TechTarget Inc
Form 10-Q
November 14, 2008

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2008

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

For the transition period from _____ to _____

Commission File Number: 1-33472

TECHTARGET, INC.
(Exact name of registrant as specified in its charter)

Delaware	04-3483216
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

117 Kendrick Street, Suite 800
Needham, Massachusetts 02494
(Address of principal executive offices) (zip code)

(781) 657-1000
(Registrant's telephone number, including area code)

(Former name, former address and formal fiscal year, if changed since last report): Not applicable

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

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

Large Accelerated Filer o	Accelerated Filer o	Non-Accelerated Filer þ (Do not check if a smaller reporting company)	Smaller Reporting Company o

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

As of September 30, 2008, there were outstanding 41,550,724 shares of the registrant’s common stock, par value $0.001.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

TECHTARGET, INC.
Consolidated Balance Sheets
(In thousands, except share and per share data)

Assets	September 30, 2008 (Unaudited)	December 31, 2007
Current assets:		
Cash and cash equivalents	$ 38,212	$ 10,693
Short-term investments	21,097	51,308
Accounts receivable, net of allowance for doubtful accounts of $607 and $424 as of September 30, 2008 (unaudited) and December 31, 2007, respectively	17,529	15,198
Prepaid expenses and other current assets	6,279	1,962
Deferred tax assets	2,642	2,947
Total current assets	85,759	82,108
Property and equipment, net	4,044	4,401
Long-term investments	7,770	-
Goodwill	88,326	88,326
Intangible assets, net of accumulated amortization	17,917	21,939
Deferred tax assets	3,617	2,910
Other assets	180	203
Total assets	$ 207,613	$ 199,887
Liabilities and Stockholders' Equity		
Current liabilities:		
Current portion of bank term loan payable	$ 3,000	$ 3,000
Accounts payable	2,794	2,919
Income taxes payable	-	1,031
Accrued expenses and other current liabilities	2,107	2,473
Accrued compensation expenses	926	2,600
Deferred revenue	5,698	3,761
Total current liabilities	14,525	15,784
Long-term liabilities:		
Other liabilities	324	455
Bank term loan payable, net of current portion	750	3,000
Total liabilities	15,599	19,239
Commitments (Note 9)	-	-
Stockholders' equity:		
Preferred stock, 5,000,000 shares authorized; no shares issued or outstanding	-	-
Common stock, $0.001 par value per share, 100,000,000 shares authorized, 41,550,724 and 41,081,616 shares issued and outstanding at September 30, 2008 (unaudited) and December 31, 2007, respectively	42	41

Additional paid-in capital		219,872		209,773
Warrants		2		13
Accumulated other comprehensive loss		(130)		(102)
Accumulated deficit		(27,772)		(29,077)
Total stockholders' equity		192,014		180,648
Total liabilities and stockholders' equity	$	207,613	$	199,887

See accompanying notes.

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TECHTARGET, INC.
Consolidated Statements of Operations
(In thousands, except share and per share data)

	Three Months Ended September 30, 2008	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
	(Unaudited)			
Revenues:				
Online	$ 18,631	$ 14,687	$ 58,338	$ 44,726
Events	5,496	6,912	16,743	16,201
Print	1,088	1,702	3,384	5,323
Total revenues	25,215	23,301	78,465	66,250
Cost of revenues:				
Online (1)	5,462	3,769	16,113	11,194
Events (1)	2,328	2,283	7,078	6,065
Print (1)	580	862	1,758	2,990
Total cost of revenues	8,370	6,914	24,949	20,249
Gross profit	16,845	16,387	53,516	46,001
Operating expenses:				
Selling and marketing (1)	8,161	7,271	25,490	19,811
Product development (1)	2,788	1,677	8,440	5,021
General and administrative (1)	3,662	3,364	10,915	8,917
Depreciation	579	401	1,884	1,095
Amortization of intangible assets	1,259	1,171	4,071	2,971
Total operating expenses	16,449	13,884	50,800	37,815
Operating income	396	2,503	2,716	8,186
Interest income (expense):				
Interest income	336	1,043	1,236	2,058
Interest expense	(88)	(146)	(302)	(851)
Total interest income	248	897	934	1,207
Income before provision for income taxes	644	3,400	3,650	9,393
Provision for income taxes	958	1,568	2,345	3,996
Net (loss) income	$ (314)	$ 1,832	$ 1,305	$ 5,397
Net (loss) income per common share:				
Basic	$ (0.01)	$ 0.05	$ 0.03	$ 0.06
Diluted	$ (0.01)	$ 0.04	$ 0.03	$ 0.05
Weighted average common shares outstanding:				
Basic	41,533,020	40,354,796	41,355,812	24,282,474
Diluted	41,533,020	43,336,498	43,393,429	27,184,670

(1) Amounts include stock-based compensation expense as follows:

Cost of online revenue	$ 264	$ 16	$ 401	$ 156
Cost of events revenue	53	20	100	43
Cost of print revenue	1	(1)	5	18
Selling and marketing	1,057	930	3,796	2,054
Product development	140	84	420	230
General and administrative	648	604	2,107	1,421

See accompanying notes.

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TECHTARGET, INC.
Consolidated Statements of Cash Flows
(In thousands)

	Nine Months Ended September 30, 2008	Nine Months Ended September 30, 2007
	(Unaudited)	
Operating Activities:		
Net income	$ 1,305	$ 5,397
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	5,955	4,066
Provision for bad debt	378	117
Stock-based compensation expense	6,829	3,922
Non-cash interest expense	5	310
Deferred tax benefit	(402)	(373)
Excess tax benefit - stock options	(1,015)	(2,518)
Changes in operating assets and liabilities, net of businesses acquired:		
Accounts receivable	(2,709)	(441)
Prepaid expenses and other current assets	(3,255)	193
Other assets	18	745
Accounts payable	(125)	193
Income taxes payable	(1,031)	(1,854)
Accrued expenses and other current liabilities	(366)	(344)
Accrued compensation expenses	(1,674)	(543)
Deferred revenue	1,937	3,046
Other liabilities	(84)	(110)
Net cash provided by operating activities	5,766	11,806
Investing activities:		
Purchases of property and equipment, and other assets	(1,527)	(2,344)
Purchases of short-term investments	(50,407)	(284,247)
Purchases of long-term investments	(7,885)	-
Proceeds from sales and maturities of short-term investments	80,618	196,346
Proceeds from sales and maturities of long-term investments	41	-
Acquisition of assets	(50)	(1,013)
Acquisition of businesses, net of cash acquired	-	(15,015)
Net cash provided by (used in) investing activities	20,790	(106,273)
Financing activities:		
Proceeds from revolving credit facility	-	12,000
Payments made on revolving credit facility	-	(12,000)
Payments on bank term loan payable	(2,250)	(2,250)
Proceeds from initial public offering, net of stock issuance costs	-	83,161
Excess tax benefit - stock options	1,015	2,518
Proceeds from exercise of warrants and stock options	2,198	977
Net cash provided by financing activities	963	84,406
Net increase in cash and cash equivalents	27,519	(10,061)
Cash and cash equivalents at beginning of period	10,693	30,830

Cash and cash equivalents at end of period	$	38,212	$	20,769
Supplemental disclosure of cash flow information:				
Cash paid for interest	$	258	$	489
Cash paid for taxes	$	4,484	$	4,437

See accompanying notes.

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TECHTARGET, INC.
Notes to Consolidated Financial Statements
(In thousands, except share and per share data)

1. Organization and Operations

TechTarget, Inc. (the Company) is a leading provider of specialized online content that brings together buyers and sellers of corporate information technology, or IT, products. The Company sells customized marketing programs that enable IT vendors to reach corporate IT decision makers who are actively researching specific IT purchases.

The Company’s integrated content platform consists of a network of over 50 websites that are complemented with targeted in-person events and two specialized IT magazines. Throughout all stages of the purchase decision process, these content offerings meet IT professionals' needs for expert, peer and IT vendor information, and provide a platform on which IT vendors can launch targeted marketing campaigns that generate measurable, high return on investment (ROI). As IT professionals have become increasingly specialized, they have come to rely on our sector-specific websites for purchasing decision support. The Company’s content enables IT professionals to navigate the complex and rapidly changing IT landscape where purchasing decisions can have significant financial and operational consequences. Based upon the logical clustering of users' respective job responsibilities and the marketing focus of the products that the Company’s customers are advertising, content offerings are currently categorized across eleven distinct media groups: Application Development; Channel; CIO and IT Management; Data Center; Enterprise Applications; Laptops and Mobile Technology; Networking; Security; Storage; Vertical Software; and Windows and Distributed Computing.

2. Summary of Significant Accounting Policies

The accompanying consolidated financial statements reflect the application of certain significant accounting policies as described below and elsewhere in these notes to the consolidated financial statements.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, which include KnowledgeStorm, Inc., Bitpipe, Inc., TechTarget Securities Corporation and TechTarget, Ltd. KnowledgeStorm, Inc. was acquired by the Company on November 6, 2007 and is a leading online search resource providing vendor generated content targeted toward corporate IT professionals. Bitpipe, Inc. is a leading provider of in-depth IT content including white papers, product literature, and case studies from IT vendors. TechTarget Securities Corporation is a Massachusetts Securities Corporation incorporated in 2004. TechTarget, Ltd. is a subsidiary doing business principally in the United Kingdom. All significant intercompany accounts and transactions have been eliminated in consolidation.

Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. All adjustments, which, in the opinion of management, are considered necessary for a fair presentation of the results of operations for the periods shown, are of a normal recurring nature and have been reflected in the consolidated financial statements. The results of operations for the periods presented are not necessarily indicative of results to be expected for any other interim periods or for the full year. The information included in these consolidated financial statements should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and

Results of Operations" contained in this report and the consolidated financial statements and accompanying notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

Use of Estimates

The preparation of financial statements in conformity with U.S. accounting principles generally accepted requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures 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.

Revenue Recognition

The Company generates substantially all of its revenue from the sale of targeted advertising campaigns that are delivered via its network of websites, events and print publications. Revenue is recognized in accordance with Staff Accounting Bulletin (SAB) No. 104, Revenue Recognition, and Financial Accounting Standards Board's (FASB) Emerging Issues Task Force (EITF) Issue No. 00-21, Revenue Arrangements With Multiple Deliverables. Revenue is recognized only when the service has been provided and when there is persuasive evidence of an arrangement, the fee is fixed or determinable and collection of the receivable is reasonably assured.

Online media. Revenue for online media offerings is recognized for specific online media offerings as follows:

- White Papers. White paper revenue is recognized ratably over the period in which the white paper is available on the Company's websites.

- Webcasts, Podcasts and Videocasts. Webcast and videocast revenue is recognized in the period in which the webcast or videocast occurs. Podcast revenue is recognized in the period in which it is first posted and becomes available on the Company's websites.

- Software Package Comparisons. Software package comparison revenue is recognized ratably over the period in which the software information is available on the Company's websites.

- Dedicated E-mails, E-mail Newsletters. Dedicated e-mail and e-newsletter revenue is recognized in the period in which the e-mail or e-newsletter is sent to registered members.

- List Rentals. List rental revenue is recognized in the period in which the e-mails are sent to the list of registered members.

- Banners. Banner revenue is recognized in the period in which the banner impressions occur.

- Contextual Advertising. Our contextual advertising programs associate IT vendor white papers, webcasts, podcasts or other content on a particular topic with our related sector-specific content. Revenue on these program components is recognized in accordance with the specific component's policy as described above.

- Third Party Revenue Sharing Arrangements. The Company has arrangements with certain third parties, including for the licensing of its online content, for the renting of its database of opted-in email subscribers and for which advertising from customers of certain third parties is made available to the Company's website visitors. In each of these arrangements the Company is paid a share of the resulting revenue, and the revenue is recognized in the period in which the services are performed.

The Company offers customers the ability to purchase integrated ROI program offerings, which can include multiple online media offerings packaged together to address the particular customer's specific advertising requirements. As part of these offerings, the Company may guarantee a minimum number of qualified sales leads to be delivered over the course of the integrated ROI program advertising campaign. Throughout the advertising campaign, revenue is recognized as individual offerings are delivered, and the lead guarantee commitments are closely monitored to assess campaign performance. If the minimum number of qualified sales leads is not met by the scheduled completion date of the advertising campaign, the campaign is extended, as a result of which the Company will extend the time period over which it recognizes revenue. In accordance with EITF Issue No. 00-21, revenue is deferred for any undelivered offerings equal to a pro-rata amount of the fair value of the additional media offerings as compared to the total combined value of the original contract and the fair value of the additional media offerings. The fair value of the additional media offerings is determined based on standard rate card pricing for each of the additional media offerings. The Company estimates the additional media offerings to be delivered during the extended period based on historical lead generation performance for each of the offerings. The Company has managed and completed over 1,000 integrated ROI program offerings since 2004, which it feels provides a reasonable basis to establish these estimates. For the three months ended September 30, 2008, the Company has deferred approximately $750 of revenue related to integrated ROI program offerings for which it has not yet delivered the guaranteed minimum number of qualified sales leads. Standard contractual terms and conditions for integrated ROI program offerings provide that the Company has the right to extend the advertising campaign in order to satisfy lead shortfalls. During the twelve months ended September 30, 2008, lead shortfalls for integrated ROI program offerings were satisfied, and revenue was recognized, within an average extended period of 41 days.

Amounts collected or billed prior to satisfying the above revenue recognition criteria are recorded as deferred revenue.

While each online media offering can be sold separately, most of the Company's online media sales involve multiple online offerings. At inception of the arrangement, the Company evaluates the deliverables to determine whether they represent separate units of accounting under EITF Issue No. 00-21. Deliverables are deemed to be separate units of accounting if all of the following criteria are met: the delivered item has value to the customer on a standalone basis; there is objective and reliable evidence of the fair value of the item(s); and delivery or performance of the item(s) is considered probable and substantially in the Company's control. The Company allocates revenue to each unit of accounting in a transaction based upon its fair value as determined by vendor objective evidence. Vendor objective evidence of fair value for all elements of an arrangement is based upon the normal pricing and discounting practices for those online media offerings when sold to other similar customers. If vendor objective evidence of fair value has not been established for all items under the arrangement, no allocation can be made, and the Company recognizes revenue on all online media offerings over the term of the arrangement.

Event sponsorships. Sponsorship revenues from events are recognized upon completion of the event in the period that the event occurs. Amounts collected or billed prior to satisfying the above revenue recognition criteria are recorded as deferred revenue. The majority of the Company's events are free to qualified attendees, however certain of the Company's events are based on a paid attendee model. Revenue is recognized for paid attendee events upon completion of the event and receipt of payment from the attendee. Deferred revenue relates to collection of the attendance fees in advance of the event.

Print publications. Advertising revenues from print publications are recognized at the time the applicable publication is distributed. Amounts collected or billed prior to satisfying the above revenue recognition criteria are recorded as deferred revenue.

Fair Value of Financial Instruments

Financial instruments consist of cash and cash equivalents, short and long-term investments, accounts receivable, accounts payable, a term loan payable and an interest rate swap. The carrying value of these instruments approximates their estimated fair values.

Long-lived Assets

Long-lived assets consist of property and equipment, goodwill and other intangible assets. Goodwill and other intangible assets arise from acquisitions and are recorded in accordance with Statement of Financial Accounting Standards (SFAS) No. 142, Goodwill and Other Intangible Assets. In accordance with this statement, a specifically identified intangible asset must be recorded as a separate asset from goodwill if either of the following two criteria is met: (1) the intangible asset acquired arises from contractual or other legal rights; or (2) the intangible asset is separable. Accordingly, intangible assets consist of specifically identified intangible assets. Goodwill is the excess of any purchase price over the estimated fair market value of net tangible assets acquired not allocated to specific intangible assets.

As required by SFAS No. 142, goodwill and indefinite-lived intangible assets are not amortized, but are reviewed annually for impairment or more frequently if impairment indicators arise. Separable intangible assets that are not deemed to have an indefinite life are amortized over their estimated useful lives, which range from one to nine years, using methods of amortization that are expected to reflect the estimated pattern of economic use, and are reviewed for impairment when events or changes in circumstances suggest that the assets may not be recoverable under SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. The Company performs its annual test of impairment of goodwill on December 31st of each year, and whenever events or changes in circumstances suggest that the carrying amount may not be recoverable. Based on this evaluation, the Company believes that, as of each of the balance sheet dates presented, none of the Company's goodwill or other long-lived assets was impaired.

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Internal Use Software and Website Development Costs

The Company accounts for website development costs according to the guidance in the EITF Issue No. 00-2, Accounting for Web Site Development Costs, which requires that costs incurred during the development of website applications and infrastructure involving developing software to operate a website be capitalized. Additionally, all costs relating to internal use software are accounted for under Statement of Position (SOP) 98-1, Accounting for the Cost of Computer Software Developed or Obtained for Internal Use. The estimated useful life of costs capitalized is evaluated for each specific project. Capitalized internal use software and website development costs are reviewed for recoverability whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. An impairment loss shall be recognized only if the carrying amount of the asset is not recoverable and exceeds its fair value. The Company capitalized internal-use software and website development costs of $320 and $191 for the three months ended September 30, 2008 and 2007, respectively, and $342 and $889 for the nine months ended September 30, 2008 and 2007, respectively.

Income Taxes

The Company accounts for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes, which is the asset and liability method for accounting and reporting for income taxes. Under SFAS No. 109, deferred tax assets and liabilities are recognized based on temporary differences between the financial reporting and income tax bases of assets and liabilities using statutory rates. In addition, SFAS No. 109 requires a valuation allowance against net deferred tax assets if, based upon available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

In July 2006, the FASB issued Financial Accounting Standards Interpretation No. 48, Accounting for Uncertainty in Income Taxes, (FIN 48), which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109. FIN 48 prescribes a recognition and measurement method of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosures and transitions. The Company adopted the provisions of FIN 48 effective January 1, 2007. In accordance with FIN 48, the Company recognizes any interest and penalties related to unrecognized tax benefits in income tax expense.

Stock-Based Compensation

At September 30, 2008, the Company had two stock-based employee compensation plans which are more fully described in Note 11. Effective January 1, 2006, the Company adopted SFAS No. 123(R), Share-Based Payment, which requires companies to expense the fair value of employee stock options and other forms of stock-based compensation. SFAS No. 123(R) requires nonpublic companies that used the minimum value method under SFAS No. 123 for either recognition or pro forma disclosures to apply SFAS No. 123(R) using the prospective-transition method. As such, the Company will continue to apply APB Opinion No. 25 in future periods to equity awards outstanding at the date of adoption of SFAS No. 123(R) that were measured using the minimum value method. In accordance with SFAS No. 123(R), the Company recognizes the compensation cost of employee stock-based awards in the statement of operations using the straight line method over the vesting period of the award. Effective with the adoption of SFAS No. 123(R), the Company has elected to use the Black-Scholes option pricing model to determine the fair value of stock options granted.

Net Income (Loss) Per Share

The Company calculates net income (loss) per share in accordance with SFAS No. 128, Earnings Per Share (SFAS No. 128). Through May 16, 2007, the Company calculated net income per share in accordance with SFAS No. 128, as clarified by EITF Issue No. 03-6, Participating Securities and the Two-Class Method Under FASB Statement No. 128, Earnings Per Share. EITF Issue No. 03-6 clarifies the use of the "two-class" method of calculating earnings per share as originally prescribed in SFAS No. 128. Effective for periods beginning after March 31, 2004, EITF Issue No. 03-6 provides guidance on how to determine whether a security should be considered a "participating security" for purposes of computing earnings per share and how earnings should be allocated to a participating security when using the two-class method for computing basic earnings per share. The Company determined that its convertible preferred stock represented a participating security and therefore adopted the provisions of EITF Issue No. 03-6.

Under the two-class method, basic net income (loss) per share is computed by dividing the net income (loss) applicable to common stockholders by the weighted-average number of common shares outstanding for the fiscal period. Diluted net income (loss) per share is computed using the more dilutive of (a) the two-class method or (b) the if-converted method. The Company allocates net income first to preferred stockholders based on dividend rights under the Company's charter and then to preferred and common stockholders based on ownership interests. Net losses are not allocated to preferred stockholders.

As of May 16, 2007, the effective date of the Company’s initial public offering, the Company transitioned from having two classes of equity securities outstanding, common and preferred stock, to a single class of equity securities outstanding, common stock, upon automatic conversion of all shares of redeemable convertible preferred stock into shares of common stock. In calculating diluted earnings per share for the period January 1, 2007 to May 16, 2007 shares related to redeemable convertible preferred stock were excluded because they were anti-dilutive.

Subsequent to the Company's initial public offering, basic earnings per share is computed based only on the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common shares outstanding during the period, plus the dilutive effect of potential future issuances of common stock relating to stock option programs and other potentially dilutive securities using the treasury stock method. In calculating diluted earnings per share, the dilutive effect of stock options is computed using the average market price for the respective period. In addition, under SFAS No. 123(R), the assumed proceeds under the treasury stock method include the average unrecognized compensation expense and assumed tax benefit of stock options that are in-the-money. This results in the “assumed” buyback of additional shares, thereby reducing the dilutive impact of stock options.

Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141 (revised 2007), Business Combinations (“SFAS 141R”), replacing SFAS No. 141, Business Combinations (“SFAS 141”). SFAS 141R retains the fundamental requirements of purchase method accounting for acquisitions as set forth previously in SFAS 141. However, this statement defines the acquirer as the entity that obtains control of a business in the business combination, thus broadening the scope of SFAS 141 which applied only to business combinations in which control was obtained through transfer of consideration. SFAS 141R also requires several changes in the way assets and liabilities are recognized and measured in purchase accounting including expensing acquisition-related costs as incurred, recognizing assets and liabilities arising from contractual contingencies at the acquisition date, and capitalizing in-process research and development. SFAS 141R also requires the acquirer to recognize a gain in earnings for bargain purchases, or the excess of the fair value of net assets over the consideration transferred plus any noncontrolling interest in the acquiree, a departure from the concept of “negative goodwill” previously recognized under SFAS 141. SFAS 141R is effective for the Company beginning January 1, 2009, and will apply prospectively to business combinations completed on or after that date.

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In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities—an amendment of FASB Statement No. 133 ("SFAS 161"). SFAS 161 changes the disclosure requirements for derivative instruments and hedging activities. Entities are required to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under Statement 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. SFAS 161 encourages, but does not require, comparative disclosures for earlier periods at initial adoption. The Company is currently evaluating the provisions of SFAS 161.

3. Fair Value Measurements

On January 1, 2008, the Company adopted SFAS No. 157, Fair Value Measurements, which, among other things, defines fair value, establishes a consistent framework for measuring fair value and expands disclosure for each major asset and liability category measured at fair value on either a recurring or nonrecurring basis. SFAS No. 157 clarifies that fair value is an exit price, representing the amount that would either be received to sell an asset or be paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, SFAS No. 157 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

- Level 1. Quoted prices in active markets for identical assets and liabilities;
- Level 2. Observable inputs other than quoted prices in active markets; and
- Level 3. Unobservable inputs.

The fair value hierarchy of the Company's financial assets and liabilities carried at fair value and measured on a recurring basis is as follows:

		Fair Value Measurements at Reporting Date Using		
	September 30, 2008	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(Unaudited)		
Money market funds (1)	$ 30,239	$ 30,239	$ -	$ -
Short-term investments	21,097	-	21,097	-
Long-term investments	7,770	-	7,770	-
Interest rate swap (2)	55	-	55	-
Total	$ 59,161	$ 30,239	$ 28,922	$ -

(1) Included in cash equivalents on the accompanying consolidated balance sheet.
(2) Included in other liabilities on the accompanying consolidated balance sheet.

At September 30, 2008, the Company held $1.45 million in one auction rate security classified as a short-term investment in the accompanying consolidated balance sheet. Auction rate securities are variable-rate bonds tied to short-term interest rates with maturities in excess of 90 days.   The interest rate on this security resets through a modified Dutch auction every 35 days. These auctions have historically provided a liquid market for this security. Beginning in March 2008, the Company's investment in this security started failing at auction due to sell orders exceeding buy orders.

The Company considered multiple Level 2 inputs when determining the fair value of the auction rate security at September 30, 2008 as follows;

- The fair value assessment performed by the Company’s investment adviser; and
- Sales activity at par value prior and subsequent to September 30, 2008.

Based on the Level 2 inputs noted above, the Company concluded that the par value of the auction rate securities represents their fair value at September 30, 2008. Subsequent to September 30, 2008, the Company sold $1.45 million of auction rate securities at par value and no longer holds any auction rate securities.

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4. Acquisitions

KnowledgeStorm, Inc.

On November 6, 2007, the Company acquired KnowledgeStorm, Inc. (KnowledgeStorm), which was a privately held company based in Alpharetta, Georgia, for $51,730 in cash and 359,820 shares of common stock of TechTarget valued at $6,000, as well as $230 in transaction costs. KnowledgeStorm is a leading online search resource providing vendor generated content addressing corporate IT professionals. KnowledgeStorm offers IT marketers products with a lead generation and branding focus to reach these corporate IT professionals throughout the purchasing decision process. The acquisition of KnowledgeStorm strengthens the Company’s competitive position and increases its scale, customer penetration and product offerings for advertisers. Once KnowledgeStorm has been fully integrated, the Company expects that cost savings can be achieved as a result of sales and operating efficiencies from the combined operations. Additionally, the Company anticipates that integration of KnowledegeStorm employees into its workforce will increase its capabilities in support of product development, product management and search engine optimization and marketing.

The Company applied the guidance included in EITF Issue No. 98-3, Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or a Business, to conclude that the acquisition of KnowledgeStorm constituted the acquisition of a business. In connection with the acquisition, the Company recorded $45,101 of goodwill and $11,620 of other intangible assets related to customer relationships, technology, trade name, customer backlog and non-compete agreements with estimated useful lives ranging from 12 to 108 months. Of the goodwill recorded in conjunction with the acquisition, none is deductible for income tax purposes.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition.

	As of November 6, 2007	
Cash and cash equivalents	$	2,813
Current assets		1,328
Property and equipment, net		782
Other assets		39
Deferred tax assets		1,797
Intangible assets		11,620
Goodwill		45,101
Total assets acquired		63,480
Total liabilities assumed		(5,520)
Net assets acquired	$	57,960

Within approximately thirty days from the acquisition date, the Company’s management completed its reorganization plan to consolidate KnowledgeStorm's operations. Liabilities assumed in the acquisition include approximately $627 of involuntary termination benefits payable to terminated employees through May 2008, as well as approximately $111 of costs associated with exiting certain operating leases on office space leased by KnowledgeStorm under noncancelable leases that expire through September 2008. As of September 30, 2008 and December 31, 2007, approximately $0 and $616 remained payable under these obligations, respectively.

The estimated fair value of $11,620 of acquired intangible assets is assigned as follows:

	Useful Life	Estimated Fair Value	
Customer relationship intangible asset	108 months	$	4,770

Member database intangible asset	60 months		4,060
Trade name intangible asset	84 months		1,100
Customer order backlog intangible asset	12 months		940
SEO/SEM process intangible asset	36 months		690
Non-compete agreement intangible asset	12 months		60
Total intangible assets		$	11,620

The Company engaged a third party valuation specialist to assist management in determining the fair value of the acquired assets of KnowledgeStorm. To value the customer relationship and backlog intangible assets, an income approach was used, specifically a variation of the discounted cash-flow method. The projected net cash flows for KnowledgeStorm were tax affected using an effective rate of 41% and then discounted using a discount rate of 20.6%. Additionally, the present value of the sum of projected tax benefits was added to arrive at the total fair value of the customer relationship and backlog intangible assets. To value the member database intangible asset, a replacement cost methodology approach was used. The replacement cost of the member database was determined by applying the actual costs incurred to register a new member to the total number of registered members in the acquired database. Additionally, opportunity costs and the present value of the sum of projected tax benefits were added to arrive at the total fair value of the member database intangible asset. To value the trade name intangible asset a relief from royalty method was used to estimate the pre-tax royalty savings to the Company related to the KnowledgeStorm trade name. The projected net cash flows from the pre-tax royalty savings were tax affected using an effective rate of 41% and then discounted using a discount rate of 20.6% to calculate the value of the trade name intangible asset. To value the Search Engine Optimization (SEO)/ Search Engine Marketing (SEM) process intangible asset, a comparative business valuation method was used. Based on an expected life of three years, management projected net cash flows for the Company with and without the SEO/SEM process in place. The present value of the sum of the difference between the net cash flows with and without the SEO/SEM process in place was calculated using a discount rate of 20.6%. Additionally, the present value of the sum of projected tax benefits was added to arrive at the total fair value of the SEO/SEM process intangible asset.

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The following pro forma results of operations for the three and nine months ended September 30, 2007 have been prepared as though the acquisition of KnowledgeStorm had occurred on January 1, 2007. This pro forma unaudited financial information is not indicative of the results of operations that may occur in the future.

	Three Months Ended September 30, 2007	Nine Months Ended September 30, 2007
	(unaudited)	
Total revenues	$ 26,808	$ 78,555
Net income	$ 49	$ 1,047
Net income per common share:		
Basic and diluted	$ 0.00	$ (0.12)

Results of operations for KnowledgeStorm have been included in the Company’s results of operations since the acquisition date of November 6, 2007.

TechnologyGuide.com

On April 26, 2007, the Company acquired substantially all of the assets of TechnologyGuide.com from TechnologyGuide, Inc., which was a privately-held company based in Cincinnati, OH, for $15,000 in cash, plus $15 in acquisition related transaction costs. TechnologyGuide.com is a website business consisting of a portfolio of five websites; Notebookreview.com, Brighthand.com, TabletPCReview.com, DigitalCameraReview.com and SpotStop.com. The websites offer independent product reviews, price comparisons, and forum-based discussions for selected technology products. The acquisition provides the Company with opportunities for growth within the laptop/notebook PC and "smart phone" markets in which it currently does not have a significant presence.

The Company applied the guidance included in EITF Issue No. 98-3, Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or a Business, to conclude that the acquisition of TechnologyGuide.com constituted the acquisition of a business. In connection with this acquisition, the Company recorded $7,035 of goodwill and $7,980 of intangible assets related to developed websites, customer relationships, and non-compete agreements with estimated useful lives ranging from 36 to 72 months.

The estimated fair value of $7,980 of acquired intangible assets is assigned as follows:

	Useful Life	Estimated Fair Value
Developed websites intangible asset	72 months	$ 5,400
Customer relationship intangible asset	60 months	1,790
Non-compete agreements intangible asset	36 months	790
Total intangible assets		$ 7,980

Management engaged a third party valuation specialist to assist in determining the fair value of the acquired assets of TechnologyGuide.com. To value the websites and customer relationship intangible assets, an income approach was used, specifically a variation of the discounted cash-flow method. For the websites intangible asset, expenses and income taxes were deducted from estimated revenues attributable to the existing websites. For the customer relationship intangible asset, expenses and income taxes were deducted from estimated revenues attributable to the existing customers. The projected net cash flows for each were then tax affected using an effective rate of 41% and then discounted using a discount rate of 22.3% to determine the value of the intangible assets, respectively. Additionally, the present value of the sum of projected tax benefits was added to arrive at the total fair value of the intangible assets, respectively. To value the non-compete agreements a comparative business valuation method was used. Based on non-compete terms of 36 months, management projected net cash flows for the Company with and without the non-compete agreements in place. The present value of the sum of the difference between the net cash flows with and without the non-compete agreements in place was calculated, based on a discount rate of 22.3%.

Results of operations for TechnologyGuide.com have been included in the Company's results of operations since the acquisition date of April 26, 2007.

Ajaxian.com

On February 27, 2007, the Company acquired substantially all of the assets of Ajaxian, Inc. (Ajaxian) for a purchase price of $1,013 in cash. Ajaxian is a provider of a website and two events dedicated to providing information and support for the community of developers for "Ajax" (Asynchronous JavaScript and XML), a web development technique for creating interactive web applications.

The Company applied the guidance included in EITF Issue No. 98-3 to conclude that the acquisition of Ajaxian constituted the acquisition of assets. The Company did not acquire any tangible assets from Ajaxian. The following table summarizes the estimated fair value of the intangible assets acquired by the Company at the date of acquisition:

	Useful Life	Estimated Fair Value	
Customer relationship intangible asset	48 months	$	552
Non-compete agreement intangible asset	36 months		335
Trade name intangible asset	60 months		126
Total intangible assets		$	1,013

A contingent payment of $250 in May 2009 is due if certain event revenue and website traffic milestones are met as defined in the purchase agreement. Operating expense will be recorded in the period in which payment of these respective obligations becomes probable under the terms of the agreement.

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5. Cash, Cash Equivalents and Investments

Cash and cash equivalents consist of highly liquid investments with maturities of three months or less at date of purchase. Cash equivalents are carried at cost, which approximates their fair market value. Cash and cash equivalents consisted of the following:

	September 30, 2008 (Unaudited)	December 31, 2007
Cash	$ 7,973	$ 6,714
Money market funds	30,239	3,979
Total cash and cash equivalents	$ 38,212	$ 10,693

Short and long-term investments consist of municipal bonds, auction rate securities and variable rate demand notes. Auction rate securities are variable-rate bonds tied to short-term interest rates with maturities in excess of 90 days. Interest rates on these securities typically reset through a modified Dutch auction at predetermined short-term intervals, usually every 7, 28 or 35 days. Variable rate demand notes are long-term, taxable, or tax-exempt bonds issued on a variable rate basis that can be tendered by the Company for purchase at par whenever interest rates reset, usually every 7 days. Despite the long-term nature of the stated contractual maturities of these variable rate demand notes, the Company has the intent and the ability to quickly liquidate these securities. Auction rate securities and variable rate demand notes are recorded at fair market value, which approximates cost because of their short-term interest rates.

The Company accounts for its short and long-term investments under SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities. All of its investments are treated as "available for sale" under SFAS No. 115, as it is the Company's intention to convert them into cash for general corporate purposes. These investments are recorded at fair value with the related unrealized gains and losses included in accumulated other comprehensive loss, a component of stockholders' equity, net of tax. The unrealized loss as of September 30, 2008 was $74. There was no unrealized gain or loss as of December 31, 2007.

Short and long-term investments consisted of the following:

	September 30, 2008 (Unaudited)	December 31, 2007
Short-term investments:		
Municipal bonds	$ 19,647	$ 19,808
Auction rate securities	1,450	17,000
Variable rate demand notes	-	14,500
Total short-term investments	$ 21,097	$ 51,308

	September 30, 2008 (Unaudited)	December 31, 2007
Long-term investments:		
Municipal bonds	$ 7,770	$ -
Total long-term investments	$ 7,770	$ -

As of September 30, 2008, the auction rate security held by the Company had a maturity date of 2031. Municipal bonds have contractual maturity dates within eighteen months. All income generated from these investments is recorded as interest income.

6. Intangible Assets

Intangible assets subject to amortization as of September 30, 2008 and December 31, 2007 consist of the following:

	As of September 30, 2008			
	Estimated Useful Lives (Years)	Gross Carrying Amount	Accumulated Amortization (Unaudited)	Net
Customer, affiliate and advertiser relationships	1 - 9	$ 12,222	$ (4,156)	$ 8,066
Developed websites, technology and patents	3 - 6	5,400	(1,275)	4,125
Trademark, trade name and domain name	5 - 7	2,044	(811)	1,233
Proprietary user information database and Internet traffic	3 - 5	4,750	(955)	3,795
Non-compete agreements	1 - 3	1,735	(1,037)	698
Total intangible assets		$ 26,151	$ (8,234)	$ 17,917

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	As of December 31, 2007			
	Estimated Useful Lives (Years)	Gross Carrying Amount	Accumulated Amortization	Net
Customer, affiliate and advertiser relationships	1 - 9	$ 19,077	$ (9,140)	$ 9,937
Developed websites, technology and patents	3 - 6	5,976	(1,176)	4,800
Trademark, trade name and domain name	5 - 7	1,994	(521)	1,473
Proprietary user information database and Internet traffic	3 - 5	4,750	(174)	4,576
Non-compete agreements	1 - 3	1,735	(582)	1,153
Total intangible assets		$ 33,532	$ (11,593)	$ 21,939

The Company wrote off approximately $7,431 of fully amortized intangible assets during the nine months ended September 30, 2008 that were no longer in use.

Intangible assets are amortized over their estimated useful lives, which range from one to nine years, using methods of amortization that are expected to reflect the estimated pattern of economic use. The remaining amortization expense will be recognized over a weighted-average period of approximately 2.91 years. Amortization expense was $1,259 and $1,171 for the three months ended September 30, 2008 and 2007 respectively, and $4,071 and $2,971 for the nine months ended September 30, 2008 and 2007, respectively.

The Company expects amortization expense of intangible assets to be as follows:

Years Ending December 31:	Amortization Expense
2008 (October 1st - December 31st)	$ 1,211
2009	4,565
2010	4,052
2011	3,083
2012	2,387
Thereafter	2,619
	$ 17,917

7. Net Income (Loss) Per Common Share

A reconciliation of the numerator and denominator used in the calculation of basic and diluted net (loss) income per common share is as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2008	2007	2008	2007
	(Unaudited)			
Numerator:				
Net (loss) income	$ (314)	$ 1,832	$ 1,305	$ 5,397
Allocation of net (loss) income:				
Accretion of preferred stock dividends	-	-	-	3,948
Net income applicable to preferred stockholders	-	-	-	3,948
Net (loss) income applicable to common stockholders	$ (314)	$ 1,832	$ 1,305	$ 1,449

Denominator:				
Basic:				
Weighted average shares of common stock outstanding	41,533,020	40,354,796	41,355,812	24,282,474
Diluted:				
Weighted average shares of common stock outstanding	41,533,020	40,354,796	41,355,812	24,282,474
Effect of potentially dilutive shares (1)	-	2,981,702	2,037,617	2,902,196
Total weighted average shares of common stock outstanding	41,533,020	43,336,498	43,393,429	27,184,670
Calculation of Net (Loss) Income Per Common Share:				
Basic:				
Net (loss) income applicable to common stockholders	$ (314)	$ 1,832	$ 1,305	$ 1,449
Weighted average shares of stock outstanding	41,533,020	40,354,796	41,355,812	24,282,474
Net (loss) income per common share	$ (0.01)	$ 0.05	$ 0.03	$ 0.06
Diluted:				
Net (loss) income applicable to common stockholders	$ (314)	$ 1,832	$ 1,305	$ 1,449
Weighted average shares of stock outstanding	41,533,020	43,336,498	43,393,429	27,184,670
Net (loss) income per common share	$ (0.01)	$ 0.04	$ 0.03	$ 0.05

(1) In calculating diluted earnings per share, shares related to redeemable convertible preferred stock and outstanding stock options and warrants were excluded for the three months ended September 30, 2008 because they were anti-dilutive.

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8. Bank Term Loan Payable

In August 2006, the Company entered into a credit agreement (the "Credit Agreement") with a commercial bank, which included a $10.0 million term loan (the "Term Loan") and a $20.0 million revolving credit facility (the "Revolving Credit Facility"). Initial borrowings under the Term Loan were used to repay the remaining principal and accrued interest balance of the Bank Term Loan.

The Revolving Credit Facility matures on August 30, 2011. Unless earlier payment is required by an event of default, all principal and unpaid interest will be due and payable on August 30, 2011. At the Company's option, the Revolving Credit Facility bears interest at either the Prime Rate less 1.00% or the LIBOR rate plus the applicable LIBOR margin. The Company is also required to pay an unused line fee on the daily unused amount of its Revolving Credit Facility at a per annum rate of 0.25%. As of September 30, 2008, unused availability under the Revolving Credit Facility totaled $20.0 million.

In August 2007, the Company entered into an amendment to the Credit Agreement. The amendment changed the applicable LIBOR margin from 1.50% to a sliding scale based on the ratio of total funded debt to EBITDA for the preceding four fiscal quarters. As of September 30, 2008, the applicable LIBOR margin was 1.25%.

The Term Loan requires 39 consecutive monthly principal payments of $250, plus interest, beginning on September 30, 2006 through December 30, 2009. As of September 30, 2008, the outstanding balance due under the Term Loan was $3,750. There was no accrued interest on the Term Loan at September 30, 2008.

In September 2006, the Company entered into an interest rate swap agreement with a commercial bank to mitigate the interest rate fluctuations on the Term Loan. With this interest rate swap agreement in place, the Company fixed the annual interest rate at 6.98% for the Term Loan. The interest rate swap agreement terminates in December 2009. Under SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, the interest rate swap agreement is deemed to be a cash flow hedge and qualifies for special accounting using the shortcut method. Accordingly, changes in the fair value of the interest rate swap agreement are recorded in "accumulated other comprehensive loss" on the consolidated balance sheet. As of September 30, 2008 and December 31, 2007, the fair value of the cash flow hedge was $55 and $102, respectively, and is recorded in other liabilities.

Borrowings under the Credit Agreement are collateralized by a security interest in substantially all assets of the Company. Covenants governing the Credit Agreement require the maintenance of certain financial ratios. The Company was in compliance with all financial covenants as of September 30, 2008.

The future maturities of the Term Loan at September 30, 2008 are as follows:

Year Ending December 31,	As of September 30, 2008 (Unaudited)
2008 (October 1st - December 31st)	$ 750
2009	3,000
	3,750
Less current portion	(3,000)
	$ 750

9. Commitments and Contingencies

Operating Leases

The Company conducts its operations in leased office facilities under various noncancelable operating lease agreements. On September 12, 2008, the Company entered into a lease agreement pursuant to which it has agreed to lease approximately 113,017 square feet of a building to be constructed. The Company intends to move all of its operations currently conducted at its Needham, Massachusetts location to these leased premises on or about January 1, 2010.

Future minimum lease payments under noncancelable operating leases at September 30, 2008 are as follows:

Years Ending December 31:	Minimum Lease Payments (Unaudited)
2008 (October 1st - December 31st)	$ 906
2009	3,572
2010	4,140
2011	3,543
2012	3,561
Thereafter	27,400
	$ 43,122

From time to time and in the ordinary course of business, the Company may be subject to various claims, charges, and litigation. At September 30, 2008 and December 31, 2007, the Company did not have any pending claims, charges, or litigation that it expects would have a material adverse effect on its consolidated financial position, results of operations, or cash flows.

10. Comprehensive Income

SFAS No. 130, Reporting Comprehensive Income, establishes standards for reporting and displaying comprehensive income and its components in financial statements. Comprehensive income is defined to include all changes in equity during a period, except those resulting from investments by stockholders and distributions to stockholders. For the three and nine months ended September 30, 2008 and 2007 the Company's comprehensive (loss) income is the sum of net (loss) income, the change in the fair value of the Company's cash flow hedge and unrealized loss on investments, as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2008	2007	2008	2007
	(Unaudited)			
Net (loss) income	$ (314)	$ 1,832	$ 1,305	$ 5,397
Other comprehensive income:				
Unrealized loss on investments	(74)	-	(74)	-
Change in fair value of cash flow hedge	36	(47)	47	(14)
Total comprehensive (loss) income	$ (352)	$ 1,785	$ 1,278	$ 5,383

11. Stock-Based Compensation

Stock Option Plans

In September 1999, the Company approved a stock option plan (the 1999 Plan) that provides for the issuance of up to 12,384,646 shares of common stock incentives. The 1999 Plan provides for the granting of incentive stock options (ISOs), nonqualified stock options (NSOs), and stock grants. These incentives may be offered to the Company's employees, officers, directors, consultants, and advisors, as defined. ISOs may be granted at no less than fair market value on the date of grant, as determined by the Company's Board of Directors (the Board) (no less than 110% of fair market value on the date of grant for 10% or greater stockholders), subject to limitations, as defined. Each option shall be exercisable at such times and subject to such terms as determined by the Board, generally four years, and shall expire within ten years of issuance. No further awards will be made pursuant to the 1999 Plan, but any outstanding awards under the 1999 Plan will remain in effect and will continue to be subject to the terms of the 1999 Plan.

In April 2007, the Board approved the 2007 Stock Option and Incentive Plan (the 2007 Plan), which was approved by the stockholders and became effective upon the consummation of the Company's IPO in May 2007. The 2007 Plan allows the Company to grant ISOs, NSOs, stock appreciation rights, deferred stock awards, restricted stock and other awards. Under the 2007 Plan, stock options may not be granted at less than fair market value on the date of grant, and options generally vest over a four year period. Stock options granted under the 2007 Plan expire no later than ten years after the grant date. The Company originally reserved for issuance an aggregate of 2,911,667 shares of common stock under the 2007 Plan plus an additional annual increase to be added automatically on January 1 of each year, beginning on January 1, 2008, equal to the lesser of (a) 2% of the outstanding number of shares of common stock (on a fully-diluted basis) on the immediately preceding December 31 and (b) such lower number of shares as may be determined by our compensation committee. The number of shares available for issuance under the 2007 Plan is subject to adjustment in the event of a stock split, stock dividend or other change in capitalization. Generally, shares that are forfeited or canceled from awards under the 2007 Plan will be available for future awards. In addition, shares subject to stock options returned to the 1999 Plan, as a result of their expiration, cancellation or termination, are automatically made available for issuance under the 2007 Plan. As of September 30, 2008 a total of 2,623,002 shares were available for grant under the 2007 Plan.

Accounting for Stock-Based Compensation

The Company uses the Black-Scholes option pricing model to calculate the grant-date fair value of an award. The Company calculated the fair values of the options granted using the following assumptions:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Expected volatility	41%	*	41%-46%	49%-50%
Expected term (in years)	6.25	*	6.25	6.25
Risk-free interest rate	3.07%	*	3.07%-3.15%	4.61%-5.04%
Expected dividend yield	-%	*	-%	-%
Weighted-average grant date fair value per share	$ 3.43	*	$ 4.68	$ 7.71

* The Company did not grant any stock option awards during the three months ended September 30, 2007

As there was no public market for the Company's common stock prior to the Company's IPO in May 2007, and limited historical information on the volatility of its common stock since the date of the Company's IPO, the Company determined the volatility for options granted in the nine months ended September 30, 2008 based on an analysis of reported data for a peer group of companies that issued options with substantially similar terms. The expected volatility of options granted has been determined using an average of the historical volatility measures of this peer group of companies for a period equal to the expected term of the option. The expected term of options has been determined utilizing the "simplified" method as prescribed by the SEC's Staff Accounting Bulletin No. 107, Share-Based Payment. The risk-free interest rate is based on a zero coupon United States treasury instrument whose term is consistent with the expected life of the stock options. The Company has not paid and does not anticipate paying cash dividends on its shares of common stock; therefore, the expected dividend yield is assumed to be zero. In addition, SFAS No. 123(R) requires companies to utilize an estimated forfeiture rate when calculating the expense for the period. The Company applied a forfeiture rate of 4.00% based on its historical forfeiture experience during the previous two years in determining the expense recorded in the nine months ended September 30, 2008 and 2007.

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A summary of the activity under the Company's stock option plan as of September 30, 2008 and changes during the three and nine month periods then ended is presented below:

Quarter-to-Date Activity	Options Outstanding	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term in Years	Aggregate Intrinsic Value
		(Unaudited)		
Options outstanding at June 30, 2008	6,963,989	$ 6.64		
Options granted	40,000	7.62		
Options exercised	(25,372)	4.43		
Options forfeited	(45,933)	10.46		
Options canceled	(39,684)	12.07		
Options outstanding at September 30, 2008	6,893,000	$ 6.60	6.7	$ 10,357
Options exercisable at September 30, 2008	4,133,836	$ 4.88	5.7	$ 10,280
Options vested or expected to vest at September 30, 2008 (1)	6,782,633	$ 6.56	6.7	$ 10,354

(1) In addition to the vested options, the Company expects a portion of the unvested options to vest at some point in the future. Options expected to vest is calculated by applying an estimated forfeiture rate to the unvested options.

Year-to-Date Activity	Options Outstanding	Weighted-Average Exercise Price Per Share
	(unaudited)	
Options outstanding at December 31, 2007	7,534,641	$ 6.57
Options granted	62,295	9.95
Options exercised	(457,582)	4.80
Options forfeited	(202,312)	9.55
Options canceled	(44,042)	11.60
Options outstanding at September 30, 2008	6,893,000	$ 6.60

During the three and nine months ended September 30, 2008, the total intrinsic value of options exercised (i.e. the difference between the market price at exercise and the price paid by the employee to exercise the options) was $94 and $3,660, respectively, and the total amount of cash received from exercise of these options was $112 and $2,196, respectively. The total grant-date fair value of stock options granted after the adoption of SFAS No. 123(R) on January 1, 2006 that vested during the three and nine months ended September 30, 2008 was $1,172 and $4,153, respectively.

During the three and nine months ended September 30, 2007, the total intrinsic value of options exercised was $677 and $11,424, respectively, and the total amount of cash received from exercise of these options was $204 and $984, respectively. The total grant-date fair value of stock options granted after the adoption of SFAS No. 123(R) on January 1, 2006 that vested during the three and nine months ended September 30, 2007 was $4,455 and $4,627, respectively.

Unrecognized stock-based compensation expense of non-vested stock options of $14.0 million is expected to be recognized using the straight line method over a weighted-average period of 1.31 years.

Restricted Stock Awards

Restricted stock awards are valued at the market price of a share of the Company’s common stock on the date of grant. A summary of the restricted stock award activity under the Company's stock option plan for the three and nine months ended September 30, 2008 is presented below:

Quarter-to-Date Activity	Shares (Unaudited)	Weighted-Average Grant Date Fair Value Per Share
Nonvested outstanding at June 30, 2008	631,774	$ 14.50
Granted	-	-
Vested	-	-
Forfeited	-	-
Nonvested outstanding at September 30, 2008	631,774	$ 14.50

Year-to-Date Activity	Shares (Unaudited)		Weighted-Average Grant Date Fair Value Per Share
Nonvested outstanding at December 31, 2007	614,775	$	14.52
Granted	21,639		13.36
Vested	(4,640)		10.56
Forfeited	-		-
Nonvested outstanding at September 30, 2008	631,774	$	14.50

Unrecognized stock-based compensation expense of non-vested restricted stock awards of $7.1 million is expected to be recognized using the straight line method over a weighted-average period of 1.72 years.

12. Stockholders' Equity

Shares Authorized

In April 2007, the Board of Directors approved an amendment and restatement of the Company's Certificate of Incorporation to increase the authorized number of shares of common stock from 44,344,656 to 100,000,000, to authorize 5,000,000 shares of undesignated preferred stock, par value $0.001 per share, and to eliminate all reference to the designated Series Preferred Stock.

Stock Offering

In May 2007, the Company completed its initial public offering (IPO) of 8,855,000 shares of its common stock, of which 7,072,097 shares were sold by the Company and 1,782,903 shares were sold by certain of the Company's existing shareholders at a price to the public of $13.00 per share. The Company raised a total of $91,937 in gross proceeds from the offering, or $83,161 in net proceeds after deducting underwriting discounts and commissions of $6,436 and other offering costs of approximately $2,340. Upon the closing of the offering, all shares of the Company's redeemable convertible preferred stock automatically converted into 24,372,953 shares of common stock.

Reverse Stock Split

On April 26, 2007, the Company's board of directors approved a 1-for-4 reverse stock split of the Company's outstanding common stock. The reverse stock split became effective immediately and all common share and per share amounts in the accompanying consolidated financial statements and notes to the consolidated financial statements have been retroactively adjusted for all periods presented to give effect to the reverse stock split.

Warrants

In connection with the Company's original Bank Term Loan agreement, in July 2001 the Company issued to the lender for the Bank Term Loan (the "Lender") a fully exercisable warrant to purchase up to 74,074 shares of series A redeemable convertible preferred stock at $0.5411 per share. In connection with an amendment to the Bank Term Loan agreement in April 2002 the Company issued to the Lender an additional fully exercisable warrant to purchase 55,443 shares of series A redeemable convertible preferred stock at a price of $0.5411 per share. Upon the closing of the Company's IPO in May 2007, these warrants outstanding converted into warrants to purchase an aggregate of 32,378 shares of the Company's common stock at an exercise price of $2.1644 per share. In 2007, the Lender exercised their warrants to purchase 32,378 shares of common stock using the conversion rights in the warrants. As result of the exercise using the conversion rights, the Company issued 26,740 shares of common stock to the Lender and cancelled the 5,638 shares received in lieu of payment of the exercise price. In connection with an acquisition in May 2000, the Company issued to the seller a warrant to purchase 40,625 shares of common stock at a price of $2.36 per share. The warrant is exercisable immediately and expires on May 10, 2010. In 2007, the seller exercised warrants to purchase 30,981 shares of common stock using the conversion rights in the warrants. As result of the exercise using the conversion rights, the Company issued 26,024 shares of common stock to the seller and cancelled the 4,957 shares received in lieu of payment of the exercise price. In 2008, the seller exercised additional warrants to purchase 8,375 shares of common stock using the conversion rights in the warrants. As result of the exercise using the conversion rights, the Company issued 6,886 shares of common stock to the seller and cancelled the 1,489 shares received in lieu of payment of the exercise price. At September 30, 2008 and December 31, 2007, there were 1,269 and 9,644 shares, respectively, of the Company's common stock reserved for the exercise of all warrants.

Reserved Common Stock

As September 30, 2008 the Company has reserved common stock for the following:

	Number of Shares (Unaudited)
Options outstanding and available for grant under stock option plans	10,147,776
Warrants	1,269
Total common stock reserved	10,149,045

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