both institutional and retail investor notes. Institutional and Retail notes are sold as funding agreement backed notes through trusts and may also be issued directly from the company to investors. Institutional also offers mutual funds to institutional investors. Furthermore, Institutional offers additional individual products including structured settlements, single premium immediate annuities and longevity assurance.

Individual Life sells a variety of life insurance products, including variable universal life, universal life, interest sensitive whole life and term life.

Group Benefits provides employers, associations, affinity groups and financial institutions with group life, accident and disability coverage, along with other products and services, including voluntary benefits, group retiree health, and medical stop loss.

International, which has operations located in Japan, Brazil, Ireland and the United Kingdom, provides investments, retirement savings and other insurance and savings products to individuals and groups outside the United States and Canada.

Life charges direct operating expenses to the appropriate segment and allocates the majority of indirect expenses to the segments based on an intercompany expense arrangement. Intersegment revenues primarily occur between Life s Other category and the operating segments. These amounts primarily include interest income on allocated surplus, interest charges on excess separate account surplus, the allocation of certain net realized capital gains and losses and the allocation of credit risk charges.

The accounting policies of the reportable operating segments are the same as those described in the summary of significant accounting policies in Note 1. Life evaluates performance of its segments based on revenues, net income and the segment s return on allocated capital. Each operating segment is allocated corporate surplus as needed to support its business. Portfolio management is a corporate function and net realized capital gains and losses on invested assets are recognized in Life s Other category. Net realized capital gains and losses generated from credit related events, other than net periodic coupon settlements on credit derivatives, are retained by Corporate. However, in exchange for retaining credit related losses, the Other category charges each operating segment a credit-risk fee through realized capital gains and losses.

The credit-risk fee covers fixed income assets included in each operating segment s general account. The credit-risk fee is based upon historical default rates in the corporate bond market, the Company s actual default experience and estimates of future losses.

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

3. Segment Information (continued)

The positive (negative) impact on realized gains and losses of the segments for allocated interest rate related realized gains and losses and the credit-risk fees were as follows:

	2006	2005	2004
Retail			
Realized gains (losses)	$ 32	$ 34	$ 24
Credit risk fees	(26)	(26)	(22)
Retirement Plans			
Realized gains (losses)	10	6	5
Credit risk fees	(9)	(8)	(8)
Institutional			
Realized gains (losses)	17	13	9
Credit risk fees	(23)	(19)	(17)
Individual Life			
Realized gains (losses)	11	11	13
Credit risk fees	(7)	(6)	(6)
Group Benefits			
Realized gains (losses)	3	10	8
Credit risk fees	(9)	(9)	(9)
International			
Realized gains (losses)	1		
Credit risk fees	(2)		
Other			
Realized gains (losses)	(74)	(74)	(59)
Credit risk fees	76	68	62
Total	**$**	**$**	**$**

Property & Casualty

Property & Casualty is organized into four reportable operating segments: the underwriting segments of Business Insurance, Personal Lines, and Specialty Commercial (collectively Ongoing Operations); and the Other Operations segment.

Business Insurance provides standard commercial insurance coverage to small commercial and middle market commercial businesses primarily throughout the United States. This segment offers workers compensation, property, automobile, liability, umbrella and marine coverages. Commercial risk management products and services are also provided.

Personal Lines provides automobile, homeowners and home-based business coverages to the members of AARP through a direct marketing operation and to individuals who prefer local agent involvement through a network of independent agents in the standard personal lines market. Up until the sale of the business on November 30, 2006, the Company also sold non-standard auto insurance through the Company s Omni Insurance Group, Inc. (Omni) subsidiary (refer to Note 20 for further discussion). Personal Lines also operates a member contact center for health insurance products offered through AARP s Health Care Options. AARP accounts for earned premiums of $2.5 billion, $2.3 billion and $2.1 billion in 2006, 2005 and 2004, respectively, which represented 24%, 23% and 23% of total Property & Casualty earned premiums in 2006, 2005 and 2004, respectively.

The Specialty Commercial segment offers a variety of customized insurance products and risk management services. Specialty Commercial provides standard commercial insurance products including workers compensation, automobile and liability coverages to large-sized companies. Specialty Commercial also provides professional liability, fidelity, surety, specialty casualty and livestock coverages, core property and excess and surplus lines coverages not normally written by standard lines insurers, and insurance products and services to captive insurance companies, pools and self-insurance groups. In addition, Specialty Commercial provides third party administrator services for claims Administration, integrated benefits, loss control and performance measurement through Specialty Risk Services, a subsidiary of the Company.

The Other Operations segment consists of certain property and casualty insurance operations of The Hartford which have discontinued writing new business and includes substantially all of the Company s asbestos and environmental exposures.

Through inter-segment arrangements, Specialty Commercial reimburses Business Insurance and Personal Lines for certain losses, including, among other coverages, losses incurred from uncollectible reinsurance. In addition, the Company retains a portion of the

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

3. Segment Information (continued)

risks ceded under the Company s principal catastrophe reinsurance program and other reinsurance programs and the financial results of the Company s retention are recorded in the Specialty Commercial segment. Apart from the Company s retention, the amount of premiums ceded to third party reinsurers under the principal catastrophe reinsurance program and other reinsurance programs are allocated to the operating segments based on the risks written by each operating segment that are subject to the programs.

Earned premiums assumed (ceded) under the inter-segment arrangements and retention were as follows:

Net assumed (ceded) earned premiums under inter-segment arrangements and retention	**For the years ended December 31, 2006**	**2005**	**2004**
Business Insurance	$ (73)	$ (78)	$ (34)
Personal Lines	(21)	(25)	(21)
Specialty Commercial	94	103	55
Total	**$**	**$**	**$**

Financial Measures and Other Segment Information

The measure of profit or loss used by The Hartford s management in evaluating the performance of its Life segments is net income. Net income is the measure of profit or loss used in evaluating the performance of Ongoing Operations and the Other Operations segment. Within Ongoing Operations, the underwriting segments of Business Insurance, Personal Lines and Specialty Commercial are evaluated by The Hartford s management primarily based upon underwriting results. Underwriting results represent premiums earned less incurred losses, loss adjustment expenses and underwriting expenses. The sum of underwriting results, net investment income, net realized capital gains and losses, other expenses, and related income taxes is net income (loss).

Certain transactions between segments occur during the year that primarily relate to tax settlements, insurance coverage, expense reimbursements, services provided, security transfers and capital contributions. In addition, certain reinsurance stop loss arrangements exist between the segments which specify that one segment will reimburse another for losses incurred in excess of a predetermined limit. Also, one segment may purchase group annuity contracts from another to fund pension costs and annuities to settle casualty claims. In addition, certain intersegment transactions occur in Life. These transactions include interest income on allocated surplus and the allocation of certain net realized capital gains and losses through net investment income utilizing the duration of the segment s investment portfolios. Consolidated Life net investment income and net realized capital gains and losses are unaffected by such transactions.

The following tables present revenues and net income (loss). Underwriting results are presented for the Business Insurance, Personal Lines and Specialty Commercial segments, while net income is presented for each of Life s reportable segments, total Property & Casualty Ongoing Operations, Property & Casualty Other Operations and Corporate.

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

3. Segment Information (continued)

Revenues by Product Line	**For the years ended December 31,**		
Revenues	**2006**	**2005**	**2004**
Life			
Earned premiums, fees, and other considerations			
Retail			
Individual annuity	$ 1,959	$ 1,780	$ 1,618
Retail mutual funds	524	416	393
Other	128	77	13
Total Retail	2,611	2,273	2,024
Retirement Plans			
401(k)	159	111	81
Governmental	52	51	50
Total Retirement Plans	211	162	131
Institutional			
Institutional	630	518	474
PPLI	101	105	150
Total Institutional	731	623	624
Individual Life			
Total Individual Life	830	769	746
Group Benefits			
Group disability	1,850	1,749	1,602
Group life	1,830	1,643	1,655
Other	470	418	395
Total Group Benefits	4,150	3,810	3,652
International			
Total International	700	483	240
Other	83	83	119
Total Life premiums, fees, and other considerations	9,316	8,203	7,536
Net investment income			
Securities available-for-sale and other	3,184	2,998	2,876
Equity securities held for trading	1,824	3,847	799
Net investment income	5,008	6,845	3,675
Net realized capital gains (losses)	(260)	(25)	164
Total Life	**14,064**	**15,023**	**11,375**
Property & Casualty			

Ongoing Operations			
Earned premiums			
Business Insurance			
Workers Compensation	2,001	1,791	1,512
Property	1,427	1,348	1,235
Automobile	772	780	754
Liability	454	453	445
Other	464	413	353
Total Business Insurance	5,118	4,785	4,299
Personal Lines			
Automobile	2,792	2,728	2,622
Homeowners	968	882	823
Total Personal Lines	3,760	3,610	3,445
Specialty Commercial			
Workers Compensation	79	72	61
Property	113	136	201
Automobile	19	18	21
Liability	40	51	46
Fidelity and surety	231	210	188
Professional Liability	419	345	335
Other	649	925	874
Total Specialty Commercial	1,550	1,757	1,726
Total Ongoing Operations	10,428	10,152	9,470
Other Operations	5	4	24
Total earned premiums	10,433	10,156	9,494
Servicing revenue	473	463	436
Net investment income	1,486	1,365	1,248
Net realized capital gains	9	44	133
Total Property & Casualty	**12,401**	**12,028**	**11,311**
Corporate	**35**	**32**	**22**
Total revenues	**$26,500**	**$27,083**	**$22,708**

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
3. Segment Information (continued)

	For the years ended December 31,		
Net Income (Loss)	**2006**	**2005**	**2004**
Life			
Retail	$ 628	$ 622	$ 503
Retirement Plans	109	75	66
Institutional	99	88	68
Individual Life	170	166	155
Group Benefits	303	272	229
International	246	96	39
Other [1] [2]	(114)	(115)	322
Total Life	1,441	1,204	1,382
Property & Casualty			
Ongoing Operations			
Underwriting Results			
Business Insurance	618	396	360
Personal Lines	429	460	138
Specialty Commercial	64	(165)	(53)
Total Ongoing Operations underwriting results	1,111	691	445
Net servicing and other income [3]	53	49	42
Net investment income	1,225	1,082	903
Net realized capital gains (losses)	(17)	19	98
Other expenses	(222)	(202)	(198)
Income tax expense [1]	(596)	(474)	(335)
Ongoing Operations	1,554	1,165	955
Other Operations	(35)	71	(45)
Total Property & Casualty	1,519	1,236	910
Corporate	(215)	(166)	(177)
Net income	**$2,745**	**$2,274**	**$2,115**

[1] For the year ended December 31, 2004 Life includes a $190 tax benefit recorded in its

Other category, and Property & Casualty includes a $26 tax benefit, which relate to an agreement with the IRS on the resolution of matters pertaining to tax years prior to 2004. For further discussion of this tax benefit, see Note 12.

[2] *Amount for the year ended December 31, 2005, reflects an after-tax charge of $102 to reserve for investigations related to market timing by the SEC and New York Attorney General s Office, directed brokerage by the SEC and single premium group annuities by the New York Attorney General s Office and the Connecticut Attorney General s Office, as discussed in Note 12.*

[3] *Amount is net of expenses related to service*

business.

Amortization of deferred policy acquisition costs and present value of future profits	**For the years ended December 31, 2006**	**2005**	**2004**
Life			
Retail	$ 930	$ 744	$ 647
Retirement Plans	1	26	29
Institutional	32	32	26
Individual Life	241	205	185
Group Benefits	41	31	23
International	167	133	77
Other	40	1	6
Total Life	1,452	1,172	993
Property & Casualty			
Ongoing Operations			
Business Insurance	1,184	1,138	1,058
Personal Lines	622	581	530
Specialty Commercial	300	281	257
Total Ongoing Operations	2,106	2,000	1,845
Other Operations		(3)	5
Total Property & Casualty	2,106	1,997	1,850
Total amortization of deferred policy acquisition costs and present value of future profits	**$ 3,558**	**$ 3,169**	**$ 2,843**

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

3. Segment Information (continued)

Income tax expense	For the years ended December 31, 2006	2005	2004
Life			
Retail	$ 85	$ 85	$ 105
Retirement Plans	43	23	22
Institutional	36	32	26
Individual Life	72	72	71
Group Benefits	111	90	83
International	135	65	12
Other [1]	(59)	(51)	(117)
Total Life	423	316	202
Property & Casualty			
Ongoing Operations [1]	596	474	335
Other Operations	(45)	10	(60)
Total Property & Casualty	551	484	275
Corporate	(117)	(89)	(92)
Total income tax expense	**$ 857**	**$711**	**$ 385**

[1] For the year ended December 31, 2004 Life includes a $190 tax benefit recorded in its Other category, and Property & Casualty includes a $26 tax benefit, which relate to an agreement with the IRS on the resolution of matters pertaining to tax years prior to 2004. For further discussion of

this tax benefit, see Note 12.

Geographical Segment Information	**For the years ended December 31,**		
Revenues	**2006**	**2005**	**2004**
North America	$23,840	$22,349	$21,328
Other	2,660	4,734	1,380
Total revenues	**$26,500**	**$27,083**	**$22,708**

	As of December 31,	
Assets	**2006**	**2005**
Life		
Retail	$130,138	$120,438
Retirement Plans	24,394	20,064
Institutional	66,383	48,825
Individual Life	14,306	12,950
Group Benefits	9,056	8,438
International	33,890	27,822
Other	5,581	5,283
Total Life	283,748	243,820
Property & Casualty		
Ongoing Operations	34,167	31,780
Other Operations	6,852	8,502
Total Property & Casualty	41,019	40,282
Corporate	1,943	1,455
Total Assets	$**326,710**	$**285,557**

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

4. Investments and Derivative Instruments

	For the years ended December 31,		
Components of Net Investment Income	**2006**	**2005**	**2004**
Fixed maturities	$4,266	$3,952	$3,689
Equity securities held for trading	1,824	3,847	799
Policy loans	142	144	186
Mortgage loans on real estate	158	84	59
Other investments	212	267	265
Gross investment income	6,602	8,294	4,998
Less: Investment expenses	87	63	55
Net investment income	**$6,515**	**$8,231**	**$4,943**

Components of Net Realized Capital Gains (Losses)			
Fixed maturities	$(113)	$ 95	$297
Equity securities	(11)	3	3
Foreign currency transaction remeasurements	17	162	(7)
Derivatives and other [1]	(144)	(243)	(2)
Net realized capital gains (losses)	**$(251)**	**$ 17**	**$291**

[1] Primarily consists of changes in fair value on non-qualifying derivatives, changes in fair value of certain derivatives in fair value hedge relationships and hedge ineffectiveness on qualifying derivative instruments.

Components of Net Unrealized Gains (Losses) on Available-for-Sale Securities

Fixed maturities	$1,466	$ 1,674	$3,741
Equity securities	204	131	90
Net unrealized gains credited to policyholders	(4)	(9)	(20)
Net unrealized gains	1,666	1,796	3,811
Deferred income taxes	608	827	1,649
Net unrealized gains, net of tax end of year	1,058	969	2,162
Net unrealized gains, net of tax beginning of year	969	2,162	1,764
Change in unrealized gains (losses) on available-for-sale securities	**$ 89**	**$(1,193)**	**$ 398**

The change in net unrealized gain on equity securities classified as trading is included in net investment income during the years ended December 31, 2006, 2005 and 2004, was $1.3 billion, $3.6 billion and $710, respectively, substantially all of which have corresponding amounts credited to policyholders. This amount was not included in the gross unrealized gains (losses) in the table above.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

4. Investments and Derivative Instruments (continued)

Components of Fixed Maturity Investments

	As of December 31, 2006				As of December 31, 2005			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Bonds and Notes								
ABS	$ 7,924	$ 54	$ (53)	$ 7,925	$ 7,907	$ 60	$ (89)	$ 7,878
Collateralized mortgage obligations (CMOs)								
Agency backed	1,184	17	(8)	1,193	860	3	(6)	857
Non-agency backed	116		(1)	115	133			133
CMBS								
Agency backed	756	12	(1)	767	70	1		71
Non-agency backed	15,823	220	(144)	15,899	12,860	233	(162)	12,931
Corporate	35,069	1,193	(371)	35,891	33,019	1,395	(396)	34,018
Government/Government agencies								
Foreign	1,213	87	(6)	1,294	1,378	96	(7)	1,467
United States	848	5	(7)	846	877	27	(6)	898
Mortgage-backed securities (MBS) agency backed	2,742	5	(45)	2,702	3,914	7	(60)	3,861
States, municipalities and political subdivisions	11,897	536	(27)	12,406	11,641	601	(24)	12,218
Redeemable preferred stock	36			36	44	1		45
Short-term investments	1,681			1,681	2,063			2,063
Total fixed maturities	**$79,289**	**$2,129**	**$(663)**	**$80,755**	**$74,766**	**$2,424**	**$(750)**	**$76,440**

The amortized cost and estimated fair value of fixed maturity investments at December 31, 2006 by contractual maturity year are shown below.

Maturity	Amortized Cost	Fair Value
One year or less	$ 3,220	$ 3,276
Over one year through five years	12,368	12,728
Over five years through ten years	13,382	13,570
Over ten years	38,353	39,246
Subtotal	67,323	68,820
Mortgage- and asset-backed securities	11,966	11,935

Total	**$ 79,289**	**$80,755**

Estimated maturities may differ from contractual maturities due to call or prepayment provisions because of the potential for prepayment on mortgage- and asset-backed securities; they are not categorized by contractual maturity. The commercial mortgage-backed securities are categorized by contractual maturity because they generally are not subject to prepayment risk.

Sales of Fixed Maturity and Available-for-Sale Equity Security Investments

	For the years ended December 31,		
	2006	**2005**	**2004**
Sale of Fixed Maturities			
Sale proceeds	$32,307	$25,470	$21,339
Gross gains	427	497	525
Gross losses	(407)	(364)	(202)
Sale of Available-for-Sale Equity Securities			
Sale proceeds	$ 514	$ 105	$ 127
Gross gains	11	12	21
Gross losses	(14)		(6)

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

4. Investments and Derivative Instruments (continued)

Concentration of Credit Risk

The Company aims to maintain a diversified investment portfolio including issuer, sector and geographic stratification, where applicable, and has established certain exposure limits, diversification standards and review procedures to mitigate credit risk.

The Company is not exposed to any concentration of credit risk of a single issuer greater than 10% of the Company s stockholders equity other than U.S. government and certain U.S. government agencies. Other than U.S. government and U.S. government agencies, the Company s largest three exposures by issuer as of December 31, 2006 were the State of California, General Electric Company and UBS AG and as of December 31, 2005 were the State of California, AT&T Inc. and the State of Massachusetts, which each comprise less than 0.5% of total invested assets. The Company s largest three exposures by industry sector, as of both December 31, 2006 and 2005, were financial services, utilities, and technology and communications which comprised approximately 9%, 4% and 4%, respectively, of total invested assets.

The Company s investments in states, municipalities and political subdivisions are geographically dispersed throughout the United States. The largest concentrations, as of December 31, 2006, were in California, New York and Illinois and as of December 31, 2005, were in California, New York and Texas which each comprise 2% or less of total invested assets, respectively.

Security Unrealized Loss Aging

The Company has a security monitoring process overseen by a committee of investment and accounting professionals that, on a quarterly basis, identifies securities in an unrealized loss position that could potentially be other-than-temporarily impaired. For further discussion regarding the Company s other-than-temporary impairment policy, see the Investments section of Note 1. Due to the issuers continued satisfaction of the securities obligations in accordance with their contractual terms and the expectation that they will continue to do so, management s intent and ability to hold these securities for a period of time sufficient to allow for any anticipated recovery in market value, as well as the evaluation of the fundamentals of the issuers financial condition and other objective evidence, the Company believes that the prices of the securities in the sectors identified in the tables below were temporarily depressed as of December 31, 2006 and 2005.

The following table presents amortized cost, fair value and unrealized losses for the Company s fixed maturity and available-for-sale equity securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of December 31, 2006.

	2006								
	Less Than 12 Months			12 Months or More			Total		
	Amortized Cost	Fair Value	Unrealized Losses	Amortized Cost	Fair Value	Unrealized Losses	Amortized Cost	Fair Value	Unrealized Losses
ABS	$ 1,115	$ 1,105	$ (10)	$ 994	$ 951	$ (43)	$ 2,109	$ 2,056	$ (53)
CMOs									
Agency backed	131	130	(1)	360	353	(7)	491	483	(8)
Non-agency backed	37	37		50	49	(1)	87	86	(1)
CMBS									
Agency backed	101	101		10	9	(1)	111	110	(1)
Non-agency backed	3,741	3,711	(30)	4,226	4,112	(114)	7,967	7,823	(144)
Corporate	8,478	8,365	(113)	7,425	7,167	(258)	15,903	15,532	(371)
Government/Government agencies									
Foreign	255	251	(4)	86	84	(2)	341	335	(6)

United States	515	511	(4)	147	144	(3)	662	655	(7)
MBS U.S. Government/Government agencies	450	446	(4)	1,626	1,585	(41)	2,076	2,031	(45)
States, municipalities and political subdivisions	924	913	(11)	393	377	(16)	1,317	1,290	(27)
Short-term investments	1,081	1,081					1,081	1,081	
Total fixed maturities	16,828	16,651	(177)	15,317	14,831	(486)	32,145	31,482	(663)
Common stock	49	47	(2)	3	3		52	50	(2)
Non-redeemable preferred stock	216	213	(3)	82	77	(5)	298	290	(8)
Total equity	265	260	(5)	85	80	(5)	350	340	(10)
Total temporarily impaired securities	**$17,093**	**$16,911**	**$(182)**	**$15,402**	**$14,911**	**$(491)**	**$32,495**	**$31,822**	**$(673)**

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

4. Investments and Derivative Instruments (continued)

As of December 31, 2006, fixed maturities accounted for approximately 99% of the Company s total unrealized loss amount, which was comprised of approximately 4,700 different securities. The Company held no securities as of December 31, 2006, that were in an unrealized loss position in excess of $12. Other-than-temporary impairments for certain ABS and CMBS are recognized if the fair value of the security, as determined by external pricing sources, is less than its cost or amortized cost and there has been a decrease in the present value of the expected cash flows since the last reporting period. Based on management s best estimate of future cash flows, there were no such ABS and CMBS in an unrealized loss position as of December 31, 2006 that were deemed to be other-than-temporarily impaired.

Securities in an unrealized loss position for less than twelve months were comprised of approximately 2,740 securities, of which 92% of the unrealized loss were securities with fair value to amortized cost ratios at or greater than 90%. The majority of these securities are investment grade fixed maturities depressed due to changes in interest rates from the date of purchase.

The securities depressed for twelve months or more as of December 31, 2006 were comprised of approximately 2,200 securities, with the majority of the unrealized loss amount relating to CMBS, corporate fixed maturities within the financial services and utilities sectors and ABS. A description of the events contributing to the security types unrealized loss position and the factors considered in determining that recording an other-than-temporary impairment was not warranted are outlined below.

CMBS The CMBS in an unrealized loss position for twelve months or more as of December 31, 2006, were primarily the result of an increase in interest rates from the security s purchase date. Substantially all of these securities are investment grade securities priced at or greater than 90% of amortized cost as of December 31, 2006. Additional changes in fair value of these securities are primarily dependent on future changes in interest rates.

Financial services Securities in financial services account for approximately $52 of the corporate securities in an unrealized loss position for twelve months or more. Substantially all of these securities are investment grade securities with fair values at or greater than 90% of amortized cost. These positions are a mixture of fixed and variable rate securities with extended maturity dates, which have been adversely impacted by changes in interest rates after the purchase date. Additional changes in fair value of these securities are primarily dependent on future changes in general market conditions, including interest rates and credit spread movements.

Utilities Securities in utilities account for approximately $46 of the corporate securities in an unrealized loss position for twelve months or more. Most of these securities are fixed rate, investment grade securities with extended maturity dates, which have been adversely impacted by changes in interest rates after the purchase date. Additional changes in fair value of these securities are primarily dependent on future changes in general market conditions, including interest rates and credit spread movements.

ABS As of December 31, 2006, $27 of the Company s total unrealized losses in asset-backed securities is secured by leases to airlines primarily outside of the United States. Based on the current and expected future collateral values of the underlying aircraft, recent improvement in lease rates and an overall increase in worldwide travel, the Company expects to recover the full amortized cost of these investments. However, future price recovery will depend on continued improvement in economic fundamentals, political stability, airline operating performance and collateral value.

The remaining balance of $236 in the twelve months or more unrealized loss category is comprised of approximately 1,220 securities, most all of which were depressed only to a minor extent with fair value to amortized cost ratios at or greater than 90% as of December 31, 2006. The decline in market value for these securities is primarily attributable to changes in general market conditions, including interest rates and credit spread movements.

Mortgage Loans

The carrying value of mortgage loans was $3.3 billion and $1.7 billion as of December 31, 2006 and 2005, respectively. The Company s mortgage loans are collateralized by a variety of commercial and agricultural properties. The largest concentrations by property type at December 31, 2006, are office buildings (approximately 41%), hotels (approximately 15%) and industrial properties (approximately 14%). The largest concentrations by property type at December 31, 2005, were office buildings (approximately 39%), retail stores (approximately 22%) and hotels (approximately 15%). The properties collateralizing mortgage loans are geographically dispersed throughout the United States, with the largest concentration in California (approximately 17% and 18% at December 31, 2006 and 2005, respectively). At December 31, 2006 and 2005, the Company held no impaired, restructured, delinquent or in-process-of-foreclosure mortgage loans. The Company had no valuation allowance for mortgage loans at December 31, 2006 and 2005.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

4. Investments and Derivative Instruments (continued)

Variable Interest Entities (VIE)

In the normal course of business, the Company becomes involved with variable interest entities primarily as a collateral manager and through normal investment activities. The Company s involvement includes providing investment management and administrative services, and holding ownership or other investment interests in the entities.

The following table summarizes the total assets, liabilities and maximum exposure to loss relating to VIEs for which the Company has concluded it is the primary beneficiary. Accordingly, the results of operations and financial position of these VIEs are included along with the corresponding minority interest liabilities in the consolidated financial statements.

	December 31, 2006			December 31, 2005		
	Total Assets	Liability [4]	Maximum Exposure to Loss[2][3]	Total Assets	Liability [4]	Maximum Exposure to Loss[2][3]
Collaterized debt obligations (CDOs) and other funds [1] [2]	$296	$ 99	$ 197	$77	$ 42	$ 35
Limited partnerships [3]	103	5	98			
Total [5]	$399	$ 104	$ 295	$77	$ 42	$ 35

[1] The Company provides collateral management services and earns a fee associated with these structures.

[2] The maximum exposure to loss is the Company s co-investment in these structures.

[3] The maximum exposure to loss is equal to the carrying value of the

investment plus any unfunded commitments.

[4] *Creditors have no recourse against the Company in the event of default by the VIE.*

[5] *As of December 31, 2006 and 2005, the Company had relationships with four and two VIEs, respectively, where the Company was the primary beneficiary.*

In addition to the VIEs described above, as of December 31, 2006 and 2005, the Company holds variable interest in three CDOs that are managed by Hartford Investment Management Company, a wholly-owned subsidiary of The Hartford, where the Company is not the primary beneficiary. As a result, these are not consolidated by the Company. These investments have been held by the Company for a period of one to three years. The Company s maximum exposure to loss from the non-consolidated CDOs (consisting of the Company s investments) was approximately $20 and $21 as of December 31, 2006 and 2005, respectively.

Derivative Instruments

The Company utilizes a variety of derivative instruments, including swaps, caps, floors, forwards, futures and options through one of four Company-approved objectives: to hedge risk arising from interest rate, equity market, price or currency exchange rate risk or volatility; to manage liquidity; to control transaction costs; or to enter into replication transactions.

On the date the derivative contract is entered into, the Company designates the derivative as a fair-value hedge, cash-flow hedge, foreign-currency hedge, net investment hedge, or held for other investment and risk management purposes.

The Company s derivative transactions are used in strategies permitted under the derivative use plans required by the State of Connecticut, the State of Illinois and the State of New York insurance departments.

Derivative instruments are recorded in the consolidated balance sheets at fair value. Asset and liability values are determined by calculating the net position for each derivative counterparty by legal entity and are presented as of December 31, as follows:

	Asset Values		**Liability Values**	
	2006	**2005**	**2006**	**2005**
Other investments	$ 287	$ 181	$	$
Reinsurance recoverables			22	17
Other policyholder funds and benefits payable	53	8	1	
Other liabilities			772	450

Total	**$ 340**	**$ 189**	**$ 795**	**$ 467**

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

4. Investments and Derivative Instruments (continued)

The following table summarizes the derivative instruments used by the Company and the primary hedging strategies to which they relate. Derivatives in the Company s separate accounts are not included because the associated gains and losses accrue directly to policyholders. The notional value of derivative contracts represents the basis upon which pay or receive amounts are calculated and are not reflective of credit risk. The fair value amounts of derivative assets and liabilities are presented on a net basis as of December 31, 2006 and 2005. The total ineffectiveness of all cash-flow, fair-value and net investment hedges and total change in value of other derivative-based strategies which do not qualify for hedge accounting treatment, including periodic derivative net coupon settlements, are presented below on an after-tax basis for the years ended December 31, 2006 and 2005.

	Notional Amount		Fair Value		Hedge Ineffectiveness, After-tax	
Hedging Strategy	**2006**	**2005**	**2006**	**2005**	**2006**	**2005**
Cash-Flow Hedges						
Interest rate swaps						
Interest rate swaps are primarily used to convert interest receipts on floating-rate fixed maturity securities to fixed rates. These derivatives are predominantly used to better match cash receipts from assets with cash disbursements required to fund liabilities.						
The Company also enters into forward starting swap agreements to hedge the interest rate exposure of anticipated future cash flows on floating-rate fixed maturity securities due to changes in the benchmark interest rate, London-Interbank Offered Rate (LIBOR). These derivatives were structured to hedge interest rate exposure inherent in the assumptions used to price primarily certain long-term disability products.						

Interest rate swaps are also used to hedge a portion of the Company s floating-rate guaranteed investment contracts. These derivatives convert the floating rate guaranteed investment contract payments to a fixed rate to better match the cash receipts earned from the supporting investment portfolio.	$ 6,093	$5,753	$ (22)	$ (18)	$ (9)	$(11)
Foreign currency swaps						
Foreign currency swaps are used to convert foreign denominated cash flows associated with certain foreign denominated fixed maturity investments to U.S. dollars. The foreign fixed maturities are primarily denominated in euros and are swapped to minimize cash flow fluctuations due to changes in currency rates. In addition, foreign currency swaps are also used to convert foreign denominated cash flows associated with certain liability payments in order to minimize cash flow fluctuations due to changes in currency rates.	1,871	1,758	(370)	(242)	(4)	4
Fair-Value Hedges						
Interest rate swaps						
Interest rate swaps are used to hedge the changes in fair value of certain fixed rate liabilities and fixed maturity securities due to changes in the benchmark interest rate, LIBOR. In addition, a portion of the Company s fixed debt was hedged against increases in LIBOR, the designated benchmark interest rate.	3,846	2,476	10	(12)	(1)	2
Foreign currency swaps	492		(9)			

Foreign currency swaps are used to hedge the changes in fair value of certain foreign denominated fixed rate liabilities due to changes in foreign currency rates.						
Total cash-flow and fair-value hedges	**$12,302**	**$9,987**	**$(391)**	**$(272)**	**$(14)**	**$ (5)**

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
4. Investments and Derivative Instruments (continued)

Hedging Strategy	Notional Amount 2006	Notional Amount 2005	Fair Value 2006	Fair Value 2005	Derivative Change in Value, After-tax 2006	Derivative Change in Value, After-tax 2005
Other Investment and Risk Management Activities						
Interest rate caps and swaption contracts						
The Company is exposed to policyholder surrenders during a rising interest rate environment. Interest rate cap and swaption contracts are used to mitigate the Company s loss in a rising interest rate environment. The increase in yield from the cap and swaption contracts in a rising interest rate environment may be used to raise credited rates, thereby increasing the Company s competitiveness and reducing the policyholder s incentive to surrender. The Company also may use an interest rate cap as an economic hedge of the interest rate risk related to Company issued debt. In a rising interest rate environment, the cap will limit the net interest expense on the hedged fixed rate debt.	$1,100	$1,616	$	$ 3	$ (1)	$ (1)
Interest rate swaps, caps and floors						
The Company uses interest rate swaps and floors to manage duration risk between assets and liabilities in certain portfolios. In addition, the Company enters	5,460	2,223	(30)	(4)	(33)	1

into interest rate swaps to terminate existing swaps in hedging relationships, thereby offsetting the changes in value of the original swap. The Company also enters into interest rate caps to manage the duration risk in certain investment portfolios.						
Interest rate forwards						
The Company uses interest rate forwards to replicate the purchase of mortgage-backed securities to manage duration risk and liquidity.	1,269		(7)		10	
Foreign currency swaps and forwards						
The Company enters into foreign currency swaps and forwards to hedge the foreign currency exposures in certain of its foreign fixed maturity investments.	663	766	(14)	(9)	(8)	20
Credit default and total return swaps						
The Company enters into swap agreements in which the Company assumes credit exposure of an individual entity, referenced index or asset pool. These contracts entitle the company to receive a periodic fee in exchange for an obligation to compensate the derivative counterparty should a credit event occur on the part of the referenced security issuers. The maximum potential future exposure to the Company is the notional value of the swap contracts, which is $1,203 and $455, after-tax, as of December 31, 2006 and 2005, respectively. The Company also assumes exposure to the change in value of indices or asset pools through total return						

swaps and credit spreadlocks. As of December 31, 2006 and 2005, the maximum potential future exposure to the Company from such contracts is $1,386 and $899, after-tax, respectively.						
The Company enters into credit default swap agreements, in which the Company pays a derivative counterparty a periodic fee in exchange for compensation from the counterparty should a credit event occur on the part of the referenced security issuer. The Company entered into these agreements as an efficient means to reduce credit exposure to specified issuers or sectors. In addition, the Company enters into option contracts to receive protection should a credit event occur on the part of the referenced security issuer.	7,611	2,839	(194)	3	25	13

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

4. Investments and Derivative Instruments (continued)

Hedging Strategy	Notional Amount 2006	Notional Amount 2005	Fair Value 2006	Fair Value 2005	Derivative Change in Value, After-tax 2006	Derivative Change in Value, After-tax 2005
Yen fixed annuity hedging instruments The Company enters into currency rate swaps and forwards to mitigate the foreign currency exchange rate and yen interest rate exposures associated with the yen denominated individual fixed annuity product. The associated liability is adjusted for changes in spot rates which was $12 and $102, after-tax, as of December 31, 2006 and 2005, respectively, and partially offset the derivative change in value.	$ 1,869	$ 1,675	$(225)	$(179)	$ (64)	$(143)
GMWB product derivatives The Company offers certain variable annuity products with a GMWB rider. The GMWB is a bifurcated embedded derivative that provides the policyholder with a GRB if the account value is reduced to zero through a combination of market declines and withdrawals. The GRB is generally equal to premiums less withdrawals. The policyholder also has the option, after a specified time period, to reset the GRB to the then-current account value, if greater. For a further discussion, see the Derivative Instruments	37,769	31,803	53	8	79	(42)

section of Note 1. The notional value of the embedded derivative is the GRB balance.						
GMWB reinsurance contracts						
Reinsurance arrangements are used to offset the Company s exposure to the GMWB embedded derivative for the lives of the host variable annuity contracts. The notional amount of the reinsurance contracts is the GRB amount.	7,172	8,575	(22)	(17)	(19)	19
GMWB hedging instruments						
The Company enters into interest rate futures, S&P 500 and NASDAQ index futures contracts and put and call options, as well as interest rate, EAFE index and equity volatility swap contracts to economically hedge exposure to the volatility associated with the portion of the GMWB liabilities which are not reinsured. In addition, the Company periodically enters into forward starting S&P 500 put options as well as S&P index futures and interest rate swap contracts to economically hedge the equity volatility risk exposure associated with anticipated future sales of the GMWB rider. [1]	8,379	5,086	346	175	(77)	1
Equity index swaps and options						
The Company offers certain equity indexed products, which may contain an embedded derivative that requires bifurcation. The Company enters into S&P	30	16				(1)

index swaps and options to economically hedge the equity volatility risk associated with these embedded derivatives. In addition, the Company is exposed to bifurcated options embedded in certain fixed maturity investments.						
Statutory reserve hedging instruments						
The Company purchases one and two year S&P 500 put option contracts to economically hedge the statutory reserve impact of equity exposure arising primarily from GMDB and GMWB obligations against a decline in the equity markets.	2,220	1,142	29	14	(9)	(20)
Total other investment and risk management activities	**$73,542**	**$55,741**	**$ (64)**	**$ (6)**	**$ (97)**	**$(153)**
Total derivatives [2]	**$85,844**	**$65,728**	**$(455)**	**$(278)**	**$(111)**	**$(158)**

[1] The after-tax net gain related to derivatives purchased to hedge the anticipatory sales of the GMWB rider is $0 and $8 for the years ended December 31, 2006 and 2005, respectively.

[2] Derivative change in value includes hedge ineffectiveness for cash-flow hedges, fair-value

hedges, and total change in value, including periodic derivative net coupon settlements, of other investment and risk management activities.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

4. Investments and Derivative Instruments (continued)

The increase in notional amount since December 31, 2005, is primarily due to an increase in derivatives associated with guaranteed minimum withdrawal benefit (GMWB) product sales and additional options purchased to hedge the GMWB, credit derivatives and derivatives hedging interest rate duration risk. The Company increased its use of credit derivatives primarily to reduce credit exposure as well as to enter into replication transactions. During 2006, the Company began using credit default swaps to replicate residual CDO interests. These transactions involve the receipt of cash upon entering into the transaction as well as coupon payments throughout the life of the contract. The upfront cash receipts for positions at December 31, 2006, totaled $201, which represents the original liability value of the credit default swaps. As of December 31, 2006, the notional and fair value of credit default swaps used in this replication strategy is $400 and $(189), respectively.

The decrease in net fair value of derivative instruments since December 31, 2005, was primarily related to the initial cash received on credit default swaps replicating residual CDO interests as well as declines in fair value of derivatives hedging foreign bonds, the Japanese fixed annuity, and interest rate duration risk between assets and liabilities, partially offset by additional options purchased to hedge GMWB. Derivatives hedging foreign bonds declined in value primarily as a result of the weakening of the U.S. dollar in comparison to certain foreign currencies. The Japanese fixed annuity hedging instruments declined in value primarily due to a rise in Japanese interest rates and the depreciation of the yen in comparison to the U.S. dollar. Derivatives hedging interest rate duration risk declined in value primarily due to rising interest rates. For further discussion on the GMWB product, which is accounted for as an embedded derivative, refer to Note 6 of Notes to Condensed Consolidated Financial Statements.

During 2006, the Company terminated an interest rate swap and an interest rate cap that were used to hedge the Company s $500 fixed rate debt which was callable in 2006. Additionally, during 2006, interest rate swaps and the respective hedged fixed rate non-callable debt of $250 matured. The notional and fair value of the contracts terminated were $1.3 billion and $(11), respectively.

The total change in value for derivative-based strategies that do not qualify for hedge accounting treatment, including periodic derivative net coupon settlements, are reported in net realized capital gains (losses). For the years ended December 31, 2006 and 2005, these strategies resulted in the recognition of after-tax net gains (losses) of $(97) and $(153), respectively. For the year ended December 31, 2006, net realized capital losses were primarily driven by losses on the Japanese fixed annuity hedging instruments and interest rate swaps used to manage portfolio duration primarily due to rising interest rates as well as losses on GMWB related derivatives primarily driven by liability model refinements and assumption updates reflecting in-force demographics, actuarial experience, and future expectations. For the year ended December 31, 2005, net realized capital losses were predominantly comprised of net losses on the Japanese fixed annuity hedging instruments primarily due to the weakening of the Yen in comparison to the U.S. dollar, as well as, an increase in Japanese interest rates.

As of December 31, 2006 and 2005, the after-tax deferred net gains (losses) on derivative instruments recorded in AOCI that are expected to be reclassified to earnings during the next twelve months are $(7) and $1, respectively. This expectation is based on the anticipated interest payments on hedged investments in fixed maturity securities that will occur over the next twelve months, at which time the Company will recognize the deferred net gains (losses) as an adjustment to interest income over the term of the investment cash flows. The maximum term over which the Company is hedging its exposure to the variability of future cash flows (for all forecasted transactions, excluding interest payments on variable-rate financial instruments) is twenty-four months. For the years ended December 31, 2006, 2005 and 2004, the Company had less than $1 of net reclassifications from AOCI to earnings resulting from the discontinuance of cash-flow hedges due to forecasted transactions that were no longer probable of occurring.

For the year ended December 31, 2004, after-tax net gain (loss) representing ineffectiveness of cash-flow hedges was $(11) while ineffectiveness of fair-value hedges and net investment hedges were both less than $1.

Securities Lending and Collateral Arrangements

The Company participates in securities lending programs to generate additional income, whereby certain domestic fixed income securities are loaned for a specified period of time from the Company s portfolio to qualifying third parties, via two lending agents. Borrowers of these securities provide collateral of 102% of the market value of the loaned securities. Acceptable collateral may be in the form of cash or U.S. Government securities. The market value of the loaned securities is monitored and additional collateral is obtained if the market value of the collateral falls below 100% of the market value of the loaned securities. Under the terms of securities lending programs, the lending agent indemnifies the Company against borrower defaults. As of December 31, 2006 and 2005, the fair value of the loaned securities was approximately $2.2 billion and $1.2 billion, respectively, and was included in fixed maturities in the consolidated balance sheets. The Company earns income from the cash collateral or receives a fee from the borrower. The Company recorded before-tax income from securities lending transactions, net of lending fees, of $3 for each of the years ended December 31, 2006 and 2005, which was included in net investment income.

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

4. Investments and Derivative Instruments (continued)

The Company enters into various collateral arrangements in connection with its derivative instruments, which require both the pledging and accepting of collateral. As of December 31, 2006 and 2005, collateral pledged having a fair value of $504 and $308, respectively, was included in fixed maturities in the consolidated balance sheets.

From time to time, the Company enters into secured borrowing arrangements as a means to increase investment income. The cash collateral received from third parties by the Company in exchange for financial interests granted in certain securities was $57 and $38 as of December 31, 2006 and 2005, respectively.

The classification and carrying amount of the loaned securities and the derivative instrument collateral pledged at December 31, 2006 and 2005 were as follows:

Loaned Securities and Collateral Pledged	2006	2005
ABS	$ 20	$ 29
CMBS	216	198
Corporate	1,867	889
MBS	152	138
Government/Government Agencies		
Foreign	19	63
United States	463	285
Total	**$2,737**	**$1,602**

As of December 31, 2006 and 2005, the Company had accepted collateral relating to securities lending programs and derivative instruments consisting of cash, U.S. Government and U.S. Government agency securities with a fair value of $2.4 billion and $1.4 billion, respectively. At December 31, 2006 and 2005, cash collateral of $2.3 billion and $1.3 billion, respectively, was invested and recorded in the consolidated balance sheets in fixed maturities with a corresponding amount recorded in other liabilities. The Company is only permitted by contract to sell or repledge the noncash collateral in the event of a default by the counterparty and none of such collateral has been sold or repledged at December 31, 2006 and 2005. As of December 31, 2006 and 2005, noncash collateral accepted was held in separate custodial accounts.

Securities on Deposit with States

The Company is required by law to deposit securities with government agencies in states where it conducts business. As of December 31, 2006 and 2005, the fair value of securities on deposit was approximately $1.2 billion and $1.1 billion, respectively.

5. Fair Value of Financial Instruments

SFAS No. 107, Disclosures about Fair Value of Financial Instruments , requires disclosure of fair value information of financial instruments.

For certain financial instruments where quoted market prices are not available, other independent valuation techniques and assumptions are used. Because considerable judgment is used, these estimates are not necessarily indicative of amounts that could be realized in a current market exchange. SFAS No. 107 excludes certain financial instruments from disclosure, including insurance contracts, other than financial guarantees and investment contracts.

The Hartford uses the following methods and assumptions in estimating the fair value of each class of financial instrument. Fair value for fixed maturities and marketable equity securities approximates those quotations published by applicable stock exchanges or received from other reliable sources.

For policy loans, carrying amounts approximate fair value.

For mortgage loans on real estate, fair values were estimated using discounted cash flow calculations based on current incremental lending rates for similar type loans.

Derivative instruments are reported at fair value based upon either pricing valuation models, which utilize market data inputs or independent broker quotations.

Other policyholder funds and benefits payable fair value information is determined by estimating future cash flows, discounted at the current market rate. For further discussion of other policyholder funds and derivatives, see Note 1.

For commercial paper, carrying amounts approximate fair value.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

5. Fair Value of Financial Instruments (continued)

Fair value for long-term debt is based on market quotations from independent third party pricing services.

Fair value for consumer notes is based on discounted cash flow calculations based on current market rates.

The carrying amounts and fair values of The Hartford s financial instruments at December 31, 2006 and 2005 were as follows:

	2006		2005	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets				
Fixed maturities	$80,755	$80,755	$76,440	$76,440
Equity securities	31,132	31,132	25,495	25,495
Policy loans	2,051	2,051	2,016	2,016
Mortgage loans on real estate	3,318	3,298	1,731	1,718
Other investments [1]	673	673	583	583
Liabilities				
Other policyholder funds and benefits payable [2]	$14,233	$13,488	$11,691	$11,278
Commercial paper [3]	299	299	471	471
Long-term debt [4]	3,804	3,974	4,296	5,073
Consumer notes	258	260		
Derivative related liabilities [5]	772	772	450	450

[1] 2006 and 2005 include $287 and $181 of derivative related assets, respectively.

[2] Excludes group accident and health and universal life insurance contracts, including corporate owned life insurance.

[3] Included in short-term debt in the consolidated

balance sheets.

[4] *Includes current maturities of long-term debt.*

[5] *Included in other liabilities in the consolidated balance sheets.*

6. Reinsurance

The Hartford cedes insurance to other insurers in order to limit its maximum losses and to diversify its exposures. Such transfers do not relieve The Hartford of its primary liability under policies it wrote and, as such, failure of reinsurers to honor their obligations could result in losses to The Hartford. The Hartford also is a member of and participates in several reinsurance pools and associations. The Hartford evaluates the financial condition of its reinsurers and monitors concentrations of credit risk. The Hartford s property and casualty reinsurance is placed with reinsurers that meet strict financial criteria established by a credit committee. As of December 31, 2006 and 2005, The Hartford had no reinsurance-related concentrations of credit risk greater than 10% of the Company s stockholders equity.

Life

In accordance with normal industry practice, Life is involved in both the cession and assumption of insurance with other insurance and reinsurance companies. As of December 31, 2006 and 2005, the Company s policy for the largest amount of life insurance retained on any one life by any one of the life operations was approximately $5. In addition, the Company reinsures the majority of minimum death benefit guarantees as well as guaranteed minimum withdrawal benefits, on contracts issued prior to July 2003, offered in connection with its variable annuity contracts.

Life insurance fees, earned premiums and other were comprised of the following:

	For the years ended December 31,		
	2006	**2005**	**2004**
Gross fee income, earned premiums and other	$ 9,372	$ 8,194	$ 7,223
Reinsurance assumed	313	464	811
Reinsurance ceded	(369)	(455)	(498)
Net fee income, earned premiums and other	**$ 9,316**	**$ 8,203**	**$ 7,536**

Life reinsures certain of its risks to other reinsurers under yearly renewable term, coinsurance, and modified coinsurance arrangements. Yearly renewable term and coinsurance arrangements result in passing all or a portion of the risk to the reinsurer. Generally, the reinsurer receives a proportionate amount of the premiums less an allowance for commissions and expenses and is liable for a corresponding proportionate amount of all benefit payments. Modified coinsurance is similar to coinsurance except that the cash and investments that support the liabilities for contract benefits are not transferred to the assuming company, and settlements are made on a net basis between the companies.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

6. Reinsurance (continued)

The cost of reinsurance related to long-duration contracts is accounted for over the life of the underlying reinsured policies using assumptions consistent with those used to account for the underlying policies. Life insurance recoveries on ceded reinsurance contracts, which reduce death and other benefits, were $59, $351 and $478 for the years ended December 31, 2006, 2005 and 2004, respectively. Life also assumes reinsurance from other insurers.

Property and Casualty

In managing risk, The Hartford utilizes reinsurance to transfer risk to well-established and financially secure reinsurers. Reinsurance is used to manage aggregations of risk as well as specific risks based on accumulated property and casualty liabilities in certain geographic zones. All treaty purchases related to the Company s property and casualty operations are administered by a centralized function to support a consistent strategy and ensure that the reinsurance activities are fully integrated into the organization s risk management processes.

A variety of traditional reinsurance products are used as part of the Company s risk management strategy, including excess of loss occurrence-based products that protect aggregate property and workers compensation exposures, and individual risk or quota share arrangements, that protect specific classes or lines of business. There are no significant finite risk contracts in place and the statutory surplus benefit from all such prior year contracts is immaterial. Facultative reinsurance is also used to manage policy-specific risk exposures based on established underwriting guidelines. The Hartford also participates in governmentally administered reinsurance facilities such as the Florida Hurricane Catastrophe Fund (FHCF), the Terrorism Risk Insurance Program established under The Terrorism Risk Insurance Extension Act of 2005 and other reinsurance programs relating to particular risks or specific lines of business.

The Company has several catastrophe reinsurance programs, including reinsurance treaties that cover property and workers compensation losses aggregating from single catastrophe events.

The effect of reinsurance on property and casualty premiums written and earned was as follows:

	For the years ended December 31,		
	2006	**2005**	**2004**
Premiums Written			
Direct	$ 11,600	$ 11,653	$ 11,181
Assumed	265	233	231
Ceded	(1,203)	(1,399)	(1,450)
Net	**$ 10,662**	**$ 10,487**	**$ 9,962**
Premiums Earned			
Direct	$ 11,465	$ 11,356	$ 10,811
Assumed	259	218	218
Ceded	(1,291)	(1,418)	(1,535)
Net	**$ 10,433**	**$ 10,156**	**$ 9,494**

Ceded losses which reduce losses and loss adjustment expenses incurred, were $370, $1.7 billion and $960 for the years ended December 31, 2006, 2005 and 2004, respectively.

Ceded incurred losses decreased from $1.7 billion in 2005 to $370 in 2006, primarily because of a $970 decrease in current accident year catastrophe losses ceded to reinsurers and a $243 reduction in net reinsurance recoverables in

2006 as a result of an agreement with Equitas and the Company s evaluation of the reinsurance recoverables and allowance for uncollectible reinsurance associated with older, long-term casualty liabilities reported in the Other Operations segment.

Ceded incurred losses increased by $740 from 2004 to 2005, from $960 to $1.7 billion, primarily because of a $686 increase in current accident year catastrophe losses ceded to reinsurers and a $181 reduction in the reinsurance recoverable asset associated with older, long-term casualty liabilities recorded in 2004, partially offset by a decrease in the amount of losses ceded on professional liability business as a result of the Company increasing its retention on that business. Current accident year catastrophe losses ceded increased by $686 from 2004 to 2005, from $288 to $974. The increase was primarily due to an increase in gross current accident year catastrophe losses from $811 in 2004 to $1.3 billion in 2005. The amount of gross losses ceded to reinsurers depends, in large part, on the extent to which gross losses incurred from a single event exceed the Company s attachment point under its principal property catastrophe reinsurance program. Compared to the hurricanes of 2004, the individual hurricanes in 2005 significantly exceeded the attachment point, resulting in greater reinsurance recoveries.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

6. Reinsurance (continued)

Reinsurance recoverables include balances due from reinsurance companies for paid and unpaid losses and loss adjustment expenses and are presented net of an allowance for uncollectible reinsurance. The reinsurance recoverables balance includes an estimate of the amount of gross losses and loss adjustment expense reserves that may be ceded under the terms of the reinsurance agreements, including incurred but not reported unpaid losses. The Company s estimate of losses and loss adjustment expense reserves ceded to reinsurers is based on assumptions that are consistent with those used in establishing the gross reserves for business ceded to the reinsurance contracts. The Company calculates its ceded reinsurance projection based on the terms of any applicable facultative and treaty reinsurance, including an estimate of how incurred but not reported losses will ultimately be ceded by reinsurance agreement. Accordingly, the Company s estimate of reinsurance recoverables is subject to similar risks and uncertainties as the estimate of the gross reserve for unpaid losses and loss adjustment expenses.

The allowance for uncollectible reinsurance was $412 and $413 as of December 31, 2006 and 2005, respectively. The allowance for uncollectible reinsurance reflects management s best estimate of reinsurance cessions that may be uncollectible in the future due to reinsurers unwillingness or inability to pay. The Company analyzes recent developments in commutation activity between reinsurers and cedants, recent trends in arbitration and litigation outcomes in disputes between reinsurers and cedants and the overall credit quality of the Company s reinsurers. Where its contracts permit, the Company secures future claim obligations with various forms of collateral, including irrevocable letters of credit, secured trusts, funds held accounts and group-wide offsets.

Due to the inherent uncertainties as to collection and the length of time before reinsurance recoverables become due, it is possible that future adjustments to the Company s reinsurance recoverables, net of the allowance, could be required, which could have a material adverse effect on the Company s consolidated results of operations or cash flows in a particular quarter or annual period.

7. Deferred Policy Acquisition Costs and Present Value of Future Profits

Life

Changes in deferred policy acquisition costs and present value of future profits are as follows:

	2006	**2005**	**2004**
Balance, January 1	**$ 8,568**	**$ 7,438**	**$ 6,624**
Deferred Costs	1,923	2,071	1,968
Amortization Deferred Policy Acquisitions Costs and Present Value of Future Profits	(1,269)	(1,172)	(993)
Amortization Unlock	(183)		
Adjustments to unrealized gains and losses on securities available-for-sale and other	47	380	(75)
Cumulative effect of accounting change (SOP 03-1)			(105)
Effect of currency translation	(15)	(149)	72
Acquisition of Hartford Life Group Insurance Company [1]			(53)
Balance, December 31	**$ 9,071**	**$ 8,568**	**$ 7,438**

[1] *For the year ended December 31, 2004, reflects the purchase price adjustment related to the acquisition of CNA Group Life Assurance Company.*

Estimated future net amortization expense of present value of future profits for the succeeding five years is as follows:

For the years ended December 31,

2007	$64
2008	64
2009	56
2010	49
2011	44

Property & Casualty

Changes in deferred policy acquisition costs are as follows:

	2006	**2005**	**2004**
Balance, January 1	**$ 1,134**	**$ 1,071**	**$ 975**
Deferred costs	2,169	2,060	1,946
Amortization	(2,106)	(1,997)	(1,850)
Balance, December 31	**$ 1,197**	**$ 1,134**	**$ 1,071**

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

8. Goodwill and Other Intangible Assets

The carrying amount of goodwill as of December 31 is shown below.

	2006	2005
Life		
Retail	$ 572	$ 572
Individual Life	224	224
Total Life	**796**	**796**
Property & Casualty		
Personal Lines	119	122
Specialty Commercial	30	30
Total Property & Casualty	**149**	**152**
Corporate	**772**	**772**
Total Goodwill	**$ 1,717**	**$ 1,720**

The Company s goodwill impairment test performed in accordance with SFAS No. 142 Goodwill and Other Intangible Assets , resulted in no write-downs for the years ended December 31, 2006 and 2005.

The following table shows the Company s acquired intangible assets that continue to be subject to amortization and aggregate amortization expense, net of interest accretion, if any. Except for goodwill, the Company has no intangible assets with indefinite useful lives.

	2006		2005	
Acquired Intangible Assets	**Gross Carrying Amount**	**Accumulated Net Amortization**	**Gross Carrying Amount**	**Accumulated Net Amortization**
Renewal rights	$ 22	$ 20	$ 22	$ 17
Other	14	10	14	7
Total Acquired Intangible Assets	**$ 36**	**$ 30**	**$ 36**	**$ 24**

Net amortization expense for the years ended December 31, 2006, 2005 and 2004 was $6, $7 and $7, respectively. As of December 31, 2006, the weighted average amortization period was 7.0 years for renewal rights, 5.0 years for other and 5.3 years for total acquired intangible assets.

The following is detail of the net acquired intangible asset activity for the years ended December 31, 2006, 2005 and 2004, respectively.

For the year ended December 31, 2006	Renewal Rights	Other	Total
Balance, beginning of year	**$ 5**	**$ 7**	**$ 12**

Amortization, net of the accretion of interest	(3)	(3)	(6)
Balance, ending of year	**$ 2**	**$ 4**	**$ 6**
For the year ended December 31, 2005			
Balance, beginning of year	**$ 9**	**$ 9**	**$ 18**
Acquisition of business		1	1
Amortization, net of the accretion of interest	(4)	(3)	(7)
Balance, ending of year	**$ 5**	**$ 7**	**$ 12**
For the year ended December 31, 2004			
Balance, beginning of year	**$ 13**	**$ 10**	**$ 23**
Acquisition of business		2	2
Amortization, net of the accretion of interest	(4)	(3)	(7)
Balance, ending of year	**$ 9**	**$ 9**	**$ 18**

Estimated future net amortization expense for the succeeding five years is as follows:

For the years ended December 31,	
2007	$3
2008	2
2009	1
2010	
2011	

For a discussion of present value of future profits that continue to be subject to amortization and aggregate amortization expense, see Note 7.

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

9. Separate Accounts, Death Benefits and Other Insurance Benefit Features

The Hartford records the variable portion of individual variable annuities, 401(k), institutional, governmental, private placement life and variable life insurance products within separate account assets and liabilities, which are reported at fair value. Separate account assets are segregated from other investments. Investment income and gains and losses from those separate account assets, which accrue directly to, and whereby investment risk is borne by the policyholder, are offset by the related liability changes within the same line item in the statement of income. The fees earned for administrative and contract holder maintenance services performed for these separate accounts are included in fee income. During 2006, 2005 and 2004, there were no gains or losses on transfers of assets from the general account to the separate account.

Many of the variable annuity contracts issued by the Company offer various guaranteed minimum death, withdrawal and income benefits. Guaranteed minimum death and income benefits are offered in various forms as described in the footnotes to the table below. The Company currently reinsures a significant portion of the death benefit guarantees associated with its in-force block of business. Effective April 1, 2006, the Company began reinsuring certain of its death benefit guarantees associated with the inforce block of variable annuity products offered in Japan. Changes in the gross U.S. guaranteed minimum death benefit (GMDB) and Japan GMDB/guaranteed minimum income benefits (GMIB) liability balance sold with annuity products are as follows:

	U.S. GMDB [1]	Japan GMDB/GMIB
Liability balance as of January 1, 2006	**$ 158**	**$ 50**
Incurred	129	28
Paid	(106)	(1)
Unlock	294	(41)
Currency translation adjustment		(1)
Liability balance as of December 31, 2006	**$ 475**	**$ 35**

[1] The reinsurance recoverable asset related to the U.S. GMDB was $316 as of December 31, 2006. The reinsurance recoverable asset related to the Japan GMDB was $4 as of December 31, 2006.

	U.S. GMDB [1]	Japan GMDB/GMIB
Liability balance as of January 1, 2005	**$ 174**	**$ 28**
Incurred	123	29
Paid	(139)	(1)
Currency translation adjustment		(6)
Liability balance as of December 31, 2005	**$ 158**	**$ 50**

[1] The reinsurance recoverable asset related to the U.S. GMDB was $40 as of December 31, 2005.

The net GMDB and GMIB liability is established by estimating the expected value of net reinsurance costs and death and income benefits in excess of the projected account balance. The excess death and income benefits and net reinsurance costs are recognized ratably over the accumulation period based on total expected assessments. The GMDB and GMIB liabilities are recorded in Reserve for Future Policy Benefits on the Company s balance sheet. Changes in the GMDB and GMIB liability are recorded in Benefits, Losses and Loss Adjustment Expenses on the

Company s statements of operations. In a manner consistent with the Company s accounting policy for deferred acquisition costs, the Company regularly evaluates estimates used and adjusts the additional liability balances, with a related charge or credit to benefit expense if actual experience or other evidence suggests that earlier assumptions should be revised. As described in Note 1, the Company unlocked its assumptions related to GMDB during the fourth quarter of 2006.

The determination of the GMDB and GMIB liabilities and related GMDB reinsurance recoverable is based on models that involve a range of scenarios and assumptions, including those regarding expected market rates of return and volatility, contract surrender rates and mortality experience. The following assumptions were used to determine the GMDB and GMIB liabilities as of December 31, 2006 and 2005:

U.S. GMDB:

1000 stochastically generated investment performance scenarios for all issue years.

For all issue years, the weighted average return is 8%; it varies by asset class with a low of 3% for cash and a high of 10% for aggressive equities.

Discount rate of 7.5% for issue year 2002 & prior; discount rate of 7% for issue year 2003 & 2004 and discount rate of 5.6% for issue year 2005 and 2006.

Volatilities also vary by asset class with a low of 1% for cash, a high of 12% for aggressive equities, and a weighted average of 11%.

100% of the Hartford experience mortality table was used for the mortality assumptions.

Lapse rates by calendar year vary from a low of 8% to a high of 14%, with an average of 12%.

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

9. Separate Accounts, Death Benefits and Other Insurance Benefit Features (continued)

Japan GMDB and GMIB:

1,000 stochastically generated investment performance scenarios.

Separate account returns, representing the Company s long-term assumptions, varied by asset class with a low of 2.7% for Japan bonds, a high of 9.3% for foreign equities and a weighted average of 5.0%.

Volatilities also varied by asset class with a low of 5.6% for Japan bonds, a high of 21.3% for foreign equities and a weighted average of 13.4%.

70% of the 1996 Japan Standard Mortality Table was used for mortality assumptions.

Lapse rates by age vary from a low of 1% to a high of 6%, with an average of 4%.

Average discount rate of 2.7%.

The following table provides details concerning GMDB and GMIB exposure as of December 31, 2006:

Breakdown of Individual Variable and Group Annuity Account Value by GMDB/GMIB Type at December 31, 2006

Maximum anniversary value (MAV) [1]	Account Value	Net Amount at Risk	Retained Net Amount at Risk	Weighted Average Attained Age of Annuitant
MAV only	$ 53,358	$ 3,664	$ 343	65
With 5% rollup [2]	3,830	349	67	63
With Earnings Protection Benefit Rider (EPB) [3]	5,576	471	77	61
With 5% rollup & EPB	1,411	149	28	63
Total MAV	64,175	4,633	515	
Asset Protection Benefit (APB) [4]	36,710	61	32	62
Lifetime Income Benefit (LIB) Death Benefit [5]	4,045	9	9	61
Reset [6] (5-7 years)	6,862	243	243	65
Return of Premium [7] /Other	10,015	28	25	54
Subtotal U.S. Guaranteed Minimum Death Benefits	**121,807**	**4,974**	**824**	
Japan Guaranteed Minimum Death and Income Benefit [8]	29,653	54	19	66
Total at December 31, 2006	**$151,460**	**$ 5,028**	**$ 843**	

[1] MAV: the death benefit is the greatest of current account value, net premiums paid and the highest account value

on any anniversary before age 80 (adjusted for withdrawals).

[2] *Rollup: the death benefit is the greatest of the MAV, current account value, net premium paid and premiums (adjusted for withdrawals) accumulated at generally 5% simple interest up to the earlier of age 80 or 100% of adjusted premiums.*

[3] *EPB: the death benefit is the greatest of the MAV, current account value, or contract value plus a percentage of the contract s growth. The contract s growth is account value less premiums net of withdrawals, subject to a cap of 200% of premiums net of withdrawals.*

[4] *APB: the death benefit is the greater of current account value or MAV,*

not to exceed current account value plus 25% times the greater of net premiums and MAV (each adjusted for premiums in the past 12 months).

[5] LIB: the death benefit is the greater of current account value or MAV, net premiums paid, or a benefit amount that rachets over time, generally based on market performance.

[6] Reset: the death benefit is the greatest of current account value, net premiums paid and the most recent five to seven year anniversary account value before age 80 (adjusted for withdrawals).

[7] Return of premium: the death benefit is the greater of current account value and net premiums paid.

[8] Death benefits include a Return of Premium and

MAV (before age 75) death benefit and income benefits include a guarantee to return initial investment, which is adjusted for earnings liquidity or a maximum annual withdrawal of 3% of premiums, depending on product, through a fixed annuity, after a minimum deferral period of 10, 15, or 20 years. The guaranteed remaining account value balance related to the Japan GMIB was $19.7 billion and $15.2 billion as of December 31, 2006 and 2005, respectively.

The Company offers certain variable annuity products with a GMWB rider. The GMWB provides the policyholder with a guaranteed remaining balance (GRB) if the account value is reduced to zero through a combination of market declines and withdrawals. The GRB is generally equal to premiums less withdrawals. However, annual withdrawals that exceed a specific percentage of the premiums paid may reduce the GRB by an amount greater than the withdrawals and may also impact the guaranteed annual withdrawal amount that subsequently applies after the excess annual withdrawals occur. For certain of the withdrawal benefit features, the policyholder also has the option, after a specified time period, to reset the GRB to the then-current account value, if greater. In addition, the Company has introduced features, for contracts issued beginning in the fourth quarter of 2005, that allow the policyholder to receive the guaranteed annual withdrawal amount for as long as they are alive. In this feature, in all cases the contract holder or their beneficiary will receive the GRB and the GRB is reset on an annual basis to the maximum anniversary account value subject to a cap.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

9. Separate Accounts, Death Benefits and Other Insurance Benefit Features (continued)

The GMWB represents an embedded derivative in the variable annuity contracts that is required to be reported separately from the host variable annuity contract. It is carried at fair value and reported in other policyholder funds. The fair value of the GMWB obligation is calculated based on actuarial and capital market assumptions related to the projected cash flows, including benefits and related contract charges, over the lives of the contracts, incorporating expectations concerning policyholder behavior. Because of the dynamic and complex nature of these cash flows, best estimate assumptions and stochastic techniques under a variety of market return scenarios are used. Estimating these cash flows involves numerous estimates and subjective judgments including those regarding expected market rates of return, market volatility, correlations of market returns and discount rates. At each valuation date, the Company assumes expected returns based on risk-free rates as represented by the current LIBOR forward curve rates; market volatility assumptions for each underlying index based on a blend of observed market implied volatility data and annualized standard deviations of monthly returns using the most recent 20 years of observed market performance; correlations of market returns across underlying indices based on actual observed market returns and relationships over the ten years preceding the valuation date; and current risk-free spot rates as represented by the current LIBOR spot curve to determine the present value of expected future cash flows produced in the stochastic projection process. As markets change, mature and evolve and actual policyholder behavior emerges, management continually evaluates the appropriateness of its assumptions. In addition, management regularly evaluates the valuation model, incorporating emerging valuation techniques where appropriate, including drawing on the expertise of market participants and valuation experts.

As of December 31, 2006 and December 31, 2005, the embedded derivative asset recorded for GMWB, before reinsurance or hedging, was $53 and $8, respectively. During 2006, 2005 and 2004, the increase (decrease) in value of the GMWB, before reinsurance and hedging, reported in realized gains was $121 and $(64) and $54, respectively. Included in realized gain (loss) were liability model refinements and changes in policyholder behavior assumptions for the year ended December 31, 2006 of $(2). There were no benefit payments made for the GMWB during 2006, 2005 or 2004.

As of December 31, 2006 and December 31, 2005, $37.3 billion, or 77%, and $26.4 billion, or 69%, respectively, of account value representing substantially all of the contracts written after July 2003, with the GMWB feature were unreinsured. In order to minimize the volatility associated with the unreinsured GMWB liabilities, the Company has established an alternative risk management strategy. In 2003, the Company began hedging its unreinsured GMWB exposure using interest rate futures and swaps and Standard and Poor s (S&P) 500 and NASDAQ index options and futures contracts. During 2004, the Company began using Europe, Australasia and Far East (EAFE) Index swaps to hedge GMWB exposure to international equity markets. The total (reinsured and unreinsured) GRB as of December 31, 2006 and 2005 was $37.8 billion and $31.8 billion, respectively.

A contract is in the money if the contract holder s GRB is greater than the account value. For contracts that were in the money , the Company s exposure as of December 31, 2006, was $8. However, the only ways the contract holder can monetize the excess of the GRB over the account value of the contract is upon death or if their account value is reduced to zero through a combination of a series of withdrawals that do not exceed a specific percentage of the premiums paid per year and market declines. If the account value is reduced to zero, the contract holder will receive a period certain annuity equal to the remaining GRB or a period certain plus life contingent annuity. As the amount of the excess of the GRB over the account value can fluctuate with equity market returns on a daily basis the ultimate amount to be paid by the Company, if any, is uncertain and could be significantly more or less than $8.

Account balances of contracts with guarantees were invested in variable separate accounts as follows:

Asset type	As of December 31, 2006
Equity securities (including mutual funds)	$ 104,687

Cash and cash equivalents	8,931
Total	**$ 113,618**

As of December 31, 2006, approximately 12% of the equity securities above were invested in fixed income securities through these funds and approximately 88% were invested in equity securities.

10. Sales Inducements

The Company currently offers enhanced crediting rates or bonus payments to contract holders on certain of its individual and group annuity products. The expense associated with offering a bonus is deferred and amortized over the life of the related contract in a pattern consistent with the amortization of deferred policy acquisition costs. Amortization expense associated with expenses previously deferred is recorded over the remaining life of the contract. Consistent with the Company s DAC unlock, the Company unlocked the amortization of the sales inducement asset. See Note 1, for more information concerning the DAC unlock.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

10. Sales Inducements (continued)

Changes in deferred sales inducement activity were as follows for the year ended December 31:

	2006	2005
Balance, beginning of period	$ 355	$ 309
Sales inducements deferred	88	85
Amortization charged to income	(42)	(39)
Amortization DAC unlock	(4)	
Balance, end of period	**$ 397**	**$ 355**

11. Reserves for Losses and Loss Adjustment Expenses

As described in Note 1, The Hartford establishes reserves for losses and loss adjustment expenses on reported and unreported claims. These reserve estimates are based on known facts and interpretations of circumstances, and consideration of various internal factors including The Hartford s experience with similar cases, historical trends involving claim payment patterns, loss payments, pending levels of unpaid claims, loss control programs and product mix. In addition, the reserve estimates are influenced by consideration of various external factors including court decisions, economic conditions and public attitudes. The effects of inflation are implicitly considered in the reserving process.

The establishment of appropriate reserves, including reserves for catastrophes and asbestos and environmental claims, is inherently uncertain. The Hartford regularly updates its reserve estimates as new information becomes available and events unfold that may have an impact on unsettled claims. Changes in prior year reserve estimates, which may be material, are reflected in the results of operations in the period such changes are determined to be necessary. For further discussion of asbestos and environmental claims, see Note 12.

Life

The following table displays the development of the loss reserves (included in reserve for future policy benefits and unpaid losses and loss adjustment expenses in the Consolidated Balance Sheets) resulting primarily from group disability products.

	For the years ended December 31,		
	2006	2005	2004
Beginning loss reserves-gross	**$ 4,832**	**$ 4,714**	**$ 4,480**
Purchase of CNA Group Life Assurance Company			20
Reinsurance recoverables	238	297	250
Beginning loss reserves-net	**4,594**	**4,417**	**4,210**
Incurred expenses related to			
Current year	2,140	1,994	1,864
Prior years	(128)	(112)	(73)
Total incurred expenses	**2,012**	**1,882**	**1,791**
Paid expenses related to			
Current year	724	645	564

Prior years	1,130	1,060	1,020
Total paid expenses	**1,854**	**1,705**	**1,584**
Ending loss reserves-net	**4,752**	**4,594**	**4,417**
Reinsurance recoverable, December 31	233	238	297
Ending loss reserves-gross	**$ 4,985**	**$ 4,832**	**$ 4,714**

The favorable prior year claim development in 2006 and 2005 is principally due to continued strong disability claims management as well as favorable development on the experience rated financial institutions block. The favorable loss experience on the financial institutions block inversely impacts the commission expenses incurred.
The liability for future policy benefits and unpaid losses and loss adjustment expenses is comprised of the following:

	2006	**2005**
Group Disability and Accident and Other unpaid losses and loss adjustment expenses	$ 4,985	$ 4,832
Group Life unpaid losses and loss adjustment expenses	1,132	910
Individual Life unpaid losses and loss adjustment expenses	110	84
Future Policy Benefits	7,789	7,161
Future Policy Benefits and Unpaid Losses and Loss Adjustment Expenses	**$ 14,016**	**$ 12,987**

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

11. Reserves for Losses and Loss Adjustment Expenses (continued)

The liability for future policy benefits and unpaid losses and loss adjustment expenses by segment/product is as follows:

	2006	2005
Life		
Retail		
Individual annuity variable	$ 372	$ 171
Individual annuity fixed	488	575
Other	3	1
Total Retail	863	747
Retirement Plans		
401(k)	67	56
Governmental	290	310
Total Retirement Plans	357	366
Institutional		
Structured settlements	3,285	3,028
Institutional annuities	2,317	2,167
SPIA	206	
PPLI	117	120
Total Institutional	5,925	5,315
Individual Life		
Variable universal life	16	15
Universal life/other interest sensitive	87	81
Term insurance and other	520	490
Total Individual Life	623	586
Group Benefits		
Group disability	4,695	4,544
Group life and accident	1,236	1,058
Other	219	226
Total Group Benefits	6,150	5,828
International		
Variable	38	51
Total International	38	51

Other	60	94
Total Life	**$ 14,016**	**$ 12,987**

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

11. Reserves for Losses and Loss Adjustment Expenses (continued)

The liability for other policyholder funds and benefits payable by segment/product is as follows:

	2006	2005
Life		
Retail		
Individual annuity variable	$ 9,425	$ 6,861
Individual annuity fixed	5,663	9,539
Other	7	10
Total Retail	15,095	16,410
Retirement Plans		
401(k)	1,257	1,181
Governmental	4,287	4,013
Total Retirement Plans	5,544	5,194
Institutional		
Structured settlements	1,973	1,731
Stable value/Funding agreements	6,169	4,142
GICs	2,875	3,117
SPIA	140	
PPLI	235	232
Institutional annuities	13	11
Total Institutional	11,405	9,233
Individual Life		
Variable universal life	515	474
Universal life/other interest sensitive	4,599	4,284
Other	229	232
Total Individual Life	5,343	4,990
Group Benefits		
Group life and accident	352	535
Total Group Benefits	352	535
International		
Variable	30,085	24,641
Fixed	1,697	1,461
Total International	31,782	26,102

Other	1,790	1,988
Total Life	**$ 71,311**	**$ 64,452**

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

11. Reserves for Losses and Loss Adjustment Expenses (continued)

Property & Casualty

A rollforward of liabilities for property and casualty unpaid losses and loss adjustment expenses follows:

	For the years ended December 31,		
	2006	**2005**	**2004**
Beginning liabilities for property and casualty unpaid losses and loss adjustment expenses-gross	**$ 22,266**	**$ 21,329**	**$ 21,715**
Reinsurance and other recoverables	5,403	5,138	5,497
Beginning liabilities for property and casualty unpaid losses and loss adjustment expenses-net	**16,863**	**16,191**	**16,218**
Add provision for property & casualty unpaid losses and loss adjustment expenses			
Current year	6,706	6,715	6,590
Prior years	296	248	414
Total provision for property and casualty unpaid losses and loss adjustment expenses	**7,002**	**6,963**	**7,004**
Less payments			
Current year	2,448	3,593	2,616
Prior years	3,702	2,698	4,415
Total payments	**6,150**	**6,291**	**7,031**
Less net reserves for Omni business sold	**111**		
Ending liabilities for property and casualty unpaid losses and loss adjustment expenses-net	**17,604**	**16,863**	**16,191**
Reinsurance and other recoverables	4,387	5,403	5,138
Ending liabilities for property and casualty unpaid losses and loss adjustment expenses-gross	**$ 21,991**	**$ 22,266**	**$ 21,329**

In the opinion of management, based upon the known facts and current law, the reserves recorded for The Hartford s property and casualty businesses at December 31, 2006 represent the Company s best estimate of its ultimate liability for losses and loss adjustment expenses related to losses covered by policies written by the Company. Based on information or trends that are not presently known, future reserve reestimates may result in adjustments to these reserves. Such adjustments could possibly be significant, reflecting any variety of new and adverse or favorable trends. Because of the significant uncertainties surrounding environmental and particularly asbestos exposures, it is possible that management s estimate of the ultimate liabilities for these claims may change and that the required adjustment to recorded reserves could exceed the currently recorded reserves by an amount that could be material to The Hartford s results of operations, financial condition and liquidity. For a further discussion, see Note 12.

Examples of current trends affecting frequency and severity include increases in medical cost inflation rates, the changing use of medical care procedures, the introduction of new products such as the Dimensions for auto product in

Personal Lines, changes in internal claim practices, changes in the legislative and regulatory environment over workers compensation claims, evolving exposures to claims asserted against religious institutions and other organizations relating to molestation or abuse and other mass torts. In the case of the reserves for asbestos exposures, factors contributing to the high degree of uncertainty include inadequate loss development patterns, plaintiffs expanding theories of liability, the risks inherent in major litigation, and inconsistent emerging legal doctrines. In the case of the reserves for environmental exposures, factors contributing to the high degree of uncertainty include expanding theories of liabilities and damages; the risks inherent in major litigation; inconsistent decisions concerning the existence and scope of coverage for environmental claims; and uncertainty as to the monetary amount being sought by the claimant from the insured.

The prior year provision of $296 in 2006 includes $243 of prior accident year development resulting from an agreement with Equitas and the Company s evaluation of the reinsurance recoverables and allowance for uncollectible reinsurance associated with older, long-term casualty liabilities reported in the Other Operations. In addition, the prior year provision in 2006 includes strengthening of Specialty Commercial construction defect claim reserves for accident years 1997 and prior and adverse development in environmental reserves. The 2006 reserve strengthening was partially offset by a reduction in catastrophe reserves related to the 2005 and 2004 hurricanes and a release of Business Insurance allocated loss adjustment expense reserves for workers compensation and package business related to accident years 2003 to 2005. The prior year provision of $248 in 2005 includes reserve strengthening for workers compensation claim payments expected to emerge after 20 years of development, an increase in reserves for assumed casualty reinsurance, adverse development in environmental reserves, strengthening of reserves for the 2004 hurricanes and an increase in general liability reserves for accident years 2000 to 2003. The 2005 reserve strengthening was partially offset by reserve releases for allocated loss adjustment expenses and workers compensation reserves for accident years 2003 and 2004. The

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

11. Reserves for Losses and Loss Adjustment Expenses (continued)

prior year provision of $414 in 2004 includes reserve strengthening for construction defects claims, assumed casualty reinsurance and environmental claims as well as a reduction in the reinsurance recoverable asset associated with older, long-term casualty liabilities. The 2004 reserve strengthening was partially offset by a reduction in September 11 reserves.

12. Commitments and Contingencies

Litigation

The Hartford is involved in claims litigation arising in the ordinary course of business, both as a liability insurer defending or providing indemnity for third-party claims brought against insureds and as an insurer defending coverage claims brought against it. The Hartford accounts for such activity through the establishment of unpaid loss and loss adjustment expense reserves. Subject to the uncertainties discussed below under the caption Asbestos and Environmental Claims, management expects that the ultimate liability, if any, with respect to such ordinary-course claims litigation, after consideration of provisions made for potential losses and costs of defense, will not be material to the consolidated financial condition, results of operations or cash flows of The Hartford.

The Hartford is also involved in other kinds of legal actions, some of which assert claims for substantial amounts. These actions include, among others, putative state and federal class actions seeking certification of a state or national class. Such putative class actions have alleged, for example, underpayment of claims or improper underwriting practices in connection with various kinds of insurance policies, such as personal and commercial automobile, property, life and inland marine; improper sales practices in connection with the sale of life insurance and other investment products; and improper fee arrangements in connection with mutual funds and structured settlements. The Hartford also is involved in individual actions in which punitive damages are sought, such as claims alleging bad faith in the handling of insurance claims. Like many other insurers, The Hartford also has been joined in actions by asbestos plaintiffs asserting that insurers had a duty to protect the public from the dangers of asbestos and in a putative class action filed in West Virginia state court by asbestos plaintiffs alleging that insurers committed unfair trade practices by asserting defenses on behalf of their policyholders in the underlying asbestos cases. Management expects that the ultimate liability, if any, with respect to such lawsuits, after consideration of provisions made for estimated losses, will not be material to the consolidated financial condition of The Hartford. Nonetheless, given the large or indeterminate amounts sought in certain of these actions, and the inherent unpredictability of litigation, an adverse outcome in certain matters could, from time to time, have a material adverse effect on the Company s consolidated results of operations or cash flows in particular quarterly or annual periods.

Broker Compensation Litigation On October 14, 2004, the New York Attorney General s Office filed a civil complaint (the NYAG Complaint) against Marsh Inc. and Marsh & McLennan Companies, Inc. (collectively, Marsh) alleging, among other things, that certain insurance companies, including The Hartford, participated with Marsh in arrangements to submit inflated bids for business insurance and paid contingent commissions to ensure that Marsh would direct business to them. The Hartford was not joined as a defendant in the action, which has since settled. Since the filing of the NYAG Complaint, several private actions have been filed against the Company asserting claims arising from the allegations of the NYAG Complaint.

Two securities class actions, now consolidated, have been filed in the United States District Court for the District of Connecticut alleging claims against the Company and certain of its executive officers under Section 10(b) of the Securities Exchange Act and SEC Rule 10b-5. The consolidated amended complaint alleges on behalf of a putative class of shareholders that the Company and the four named individual defendants, as control persons of the Company, failed to disclose to the investing public that The Hartford s business and growth was predicated on the unlawful activity alleged in the NYAG Complaint. The class period alleged is August 6, 2003 through October 13, 2004, the day before the NYAG Complaint was filed. The complaint seeks damages and attorneys fees. Defendants filed a motion to dismiss in June 2005, and, on July 13, 2006, the district court granted the motion. The plaintiffs have noticed an appeal of the dismissal.

Two corporate derivative actions, now consolidated, also have been filed in the same court. The consolidated amended complaint, brought by shareholders on behalf of the Company against its directors and an executive officer, alleges that the defendants knew adverse non-public information about the activities alleged in the NYAG Complaint and concealed and misappropriated that information to make profitable stock trades, thereby breaching their fiduciary duties, abusing their control, committing gross mismanagement, wasting corporate assets, and unjustly enriching themselves. The complaint seeks damages, injunctive relief, disgorgement, and attorneys fees. Defendants filed a motion to dismiss in May 2005, and the plaintiffs thereafter agreed to stay further proceedings pending resolution of the motion to dismiss the securities class action. All defendants dispute the allegations and intend to defend these actions vigorously.

The Company is also a defendant in a multidistrict litigation in federal district court in New Jersey. There are two consolidated amended complaints filed in the multidistrict litigation, one related to alleged conduct in connection with the sale of property-casualty insurance and the other related to alleged conduct in connection with the sale of group benefits products. The Company and various of its subsidiaries are named in both complaints. The actions assert, on behalf of a class of persons who purchased insurance through the broker defendants, claims under the Sherman Act, the Racketeer Influenced and Corrupt Organizations Act (RICO),

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Commitments and Contingencies (continued)

state law, and in the case of the group benefits complaint, claims under ERISA arising from conduct similar to that alleged in the NYAG Complaint. The class period alleged is 1994 through the date of class certification, which has not yet occurred. The complaints seek treble damages, injunctive and declaratory relief, and attorneys fees. On October 3, 2006, the court denied in part the defendants motions to dismiss the two consolidated amended complaints but found the complaints deficient in other respects and ordered the plaintiffs to file supplemental pleadings. After the plaintiffs filed their supplemental pleadings, the defendants renewed their motions to dismiss. The renewed motions to dismiss and the plaintiffs motions for class certification are pending. The Company also has been named in two similar actions filed in state courts, which the defendants have removed to federal court. Those actions currently are transferred to the court presiding over the multidistrict litigation. The Company disputes the allegations in all of these actions and intends to defend the actions vigorously. In addition, the Company was joined as a defendant in an action by the California Commissioner of Insurance alleging similar conduct by various insurers in connection with the sale of group benefits products. The Commissioner s action asserted claims under California insurance law and sought injunctive relief only. The Company has settled the Commissioner s action.

Additional complaints may be filed against the Company in various courts alleging claims under federal or state law arising from the conduct alleged in the NYAG Complaint. The Company s ultimate liability, if any, in the pending and possible future suits is highly uncertain and subject to contingencies that are not yet known, such as how many suits will be filed, in which courts they will be lodged, what claims they will assert, what the outcome of investigations by the New York Attorney General s Office and other regulatory agencies will be, the success of defenses that the Company may assert, and the amount of recoverable damages if liability is established. In the opinion of management, it is possible that an adverse outcome in one or more of these suits could have a material adverse effect on the Company s consolidated results of operations or cash flows in particular quarterly or annual periods.

Fair Credit Reporting Act Putative Class Action In October 2001, a complaint was filed in the United States District Court for the District of Oregon, on behalf of a putative class of homeowners and automobile policyholders from 1999 to the present, alleging that the Company willfully violated the Fair Credit Reporting Act (FCRA) by failing to send appropriate notices to new customers whose initial rates were higher than they would have been had the customer had a more favorable credit report. In July 2003, the district court granted summary judgment for the Company, holding that FCRA s adverse action notice requirement did not apply to the rate first charged for an initial policy of insurance. The plaintiff appealed and, in August 2005, a panel of the United States Court of Appeals for the Ninth Circuit reversed the district court, holding that the adverse action notice requirement applies to new business and that the Company s notices, even when sent, contained inadequate information. Although no court previously had decided the notice requirements applicable to insurers under FCRA, and the district court had not addressed whether the Company s alleged violations of FCRA were willful because it had agreed with the Company s interpretation of FCRA and found no violation, the Court of Appeals further held, over a dissent by one of the judges, that the Company s failure to send notices conforming to the Court s opinion constituted a willful violation of FCRA as a matter of law. FCRA provides for a statutory penalty of $100 to $1,000 per willful violation. Simultaneously, the Court of Appeals issued decisions in related cases against four other insurers, reversing the district court and holding that those insurers also had violated FCRA in similar ways. On October 3, 2005, the Court of Appeals withdrew its opinion in the Hartford case and issued a revised opinion, which changed certain language of the opinion but not the outcome.

On October 31, 2005, the Company timely filed a petition for rehearing and for rehearing en banc in the Ninth Circuit. While that petition was pending, on January 25, 2006, the Court of Appeals again withdrew its opinion in the Hartford case and issued a second revised opinion. The new opinion vacated the Court s earlier ruling that the Company had willfully violated FCRA as a matter of law and remanded the case to the district court for further proceedings. On February 15, 2006, the Company filed a new petition for rehearing and rehearing en banc, and on April 20, 2006, the Court of Appeals denied the petition. On July 19, 2006, the Company filed a petition for a writ of certiorari in the United States Supreme Court. On September 26, 2006, the Supreme Court granted petitions filed by insurers in two of the related cases, and on January 16, 2007, it heard argument in those cases. The Supreme Court has not yet acted on the Company s petition.

On July 25, 2006, the parties entered into a memorandum of understanding setting forth the essential terms of a class settlement in this action, and, on September 8, 2006, the parties executed and filed with the district court a Stipulation of Settlement. On September 11, 2006, the district court preliminarily approved the settlement and scheduled a hearing for final approval of the settlement for February 26, 2007. The settlement is subject to certain contingencies, including final approval by the district court. If the settlement is completed, management expects that the Company s ultimate obligations under the settlement agreement, after consideration of provisions made for this matter, will not have a material adverse effect on the Company s consolidated results of operations or cash flows in any particular quarterly or annual period.

Blanket Casualty Treaty Litigation The Company is engaged in pending litigation in Connecticut Superior Court against certain of its upper-layer reinsurers under its Blanket Casualty Treaty (BCT). The BCT is a multi-layered reinsurance program providing excess-of-loss coverage in various amounts from the 1930s through the 1980s. The upper layers were first placed in 1950,

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Commitments and Contingencies (continued)

predominantly with London Market reinsurers, including Lloyd s syndicates reinsured by Equitas. The action seeks, among other relief, damages for the reinsurer defendants failure to pay certain billings for asbestos and pollution claims.

In December 2003, the Company entered into a global settlement with MacArthur Company, an asbestos insulation distributor and installer then in bankruptcy, for $1.15 billion. The Company then billed the reinsurer defendants under the BCT for $117 of the settlement amount. After the reinsurers refused to pay the MacArthur billing, the Company amended its complaint to add, among other things, claims related to that billing. Most of the reinsurer defendants counterclaimed, seeking a declaration that they did not owe reinsurance for the MacArthur settlement.

The litigation concerns under what circumstances losses arising from multiple claims against a single insured may be combined and ceded as a single accident under the BCT so as to reach the upper layers of the program. The BCT contains a unique definition of accident. The application of this definition to the ceded losses is the crux of the dispute.

In April 2005, the Superior Court phased the proceedings, providing for a trial of the MacArthur billing first, in April 2006, with other billings to follow in subsequent trial settings. In September 2005, the London Market reinsurer defendants moved for summary judgment on the MacArthur-related claims. After briefing and oral argument, the Superior Court issued a decision on December 13, 2005, granting the defendants motion. The Company noticed an appeal to the Connecticut Appellate Court; the appeal has since been transferred to the Connecticut Supreme Court. The Company intends to prosecute its appeal vigorously.

On June 15, 2006, the Company announced an agreement with Equitas and all Lloyd s syndicates reinsured by Equitas (collectively, Equitas) that resolved, with minor exception, all of the Company s ceded and assumed domestic reinsurance exposures with Equitas, including the Company s reinsurance recoveries from Equitas under the BCT. Those recoveries consist predominantly of asbestos and pollution losses, including the billing for the MacArthur settlement. The pending litigation and appeal continue with other upper-layer reinsurers under the BCT.

The outcome of the appeal is uncertain. If the decision of the Superior Court is affirmed on appeal, the Company may be unable to collect from the nonsettling reinsurers not only its billing for the MacArthur settlement but also other current and future billings to which the same relevant facts and legal analysis would apply. The Company has considered the risk of non-collection of these recoveries in its allowance for uncollectible reinsurance recoverables associated with older, long-term casualty liabilities reported in the Other Operations segment. After consideration of this allowance, management expects that a negative outcome in the BCT litigation would not have a material adverse effect on the Company s consolidated results of operations or cash flows in any particular quarterly or annual period.

Asbestos and Environmental Claims

The Company continues to receive asbestos and environmental claims. Asbestos claims relate primarily to bodily injuries asserted by people who came in contact with asbestos or products containing asbestos. Environmental claims relate primarily to pollution and related clean-up costs.

The Company wrote several different categories of insurance contracts that may cover asbestos and environmental claims. First, the Company wrote primary policies providing the first layer of coverage in an insured s liability program. Second, the Company wrote excess policies providing higher layers of coverage for losses that exhaust the limits of underlying coverage. Third, the Company acted as a reinsurer assuming a portion of those risks assumed by other insurers writing primary, excess and reinsurance coverages. Fourth, subsidiaries of the Company participated in the London Market, writing both direct insurance and assumed reinsurance business.

With regard to both environmental and particularly asbestos claims, significant uncertainty limits the ability of insurers and reinsurers to estimate the ultimate reserves necessary for unpaid losses and related expenses. Traditional actuarial reserving techniques cannot reasonably estimate the ultimate cost of these claims, particularly during periods where theories of law are in flux. The degree of variability of reserve estimates for these exposures is significantly greater than for other more traditional exposures. In particular, the Company believes there is a high degree of uncertainty inherent in the estimation of asbestos loss reserves.

In the case of the reserves for asbestos exposures, factors contributing to the high degree of uncertainty include inadequate loss development patterns, plaintiffs expanding theories of liability, the risks inherent in major litigation, and inconsistent emerging legal doctrines. Furthermore, over time, insurers, including the Company, have experienced significant changes in the rate at which asbestos claims are brought, the claims experience of particular insureds, and the value of claims, making predictions of future exposure from past experience uncertain. Plaintiffs and insureds also have sought to use bankruptcy proceedings, including pre-packaged bankruptcies, to accelerate and increase loss payments by insurers. In addition, some policyholders have asserted new classes of claims for coverages to which an aggregate limit of liability may not apply. Further uncertainties include insolvencies of other carriers and unanticipated developments pertaining to the Company s ability to recover reinsurance for asbestos and environmental claims. Management believes these issues are not likely to be resolved in the near future.

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THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Commitments and Contingencies (continued)

In the case of the reserves for environmental exposures, factors contributing to the high degree of uncertainty include expanding theories of liability and damages; the risks inherent in major litigation; inconsistent decisions concerning the existence and scope of coverage for environmental claims; and uncertainty as to the monetary amount being sought by the claimant from the insured.

It is also not possible to predict changes in the legal and legislative environment and their effect on the future development of asbestos and environmental claims. It is unknown whether potential Federal asbestos-related legislation will be enacted or what its effect would be on the Company s aggregate asbestos liabilities.

The reporting pattern for assumed reinsurance claims, including those related to asbestos and environmental claims, is much longer than for direct claims. In many instances, it takes months or years to determine that the policyholder s own obligations have been met and how the reinsurance in question may apply to such claims. The delay in reporting reinsurance claims and exposures adds to the uncertainty of estimating the related reserves.

Given the factors described above, the Company believes the actuarial tools and other techniques it employs to estimate the ultimate cost of claims for more traditional kinds of insurance exposure are less precise in estimating reserves for its asbestos and environmental exposures. For this reason, the Company relies on exposure-based analysis to estimate the ultimate costs of these claims and regularly evaluates new information in assessing its potential asbestos and environmental exposures.

As of December 31, 2006 and December 31, 2005, the Company reported $2.3 billion and $2.3 billion of net asbestos reserves and $322 and $366 of net environmental reserves, respectively. The Company believes that its current asbestos and environmental reserves are appropriate. However, analyses of future developments could cause The Hartford to change its estimates and ranges of its asbestos and environmental reserves, and the effect of these changes could be material to the Company s consolidated operating results, financial condition, and liquidity.

Regulatory Developments

In June 2004, the Company received a subpoena from the New York Attorney General s Office in connection with its inquiry into compensation arrangements between brokers and carriers. In mid-September 2004 and subsequently, the Company has received additional subpoenas from the New York Attorney General s Office, which relate more specifically to possible anti-competitive activity among brokers and insurers. Since the beginning of October 2004, the Company has received subpoenas or other information requests from Attorneys General and regulatory agencies in more than a dozen jurisdictions regarding broker compensation and possible anti-competitive activity. The Company may receive additional subpoenas and other information requests from Attorneys General or other regulatory agencies regarding similar issues. In addition, the Company has received a request for information from the New York Attorney General s Office concerning the Company s compensation arrangements in connection with the administration of workers compensation plans. The Company intends to continue cooperating fully with these investigations, and is conducting an internal review, with the assistance of outside counsel, regarding broker compensation issues in its Property & Casualty and Group Benefits operations.

On October 14, 2004, the New York Attorney General s Office filed a civil complaint against Marsh & McLennan Companies, Inc., and Marsh, Inc. (collectively, Marsh). The complaint alleges, among other things, that certain insurance companies, including the Company, participated with Marsh in arrangements to submit inflated bids for business insurance and paid contingent commissions to ensure that Marsh would direct business to them. The Company was not joined as a defendant in the action, which has since settled. Although no regulatory action has been initiated against the Company in connection with the allegations described in the civil complaint, it is possible that the New York Attorney General s Office or one or more other regulatory agencies may pursue action against the Company or one or more of its employees in the future. The potential timing of any such action is difficult to predict. If such an action is brought, it could have a material adverse effect on the Company.

On October 29, 2004, the New York Attorney General s Office informed the Company that the Attorney General is conducting an investigation with respect to the timing of the previously disclosed sale by Thomas Marra, a director and executive officer of the Company, of 217,074 shares of the Company s common stock on September 21, 2004. The sale occurred shortly after the issuance of two additional subpoenas dated September 17, 2004 by the New York Attorney General s Office. The Company has engaged outside counsel to review the circumstances related to the transaction and is fully cooperating with the New York Attorney General s Office. On the basis of the review, the Company has determined that Mr. Marra complied with the Company s applicable internal trading procedures and has found no indication that Mr. Marra was aware of the additional subpoenas at the time of the sale.

There continues to be significant federal and state regulatory activity relating to financial services companies, particularly mutual funds companies. These regulatory inquiries have focused on a number of mutual fund issues, including market timing and late trading, revenue sharing and directed brokerage, fees, transfer agents and other fund service providers, and other mutual-fund related issues. The Company has received requests for information and subpoenas from the SEC, subpoenas from the New York Attorney General s Office, a subpoena from the Connecticut Attorney General s Office, requests for information from the Connecticut Securities and Investments Division of the Department of Banking, and requests for information from the New York Department of

THE HARTFORD FINANCIAL SERVICES GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Commitments and Contingencies (continued)

Insurance, in each case requesting documentation and other information regarding various mutual fund regulatory issues. The Company continues to cooperate fully with these regulators in these matters.

The Company has received subpoenas from the New York Attorney General s Office and the Connecticut Attorney General s Office requesting information relating to the Company s group annuity products, including single premium group annuities used in terminal and maturity funding programs. These subpoenas seek information about how various group annuity products are sold, how the Company selects mutual funds offered as investment options in certain group annuity products, and how brokers selling the Company s group annuity products are compensated. The Company continues to cooperate fully with these regulators in these matters.

On May 10, 2006, the Company entered into an agreement (the Agreement) with the New York Attorney General s Office and the Connecticut Attorney General s Office to resolve the outstanding investigations by these parties regarding the Company s use of expense reimbursement agreements in its terminal and maturity funding group annuity line of business. Under the terms of the Agreement, the Company paid $20, of which $16.1 was paid to certain plan sponsors that purchased terminal or maturity funding annuities between January 1, 1998 and December 31, 2004, with the balance of $3.9 divided equally between the states of New York and Connecticut. Also pursuant to the terms of the Agreement, the Company accepted a three-year prohibition on the use of contingent compensation in its terminal and maturity funding group annuity line of business. The costs associated with the settlement had already been accounted for in reserves previously established by the Company.

On November 8, 2006, the SEC issued an Order setting forth the terms of a settlement reached with three subsidiaries of the Company that resolved the SEC s Division of Enforcement s investigation of aspects of the Company s variable annuity and mutual fund operations related to directed brokerage and revenue sharing. Under the terms of the settlement, the Company has paid $55 to mutual funds that participated in the Company s program for directed brokerage in recognition of mutual fund sales, $40 of which represents disgorgement and $15 of which represents civil penalties. The costs associated with the settlement had already been accounted for in reserves previously established by the Company.

The SEC s Division of Enforcement and the New York Attorney General s Office are investigating aspects of the Company s variable annuity and mutual fund operations related to market timing. The Company continues to cooperate fully with the SEC and the New York Attorney General s Office in these matters. The Company s mutual funds are available for purchase by the separate accounts of different variable universal life insurance policies, variable annuity products, and funding agreements, and they are offered directly to certain qualified retirement plans. Although existing products contain transfer restrictions between subaccounts, some products, particularly older variable annuity products, do not contain restrictions on the frequency of transfers. In addition, as a result of the settlement of litigation against the Company with respect to certain owners of older variable annuity contracts, the Company s ability to restrict transfers by these owners has, until recently, been limited. The Company has executed an agreement with the parties to the previously settled litigation which, together with separate agreements between these contract owners and their broker, has resulted in the exchange or surrender of all of the variable annuity contracts that were the subject of the previously settled litigation.

To date, the SEC s and New York Attorney General s market timing investigations have not resulted in the initiation of any formal action against the Company by these regulators. However, the Company believes that the SEC and the New York Attorney General s Office are likely to take some action against the Company at the conclusion of the respective investigations. The Company is engaged in discussions with the SEC and the New York Attorney General s Office regarding the potential resolution of these investigations. The potential timing of any resolution of these matters or the initiation of any formal action by these regulators is difficult to predict. After giving effect to the settlement of the SEC s directed brokerage investigation, as of December 31, 2006, the Company had a reserve of $83, pre-tax, for the market timing matters. This reserve is an estimate; in view of the uncertainties regarding the outcome of these regulatory investigations, it is possible that the ultimate cost to the Company of these matters could exceed the reserve by an amount that would have a material adverse effect on the Company s consolidated results of operations or cash flows in a particular quarterly or annual period.

On May 24, 2005, the Company received a subpoena from the Connecticut Attorney General s Office seeking information about the Company s participation in finite reinsurance transactions in which there was no substantial transfer of risk between the parties. The Company is cooperating fully with the Connecticut Attorney General s Office in this matter.

On June 23, 2005, the Company received a subpoena from the New York Attorney General s Office requesting information relating to purchases of the Company s variable annuity products, or exchanges of other products for the Company s variable annuity products, by New York residents who were 65 or older at the time of the purchase or exchange. On August 25, 2005, the Company received an additional subpoena from the New York Attorney General s Office requesting information relating to purchases of or exchanges into the Company s variable annuity products by New York residents during the past five years where the purchase or exchange was funded using funds from a tax-qualified plan or where the variable annuity purchased or exchanged for was a sub-

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12. Commitments and Contingencies (continued)

account of a tax-qualified plan or was subsequently put into a tax-qualified plan. The Company is cooperating fully with the New York Attorney General s Office in these matters.

On July 14, 2005, the Company received an additional subpoena from the Connecticut Attorney General s Office concerning the Company s structured settlement business. This subpoena requests information about the Company s sale of annuity products for structured settlements, and about the ways in which brokers are compensated in connection with the sale of these products. The Company is cooperating fully with the Connecticut Attorney General s Office in these matters.

The Company has received a request for information from the New York Attorney General s Office about issues relating to the reporting of workers compensation premium. The Company is cooperating fully with the New York Attorney General s Office in this matter.

Lease Commitments

Total rental expense on operating leases was $201 in 2006, $206 in 2005 and $193 in 2004. Future minimum lease commitments are as follows:

2007	$169
2008	125
2009	96
2010	79
2011	31
Thereafter	24
Total	**$524**

On June 30, 2003, the Company entered into a sale-leaseback of certain furniture and fixtures with a net book value of $40. The sale-leaseback resulted in a gain of $15, which was deferred and will be amortized into earnings over the initial lease term of three years. The lease qualifies as an operating lease for accounting purposes. At the end of the initial lease term, the Company has the option to purchase the leased assets, renew the lease for two one-year periods or return the leased assets to the lessor. If the Company elects to return the assets to the lessor at the end of the initial lease term, the assets will be sold, and the Company has guaranteed a residual value on the furniture and fixtures of $20. If the fair value of the furniture and fixtures were to decline below the residual value, the Company would have to make up the difference under the residual value guarantee. In December 2006 the Company exercised its option to extend the lease contract until June 30, 2008. Under the sale-leaseback, the Company must maintain a minimum level of consolidated statutory surplus and risk based capital ratios. In addition, the Company must not exceed a maximum ratio of debt to capitalization. As of December 31, 2006, the Company was in compliance with all such covenants. As of December 31, 2006 and 2005, no liability was recorded for this guarantee, as the fair value of the furniture and fixtures at the end of the initial lease term was greater than the residual value guarantee.

Tax Matters

The Company s federal income tax returns are routinely audited by the Internal Revenue Service (IRS). The IRS began its audit of the 2002-2003 tax years in 2005 and is in the examination phase. Management believes that adequate provision has been made in the financial statements for any potential assessments that may result from future tax examinations and other tax-related matters for all open tax years. During 2004, the IRS completed its examination of the 1998-2001 tax years, and the IRS and the Company agreed upon all adjustments. As a result, during 2004 the Company booked a $216 tax benefit to reflect the impact of the audit settlement on tax years covered by the examination as well as all other tax years prior to 2004. The benefit relates primarily to the separate account DRD and interest.

The separate account DRD is estimated for the current year using information from the prior year-end, adjusted for current year equity market performance. The estimated DRD is generally updated in the third quarter for the provision-to-filed-return adjustments, and in the fourth quarter based on current year ultimate mutual fund distributions and fee income from The Hartford s variable insurance products. The actual current year DRD can vary from the estimates based on, but not limited to, changes in eligible dividends received by the mutual funds, amounts of distributions from these mutual funds, the utilization of capital loss carry forwards at the mutual fund level and appropriate levels of taxable income.

The Company receives a foreign tax credit (FTC) against its U.S. tax liability for foreign taxes paid by the Company including payments from its separate account assets. The separate account FTC is estimated for the current year using information from the most recent filed return, adjusted for the change in the allocation of separate account investments to the international equity markets during the current year. The actual current year FTC can vary from the estimates due to the actual FTC s passed through by the mutual funds.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

12. Commitments and Contingencies (continued)

Unfunded Commitments

At December 31, 2006, The Hartford has outstanding commitments totaling approximately $1.4 billion, of which approximately $1.0 billion is committed to fund limited partnership investments. These capital commitments can be called by the partnership during the commitment period (on average two to five years) to fund the purchase of new investments and partnership expenses. Once the commitment period expires, the Company is under no obligation to fund the remaining unfunded commitment but may elect to do so. The remaining outstanding commitments are primarily related to various funding obligations associated with investments in mortgage and construction loans. These have a commitment period of one month to three years.

Guaranty Fund and Other Insurance-related Assessments

In all states, insurers licensed to transact certain classes of insurance are required to become members of a guaranty fund. In most states, in the event of the insolvency of an insurer writing any such class of insurance in the state, members of the funds are assessed to pay certain claims of the insolvent insurer. A particular state s fund assesses its members based on their respective written premiums in the state for the classes of insurance in which the insolvent insurer was engaged. Assessments are generally limited for any year to one or two percent of premiums written per year depending on the state.

The Hartford accounts for guaranty fund and other insurance assessments in accordance with Statement of Position No. 97-3, Accounting by Insurance and Other Enterprises for Insurance-Related Assessments . Liabilities for guaranty fund and other insurance-related assessments are accrued when an assessment is probable, when it can be reasonably estimated, and when the event obligating the Company to pay an imposed or probable assessment has occurred. Liabilities for guaranty funds and other insurance-related assessments are not discounted and are included as part of other liabilities in the Consolidated Balance Sheets. As of December 31, 2006 and 2005, the liability balance was $149 and $223, respectively. As of December 31, 2006 and 2005, $20 and $20, respectively, related to premium tax offsets were included in other assets.

13. Income Tax

The provision (benefit) for income taxes consists of the following:

	For the years ended D