EPICOR SOFTWARE CORP
Form 10-Q
August 08, 2008
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# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

# FORM 10-Q

**x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
**For the quarterly period ended June 30, 2008**

**OR**

**¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
**For the transition period from _____ to _____**

**Commission File No. 000-20740**

# EPICOR SOFTWARE CORPORATION

**(Exact name of registrant as specified in its charter)**

| **Delaware** | **33-0277592** |
|---|---|
| **(State or other jurisdiction of incorporation or organization)** | **(IRS Employer Identification No.)** |

**18200 Von Karman Avenue**

**Suite 1000**

**Irvine, California 92612**

**(Address of principal executive offices, zip code)**

**Registrant s telephone number, including area code: (949) 585-4000**

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

Indicate by check mark 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. (Check one):

| | |
|---|---|
| Large accelerated filer x | Accelerated filer ¨ |
| Non-accelerated filer ¨ | Smaller reporting company ¨ |

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

As of August 1, 2008, there were 59,573,711 shares of common stock outstanding.

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**PART I**

**FINANCIAL INFORMATION**

**Item 1 Financial Statements:**

**EPICOR SOFTWARE CORPORATION**

**CONDENSED CONSOLIDATED BALANCE SHEETS**

*(in thousands)*

| | June 30, 2008 *(Unaudited)* | December 31, 2007 |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 132,431 | $ 75,158 |
| Short-term investments | | 1,371 |
| Accounts receivable, net of allowance for doubtful accounts | 93,422 | 98,533 |
| Deferred income taxes | 8,347 | 7,060 |
| Inventory, net | 9,818 | 4,539 |
| Prepaid expenses and other current assets | 22,629 | 9,184 |
| Total current assets | 266,647 | 195,845 |
| Property and equipment, net | 28,845 | 14,762 |
| Deferred income taxes | 45,773 | 45,025 |
| Intangible assets, net | 132,699 | 46,524 |
| Goodwill | 369,551 | 169,267 |
| Cash designated for acquisition | | 161,000 |
| Other assets | 16,976 | 12,958 |
| Total assets | $ 860,491 | $ 645,381 |
| **LIABILITIES AND STOCKHOLDERS EQUITY** | | |
| Current liabilities: | | |
| Accounts payable | $ 23,887 | $ 14,640 |
| Accrued compensation and benefits | 24,298 | 27,555 |
| Other accrued expenses | 35,700 | 27,372 |
| Current portion of long-term debt | 7,416 | 145 |
| Current portion of accrued restructuring costs | 6,208 | 614 |
| Current portion of deferred revenue | 90,444 | 70,378 |
| Total current liabilities | 187,953 | 140,704 |
| Long-term debt, less current portion | 380,450 | 230,491 |
| Accrued restructuring costs | 5,962 | 356 |
| Deferred revenue | 552 | 823 |
| Deferred income taxes and other income taxes | 20,888 | 10,082 |
| Other long-term liabilities | 2,280 | |
| Total long-term liabilities | 410,132 | 241,752 |

| | | |
|---|---|---|
| Commitments and contingencies (Note 12) | | |
| Stockholders equity: | | |
| Common stock | 61 | 60 |
| Additional paid-in capital | 374,526 | 366,737 |
| Less: treasury stock at cost | (18,385) | (13,883) |
| Accumulated other comprehensive income | 1,910 | 61 |
| Accumulated deficit | (95,706) | (90,050) |
| Total stockholders equity | 262,406 | 262,925 |
| Total liabilities and stockholders equity | $ 860,491 | $ 645,381 |

See accompanying notes to unaudited condensed consolidated financial statements.

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**EPICOR SOFTWARE CORPORATION**

**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

**AND COMPREHENSIVE INCOME (LOSS)**

*(in thousands, except per share amounts)*

*(Unaudited)*

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2008 | 2007 | 2008 | 2007 |
| Revenues: | | | | |
| License | $ 24,357 | $ 25,103 | $ 42,861 | $ 47,135 |
| Consulting | 41,026 | 34,100 | 72,428 | 66,823 |
| Maintenance | 48,710 | 39,700 | 94,866 | 78,753 |
| Hardware and other | 13,852 | 6,803 | 20,014 | 14,324 |
| Total revenues | 127,945 | 105,706 | 230,169 | 207,035 |
| Cost of revenues | 64,296 | 47,877 | 117,840 | 95,055 |
| Amortization of intangible assets | 8,934 | 4,304 | 16,000 | 8,486 |
| Total cost of revenues | 73,230 | 52,181 | 133,840 | 103,541 |
| Gross profit | 54,715 | 53,525 | 96,329 | 103,494 |
| Operating expenses: | | | | |
| Sales and marketing | 21,253 | 18,817 | 42,630 | 37,445 |
| Software development | 14,296 | 9,571 | 27,323 | 18,250 |
| General and administrative | 13,556 | 14,425 | 25,509 | 29,834 |
| In-process research and development | | | 200 | |
| Restructuring charges | 89 | | 4,172 | 221 |
| Total operating expenses | 49,194 | 42,813 | 99,834 | 85,750 |
| Income (loss) from operations | 5,521 | 10,712 | (3,505) | 17,744 |
| Interest expense | (4,353) | (2,725) | (7,251) | (4,852) |
| Gain on sale of non-strategic asset | | | | 1,579 |
| Interest and other income, net | 978 | 2,023 | 1,825 | 2,592 |
| Income (loss) before income taxes | 2,146 | 10,010 | (8,931) | 17,063 |
| Provision (benefit) for income taxes | 811 | 3,719 | (3,275) | 6,339 |
| Net income (loss) | $ 1,335 | $ 6,291 | $ (5,656) | $ 10,724 |
| Comprehensive income (loss): | | | | |
| Net income (loss) | $ 1,335 | $ 6,291 | $ (5,656) | $ 10,724 |
| Unrealized foreign currency translation gain | 731 | 757 | 1,849 | 790 |
| Comprehensive income (loss) | $ 2,066 | $ 7,048 | $ (3,807) | $ 11,514 |
| Net income (loss) per share: | | | | |

| | | | | |
|---|---|---|---|---|
| Basic | $ 0.02 | $ 0.11 | $ (0.10) | $ 0.19 |
| Diluted | $ 0.02 | $ 0.11 | $ (0.10) | $ 0.19 |
| Weighted average common shares outstanding: | | | | |
| Basic | 58,449 | 57,039 | 58,174 | 56,854 |
| Diluted | 58,862 | 57,881 | 58,174 | 57,804 |

See accompanying notes to unaudited condensed consolidated financial statements.

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**EPICOR SOFTWARE CORPORATION**

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

*(in thousands)*

*(Unaudited)*

| | Six Months Ended June 30, | |
|---|---|---|
| | **2008** | **2007** |
| **Operating activities** | | |
| Net income (loss) | $ (5,656) | $ 10,724 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 19,914 | 11,591 |
| Stock-based compensation expense | 4,395 | 6,694 |
| Provision for doubtful accounts | 486 | 2,397 |
| Provision for excess and obsolete inventory | 288 | |
| Restructuring charges | 4,172 | 221 |
| Excess tax benefits from share-based payment arrangements | (819) | (704) |
| In-process research and development charge | 200 | |
| Gain on sale of non-strategic asset | | (1,579) |
| Changes in operating assets and liabilities, net of effects of acquisitions and dispositions: | | |
| Accounts receivable | 23,936 | (399) |
| Inventory | (4,371) | (1,614) |
| Prepaid expenses and other current assets | 1,309 | 808 |
| Other assets | 1,414 | 999 |
| Deferred income taxes | (6,590) | 2,937 |
| Accounts payable | 2,091 | (515) |
| Accrued expenses | (3,070) | (7,623) |
| Accrued restructuring costs | (4,466) | (839) |
| Deferred revenue | 1,636 | (2,254) |
| Other long-term liabilities | (30) | |
| Net cash provided by operating activities | 34,839 | 20,844 |
| **Investing activities** | | |
| Purchases of property and equipment | (5,615) | (3,271) |
| Proceeds from sale of non-strategic asset | | 2,500 |
| Cash paid for acquisitions, net of cash designated for acquisition of $161,000 and cash acquired | (124,205) | (16,349) |
| Sale of short term investment | 1,371 | |
| Purchase of short term investment | | (1,973) |
| Net cash used in investing activities | (128,449) | (19,093) |
| **Financing activities** | | |
| Proceeds from long-term debt | 160,000 | 230,000 |
| Principal payments on long-term debt | (2,769) | (99,323) |
| Debt issuance fees | (4,990) | (8,043) |
| Proceeds from exercise of stock options | 1,569 | 1,618 |
| Proceeds from employee stock purchase plan | 326 | 399 |
| Excess tax benefits from share-based payment arrangements | 819 | 704 |
| Purchase of treasury stock | (4,502) | (2,739) |

| | | |
|---|---|---|
| Net cash provided by financing activities | 150,453 | 122,616 |
| Effect of exchange rate changes on cash | 430 | (23) |
| Net increase in cash and cash equivalents | 57,273 | 124,344 |
| Cash and cash equivalents at beginning of period | 75,158 | 70,178 |
| Cash and cash equivalents at end of period | $ 132,431 | $ 194,522 |

See accompanying notes to unaudited condensed consolidated financial statements.

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**EPICOR SOFTWARE CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**JUNE 30, 2008**

**Note 1. Basis of Presentation**

The accompanying Unaudited Condensed Consolidated Financial Statements included herein have been prepared by Epicor Software Corporation (the Company) in conformity with accounting principles generally accepted in the United States of America and pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC) for interim financial information for reporting on Form 10-Q. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. These Unaudited Condensed Consolidated Financial Statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2007.

In the opinion of management, the Unaudited Condensed Consolidated Financial Statements contain all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the Company s financial position, results of operations and cash flows.

The results of operations for the three and six months ended June 30, 2008 are not necessarily indicative of the results of operations that may be reported for any other interim period or for the entire year ending December 31, 2008. The Condensed Consolidated Balance Sheet at December 31, 2007 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements, as permitted by SEC rules and regulations for interim reporting.

Inventory is comprised solely of finished goods. Accounts receivable is net of allowance at June 30, 2008 and December 31, 2007 of $7,444,000 and $8,008,000, respectively.

**Note 2. Basic and Diluted Net Income (Loss) Per Share**

Net income (loss) per share is calculated in accordance with Statement of Financial Accounting Standards (SFAS) No. 128, Earnings per Share. Under the provisions of SFAS No. 128, basic net income (loss) per share is computed by dividing the net income (loss) for the period by the weighted average number of common shares outstanding during the period, excluding shares of unvested restricted stock. Diluted net income (loss) per share is computed by dividing the net income (loss) for the period by the weighted average number of common and potential common shares outstanding during the period if their effect is dilutive.

For the three months ended June 30, 2008 and 2007, options to purchase 1,176,000 and 450,000 shares of common stock, respectively, with weighted average prices of $12.24 and $14.69, respectively, were outstanding but not included in the computation because the effect would be anti-dilutive. For the six months ended June 30, 2008 and 2007, options to purchase 1,097,000 and 515,000 shares of common stock, respectively, with weighted average prices of $12.64 and $14.43, respectively, were outstanding but not included in the computation because the effect would be anti-dilutive.

On May 8, 2007, the Company closed an offering of $230 million aggregate principal amount of 2.375% convertible senior notes due in 2027 (Note 8). The notes are unsecured and convertible into cash or, at the Company s option, cash and shares of the Company s common stock, at an initial conversion rate of 55.2608 shares of common stock per $1,000 principal amount of notes, which is equivalent to an initial conversion price of approximately $18.10 per share. Pursuant to the terms of the notes, the principal amount of the notes is settleable in cash and only the amount of conversion value, as defined, in excess of the principal amount of the notes is settleable in cash or shares. Therefore, the notes are only dilutive when the common stock price exceeds the conversion price, and no shares have been included in the calculation of diluted net income per share as the conversion value did not exceed the principal amount of the notes.

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The following table computes basic and diluted net income (loss) per share (*in thousands, except per share amounts*):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2008 | 2007 | 2008 | 2007 |
| Net income (loss) applicable to common stockholders | $ 1,335 | $ 6,291 | $ (5,656) | $ 10,724 |
| Basic: | | | | |
| Weighted average common shares outstanding | 60,770 | 59,278 | 60,454 | 59,229 |
| Weighted average common shares of unvested restricted stock | (2,321) | (2,239) | (2,280) | (2,375) |
| Shares used in the computation of basic net income (loss) per share | 58,449 | 57,039 | 58,174 | 56,854 |
| Net income (loss) per share applicable to common stockholders basic | $ 0.02 | $ 0.11 | $ (0.10) | $ 0.19 |
| Diluted: | | | | |
| Shares used in the computation of basic net income per share | 58,449 | 57,039 | 58,174 | 56,854 |
| Stock options and employee stock purchase plan (ESPP) shares | 389 | 764 | | 760 |
| Unvested restricted stock | 24 | 78 | | 190 |
| Shares used in the computation of diluted net income per share | 58,862 | 57,881 | 58,174 | 57,804 |
| Net income per share applicable to common stockholders diluted | $ 0.02 | $ 0.11 | $ (0.10) | $ 0.19 |

**Note 3. Acquisitions and Disposition**

Acquisitions are accounted for under the purchase method of accounting, in accordance with SFAS No. 141, Business Combinations. Management is responsible for determining the fair value of the assets acquired and liabilities assumed. The fair value of the assets acquired and liabilities assumed represent management s estimate of fair value. The Company conducts an active mergers and acquisitions program. Acquisition candidates are determined to be viable if they meet the Company s stringent criteria which includes, but is not limited to, product and technology fit, culture, geography, revenue synergies and financial contribution. Because the software industry is consolidating, the purchase environment is competitive. Valuations are determined through a combination of earnings per share accretion models which assume certain cost synergies, internal rate of return calculations, discounted cash flow models, outside valuations and appraisals and market conditions. The results of the acquisitions are included in the accompanying Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) from the respective acquisition dates forward.

***Acquisitions***

*NSB Retail Systems PLC*

On February 7, 2008, the Company completed its acquisition of NSB Retail Systems PLC (NSB). NSB designs, develops, markets and supports store and merchandising solutions to retailers of apparel, footwear and specialty merchandise. The acquisition of NSB provides an expanded portfolio of products and services for large and mid-sized specialty retailers and department stores, as well as a fully hosted, managed service offering designed for smaller retailers who are interested in rapid implementation via an on-demand versus on-premise offering.

Pursuant to the terms of the acquisition agreement, shareholders of NSB received £0.38 in cash for each NSB ordinary share. The value of the fully diluted share capital of NSB was approximately $311,845,000, not including transaction costs, based on the exchange rates in effect at the time the U.S. dollars were converted to pounds sterling for purposes of the transaction. The consideration payable under the agreement was funded by the Company with approximately $161,000,000 in existing cash balances, with the balance of the consideration being funded by drawing from funds available pursuant to the 2007 credit facility (Note 8). In addition, on February 11, 2008, the Company sold the NSB acquisition British pound sterling call options that were marked to market at December 31, 2007 at $1,802,000 back to the issuing institutions for $192,000, resulting in net foreign currency loss of $1,610,000. The loss resulted from depreciation of pounds sterling against the U.S. Dollar. The net loss is included

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in Interest and other income, net, in the Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) for the six months ended June 30, 2008.

The total preliminary purchase price for NSB is shown below (*in thousands*):

| | |
|---|---|
| Cash | $ 311,845 |
| Transaction costs | 5,739 |
| Total purchase price | $ 317,584 |

The acquisition of NSB is accounted for as a purchase business combination as defined in SFAS No. 141, Business Combinations. Under the purchase method of accounting, the purchase price was allocated to NSB s tangible and intangible assets acquired and liabilities assumed based on their estimated fair values as of February 7, 2008, with any excess being ascribed to goodwill. Management is primarily responsible for determining the fair values of these assets. The fair value of the assets acquired and liabilities assumed represent management s estimate of fair values. The purchase price allocation and transaction costs are preliminary and will be adjusted upon completion of the final valuation of acquired assets and liabilities assumed, including deferred income tax assets and liabilities. See Note 4 for a discussion of goodwill and intangibles acquired.

The following table summarizes the preliminary allocation of the purchase price (*in thousands*):

| | |
|---|---|
| Fair value of tangible assets acquired: | |
| Cash and marketable securities | $ 33,181 |
| Accounts receivable | 18,274 |
| Inventory | 1,196 |
| Property and equipment | 11,933 |
| Prepaid and other assets | 4,587 |
| Deferred tax asset | 2,047 |
| Total tangible assets acquired | 71,218 |
| Acquired technology | 58,700 |
| Acquired in-process research and development | 200 |
| Customer base | 39,300 |
| Trade name | 3,500 |
| Goodwill | 198,073 |
| Accounts payable and accrued expenses | (22,900) |
| Deferred revenue | (17,328) |
| Other long-term liabilities | (2,264) |
| Deferred tax liabilities | (10,915) |
| Net assets acquired | $ 317,584 |

In connection with the acquisition, the Company formulated a restructuring plan for the NSB operations. As a result, the Company recorded a liability of $4,149,000 for the costs related to involuntary employee terminations. This liability was included in the allocation of the purchase price in accordance with SFAS No. 141, Business Combinations and EITF Issue No. 95-3 Recognition of Liabilities in Connection with a Purchase Business Combination. Execution of the restructuring plan was completed as of June 30, 2008.

Included in the Company s operating results for the six months ended June 30, 2008 is a charge of $200,000 for the acquired in-process research and development expenses related to the NSB acquisition. The in-process research and development expenses arose from new products that were under development at the date of the acquisition and were expected to eventually lead to new products but had not yet established technological feasibility and for which no future alternative use was identified. The valuation of the in-process research and development projects was based upon the discounted expected future cash flows of the products over the products expected life, reflecting the estimated stage of completion of

the projects and the estimate of the costs to complete the projects.

Goodwill is amortizable for tax purposes when determining foreign earnings subject to tax in the U.S. A portion of the goodwill is amortizable for tax in the foreign jurisdiction.

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*Professional Advantage Pty Limited*

On May 16, 2007, the Company acquired the assets of a division of Professional Advantage Pty Limited (PA), a privately held reseller located in Australia. The primary purpose of this acquisition was to increase the Company s presence and direct customer base in the territories covered by PA.

The purchase price was allocated to PA s tangible and intangible assets acquired and liabilities assumed based on their estimated fair values as of May 16, 2007. The Company is amortizing the acquired customer base asset over seven years and the acquired technology asset over five years. The following table summarizes the allocation of the purchase price (*in thousands*):

| | |
|---|---|
| Cash | $ 16,000 |
| Transaction costs | 631 |
| Total | $ 16,631 |
| Fixed assets | $ 49 |
| Customer base | 5,728 |
| Acquired technology | 1,199 |
| Goodwill | 10,626 |
| Accrued liabilities | (632) |
| Deferred revenue | (339) |
| Net assets acquired | $ 16,631 |

Goodwill is amortizable for tax purposes when determining foreign earnings subject to tax in the U.S. It is amortizable for tax in the foreign jurisdictions. The pro forma impact of this acquisition was not significant to the Company s historical results of operations.

*Pro Forma Information*

Actual results of operations of the companies acquired in 2008 and 2007 are included in the consolidated financial statements from their respective dates of acquisition forward. The unaudited pro forma statement of operations data of the Company set forth below gives effect to the acquisition by Epicor of NSB using the purchase method as if it occurred on January 1, 2007, and includes amortization of identified intangibles, interest expense on debt incurred to finance the acquisitions, elimination of amortization related to NSB intangibles not assumed in the acquisition, and the in-process research and development charge. This pro forma information is presented for illustrative purposes only and is not necessarily indicative of the combined financial results of operations for future periods or the financial results of operations that actually would have been realized had the acquisition occurred at that time (*in thousands, except per share data*).

| | *(Unaudited)* Three Months Ended June 30, | | *(Unaudited)* Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2008 Actual | 2007 Pro Forma | 2008 Pro Forma | 2007 Pro Forma |
| Total revenues | $ 127,945 | $ 127,936 | $ 235,885 | $ 247,539 |
| Net income (loss) | $ 1,335 | $ 6,690 | $ (9,628) | $ 6,598 |
| Net income (loss) per share: | | | | |
| Basic | $ 0.02 | $ 0.12 | $ (0.17) | $ 0.12 |
| Diluted | $ 0.02 | $ 0.12 | $ (0.17) | $ 0.11 |

***Disposition***

*Sale of Non-Strategic Asset*

During March 2007, the Company entered into an arrangement to sell the assets of its payroll bureau operations in Russia. In connection with this asset sale arrangement, the Company also entered into an arrangement with the same party to license the iScala payroll product for resale on an exclusive basis in certain Eastern European

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territories. This transaction was accounted for as a multiple-element arrangement under EITF Issue No. 00-21. Based on an estimated fair value of the payroll bureau, the Company allocated $2,500,000 of the total consideration to the sale of these assets. This consideration, less the carrying amounts of $786,000 of goodwill and $113,000 of net customer base intangible assets originally recorded in connection with the 2004 acquisition of Scala and $22,000 of net tangible assets, resulted in a net gain of $1,579,000 which is included in gain on sale of non-strategic asset in the accompanying Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) for six months ended June 30, 2007. The remaining consideration related to the iScala payroll product license is included in license revenues in the accompanying Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) for the six months ended June 30, 2007.

**Note 4. Goodwill and Intangible Assets**

In acquisitions accounted for using the purchase method, goodwill is recorded for the difference, if any, between the aggregate consideration paid for an acquisition and the fair value of the net tangible and identified intangible assets acquired. SFAS No. 142, Goodwill and Other Intangible Assets, requires an annual review of goodwill and indefinite-lived intangibles for possible impairment. In accordance with SFAS No. 142, the Company performed an impairment review of its recorded goodwill in 2007 and determined that no impairment of goodwill existed because the estimated fair value of each reporting unit exceeded its carrying amount. The following table represents the balance and changes in goodwill by reporting unit as of and for the six months ended June 30, 2008 (*in thousands*):

| | License | Consulting | Maintenance | Total |
|---|---|---|---|---|
| Balance as of December 31, 2007 | $ 51,670 | $ 39,471 | $ 78,126 | $ 169,267 |
| NSB acquisition | 88,388 | 31,072 | 78,613 | 198,073 |
| Additional Scala acquisition | 207 | 143 | 452 | 802 |
| Foreign currency translation | 311 | 738 | 360 | 1,409 |
| Balance as of June 30, 2008 | $ 140,576 | $ 71,424 | $ 157,551 | $ 369,551 |

The following is the average amortization period for intangible assets:

| | Average Amortization Periods |
|---|---|
| Acquired technology | 5 years |
| Customer base | 7 years |
| Trademark | 5 years |
| Covenants not to compete | 1-2 years |

The following represents the change in intangible assets recorded during 2008, including intangible assets recorded as a result of the NSB acquisition and additional change due to foreign currency translation (*in thousands*):

| | NSB | Foreign Currency Translation | Total Change |
|---|---|---|---|
| Acquired technology | $ 58,700 | $ 57 | $ 58,757 |
| Customer base | 39,300 | 1,163 | 40,463 |
| Trademark | 3,500 | 8 | 3,508 |
| Covenant not to compete | | 56 | 56 |

Intangibles assets are amortized over the estimated economic life of the assets. As of June 30, 2008, the Company has not identified any indicators of impairment associated with identified intangible assets.

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The following table summarizes the components of intangible assets *(in thousands):*

| | As of June 30, 2008 | | | As of December 31, 2007 | | |
|---|---|---|---|---|---|---|
| | Gross Carrying Amount | Accumulated Amortization | Net | Gross Carrying Amount | Accumulated Amortization | Net |
| Acquired technology | $ 137,480 | $ 64,999 | $ 72,481 | $ 78,723 | $ 54,459 | $ 24,264 |
| Customer base | 77,818 | 23,383 | 54,435 | 37,355 | 18,684 | 18,671 |
| Trademark | 13,808 | 8,025 | 5,783 | 10,300 | 6,711 | 3,589 |
| Covenant not to compete | 2,246 | 2,246 | | 2,190 | 2,190 | |
| Total | $ 231,352 | $ 98,653 | $ 132,699 | $ 128,568 | $ 82,044 | $ 46,524 |

Amortization expense of the Company s intangible assets included in cost of revenues for the three months ended June 30, 2008 and 2007 was $8,934,000 and $4,304,000, respectively. Amortization expense of the Company s intangible assets included in general and administrative expense for the three months ended June 30, 2008 and 2007 was $0 and $63,000, respectively. Amortization expense of the Company s intangible assets included in cost of revenues for the six months ended June 30, 2008 and 2007 was $16,000,000 and $8,486,000, respectively. Amortization expense of the Company s intangible assets included in general and administrative expense for the six months ended June 30, 2008 and 2007 was $0 and $109,000, respectively. Estimated amortization expense for the remainder of 2008, 2009, 2010, 2011, 2012 and thereafter is approximately $17,177,000, $31,217,000, $28,047,000, $21,703,000, $20,177,000 and $14,378,000, respectively.

**Note 5. Restructuring Charges**

During 2008, the Company recorded restructuring charges of $4,172,000. This charge represents severance costs related to management severance and cost reductions from the elimination of redundancies in the Company s retail business resulting from the NSB acquisition. In connection with these restructuring costs, the Company terminated 35 employees or approximately 1% of the Company s workforce at that time from all functional areas. As of June 30, 2008, all of these terminations had been completed.

In connection with the Company s acquisition of NSB, the Company formulated a restructuring plan for the NSB operations. In connection with this plan, the Company recorded a liability in purchase accounting of $4,149,000 for the separation costs associated with the NSB reduction in workforce. The Company terminated 79 NSB employees, or 10% of the NSB workforce. At June 30, 2008, all of these terminations have been completed.

During the six months ended June 30, 2008, the Company made $5,287,000 in cash payments, or otherwise settled, against reserves associated with its restructuring activities.

**Note 6. Stock-Based Compensation**

The following table sets forth the total stock-based compensation expense resulting from stock options, restricted stock awards and the employee stock purchase plan included in the Company s Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) (*in thousands*):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2008 | 2007 | 2008 | 2007 |
| Cost of consulting revenues | $ 107,000 | $ 355,000 | $ 358,000 | $ 725,000 |
| Cost of maintenance revenues | 100,000 | 138,000 | 211,000 | 292,000 |
| Sales and marketing | 725,000 | 1,148,000 | 1,601,000 | 2,247,000 |
| Software development | 171,000 | 216,000 | 372,000 | 479,000 |
| General and administrative | 804,000 | 1,443,000 | 1,853,000 | 2,951,000 |
| Total stock-based compensation expense | $ 1,907,000 | $ 3,300,000 | $ 4,395,000 | $ 6,694,000 |

Net cash proceeds from the exercise of stock options were $560,000 and $1,140,000 for the three months ended June 30, 2008 and 2007, respectively. Net cash proceeds from the exercise of stock options were $1,569,000 and

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$1,618,000 for the six months ended June 30, 2008 and 2007, respectively. In accordance with SFAS No. 123 (revised 2004), Share-Based Payment (SFAS 123-R), the Company presents excess tax benefits from stock-based compensation awards, if any, as financing cash flows rather than operating cash flows. For the six months ended June 30, 2008 and 2007, net cash provided by operating activities decreased by, and financing activities increased by, $819,000 and $704,000, respectively, related to excess tax benefits from exercise of stock-based awards. The tax benefit related to stock-based compensation for the three months ended June 30, 2008 and 2007 was $551,000 and $934,000, respectively. The tax benefit related to stock-based compensation for the six months ended June 30, 2008 and 2007 was $1,367,000 and $1,941,000, respectively. No share-based compensation was capitalized for the three or six months ended June 30, 2008 and 2007.

During 2008, the Company granted 1,151,000 shares of performance-based restricted stock to employees for annual promotions and new hires for the 2008 and 2009 performance plan years. The shares are subject to a vesting schedule and were granted pursuant to the terms of the Company s performance-based restricted stock plan. The recipients will vest in the restricted stock, or a portion thereof, in two equal, annual installments depending upon achievement of targets with respect to the Company s annual revenue and adjusted earnings before interest, taxes, depreciation and amortization (EBITDA) for each of two performance years, 2008 and 2009. Restricted stock is held in escrow, and the Company s reacquisition right will not lapse until the shares are fully vested. Upon an employee s termination of service with the Company, shares that have not vested will be forfeited and automatically transferred to and reacquired by the Company. In addition, restricted shares that do not vest as a result of the Company s non-achievement with respect to annual revenue and adjusted EBITDA performance conditions for either performance year will be forfeited and automatically transferred to and reacquired by the Company.

The performance conditions for each year are independent of the performance conditions for the preceding years. Therefore, although compensation expense for all years will be measured based on the grant date fair value of the shares, the related compensation expense will be recognized separately in each year related only to the shares potentially earned in each year, assuming that it is considered to be probable that the shares will be earned each year. In addition, the compensation expense for each year is estimated and a pro rata amount is accrued on a quarterly basis. Quarterly compensation expense may include a cumulative adjustment resulting from changes in the estimated number of shares expected to be earned during that plan year.

On February 15, 2008, the Company s reacquisition right lapsed on 659,646 shares related to the performance-based restricted stock plan for the 2007 performance year. These shares are included in restricted stock at December 31, 2007. The lapse occurred following the Company s determination of its achievement of 2007 performance year performance conditions. The compensation expense related to these shares was included in the Consolidated Statements of Operations for the year ended December 31, 2007.

The Company withholds, at the employee s election, a portion of the vested shares as consideration for the Company s payment of applicable employee income taxes. As of June 30, 2008, these repurchased shares are held in treasury and are available for future reissuance. In conjunction with the quarterly vesting of restricted stock grants and vesting of the performance-based restricted stock, during the three and six months ended June 30, 2008, the Company acquired 56,858 and 264,505, shares of common stock, respectively, at a value of $1,301,000 and $3,201,000, respectively.

At June 30, 2008, there was approximately $5,457,000 of total unrecognized compensation expense related to restricted stock, excluding performance-based restricted stock, and $10,596,000 related to performance-based restricted stock. These costs are expected to be recognized over a weighted-average period of approximately two years. The compensation cost related to the performance-based restricted stock depends on the estimated number of shares that will vest, based on the probable outcome of the performance conditions. Therefore, the recognized compensation could vary significantly, depending on the outcome of those conditions. The Company is required at each reporting date to assess whether achievement of any performance condition is probable. Based on the Company s current assessment, the Company has recorded stock compensation expense related to performance-based restricted stock of $1,109,000 and $2,939,000 for three and six months ended June 30, 2008.

At June 30, 2008, there was approximately $606,000 of total unrecognized compensation expense related to unvested stock options. This cost is expected to be recognized over a weighted-average period of approximately two years.

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The fair value of restricted stock that vested during the three months ended June 30, 2008 and 2007 was $360,000 and $747,000, respectively. The fair value of restricted stock that vested during the six months ended June 30, 2008 and 2007 was $9,445,000 and $6,575,000, respectively.

The Company granted 300,000 and zero options during the three months ended June 30, 2008 and 2007, respectively. The Company granted 300,000 and zero options during the six months ended June 30, 2008 and 2007, respectively. The options were granted to executives of the Company. The weighted-average grant date fair value of options granted in fiscal 2008 was $2.15 per option. The Company estimates the fair value of each option grant on the date of grant using the Black-Scholes option-pricing model. The Black-Scholes option-pricing model was developed for use in estimating the value of traded options that have no vesting restrictions and are fully transferable, while the options issued by the Company are subject to both vesting and restrictions on transfer. In addition, option-pricing models require input of highly subjective assumptions including expected stock price volatility. The Company uses historical volatility data for expected volatility and estimates the expected life of its stock options based on the historical life of the Company s options. The grant date fair value of options granted was estimated using the following weighted average assumptions:

| | Three Months Ended June 30, 2008 | Six Months Ended June 30, 2008 |
|---|---|---|
| Expected life (years) | 3.0 | 3.0 |
| Risk-free interest rate | 2.2% | 2.2% |
| Volatility | 40.5% | 40.5% |
| Dividend rate | 0.0% | 0.0% |

There were 382,000 options exercised during the six months ended June 30, 2008. As of June 30, 2008, there were 1,740,000 options exercisable with a weighted average remaining contractual term, weighted average exercise price and aggregate intrinsic value of 4.6 years, $8.32 and $3,434,000, respectively. The Company issues new shares to satisfy stock option exercises and stock purchases under the Company s share-based plans. The aggregate intrinsic value above represents the total pretax intrinsic value (the difference between the Company s closing stock price on the last trading day of the quarter and the exercise price) multiplied by the number of shares that would have been received by the option holders had all option holders exercised their options on June 30, 2008. This amount changes based on the fair market value of the Company s stock.

**Note 7. Revenue Recognition**

The Company recognizes revenue in accordance with accounting principles generally accepted in the United States of America, principally:

Statement of Position (SOP) No. 97-2, Software Revenue Recognition, issued by the American Institute of Certified Public Accountants (AICPA) and interpretations;

AICPA SOP No. 98-9, Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions;

Staff Accounting Bulletin (SAB) No. 101, Revenue Recognition in Financial Statements, issued by the United States Securities and Exchange Commission as amended by SAB No. 104;

Financial Accounting Standards Board (FASB) Emerging Issues Task Force (EITF) Issue No. 00-21 Revenue Arrangements with Multiple Deliverables; and

AICPA SOP No. 81-1, Accounting for Performance of Construction-Type and Certain Production-Type Contracts.

The Company enters into contractual arrangements with end-users of its products to sell software licenses, maintenance services and consulting services, either separately or various combinations thereof. For each arrangement, revenues are recognized when persuasive evidence of an arrangement exists, the fees to be paid by the customer are fixed or determinable, collection of the fees is probable, delivery of the product has occurred, vendor-specific objective evidence (VSOE) of the fair value of any undelivered elements exists and no other significant obligations on the part of the Company remain.

For multiple-element software arrangements, the Company accounts for the software license component using the residual method. The residual method generally requires recognition of software license revenue in a multiple-element arrangement once all software products have been delivered and accepted by the customer and the only

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undelivered elements are maintenance services and/or consulting services. The fair value of the maintenance services is determined based on VSOE of fair value and is deferred and recorded ratably over the maintenance terms. Fair value for any related consulting services is determined by VSOE of fair value and generally recognized as the services are performed. After any required fair value allocations to the undelivered maintenance and/or consulting services elements, the residual contractual consideration is allocated to the license associated with the software products in the transaction. The Company s maintenance services VSOE of fair value is determined by reference to the price the Company s customers are required to pay for the services when sold-separately (i.e. the maintenance service fees paid by the Company s customers upon renewal). VSOE of fair value for consulting services is determined by reference to the price the Company s customers are required to pay for such services when sold separately, or when sold independent of any of the Company s other product or service offerings.

In certain instances, the Company enters into arrangements that include two or more non-software products or services such as hardware and related services. Such arrangements are divided into separate units of accounting provided that the delivered item has stand-alone value and there is objective and reliable evidence of the fair value of the undelivered items. The total arrangement fee is allocated to the undelivered elements based on their fair values and to the initial delivered elements using the residual method. Revenue is recognized separately, and in accordance with the Company s revenue recognition policy, for each element.

*License Revenues:* Amounts allocated to software license revenues sold directly by the Company are recognized at the time of shipment of the software when fair value for any undelivered elements is determinable and all the other revenue recognition criteria discussed above have been met.

Revenues on sales made to the Company s resellers are recognized upon shipment of the Company s software to the reseller when the reseller has an identified end-user and all other revenue recognition criteria noted above are met. Under limited arrangements with certain distributors, all the revenue recognition criteria have been met upon delivery of the product to the distributor and, accordingly, revenues are recognized at that time. The Company does not offer a right of return on its products.

*Consulting Service Revenues:* Consulting service revenues are comprised of consulting and implementation services and, to a limited extent, training. Consulting services are generally sold on a time-and-materials basis and can include services ranging from software installation to data conversion and building non-complex interfaces to allow the software to operate in integrated environments. Consulting engagements can last anywhere from one day to several months and are based strictly on the customer s requirements and complexities and are independent of the functionality of the Company s software. The Company s software, as delivered, can generally be used by the customer for the customer s purpose upon installation. Further, implementation and integration services provided are generally not essential to the functionality of the software, as delivered, and do not result in any material changes to the underlying software code. Services are generally separable from the other elements under the same arrangement since the performance of the services are not essential to the functionality of the other elements of the transaction, the services are described in the contract such that the total price of the arrangement would be expected to vary as the result of the inclusion or exclusion of the services, and VSOE of fair value exists for the services based on sold separately data. If, in the services element of the arrangement the Company performs significant production, modification or customization of its software, the Company applies the provisions of SOP No. 81-1, otherwise SOP No. 97-2 applies. For services performed on a time-and-material basis, revenue is recognized when the services are performed and billed. On occasion, the Company enters into fixed fee arrangements or arrangements in which customer payments are tied to achievement of specific milestones. In fixed fee arrangements, revenue is recognized as services are performed as measured by hours incurred to date, as compared to total estimated hours to be incurred to complete the work. In milestone achievement arrangements, the Company recognizes revenue as the respective milestones are achieved.

The Company has recorded unbilled consulting revenues totaling $3,694,000 and $2,810,000 at June 30, 2008 and December 31, 2007, respectively. These unbilled revenues represent consulting services performed during the last few business days of the quarter but not billed until the following month. The Company cuts-off consulting billing prior to the end of each month. Unbilled consulting revenue is recorded in accounts receivable in the accompanying Condensed Consolidated Balance Sheets.

*Maintenance Service Revenues:* Maintenance service revenues consist primarily of fees for providing unspecified software upgrades on a when-and-if-available basis and technical support over a specified term, which is typically twelve months. Maintenance revenues are typically paid in advance and are recognized on a straight-line basis over the term of the contract.

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*Hardware Revenues*: In some cases, the Company resells third party hardware systems and related peripherals as part of an end-to-end solution requested by its customers. Hardware revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collection is considered probable. The Company considers delivery to occur when the product is shipped and title and risk of loss have passed to the customer.

*Software License Indemnification*: The Company s standard software license agreements contain an infringement indemnity clause under which the Company agrees to defend, indemnify and hold harmless our customers and business partners against liability and damages arising from third party claims that the Company s products violate or infringe the intellectual property rights of others. These clauses constitute a form of guarantee that is subject to the disclosure requirements, but not the initial recognition or measurement provisions, of FASB Interpretation No. 45, Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others. The Company has never lost a third party infringement claim, and, to date, the Company s costs to defend such claims and/or lawsuits have been insignificant. Although it is possible that in the future third parties may claim that the Company s current or future software solutions infringe upon their intellectual property, a maximum obligation arising out of these types of agreements is not explicitly stated and, therefore, the overall maximum amount of these obligations cannot be reasonably estimated.

Sales taxes collected from customers are recorded on a net basis.

**Note 8. Credit Facility and Debt Offering**

*Credit Facilities*

On March 30, 2006, the Company entered into a credit agreement with several financial institutions (the 2006 credit facility), consisting of a term loan and a revolver. In May 2007, the Company completed a debt offering for $230 million convertible senior notes and used a portion of the proceeds to repay the outstanding balance of the term loan. On May 1, 2007, the credit agreement for the 2006 credit facility was amended to permit this debt offering described above.

Effective December 17, 2007, the Company voluntarily terminated the 2006 credit facility as a result of entering into the 2007 credit facility described below. There were no premiums or penalties incurred by the Company in connection with the termination of the 2006 credit facility and all amounts outstanding under 2006 credit facility were deemed paid in full on the termination date.

On December 16, 2007, the Company entered into a credit agreement with several financial institutions (the 2007 credit facility), which provides for term loans in an amount up to $100 million and revolving loans in an amount up to $100 million with an option for the Company to increase the revolving loan commitments and/or the term loan commitments by an aggregate amount of up to $50 million pursuant to an accordion feature for a total secured loan facility of up to $250 million. In connection with the 2007 credit facility, the Company agreed to certain financial and other covenants. Funds available under the 2007 credit facility were allowed to be used by the Company to finance its acquisition of NSB (Note 3), to pay the fees and expenses incurred in connection with the NSB acquisition, to provide ongoing working capital and for other general corporate purposes of the Company and its subsidiaries following the NSB acquisition. The Company may also use a portion of the available borrowing capacity to repurchase outstanding shares of its common stock.

On February 11, 2008, the Company amended the 2007 credit facility to exercise the accordion feature contained in the facility and increase the total credit facility to $250 million, consisting of $100 million of term loans and $150 million of revolving loans. On February 19, 2008, the Company borrowed $100 million in term loans and $60 million of revolving loans under the 2007 credit facility and used the proceeds to finance the NSB acquisition and to pay certain fees and expenses incurred in connection with the NSB acquisition. Interest under the 2007 credit facility is based, at the option of the Company, on either (i) the base rate, which is defined as a fluctuating rate per annum equal to the higher of the average rate of the overnight federal funds and Administrative Agent s prime rate as announced from time to time, plus a margin equal to between .50% and 1.75%, depending on the Company s senior secured leverage ratio as of the fiscal quarter most recently ended or (ii) a floating per annum rate (based upon one, two, three, six or nine-month interest periods) based on BBA LIBOR plus a margin equal to between 1.50% and 2.75%, depending on the Company s senior secured leverage ratio as of the fiscal quarter most recently ended.

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On March 31, 2008 and June 30, 2008, the Company made mandatory principal payments of $1.25 million against the term loan from discretionary funds. As of June 30, 2008, the Company had unused borrowing capacity of approximately $90 million under the 2007 credit facility and the weighted average interest rate applicable to outstanding loans under the 2007 credit facility was 5.68%. As of June 30, 2008, the Company was in compliance with all covenants included in the terms of the 2007 credit facility, other than its consolidated total leverage ratio. The Company obtained a waiver from its lenders with respect to this covenant on July 23, 2008.

On April 18, 2008, the Company entered into interest rate swap agreements to convert a portion of the Company s interest rate variability to a fixed rate basis as required under the 2007 credit facility (Note 9). In July 2008, the Company made a voluntary principal payment of $5.0 million against the revolving loan from discretionary funds.

*Debt Offering*

On May 8, 2007, the Company closed an offering of $230 million aggregate principal amount of 2.375% convertible senior notes due in 2027. The notes are unsecured and pay interest semiannually at a rate of 2.375% per annum until May 15, 2027. The notes are convertible into cash or, at the Company s option, cash and shares of the Company s common stock, at an initial conversion rate of 55.2608 shares of common stock per $1,000 principal amount of notes, which is equivalent to an initial conversion price of approximately $18.10 per share. Pursuant to the terms of the notes, the principal amount of the notes may be settled in cash and only the amount of conversion value, as defined, in excess of the principal amount of the notes may be settled in cash or shares. The initial conversion price represents a 30% premium over the last reported sale price of the Company s common stock prior to the offering that began on May 2, 2007, which was $13.92 per share. The conversion rate will be adjusted upon the occurrence of certain events defined in the indenture. The share settlement feature upon conversion of the senior convertible notes is generally limited to the conversion value in excess of the par value of the notes. The notes do not contain any restrictive financial covenants.

The notes are convertible under the following circumstances: (1) during any fiscal quarter after the fiscal quarter ending June 30, 2007 (and only during such fiscal quarter), if the closing sale price of the Company s common stock for each of 20 or more trading days in a period of 30 consecutive trading days ending on the last trading day of the immediately preceding fiscal quarter exceeds 130% of the conversion price in effect on the last trading day of the immediately preceding fiscal quarter; (2) during the five consecutive business days immediately after any five consecutive trading day period (the note measurement period) in which the trading price per $1,000 principal amount of notes for each such trading day was equal to or less than 98% of the conversion value of the notes for such trading day during the note measurement period; (3) upon our calling such notes for redemption; (4) upon the occurrence of specified corporate transactions and (5) during the 30 days prior to, but excluding, any scheduled purchase date and at any time on or after May 15, 2026, and before the close of business on the business day immediately preceding the maturity date.

On or after May 15, 2014, the Company may from time to time at its option redeem the notes, in whole or in part, for cash, at a redemption price equal to 100% of the principal amount of the notes the Company redeems, plus any accrued and unpaid interest to, but excluding, the redemption date. On each May 15, 2014, May 15, 2017 and May 15, 2022, holders may require the Company to purchase all or a portion of their notes at a purchase price equal to 100% of the principal amount of the notes to be purchased, plus any accrued and unpaid interest to, but excluding, the purchase date.

The net proceeds of the offering were $222.0 million after deducting the underwriters discounts and commissions and offering expenses. On May 8, 2007, the Company used approximately $94 million of the proceeds to pay in full its term loan outstanding under the 2006 credit facility. The balance of the net proceeds of the offering will be used for working capital, capital expenditures and other general corporate purposes, which may include funding acquisitions of businesses, technologies or product lines. The Company may also use a portion of the remaining net proceeds to repurchase outstanding shares of its common stock.

**Note 9. Interest Rate Swap**

On April 18, 2008, the Company entered into interest rate swap agreements to convert a portion of the Company s interest rate variability to a fixed rate basis as required under the 2007 credit facility. The interest rate swaps qualify for hedge accounting treatment pursuant to SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended. The changes in the fair value of the interest rate swaps are reflected in the carrying value of the interest rate swap on the Condensed Consolidated Balance Sheets. The differential to be paid or received on

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the interest rate swap agreements will be accrued and recognized as an adjustment to interest expense as interest rates change. The interest rate swap agreements commenced effective June 30, 2008 and have an aggregate notional amount of $20 million maturing March 31, 2009 and $30 million maturing September 30, 2009. The effective interest rate for the notional amounts covered by the swap agreements is 5.67%.

As of June 30, 2008, the interest rate swap resulted in a net liability of $31,000 included in accrued liabilities. The change in market value during fiscal 2008 related to the effective portion of the cash flow hedge was recorded as an unrecognized loss in the accumulated other comprehensive income section of stockholders equity in the Company s Condensed Consolidated Balance Sheet.

Interest rate differentials paid or received under this agreement will be recognized as adjustments to interest expense. The Company does not hold or issue interest rate swap agreements for trading purposes. In the event that a counter-party fails to meet the terms of the interest rate swap agreement, the Company s exposure is limited to the interest rate differential. The Company manages the credit risk of counterparties by dealing only with institutions that the Company considers financially sound. The Company considers the risk of non-performance to be remote. On January 1, 2008, the company adopted SFAS No. 157, Fair Value Measurements, for financial assets and liabilities. The adoption had an immaterial impact on the consolidated financial statements. SFAS 157 established a three-tier hierarchy for fair value measurements, which prioritizes the inputs used in measuring fair value as follows:

Level 1 observable inputs such as quoted prices for identical instruments in active markets.

Level 2 inputs other than quoted prices in active markets that are observable either directly or indirectly through corroboration with observable market data.

Level 3 unobservable inputs in which there is little or no market data, which would require the Company to develop its own assumptions.

The Company s interest rate swap is required to be measured at fair value on a recurring basis. The fair value of the interest rate swap is determined based on inputs that are readily available in public markets or can be derived from information available in publicly quoted markets. Therefore, the Company has categorized the interest rate swap as Level 2. The following table presents the Company s financial liabilities as of June 30, 2008 measured at fair value on a recurring basis:

| | Fair value measurements using | | |
|---|---|---|---|
| | Level 1 | Level 2 | Level 3 |
| Interest rate swap liability | $ | $ (31) | $ |

**Note 10. Provision for Income Taxes**

The Company adopted FASB Interpretation (FIN) 48, Accounting for Uncertainty in Income Taxes (FIN 48) on January 1, 2007. At June 30, 2008, the Company had $21.5 million of gross unrecognized tax benefits, of which $2.7 million would reduce the effective tax rate if recognized. The Company s continuing practice is to recognize interest and/or penalties related to income tax matters in income tax expense. As of June 30, 2008, the Company has approximately $247,000 of accrued interest and penalties related to uncertain tax positions.

The tax years 1994 to 2008 remain open to examination by the major taxing jurisdictions to which the Company is subject. The Company is currently under examination in various locations including Canada and United Kingdom. The Company does not believe the amount of unrecognized tax benefits as of June 30, 2008 will significantly increase or decrease within 12 months.

The Company is currently in negotiations with the Canada Revenue Agency to settle the examination for years 2002 and 2003. The Company expects a favorable settlement and anticipates effectively settling the uncertain tax position in the near term. The Company does not believe the amount settled will materially differ from the unrecognized tax benefit as of June 30, 2008. The Company is also currently finalizing voluntary disclosure agreements with various states for which unrecognized tax benefits have been recorded. The Company does not believe the amount settled will differ from the unrecognized tax benefit as of June 30, 2008. The unrecognized tax benefits relating to the Canadian examination and to the state tax positions would reduce the effective tax rate if recognized.

The provision for income taxes consists of provisions for federal, state and foreign income taxes. The Company operates in an international environment with significant operations in various locations outside the U.S.

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Accordingly, the consolidated income tax rate is a composite rate reflecting the earnings in the various locations and the applicable rates.

The Company recorded a provision for income taxes of $811,000 and $3,719,000 for the three months ended June 30, 2008 and 2007, respectively. The effective income tax rates were 37.8% and 37.2% for the three months ended June 30, 2008 and 2007, respectively. The effective tax rate differs from the statutory U.S. federal income tax rate of 35% primarily due to state and foreign income tax and permanent differences between GAAP pre-tax income and taxable income.

The Company has provided a valuation allowance on certain foreign deferred tax assets and intends to maintain a valuation allowance until sufficient positive evidence exists to support its reversal. In general, any realization of these deferred tax assets will reduce the Company s effective rate in future periods. Under the provisions of SFAS No. 109, Accounting for Income Taxes, and related interpretations, future period reductions to the valuation allowance related to Scala s deferred tax assets that existed as of the date of acquisition of Scala are first credited against goodwill, then to the other identifiable intangible assets existing at the date of acquisition, and then, once these assets have been reduced to zero, credited to the income tax provision. In accordance with FIN 18, Accounting for Income Taxes in Interim Periods, (FIN 18) the Company makes its best estimate of the tax rate expected to be applicable for the full fiscal year. The rate so determined is used to provide for income taxes in an interim period. Absent a material or discrete adjustment to deferred taxes, the deferred tax accounts are adjusted at year end.

The Company regularly reviews the deferred tax assets for recoverability and the need for a valuation allowance. The Company analyzes both negative and positive evidence, and the strength of such evidence. This analysis includes assessment by jurisdiction of forecasted and historic financial performance and taxable income, performance compared to profit and revenue targets, strength or weakness of revenue generating functions, expense forecasts, and other factors. The valuation allowance will continue to be evaluated over future quarters.

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires the formulation of estimates and assumptions that affect the reported amount of tax-related assets and liabilities and income tax provisions. The Company assesses the recoverability of the deferred tax assets on an ongoing basis, analyzing all available positive and negative evidence to determine whether, based on such evidence, it is more likely than not that some portion or all of the Company s net deferred assets will be realized in future periods. This assessment requires significant judgment. In addition, the Company has made estimates involving current and deferred income taxes, tax attributes relating to the interpretation of various tax laws and historical bases of tax attributes associated with certain tangible and intangible assets. Failure to achieve the Company s operating income targets may change its assessment regarding the recoverability of the net deferred tax assets and such change could result in a valuation allowance being recorded against some or all of the deferred tax assets. Any increase in a valuation allowance would result in additional income tax expense, lower stockholders equity and could have a significant impact on the Company s earnings in future periods.

U.S. income taxes were not provided for on undistributed earnings from certain non-U.S. subsidiaries. Those earnings are considered to be permanently reinvested in accordance with Accounting Principles Board (APB) Opinion 23.

**Note 11. Segment Information**

In accordance with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, the Company has prepared operating segment information to report components that are evaluated regularly by the Company s chief operating decision maker in deciding how to allocate resources and in assessing performance.

The Company s reportable operating segments include licenses, consulting, maintenance and hardware and other. Currently, the Company does not separately allocate amortization of intangible assets or operating expenses to these segments, nor does it allocate specific assets to these segments. Therefore, the segment information reported includes only revenues, cost of segment revenues and segment gross profit. Excluded from the table below is amortization of intangible assets for the three months ended June 30, 2008 and 2007 of $8,934,000 and $4,304,000, respectively. Excluded from the table below is amortization of intangible assets for the six months ended June 30, 2008 and 2007 of $16,000,000 and $8,486,000, respectively.

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Operating segment data for the three and six months ended June 30, 2008 and 2007 is as follows (*in thousands*):

| | Licenses | Consulting | Maintenance | Hardware and Other | Total |
|---|---|---|---|---|---|
| Three months ended June 30, 2008: | | | | | |
| Revenues | $ 24,357 | $ 41,026 | $ 48,710 | $ 13,852 | $ 127,945 |
| Cost of revenues | 5,766 | 32,784 | 13,216 | 12,530 | 64,296 |
| Gross profit | $ 18,591 | $ 8,242 | $ 35,494 | $ 1,322 | $ 63,649 |
| Three months ended June 30, 2007: | | | | | |
| Revenues | $ 25,103 | $ 34,100 | $ 39,700 | $ 6,803 | $ 105,706 |
| Cost of revenues | 5,062 | 28,075 | 8,745 | 5,995 | 47,877 |
| Gross profit | $ 20,041 | $ 6,025 | $ 30,955 | $ 808 | $ 57,829 |
| Six months ended June 30, 2008: | | | | | |
| Revenues | $ 42,861 | $ 72,428 | $ 94,866 | $ 20,014 | $ 230,169 |
| Cost of revenues | 9,344 | 64,740 | 24,806 | 18,950 | 117,840 |
| Gross profit | $ 33,517 | $ 7,688 | $ 70,060 | $ 1,064 | $ 112,329 |
| Six months ended June 30, 2007: | | | | | |
| Revenues | $ 47,135 | $ 66,823 | $ 78,753 | $ 14,324 | $ 207,035 |
| Cost of revenues | 9,982 | 54,905 | 17,493 | 12,675 | 95,055 |
| Gross profit | $ 37,153 | $ 11,918 | $ 61,260 | $ 1,649 | $ 111,980 |

**Note 12. Commitments and Contingencies**

*Litigation*

The Company is subject to legal proceedings and claims in the normal course of business. The Company is currently defending these proceedings and claims, and anticipates that it will be able to resolve these matters in a manner that will not have a material adverse effect on the Company s consolidated financial position, results of operations or cash flows.

*Guarantees*

The Company from time to time enters into certain types of contracts that contingently require the Company to indemnify parties against third-party claims. These contracts primarily relate to: (i) divestiture and acquisition agreements, under which the Company may provide customary indemnifications to either (a) purchasers of the Company s businesses or assets; or (b) entities from whom the Company is acquiring assets or businesses; (ii) certain real estate leases, under which the Company may be required to indemnify property owners for environmental and other liabilities and other claims arising from the Company s use of the applicable premises; (iii) certain agreements with the Company s officers, directors and employees, under which the Company may be required to indemnify such persons for liabilities arising out of their relationship with the Company; and (iv) Company license and consulting agreements with its customers, under which the Company may be required to indemnify such customers for intellectual property infringement claims and other claims arising from the Company s provision of services to such customers.

**Note 13. Employee Benefits**

As part of the NSB acquisition (Note 3), the Company assumed a liability for a defined benefit pension plan that provides pension benefits for certain NSB employees upon retirement. The plan was closed to new entrants prior to the acquisition, and the plan participants are no longer employed by the Company.

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The net periodic benefit cost of the Company s defined benefit pension plan included the following components (*in thousands*):

| | Three Months Ended June 30, 2008 | Six Months Ended June 30, 2008 |
|---|---|---|
| Interest cost on projected benefit obligation | $ 118 | $ 186 |
| Expected return on plan assets | (82) | (130) |
| Net periodic benefit cost | $ 36 | $ 56 |

During the three and six months ended June 30, 2008, contributions of approximately $74,000 and $125,000, respectively, were made to the Company s defined benefit pension plan. The Company expects to contribute approximately $150,000 for the remainder of the year to its defined benefit pension plan.

**Note 14. New Accounting Pronouncements**

In May 2008, the FASB issued SFAS No. 162, The Hierarchy of Generally Accepted Accounting Principles (SFAS 162). SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (the GAAP hierarchy). SFAS 162 will become effective 60 days following the SEC s approval of the Public Company Accounting Oversight Board amendments to AU Section 411, The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles. The Company does not expect the adoption of SFAS 162 to have a material effect on its consolidated results of operations and financial condition.

In May 2008, the FASB issued FASB Staff Position (FSP) No. APB 14-1 Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement) (FSP APB 14-1). FSP APB 14-1 requires the issuer of certain convertible debt instruments that may be settled in cash (or other assets) on conversion to separately account for the liability (debt) and equity (conversion option) components of the instrument in a manner that reflects the issuer s non-convertible debt borrowing rate. FSP APB 14-1 is effective for fiscal years beginning after December 15, 2008 on a retroactive basis and will be adopted by the Company in the first quarter of fiscal 2009. The Company is currently evaluating the potential impact of the adoption of FSP APB 14-1 on its consolidated results of operations and financial condition.

In April 2008, the FASB issued FASB Staff Position (FSP) FAS No. 142-3, Determination of the Useful Life of Intangible Assets. This FSP amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement 142, Goodwill and Other Intangible Assets. The intent of this FSP is to improve the consistency between the useful life of a recognized intangible asset under Statement 142 and the period of expected cash flows used to measure the fair value of the asset under FASB Statement 141 (Revised 2007), Business Combinations, and other U.S. generally accepted accounting principles (GAAP). This FSP is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. Early adoption is prohibited. The Company is currently assessing the impact the adoption of this FSP will have on its consolidated results of operations and financial condition.

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). The Statement requires companies to provide enhanced disclosures regarding derivative instruments and hedging activities. It requires companies to better convey the purpose of derivative use in terms of the risks that such company is intending to manage. Disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under SFAS 133 and its related interpretations, and (c) how derivative instruments and related hedged items affect a company s financial position, financial performance, and cash flows are required. This Statement retains the same scope as SFAS 133 and is effective for fiscal years and interim periods beginning after November 15, 2008, or January 1, 2009 for the Company. The Company is currently assessing the impact, if any, that the adoption of this Statement will have on its consolidated results of operations and financial condition.

In December 2007, the FASB issued SFAS No. 141, Business Combinations (revised 2007) (SFAS 141-R), which provides greater consistency in the accounting and financial reporting of business combinations. It requires the acquiring entity in a business combination to recognize all assets acquired and liabilities assumed in the transaction,

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establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed, and requires the acquirer to disclose the nature and financial effect of the business combination. SFAS 141-R is effective for acquisitions in fiscal years beginning after December 15, 2008, or January 1, 2009 for the Company. The Company is currently assessing the impact the adoption will have on its financial position and results of operations.

In December 2007, the FASB issued SFAS 160, Noncontrolling Interests in Consolidated Financial Statements (SFAS 160). This Statement amends Accounting Research Bulletin No. 51, Consolidated Financial Statements, to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 is effective for fiscal years beginning after December 15, 2008, or January 1, 2009 for the Company. The Company is currently assessing the impact, if any, the adoption will have on its consolidated results of operations and financial condition.

On February 15, 2007, the FASB issued SFAS 159, The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115 (SFAS 159). Under this standard, the Company may elect to report financial instruments and certain other items at fair value on an investment-by-investment basis with changes in value reported in earnings. This election is irrevocable. SFAS 159 provides an opportunity to mitigate volatility in reported earnings that is caused by measuring hedged assets and liabilities that were previously required to use a different accounting method than the related hedging contracts when the complex provisions of SFAS 133, Accounting for Derivative Instruments and Hedging Activities, hedge accounting are not met. SFAS 159 is effective for years beginning after November 15, 2007. Early adoption within 120 days of the beginning of the Company s 2007 fiscal year is permissible, provided the Company has not yet issued interim financial statements for 2007 and has adopted SFAS 157, Fair Value Measurements (SFAS 157). Adoption of this standard did not have a material effect on its consolidated results of operations and financial condition.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS 157), which clarifies the definition of fair value whenever another standard requires or permits assets or liabilities to be measured at fair value. Specifically, the standard clarifies that fair value should be based on the assumptions market participants would use when pricing the asset or liability, and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. SFAS 157 does not expand the use of fair value to any new circumstances, and must be applied on a prospective basis except in certain cases. The standard also requires expanded financial statement disclosures about fair value measurements, including disclosure of the methods used and the effect on earnings.

In February 2008, FSP FAS No. 157-2, Effective Date of FASB Statement No. 157 (FSP 157-2) was issued. FSP 157-2 defers the effective date of SFAS 157 to fiscal years beginning after December 15, 2008, and interim periods within those fiscal years, for all nonfinancial assets and liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). Examples of items within the scope of FSP 157-2 are nonfinancial assets and nonfinancial liabilities initially measured at fair value in a business combination (but not measured at fair value in subsequent periods), and long-lived assets, such as property, plant and equipment and intangible assets measured at fair value for an impairment assessment under SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. The partial adoption of SFAS 157 on January 1, 2008 with respect to financial assets and financial liabilities recognized or disclosed at fair value in the financial statements on a recurring basis did not have a material effect on consolidated results of operations and financial condition. The Company is currently assessing the impact, if any, of SFAS 157 relating to its planned January 1, 2009 adoption of the remainder of the standard.

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**Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations:**

**Forward Looking Statements Safe Harbor**

Certain statements in this Quarterly Report on Form 10-Q are forward looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities and Exchange Act of 1934, as amended, that involve risks and uncertainties. Any statements contained herein (including without limitation statements to the effect that the Company or Management estimates, expects, anticipates, plans, believes, projects, continues, should, may, or will or statements concerning potential or opportunity or vari comparable terminology or the negative thereof) that are not statements of historical fact should be construed as forward-looking statements including statements about (i) the Company s future financial results, (ii) the impact of new accounting pronouncements, (iii) the Company s product development plans, (iv) the Company s capital spending, (v) the Company s future cash flow from operations, (vi) sufficient sources of financing to continue operations for next twelve months and to satisfy contractual obligations and commercial commitments, (vii) the effect of current legal proceedings, (viii) payment of obligations related to the Company s restructurings, (ix) the future use of forward or other hedging contracts, (x) the future impact of recent acquisitions on the Company, (xi) future investments in product development, (xii) schedule of amortization of intangible assets, (xiii) future impact of valuation allowance review and (xiv) future expense levels. Actual results could differ materially and adversely from those anticipated in such forward looking statements as a result of certain factors, including the factors listed at pages 38 to 46. Because these factors may affect the Company s operating results, past performance should not be considered an indicator of future performance and investors should not use historical results to anticipate results or trends in future periods. The Company undertakes no obligation to revise or publicly release the results of any revision to these forward-looking statements. Investors should carefully review the risk factors described below and in other documents the Company files from time to time with the Securities and Exchange Commission, including the Company s Annual Report on Form 10-K.

The following discussion should be read in conjunction with the consolidated financial statements and notes thereto.

***Overview***

The Company designs, develops, markets and supports computer software applications, which assist mid-sized companies as well as the divisions and subsidiaries of larger corporations in the planning, management and operation of their businesses. The Company is focused on the mid-market, which generally includes companies or divisions with annual revenues between $10 million and $1 billion. The Company s software products and related consulting and support services are designed to help these companies automate key aspects of their business operations, processes and procedures from customer relations, ordering, purchasing and planning, to production, distribution, accounting and financial reporting. By automating these processes, companies may gain faster access to more accurate information, which can improve operating efficiency, reduce cost and allow companies to be more responsive to their customers, ultimately leading to increased revenues. The Company also offers support, consulting and education services in support of its customers use of its software products. The Company s products and services are sold worldwide by its direct sales force and an authorized network of value added resellers (VARs), distributors and authorized consultants.

Total revenues for the three months ended June 30, 2008, increased 21.0% to $127.9 million, compared to $105.7 million for the three months ended June 30, 2007. This included total revenue from the NSB acquisition of $16.9 million, of which $1.4 million was related to hardware. Net license revenue decreased by 3.0% to $24.4 million for the three months ended June 30, 2008, when compared to net license revenue of $25.1 million for the three months ended June 30, 2007. Consulting revenue was $41.0 million for the three months ended June 30, 2008, an increase of 20.3 % compared to consulting revenue of $34.1 million for the three months ended June 30, 2007. Maintenance revenue for the three months ended June 30, 2008 was $48.7 million, an increase of 22.7% compared to maintenance revenue of $39.7 million for the three months ended June 30, 2007. Hardware and other revenue for the three months ended June 30, 2008 was $13.9 million, an increase of 103.6% compared to hardware and other revenue of $6.8 million for the three months ended June 30, 2007. See discussion in Results of Operations for more detailed information.

Total revenues for the six months ended June 30, 2008, increased 11.2% to $230.2 million, compared to $207.0 million for the six months ended June 30, 2007. This included total revenue from the NSB acquisition of $27.1 million, of which $2.1 million was related to hardware. Net license revenue decreased by 9.1% to $42.9 million for the six months ended June 30, 2008, compared to $47.1 million for the six months ended June 30, 2007. Consulting

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revenue was $72.4 million for the six months ended June 30, 2008, an increase of 8.4% compared to consulting revenues of $66.8 million for the six months ended June 30, 2007. Maintenance revenue for the six months ended June 30, 2008 was $94.9 million, an increase of 20.5% compared to maintenance revenues of $78.8 million for the six months ended June 30, 2007. Hardware and other revenue for the six months ended June 30, 2008 was $20.0 million, an increase of 39.7% compared to hardware and other revenue of $14.3 million for the six months ended June 30, 2007. See discussion in Results of Operations for more detailed information.

Overall gross margin was 42.8% for the three months ended June 30, 2008, compared to 50.6% during the same period in 2007, down primarily due to higher amortization related to the NSB intangible assets, as well as the addition of NSB maintenance revenues, which has relatively lower gross margins than the Company has historically reported. Overall gross margin was 41.9% for the six months ended June 30, 2008, compared to 50.0% during the same period in 2007, down primarily due to lower consulting margins, the higher amortization related to the NSB acquisition, as well as the addition of NSB maintenance revenues, which have relatively lower gross margins than the Company has historically achieved.

Cash flows from operations were $34.8 million during the six months ended June 30, 2008, compared to 2007 cash flows from operations of $20.8 million. The increase in operating cash flows is primarily due an increase in cash collections from accounts receivable, compared to the same period in 2007, as well as additional cash flow from the acquisition of NSB.

**Critical Accounting Policies**

The consolidated financial statements are prepared in conformity with United States of America generally accepted accounting principles (GAAP). As such, management is required to make judgments, estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. The significant accounting policies which are most critical to aid in fully understanding and evaluating reported financial results include the following:

*Revenue Recognition*

The Company enters into contractual arrangements with end-users that may include licensing of the Company s software products, product support and maintenance services, consulting services, resale of third-party hardware or various combinations thereof, including the sale of such products or services separately. The Company s accounting policies regarding the recognition of revenue for these contractual arrangements is fully described in Note 7 of Notes to Unaudited Condensed Consolidated Financial Statements.

The Company considers many factors when applying accounting principles generally accepted in the United States of America related to revenue recognition. These factors include, but are not limited to:

- The actual contractual terms, such as payment terms, delivery dates and pricing of the various product and service elements of a contract;
- Availability of products to be delivered;
- Time period over which services are to be performed;
- Creditworthiness of the customer;
- The complexity of customizations and integrations to the Company s software required by service contracts;
- The sales channel through which the sale is made (direct, VAR, distributor, etc.);

Discounts given for each element of a contract;

Any commitments made as to installation or implementation go live dates and

Whether vendor specific objective evidence of the fair value of undelivered elements exists.

Each of the relevant factors is analyzed to determine its impact, individually and collectively with other factors, on the revenue to be recognized for any particular contract with a customer. Management is required to make judgments regarding the significance of each factor in applying the revenue recognition standards, as well as whether or not each factor complies with such standards. Any misjudgment or error by management in its evaluation of the factors and the application of the standards, especially with respect to complex or new types of transactions, could have a material adverse affect on the Company s future revenues and operating results.

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*Allowance for Doubtful Accounts*

The Company s accounts receivable go through a collection process that is based on the age of the invoice and requires attempted contacts with customers at specified intervals and assistance from other personnel within the Company who have a relationship with the customer. The Company writes-off accounts to its allowance when the Company has determined that collection is not likely. The Company believes no significant concentrations of credit risk existed at June 30, 2008. Receivables from customers are generally unsecured.

The Company maintains an allowance for doubtful accounts based on historical collections performance and specific collection issues. If actual bad debts differ from the reserves calculated, the Company records an adjustment to bad debt expense in the period in which the difference occurs. Such adjustment could result in additional charges to the Company s results of operations.

*Intangible Assets*

The Company s intangible assets were recorded as a result of the Company s acquisitions and represent acquired technology, customer base and trademarks. These intangible assets are amortized over the estimated economic life of the asset. The Company periodically evaluates the recoverability of the intangible assets and considers any events or changes in circumstances that would indicate that the carrying amount of an asset may not be recoverable. Any material changes in circumstances, such as large decreases in revenue or the discontinuation of a particular product line, could require future write-downs in the Company s intangibles assets and could have a material adverse impact on the Company s operating results for the periods in which such write-downs occur.

*Goodwill*

The Company s goodwill was recorded as a result of the Company s acquisitions. In accordance with SFAS No. 141, Business Combinations, the Company has recorded these acquisitions using the purchase method of accounting. In accordance with SFAS No. 142, Goodwill and Other Intangible Assets, the Company performed an impairment review of its recorded goodwill in 2007 and determined that no impairment of goodwill existed because the estimated fair value of each reporting unit exceeded its carrying amount. The Company tests its recorded goodwill for impairment on an annual basis, or more often if indicators of potential impairment exist, by determining if the carrying value of each reporting unit exceeds its estimated fair value. Factors that could trigger an impairment include, but are not limited to, underperformance relative to historical or projected future operating results, significant changes in the manner of use of the acquired assets or the Company s overall business and significant negative industry or economic trends. Future impairment reviews may require write-downs in the Company s goodwill and could have a material adverse impact on the Company s operating results for the periods in which such write-downs occur.

*Stock-Based Compensation*

The Company accounts for stock-based compensation in accordance with SFAS No. 123 (revised 2004), Share-Based Payment (SFAS 123-R). The Company adopted the provisions of SFAS 123-R in the first quarter of 2006. Under the fair value recognition provisions of this statement, stock-based compensation expense is measured at the grant date based on the value of the award and is expensed ratably over the vesting period. Determining the fair value of stock options at the grant date requires judgment, including estimating expected dividends, volatility, terms and estimating the amount of share-based awards that are expected to be forfeited. If actual forfeiture rates differ significantly from the estimate, stock-based compensation expense and the Company s results of operations could be materially impacted. Beginning in 2006, the Company changed its previous practice of predominantly granting stock options to employees, and began granting restricted stock as an alternative. Compensation expense for restricted stock is based on the fair market value of the restricted stock on its grant date, and is expensed ratably over the vesting period.

*Income Taxes*

Income taxes are determined under guidelines prescribed by SFAS No. 109, Accounting for Income Taxes (SFAS 109). Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those

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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.

The Company regularly reviews the deferred tax assets for recoverability and has established a valuation allowance when it is more likely than not that some portion, or all, of the deferred tax assets will not be realized. The Company assesses the recoverability of the deferred tax assets and the need for a valuation allowance on an ongoing basis. In making this assessment, the Company is required to consider all available positive and negative evidence to determine whether, based on such evidence, it is more likely than not that some portion, or all, of the net deferred assets will be realized in future periods.

During the year ended December 31, 2007, the Company determined, primarily based on operating income during recent years and anticipated operating income and cash flows for future periods that it is more likely than not that certain foreign deferred tax assets will be realized in the future and accordingly, it was appropriate to release the valuation allowance recorded against those deferred tax assets. As a result, the Company released a portion of the valuation allowance related to certain foreign jurisdictions, resulting in a non-cash income tax benefit to net income, as well as a credit to goodwill as some of the deferred tax assets existed at the date of Scala s acquisition. The Company intends to maintain a valuation allowance for the remaining foreign deferred tax assets until sufficient positive evidence exists to support its reversal. The remaining valuation allowance will continue to be evaluated over future quarters. If it is determined that it is more likely than not that all or a portion of these remaining foreign deferred tax assets will be utilized to offset future taxable income, the valuation allowance could be decreased or eliminated altogether which will result primarily in a decrease to goodwill.

Future releases of the valuation allowance related to these assets will be accounted for as a reduction of goodwill rather than a reduction of income tax expense if the valuation allowance decrease occurs prior to the effective date of SFAS No. 141 (revised 2007), Business Combinations, or SFAS No. 141(R). Effective January 1, 2009, SFAS 141(R) provides that any reduction to the valuation allowance established in purchase accounting is to be accounted for as a reduction in income tax expense.

The Company is subject to income taxes in the U.S. and numerous foreign jurisdictions. Significant judgment is required in evaluating our uncertain tax positions and determining our provision for income taxes. Effective January 1, 2007, the Company adopted Financial Interpretation No. 48, Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109 (FIN 48). FIN 48 contains a two-step approach to recognizing and measuring uncertain tax positions accounted for in accordance with SFAS No. 109, Accounting for Income Taxes. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount that is more than 50% likely of being realized upon settlement.

Although the Company believes it has adequately reserved for our uncertain tax positions, no assurance can be given that the final tax outcome of these matters will not be different. The Company adjusts these reserves in light of changing facts and circumstances, such as the closing of a tax audit or the refinement of an estimate. To the extent that the final tax outcome of these matters is different than the amounts recorded, such differences will impact the provision for income taxes in the period in which such determination is made. The provision for income taxes includes the impact of reserve provisions and changes to reserves that are considered appropriate, as well as the related net interest.

During the ordinary course of business, there are many transactions and calculations for which the ultimate tax determination is uncertain. As a result, the Company recognizes tax liabilities based on estimates of whether additional taxes and interest will be due. These tax liabilities are recognized when, despite the Company s belief that its tax return positions are supportable, the Company believes that certain positions may not be fully sustained upon review by tax authorities. The Company believes that its accruals for tax liabilities are adequate for all open audit years based on its assessment of many factors including past experience and interpretations of tax law. This assessment relies on estimates and assumptions and may involve a series of complex judgments about future events. To the extent that the final tax outcome of these matters is different than the amounts recorded, such differences will impact income tax expense in the period in which such determination is made.

U.S. income taxes were not provided for on undistributed earnings from certain non-U.S. subsidiaries. Those earnings are considered to be permanently reinvested in accordance with Accounting Principles Board (APB) Opinion 23.

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**New Accounting Pronouncements**

For new accounting pronouncements see Note 14 in Notes to Unaudited Condensed Consolidated Financial Statements.

**Acquisitions**

*NSB Retail Systems PLC*

On February 7, 2008, the Company completed its acquisition of NSB Retail Systems PLC (NSB). NSB designs, develops, markets and supports store and merchandising solutions to retailers of apparel, footwear and specialty merchandise. The acquisition of NSB provides an expanded portfolio of products and services for large and mid-sized specialty retailers and department stores, as well as a fully hosted, managed service offering designed for smaller retailers who are interested in rapid implementation via an on-demand versus on-premise offering.

Pursuant to the terms of the acquisition agreement, shareholders of NSB received £0.38 in cash for each NSB ordinary share. The value of the fully diluted share capital of NSB was approximately $311.8 million, not including transaction costs, based on the exchange rates in effect at the time the U.S. dollars were converted to pounds sterling for purposes of the transaction. The consideration payable under the agreement was funded by the Company with approximately $161.0 million in existing cash balances, with the balance of the consideration being funded by drawing from funds available pursuant to the 2007 credit facility. In addition, on February 11, 2008, the Company sold the NSB acquisition British pound sterling call options that were marked to market at December 31, 2007 at $1.8 million back to the issuing institutions for $0.2 million, resulting in net foreign currency loss of $1.6 million. The loss resulted from depreciation of pounds sterling against the U.S. Dollar. The net loss is included in Interest and other income, net, in the Condensed Consolidated Statements of Operations.

The total preliminary purchase price for NSB is shown below (*in thousands*):

| | |
|---|---|
| Cash | $ 311,845 |
| Transaction costs | 5,739 |
| Total purchase price | $ 317,584 |

The acquisition of NSB is accounted for as a purchase business combination as defined in SFAS No. 141, Business Combinations. Under the purchase method of accounting, the purchase price was allocated to NSB s tangible and intangible assets acquired and liabilities assumed based on their estimated fair values as of February 7, 2008, with any excess being ascribed to goodwill. Management is primarily responsible for determining the fair values of these assets. The fair value of the assets acquired and liabilities assumed represent management s estimate of fair values. The purchase price allocation and transaction costs are preliminary and will be adjusted upon completion of the final valuation of acquired assets and liabilities assumed, including income tax assets and liabilities.

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The following table summarizes the preliminary allocation of the purchase price (*in thousands*):

| | |
|---|---|
| Fair value of tangible assets acquired: | |
| Cash and marketable securities | $ 33,181 |
| Accounts receivable | 18,274 |
| Inventory | 1,196 |
| Property and equipment | 11,933 |
| Prepaid and other assets | 4,587 |
| Deferred tax asset | 2,047 |
| Total tangible assets acquired | 71,218 |
| Acquired technology | 58,700 |
| Acquired in-process research and development | 200 |
| Customer base | 39,300 |
| Trade name | 3,500 |
| Goodwill | 198,073 |
| Accounts payable and accrued expenses | (22,900) |
| Deferred revenue | (17,328) |
| Other long-term liabilities | (2,264) |
| Deferred tax liability | (10,915) |
| Net assets acquired | $ 317,584 |

In connection with the acquisition, the Company formulated a restructuring plan for the NSB operations. As a result, the Company recorded a liability of $4.1 million for the costs related to involuntary employee terminations. This liability was included in the allocation of the purchase price in accordance with SFAS No. 141, Business Combinations and EITF Issue No. 95-3 Recognition of Liabilities in Connection with a Purchase Business Combination. Execution of the restructuring plan was completed as of June 30, 2008.

Included in the Company s operating results for six months ended June 30, 2008 is a charge of $0.2 million for the acquired in-process research and development expenses related to the NSB acquisition. The in-process research and development expenses arose from new products that were under development at the date of the acquisition and were expected to eventually lead to new products but had not yet established technological feasibility and for which no future alternative use was identified. The valuation of the in-process research and development projects were based upon the discounted expected future cash flows of the products over the products expected life, reflecting the estimated stage of completion of the projects and the estimate of the costs to complete the projects.

See Note 3 in Notes to Unaudited Condensed Consolidated Financial Statements for Pro Forma information related to this acquisition.

*Professional Advantage*

On May 16, 2007, the Company acquired the assets of a division of Professional Advantage Pty Limited (PA), a privately held reseller located in Australia. The primary purpose of this acquisition was to increase the Company s presence and direct customer base in the territories covered by PA.

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The purchase price was allocated to PA s tangible and intangible assets acquired and liabilities assumed based on their estimated fair values as of May 16, 2007. The following table summarizes the allocation of the purchase price (*in thousands*):

| | |
|---|---|
| Cash | $ 16,000 |
| Transaction costs | 631 |
| Total | $ 16,631 |
| Fixed assets | $ 49 |
| Customer base | 5,728 |
| Acquired technology | 1,199 |
| Goodwill | 10,626 |
| Accrued liabilities | (632) |
| Deferred revenue | (339) |
| Net assets acquired | $ 16,631 |

**Restructuring Charges**

Through the first six months of 2008, the Company recorded restructuring charges of $4.2 million. This charge represents severance costs related to management severance and cost reductions from the elimination of redundancies in the Company s retail business resulting from the NSB acquisition. In connection with these restructuring costs, the Company terminated 35 employees or approximately 1% of the Company s workforce at that time from all functional areas. As of June 30, 2008, all of these terminations had been completed.

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**Results of Operations**

The following table summarizes certain aspects of the Company s results of operations for the three and six months ended June 30, 2008, compared to the three and six months ended June 30, 2007 (*in millions, except percentages*):

| | Three Months Ended June 30, | | | | Six Months Ended June 30, | | | |
|---|---|---|---|---|---|---|---|---|
| | 2008 | 2007 | Change $ | Change % | 2008 | 2007 | Change $ | Change % |
| Revenues | | | | | | | | |
| License | $ 24.4 | $ 25.1 | $ (0.7) | (3.0)% | $ 42.9 | $ 47.1 | $ (4.2) | (9.1)% |
| Consulting | 41.0 | 34.1 | 6.9 | 20.3% | 72.4 | 66.8 | 5.6 | 8.4% |
| Maintenance | 48.7 | 39.7 | 9.0 | 22.7% | 94.9 | 78.8 | 16.1 | 20.5% |
| Hardware and other | 13.8 | 6.8 | 7.0 | 103.6% | 20.0 | 14.3 | 5.7 | 39.7% |
| Total revenues | 127.9 | 105.7 | 22.2 | 21.0% | 230.2 | 207.0 | 23.2 | 11.2% |
| Gross profit % | | | | | | | | |
| License | 76.3% | 79.8% | | | 78.2% | 78.8% | | |
| Consulting | 20.1% | 17.7% | | | 10.6% | 17.7% | | |
| Maintenance | 72.9% | 78.0% | | | 73.9% | 77.8% | | |
| Hardware and other | 9.5% | 11.9% | | | 5.3% | 11.5% | | |
| Amortization of intangible assets | $ 8.9 | $ 4.3 | $ 4.6 | 107.6% | $ 16.0 | $ 8.5 | $ 7.5 | 88.5% |
| % of total revenues | 7.0% | 4.1% | | | 7.0% | 4.1% | | |
| Gross profit | $ 54.7 | $ 53.5 | $ 1.2 | 2.2% | $ 96.3 | $ 103.5 | $ (7.2) | (6.9)% |
| % of revenues | 42.8% | 50.6% | | | 41.9% | 50.0% | | |
| Sales and marketing | $ 21.3 | $ 18.8 | $ 2.5 | 12.9% | $ 42.6 | $ 37.4 | $ 5.2 | 13.8% |
| % of revenues | 16.6% | 17.8% | | | 18.5% | 18.1% | | |
| Software development | $ 14.3 | $ 9.6 | $ 4.7 | 49.4% | $ 27.3 | $ 18.3 | $ 9.0 | 49.7% |
| % of revenues | 11.2% | 9.1% | | | 11.9% | 8.8% | | |
| General and administrative | $ 13.6 | $ 14.4 | $ (0.8) | -6.0% | $ 25.5 | $ 29.8 | $ (4.3) | (14.5)% |
| % of revenues | 10.6% | 13.6% | | | 11.1% | 14.4% | | |
| In-process research and development | $ | $ | $ | 0.0% | $ 0.2 | $ | $ 0.2 | 100.0% |
| % of revenues | 0.0% | 0.0% | | | 0.1% | 0.0% | | |
| Restructuring charge | $ 0.1 | $ | $ 0.1 | 100.0% | $ 4.2 | $ 0.2 | $ 4.0 | 1787.8% |
| % of revenues | 0.1% | 0.0% | | | 1.8% | 0.1% | | |
| Interest expense | $ 4.4 | $ 2.7 | $ 1.7 | 59.7% | $ 7.3 | $ 4.9 | $ 2.4 | 49.4% |
| % of revenues | 3.4% | 2.6% | | | 3.2% | 2.3% | | |
| Gain on sale of non-strategic asset | $ | $ | $ | 0.0% | $ | $ 1.6 | $ (1.6) | -100.0% |
| % of revenues | 0.0% | 0.0% | | | 0.0% | 0.8% | | |
| Interest and other income, net | $ 1.0 | $ 2.0 | $ (1.0) | (51.7)% | $ 1.8 | $ 2.6 | $ (0.8) | (29.6)% |
| % of revenues | 0.8% | 1.9% | | | 0.8% | 1.3% | | |
| Provision for income taxes | $ 0.8 | $ 3.7 | $ (2.9) | (78.2)% | $ (3.3) | $ 6.3 | $ (9.6) | (151.7)% |
| Effective tax rate | 37.8% | 37.2% | | | 36.9% | 37.2% | | |
| Net income | $ 1.3 | $ 6.3 | $ (5.0) | (78.8)% | $ (5.7) | $ 10.7 | $ (16.4) | (152.7)% |
| % of revenues | 1.0% | 6.0% | | | (2.5)% | 5.2% | | |

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*Revenue*

The decrease in license revenues for the three and six months ended June 30, 2008, compared to the same period in 2007, is due primarily to lengthening sales cycles and some deals that were expected to close in the second quarter of 2008 and slipped into the third quarter of 2008. In addition, customers are implementing projects on a staged basis where they purchase and roll out smaller parts of their total solution. The decreases were partially offset by additional license revenues due to the acquisition of NSB. License revenues for the three months ended June 30, 2008, included four sales greater than $0.5 million, of which one was greater than $1.0 million. License revenues for the three months ended June 30, 2007, included one deal greater than $0.5 million, which was not greater than $1.0 million. License revenues for the six months ended June 30, 2008, included six sales greater than $0.5 million, of which one was greater than $1.0 million. License revenues for the six months ended June 30, 2007, included four deals greater than $0.5 million, of which one was greater than $1.0 million. The one sale greater than $1.0 million in 2007 was related to the sale of a non-strategic asset (see Sale of Non-Strategic Asset ).

Consulting revenues increased for the three months ended June 30, 2008, compared to the same period in 2007, due primarily to additional consulting revenues from the acquisition of NSB. Consulting revenues increased for the six months ended June 30, 2008, compared to the same period in 2007, due the acquisition of NSB offset by decreased consulting revenue due to a significant international engagement in the prior period with no similar engagement in the current period. Consulting revenues were also negatively impacted by a strategic consulting deal with a large customer that required the Company to allocate significant consulting resources to this project with little additional associated revenues to date.

The increase in maintenance revenues for the three and six months ended June 30, 2008, compared to the same periods in 2007, is due primarily to the acquisition of NSB, which contributed maintenance revenues during the quarter, as well as continued high renewal rates in the Company s customer base, continuing license sales in prior periods and related maintenance contracts sold with new licenses and an increase in existing customers whose maintenance agreements had previously lapsed, but who have now renewed their maintenance agreements.

Hardware and other revenues consist primarily of the resale of third-party hardware. The increase in hardware and other revenue for the three and six months ended June 30, 2008, as compared to the same period in 2007, is due to the timing of customer hardware orders, which vary based on the customers hardware roll-out schedules, resulting in a high degree of variability in the Company s hardware revenues.

International revenue was $43.1 million and $40.4 million for the three months ended June 30, 2008 and 2007, representing 33.7% and 38.2%, respectively, of total revenues. International revenues were $79.4 million and $82.4 million for the six months ended June 30, 2008 and 2007, representing 34.5% and 39.8%, respectively, of total revenues. The increase in international revenue in absolute dollars for the three months ended June 30, 2008 compared to the same period in 2007 is primarily due to the acquisition of PA as well as continued high renewal rates on international maintenance revenues. The decrease in international revenues as a percentage of revenues was primarily due to the addition of NSB revenue which is primarily earned in the United States. The decrease in international revenues for the six months ended June 30, 2008 compared to the same period in 2007 in both absolute dollars and as a percentage of total revenues is primarily due to the greater than $1.0 million sale that occurred in the first quarter 2007, see sale of a non-strategic asset below, with no similar sale in the current period and was also impacted by the addition of NSB revenues which are primarily earned in the United States. Foreign currency exchange rate fluctuations resulted in foreign currency-based revenues during the three months ended June 30, 2008 being reported $2.9 million, or 2.8%, higher than these revenues would have been if they had been translated at 2007 foreign currency exchange rates. Foreign currency exchange rate fluctuations resulted in foreign currency-based revenues during the six months ended June 30, 2008 being reported $5.2 million, or 2.5%, higher than these revenues would have been if they had been translated at 2007 foreign currency exchange rates.

*Cost of Revenues and Gross Margins*

Cost of license revenues consists primarily of software royalties paid for third-party software incorporated into the Company s products, referral fees paid to Value Added Resellers (VARs), costs associated with product packaging and documentation and software duplication. For the three months ended June 30, 2008, compared to the same period in 2007, gross profit of license revenue decreased as costs increased due primarily to a higher mix of third party software sales. For the six months ended June 30, 2008, compared to the same period in 2007, gross profit of license revenue was relatively flat.

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Cost of consulting revenues consists primarily of salaries, benefits, commissions, bonus, other headcount-related expenses and travel for the Company s consulting organization, which provides consulting services to customers in the implementation and integration of the Company s software products, as well as education, training and other consulting and programming services. These costs increased in absolute dollars and as a percentage of revenue during the three and six months ended June 30, 2008, compared to the same periods in 2007, due primarily to the acquisition of NSB. Consulting services margins increased for the three months ended June 30, 2008, compared to the same period in 2007, due to increasing the utilization rates of consultants. Consulting services margins decreased for the six months ended June 30, 2008, compared to the same period in 2007, due in part to a strategic consulting contract with a large customer for which the Company adjusted cost estimates and recorded future estimated losses. In addition, consulting services margins were negatively impacted in the first quarter of 2008 due to lower than expected utilization rates related to the integration of NSB and the significant hiring the Company has done in lower cost geographies over the past several quarters, which has required more training to bring these consultants up to fully billable rates.

Cost of maintenance revenues consists primarily of maintenance royalties on third-party software incorporated into the Company s products, as well as salaries, benefits and other headcount-related expenses for the Company s support organization. For the three and six months ended June 30, 2008, compared to the same periods of 2007, cost of maintenance revenues increased in absolute dollars due primarily to the acquisition of NSB. Maintenance gross profit decreased during the three and six months ended June 30, 2008, compared to the same periods in 2007, due to the addition of NSB maintenance revenue, which has lower gross margins.

Cost of hardware and other revenue increased in absolute dollars in the three and six months ended June 30, 2008 compared to the same periods in 2007, due to the timing of customer hardware orders, which vary based on the customers hardware roll-out schedules and can result in a high degree of variability in our hardware gross profit margins.

*Amortization of Intangible Assets*

Amortization of intangible assets consists of amortization of capitalized acquired technology, customer base and trademarks that were recorded as a result of acquisitions. The Company s intangible assets are amortized over the estimated economic lives of the assets. For the three months ended June 30, 2008 and 2007, the Company recorded amortization expense, included in cost of revenues, related to intangible assets of $8.9 million and $4.3 million, respectively. For the six months ended June 30, 2008 and 2007, the Company recorded amortization expense, included in cost of revenues, related to intangible assets of $16.0 million and $8.5 million, respectively. The increase in amortization expense for the three and six months ended June 30, 2008, as compared to the same periods in 2007 is due to the additional amortization expense related to the NSB acquisition. Amortization of acquired technology and trademarks will be complete in 2013 and amortization of the customer base will be complete in 2015. See Note 4 in Notes to Unaudited Condensed Consolidated Financial Statements for expected future amortization expense.

*Sales and Marketing*

Sales and marketing expenses consist primarily of salaries, commissions, travel, advertising and promotional expenses. These costs increased in absolute dollars, but decreased as a percentage of revenue, for the three months ended June 30, 2008, compared to the same period in 2007. The decrease as a percentage of revenue is due to the increased revenues. These costs increased in both absolute dollars and as a percentage of revenue for the six months ended June 30, 2008, compared to the same period in 2007. The increase in absolute dollars for the three and six months is due to increased headcount of approximately 10%, related primarily to the NSB acquisition.

*Software Development*

Software development costs consist primarily of compensation of development personnel, related overhead incurred to develop new products and upgrade and enhance the Company s current products and fees paid to outside consultants. The majority of these expenses have been incurred by the Company in the United States, Canada, Mexico, Eastern Europe and Russia, where the Company operates development centers.

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Software development expenses increased in absolute dollars and as a percentage of revenue for the three and six months ended June 30, 2008, compared to the same periods in 2007. The increase in these costs is due primarily to an increase in headcount of 47% due to increased hiring and the acquisition of NSB, as well as to additional investment the Company is making in software development ahead of the launch of Epicor 9.

*General and Administrative Expense*

General and administrative expenses consist primarily of costs associated with the Company s executive, financial, legal, human resources and information services functions. General and administrative expenses decreased in total dollars and as a percentage of total revenues during the three and six months ended June 30, 2008, compared to the same periods in 2007. This decrease is primarily attributable to reductions in provision for doubtful accounts and personnel related costs, including stock-based compensation expense, associated with changes in senior management within the Company, partially offset by an increase in costs from the acquisition of NSB.

*Stock-Based Compensation Expense*

Stock-based compensation expense includes compensation expense from stock options granted and restricted stock issued by the Company. For the three months ended June 30, 2008 and 2007, stock-based compensation expense was $1.9 million and $3.3 million, respectively. For the six months ended June 30, 2008 and 2007, stock-based compensation expense was $4.4 million and $6.7 million, respectively.

At June 30, 2008, there was approximately $10.6 million and $5.5 million of unrecognized compensation cost related to performance-based restricted stock and other restricted stock grants, respectively. These costs are expected to be recognized over weighted-average periods of approximately two years. The compensation cost related to the performance-based restricted stock depends on the estimated number of shares that will vest based on the probable outcome of the performance conditions. Therefore, the recognized compensation could vary significantly, depending on the outcome of those conditions. The Company is required at each reporting date to assess whether achievement of any performance condition is probable. Quarterly compensation expense may include a cumulative adjustment resulting from changes in the estimated number of shares expected to be earned during that plan year. Based on the Company s current assessment, the Company has recorded stock compensation expense related to these grants of $1.1 million and $2.9 million for the three and six months ended June 30, 2008, respectively.

At June 30, 2008, there was approximately $0.6 million of total unrecognized compensation cost related to unvested stock options. This cost is expected to be recognized over a weighted-average period of approximately two years.

The following table sets forth the total stock-based compensation expense resulting from stock options, restricted stock awards and the employee stock purchase plan included in the Company s Condensed Consolidated Statements of Operations (*in thousands*):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2008 | 2007 | 2008 | 2007 |
| Cost of consulting revenues | $ 107,000 | $ 355,000 | $ 358,000 | $ 725,000 |
| Cost of maintenance revenues | 100,000 | 138,000 | 211,000 | 292,000 |
| Sales and marketing | 725,000 | 1,148,000 | 1,601,000 | 2,247,000 |
| Software development | 171,000 | 216,000 | 372,000 | 479,000 |
| General and administrative | 804,000 | 1,443,000 | 1,853,000 | 2,951,000 |
| Total stock-based compensation expense | $ 1,907,000 | $ 3,300,000 | $ 4,395,000 | $ 6,694,000 |

*In-Process Research and Development*

Included in the Company s operating results for the six months ended June 30, 2008 is a charge of $0.2 million for the acquired in-process research and development expenses related to the NSB acquisition. The in-process research and development expense arose from new products that were under development at the date of the acquisition and were expected to eventually lead to new products but had not yet established technological feasibility and for which no future alternative use was identified. The valuation of the in-process research and development projects was based upon the discounted expected future cash flows of the products over the products expected life, reflecting the estimated stage of completion of the projects and the estimate of the costs to complete the projects.

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*Restructuring*

For the three and six months ended June 30, 2008, the Company recorded restructuring charges of $0.1 million and $4.2 million, respectively. This charge is related to management severance and cost reductions from the elimination of redundancies as a result of the NSB acquisition in the Company s retail business.

*Interest Expense*

Interest expense increased for the three and six months ended June 30, 2008, as compared to the same periods in 2007 due to increased interest on additional debt incurred in February for the acquisition of NSB as well as interest on the Company s convertible senior notes issued in May of 2007.

*Sale of Non-Strategic Asset*

During March of 2007, the Company entered into an arrangement to sell the assets of its payroll bureau operations in Russia. In connection with this asset sale arrangement, the Company also entered into an arrangement with the same party to license the iScala payroll product for resale on an exclusive basis in certain Eastern European territories. This transaction was accounted for as a multiple-element arrangement under EITF Issue No. 00-21. Based on an estimated fair value of the payroll bureau, the Company allocated $2.5 million of the total consideration to the sale of these assets as well. This consideration, less the carrying amounts of $0.8 million of goodwill and $0.1 million of net customer base intangible assets originally recorded in connection with the 2004 acquisition of Scala and $22,000 of net tangible assets, resulted in a net gain of $1.6 million which is included in gain on sale of non-strategic asset in the accompanying Condensed Consolidated Statements of Operations for the six months ended June 30, 2007. The remaining consideration related to the iScala payroll product license is included in license in the accompanying Condensed Consolidated Statements of Operations for the six months ended June 30, 2007.

*Interest Income and Other, Net*

Interest income and other, net, decreased for the three and six months ended June 30, 2008, as compared to the same periods in 2007, due primarily to an decrease in interest earned on the Company s cash balances. The Company had a large cash balance in the prior year due to cash received from the debt offering which occurred in May of 2007. The Company used this cash, as well as cash from a new credit facility to purchase NSB in February of 2008, resulting in a decrease of interest income. In addition to the decrease in interest income, the Company realized a foreign currency loss in the first quarter of 2008 resulting from the Company s British pound sterling call option contracts related to the NSB acquisition, which were settled for a loss of $1.6 million. This loss was offset by foreign currency gains of $0.9 million primarily due to the Company s intercompany translation.

*Provision for Income Taxes*

The provision for income taxes consists of provisions for federal, state and foreign income taxes. The Company operates in an international environment with significant operations in various locations outside the U.S. Accordingly, the consolidated income tax rate is a composite rate reflecting the earnings in the various locations and the applicable rates.

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions that affect the reported amount of tax-related assets and liabilities and income tax provisions. The Company assesses the recoverability of the deferred tax assets on an ongoing basis. In making this assessment the Company is required to consider all available positive and negative evidence to determine whether, based on such evidence, it is more likely than not that some portion or all of our net deferred assets will be realized in future periods. This assessment requires significant judgment. In addition, the Company has made estimates involving current and deferred income taxes, tax attributes relating to the interpretation of various tax laws, historical bases of tax attributes associated with certain tangible and intangible assets.

The Company recorded a provision for income taxes of $0.8 million and a provision for income taxes of $3.7 million for the three months ended June 30, 2008 and 2007, respectively. The effective income tax rates were 37.8% and 37.2% for the three months ended June 30, 2008 and 2007, respectively. The effective tax rate differs from the statutory U.S. federal income tax rate of 35% primarily due to state and foreign income tax and permanent differences between GAAP pre-tax income and taxable income.

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Future releases of the valuation allowance related to these assets will be accounted for as a reduction of goodwill rather than a reduction of income tax expense if the valuation allowance decrease occurs prior to the effective date of SFAS No. 141 (revised 2007), Business Combinations, or SFAS No. 141(R). Effective January 1, 2009, SFAS 141(R) provides that any reduction to the valuation allowance established in purchase accounting is to be accounted for as a reduction in income tax expense.

During the year ended December 31, 2007, the Company determined, primarily based on operating income during recent years and anticipated operating income and cash flows for future periods that it is more likely than not that certain foreign deferred tax assets will be realized in the future, and, accordingly, it was appropriate to release the valuation allowance recorded against those deferred tax assets. As a result, the Company released a portion of the valuation allowance related to certain foreign jurisdictions, resulting in a non-cash income tax benefit to net income as well as a credit to goodwill as some of the deferred tax assets existed at the date of Scala s acquisition. The Company intends to maintain a valuation allowance for the remaining foreign deferred tax assets until sufficient positive evidence exists to support its reversal. The remaining valuation allowance will continue to be evaluated over future quarters. If it is determined that it is more likely than not that all or a portion of these remaining foreign deferred tax assets will be utilized to offset future taxable income, the valuation allowance could be decreased or eliminated altogether which will result primarily in a decrease to goodwill.

***Liquidity and Capital Resources***

The following table summarizes the Company s cash and cash equivalents, working capital, long-term debt and cash flows as of and for the six months ended June 30, 2008 (*in millions*):

| | **June 30, 2008** |
|---|---|
| Cash and cash equivalents | $ 132.4 |
| Working capital | 78.7 |
| Net cash provided by operating activities | 34.8 |
| Net cash (used in) investing activities | (128.4) |
| Net cash provided by financing activities | 150.5 |
| Long-term debt, less current portion | 380.1 |

As of June 30, 2008, the Company s principal sources of liquidity included cash and cash equivalents of $132.4 million and unused borrowing capacity of approximately $90 million under its senior revolving credit facility. The Company s operations provided $34.8 million in cash during the six months ended June 30, 2008. As of June 30, 2008, the Company had $12.2 million in cash obligations for severance costs, lease terminations and other costs related to the Company s restructurings. These obligations are expected to be paid through 2016 and the Company believes these obligations will be funded from existing cash reserves and cash generated from continuing operations. The Company s working capital excluding deferred revenue is $169.1 million. The Company believes this is a relevant measurement of working capital as deferred revenue is an obligation for services not cash. The cost of providing these services is generally fixed in nature and ranges from 21% to 25% of the related revenues.

On November 1, 2007, the Company announced that the Board of Directors authorized the Company to institute a stock repurchase program whereby up to $50 million of its common stock may be repurchased from time to time. The duration of the repurchase program is open-ended. Under the program, the Company is able to purchase shares of common stock through open market transactions at prices deemed appropriate by management. The timing and amount of repurchase transactions under this program will depend on market conditions and corporate and regulatory considerations. The program may be discontinued at any time by the Board of Directors. Through June 30, 2008, the Company repurchased 162,000 shares of its common stock at a weighted average price of $8.03 per share under this program.

On May 8, 2007, the Company closed an offering of $230 million aggregate principal amount of 2.375% convertible senior notes due in 2027. The notes are unsecured and pay interest semiannually at a rate of 2.375% per annum until May 15, 2027. The notes are convertible into cash or, at the Company s option, cash and shares of the Company s common stock, at an initial conversion rate of 55.2608 shares of common stock per $1,000 principal amount of notes, which is equivalent to an initial conversion price of approximately $18.10 per share. Pursuant to the terms of the notes, the principal amount of the notes is settleable in cash and only the amount of conversion value, as defined, in excess of the principal amount of the notes is settleable in cash or shares. The initial conversion price represents a

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30% premium over the last reported sale price of the Company s common stock prior to the offering that began on May 2, 2007, which was $13.92 per share. The conversion rate will be adjusted upon the occurrence of certain events defined in the indenture. The notes do not contain any restrictive financial covenants.

On or after May 15, 2014, the Company may from time to time at its option redeem the notes, in whole or in part, for cash, at a redemption price equal to 100% of the principal amount of the notes we redeem, plus any accrued and unpaid interest to, but excluding, the redemption date. On each of May 15, 2014, May 15, 2017 and May 15, 2022, holders may require us to purchase all or a portion of their notes at a purchase price equal to 100% of the principal amount of the notes to be purchased, plus any accrued and unpaid interest to, but excluding, the purchase date.

The Company s days sales outstanding (DSO) for the last six quarters are set forth in the following tables:

| **Quarter Ended:** | **2007** |
|---|---|
| March 31 | 68 |
| June 30 | 71 |
| September 30 | 75 |
| December 31 | 76 |

| **Quarter Ended:** | **2008** |
|---|---|
| March 31 | 91 |
| June 30 | 66 |

The increase in DSO s in the first quarter 2008 was due primarily to the Company having higher accounts receivable balances without related revenues as a result of the NSB acquisition as well as relatively longer payment cycles. The decrease in DSO s in the second quarter is due primarily to strong cash collections.

The Company s principal investing activities for the six months ended June 30, 2008, included use of cash designated for acquisition of $161.0 million, acquisitions for $285.2 million, capital expenditures of $5.6 million and proceeds from sale of investments of $1.4 million.

Financing activities for the six months ended June 30, 2008 included $160.0 million in proceeds from long-term debt, $2.8 million in payments on long-term debt, $5.0 million in debt issuance fees and $4.5 million in the purchase of treasury stock. The Company repurchases a portion of the vested shares to satisfy employee income tax withholding requirements and expects such treasury stock activity to recur due to the various vesting schedules of restricted stock. Cash provided by financing activities also included proceeds from the issuance of stock under the employee stock purchase plan and proceeds from the exercise of employee stock options of $1.6 million.

On December 16, 2007, the Company entered into a credit agreement with several financial institutions (the 2007 credit facility), which provides for term loans in an amount up to $100 million and revolving loans in an amount up to $100 million with an option for the Company to increase the revolving loan commitments and/or the term loan commitments by an aggregate amount up to $50 million pursuant to an accordion feature for a total secured loan facility up to $250 million. In connection with the 2007 credit facility, the Company agreed to certain financial and other covenants. Funds under the 2007 credit facility are available to the Company upon completion of the NSB acquisition (See Note 3 in Notes to Unaudited Condensed Consolidated Financial Statements), to pay the fees and expenses incurred in connection with the NSB acquisition, as well as to provide ongoing working capital and for other general corporate purposes of the Company and its subsidiaries following the NSB acquisition.

On February 11, 2008, the Company amended the 2007 credit facility to exercise the accordion feature contained in the facility to increase the total credit facility to $250 million, consisting of $100 million of term loans and $150 million of revolving loans. On February 19, 2008, the Company borrowed $100 million in term loans and $60 million of revolving loans under the 2007 credit facility and used the proceeds to finance the NSB acquisition and to pay certain fees and expenses incurred in connection with the NSB acquisition.

On March 31, 2008 and on June 30, 2008, the Company made mandatory principal payments of $1.25 million against the term loan from discretionary funds. As of June 30, 2008, the Company had unused borrowing capacity of approximately $90 million under the 2007 credit facility and the weighted average interest rate applicable to outstanding loans under the 2007 credit facility was 5.68%. As of June 30, 2008, the Company was in compliance with all covenants included in the terms of the 2007 credit facility, other than its consolidated total leverage ratio. The Company obtained a waiver from its lenders with respect to this covenant on July 23, 2008.

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On July 23, 2008, the Company made a voluntary principal payment of $5.0 million against the revolving loan from discretionary funds.

On April 18, 2008, the Company entered into interest rate swap agreements to convert a portion of the Company s interest rate variability to a fixed rate basis as required under the 2007 credit facility. The interest rate swaps qualify for hedge accounting treatment pursuant to SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended. The changes in the fair value of the interest rate swaps are reflected in the carrying value of the interest rate swap on the balance sheet. The differential to be paid or received on the interest rate swap agreements will be accrued and recognized as an adjustment to interest expense as interest rates change beginning in the third quarter 2008. The interest rate swap agreements commenced effective June 30, 2008 and have an aggregate notional amount of $20 million maturing March 31, 2009 and $30 million maturing September 30, 2009. The effective interest rate for the notional amounts covered by the swap agreements is 5.67%.

As of June 30, 2008, the interest rate swap resulted in a net liability of $31,000 included in accrued liabilities. The change in market value during fiscal 2008 related to the effective portion of the cash flow hedge was recorded as an unrecognized loss in the accumulated other comprehensive income section of stockholders equity in the Company s Condensed Consolidated Balance Sheets.

The Company is dependent upon its ability to generate cash flows from license and other operating revenues, providing services to its customers and through collection of its accounts receivable to maintain current liquidity levels. If the Company is not successful in achieving targeted revenues and expenses or positive cash flows from operations, the Company may be required to take further cost-cutting measures and restructuring actions or seek alternative sources of funding. Alternative sources of funding may not be available on terms favorable to the Company or at all, in which case, the Company s business, financial condition or results of operations may be adversely affected.

Considering current cash reserves, and other existing sources of liquidity, including its revolving credit facility, management believes that the Company will have sufficient sources of financing to continue its operations through at least the next twelve months. There can be no assurance that the Company will not seek to raise additional capital through the incurrence of debt or issuance of equity securities in the future. However, the Company may require additional sources of liquidity to fund any future acquisitions and its future growth.

*Foreign Currency Risk*

The Company has several operations in foreign locations around the world. These operations incur revenue and expenses in various foreign currencies. Revenues and expenses denominated in currencies other than the U.S. dollar expose the Company to foreign currency market risk. Unfavorable movements in foreign currency exchange rates between the U.S. dollar and other foreign currencies may have an adverse impact on the Company s operations. These foreign currency market movements could create a foreign currency gain or loss that could be realized or unrealized for the Company. The Company s Board of Directors has approved a foreign currency risk policy that allows the Company to enter into forward contracts and purchase option agreements to hedge foreign currency risks. The Company has an ongoing program to evaluate its foreign currency risk and to minimize these risks whenever possible through leading and lagging accounts payables and accounts receivables, centralized cash management and other forms of natural hedging. The Company also uses forward contracts or purchased options to hedge some of its foreign currency transaction exposure. Gains and losses resulting from these transactions are included in interest and other income, net in the accompanying Condensed Consolidated Statement of Operations. As of June 30, 2008, the Company had no open forward contracts or purchase options. At June 30, 2008, the Company had foreign currency denominated LIBOR borrowings under its 2007 credit facility consisting of $10 million Australian dollars, $2 million Canadian dollars and 2 million Euro.

*Off-Balance Sheet Arrangements*

On May 8, 2007, the Company closed an offering of convertible senior notes due in 2027. These notes are due in full in 2027 and are convertible into shares of common stock at a conversion price of $18.10 per share. Pursuant to the terms of the notes, the principal amount of the notes is settleable in cash and only the amount of conversion value, as defined, in excess of the principal amount of the notes is settleable in cash or shares. In accordance with relevant authoritative pronouncements issued by the FASB and its Emerging Issues Task Force (EITF), the

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conversion feature of the notes does not qualify for separate accounting from the notes. Accordingly, no separate amounts related to the conversion feature are presented in the consolidated financial statements (see Note 8 in Notes to Unaudited Condensed Consolidated Financial Statements).

*Material Changes in Contractual Obligation*

The Company had a material change in significant contractual obligations from December 31, 2007, as a result of the Company s amendment of its 2007 credit facility and drawing down for the NSB acquisition. As of June 30, 2008, future payments related to the 2007 credit facility, which are included in Current portion of long-term debt and Long-term debt, less current portion on the Company s Condensed Consolidated Balance Sheet, are as follows:

| | Payments Due by Period *(in thousands)* | | | | |
|---|---|---|---|---|---|
| | **Less than 1 Year** | **1-3 Years** | **3-5 Years** | **More than 5 years** | **Total** |
| 2007 credit facility | $ 7,500 | $ 30,000 | $ 119,819 | $ | $ 157,319 |
| Related estimated interest payments* | 8,808 | 15,736 | 8,967 | | 33,511 |
| Total contractual obligations | $ 16,308 | $ 45,736 | $ 128,786 | $ | $ 190,830 |

* Based on effective interest rate at June 30, 2008.

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*Certain Factors That May Affect Future Results*

**We have recorded a large amount of goodwill and other acquired intangible assets which we will be required to write down and record an expense if they become impaired.**

In connection with our acquisitions, we currently have goodwill of $369.6 million and $132.7 million of amortizing acquired intangible assets on our balance sheet. Although the goodwill is not amortized, we are required to test the goodwill for impairment at least yearly and any time there is an indication an impairment may have occurred. If we determine that the carrying value of the goodwill or other acquired intangible assets is in excess of its fair value, we will be required to write down a portion or all of the goodwill or other acquired intangible assets, which would adversely impact our results of operations.

**We have a significant amount of debt following our note offering in 2007 and credit agreement in February 2008.**

As of June 30, 2008, we had approximately $230 million of outstanding debt related to our debt offering. In addition, in February 2008, we borrowed $160 million under our Credit Agreement dated December 16, 2007, as amended by the First Amendment dated February 11, 2008 and the Notice dated February 11, 2008, to finance the acquisition of NSB and to pay certain fees and expenses incurred in connection with the acquisition. Our substantial indebtedness could adversely affect our business, financial condition and results of operations and our ability to meet our payment obligations under our outstanding liabilities.

This level of debt could have significant consequences on our future operations, including:

- Making it more difficult for us to meet our payment and other obligations under our outstanding debt;
- Resulting in an event of default if we fail to comply with the financial and other restrictive covenants contained in our debt agreements, which event of default could result in all of our debt becoming immediately due and payable and, in the case of an event of default under our secured debt, such as our senior secured credit facility, could permit the lenders to foreclose on our assets securing that debt;
- Reducing the availability of our cash flow to fund working capital, capital expenditures, acquisitions and other general corporate purposes, and limiting our ability to obtain additional financing for these purposes;
- Subjecting us to the risk of increased sensitivity to interest rate increases on any indebtedness with variable interest rates;
- Limiting our flexibility in planning for, or reacting to, and increasing our vulnerability to, changes in our business, the industry in which we operate and the general economy and
- Placing us at a competitive disadvantage compared to our competitors that have less debt or are less leveraged.

Any of the above-listed factors could have an adverse effect on our business, financial condition and results of operations and our ability to meet our payment obligations under our outstanding liabilities.

**The current accounting method for our convertible debt securities is subject to change beginning January 1, 2009.**

Under current accounting rules and regulations, for the purpose of calculating diluted earnings per share, a convertible debt security providing for net share settlement and meeting specified requirements under U.S. generally accepted accounting principles (GAAP) may be accounted for similar to non-convertible debt, with the stated coupon constituting interest expense and any shares issuable to settle the conversion spread being accounted for under the treasury stock method. The effect of the treasury stock method is that the shares potentially issuable upon conversion of the notes are not included in the calculation of our earnings per share until the notes are in the money, and we are assumed to issue the number

of shares of our common stock to settle the conversion spread.

In May 2008, the FASB issued FSP Accounting Principles Board (APB) No. 14-1 Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement) (FSP APB 14-1). FSP APB 14-1 requires the issuer of certain convertible debt instruments that may be settled in cash (or other assets) on conversion to separately account for the liability (debt) and equity (conversion option) components of the instrument in a manner that reflects the issuer s non-convertible debt borrowing rate. FSP APB 14-1 is effective for fiscal years beginning after December 15, 2008 on a retroactive basis and will be adopted by the Company in the

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first quarter of fiscal 2009. The Company is currently evaluating the potential impact of the adoption of FSP APB 14-1 on its consolidated results of operations and financial condition.

Because of these and other factors affecting the Company s operating results, past financial performance should not be considered an indicator of future performance, and investors should not use historical trends to anticipate results or trends in future periods.

**If the emerging and current technologies and platforms of Microsoft and others upon which the Company builds its products do not gain or retain broad market acceptance, or if we fail to develop and introduce in a timely manner new products and services compatible with such emerging technologies, we may not be able to compete effectively and our ability to generate revenues will suffer.**

The Company s software products are built and depend upon several underlying and evolving relational database management system platforms such as Microsoft SQL Server, Progress and IBM. To date, the standards and technologies that the Company has chosen to develop its products upon have proven to be popular and have gained broad industry acceptance. However, the market for the Company s software products is subject to ongoing rapid technological developments, quickly evolving industry standards and rapid changes in customer requirements, and there may be existing or future technologies and platforms that achieve industry standard status, which are not compatible with our products. Additionally, because the Company s products rely significantly upon popular existing user interfaces to third party business applications, the Company must forecast which user interfaces will be or will remain popular in the future. For example, the Company believes the Internet has and continues to transform the way businesses operate and the software requirements of customers, who are increasingly shifting towards web-based applications and away from server-based applications. Specifically, the Company believes that customers desire business software applications that enable a customer to engage in commerce or service over the Internet. The Company is proceeding on its previously announced determination to continue with development of several of its primary product lines upon the Microsoft .NET technology. If the Company cannot continue to develop such .NET compatible products in time to effectively bring them to market, or if .NET does not become or continue to be a widely accepted industry standard, or if customers adopt competitors products when they shift to web-based applications, the ability of the Company s products to interface with popular third party applications will be negatively impacted and the Company s competitive position, operating results and revenues could be adversely affected.

**New software technologies could cause us to alter our business model resulting in adverse effects on our operating results.**

Development of new technologies may also cause the Company to change how it licenses or prices its products, which may adversely impact the Company s revenues and operating results. Emerging licensing models include Software as a Service (SaaS), hosting as well as subscription-based licensing, in which the licensee essentially rents software for a defined period of time, as opposed to the current perpetual license model. While the Company does currently offer a hosted model as well as a SaaS model to its NSB retail customers, it has to date chosen not to offer a subscription based model. The Company s future business, operating results and financial condition will depend on its ability to effectively train its sales force to sell an integrated comprehensive set of business software products and recognize and implement emerging industry standards and models, including new pricing and licensing models.

If the Company fails to respond to emerging industry standards, including licensing models and end-user requirements, the Company s competitive position and revenues could be adversely affected.

**A significant portion of our future revenue is dependent upon our existing installed base of customers continuing to license additional products, as well as purchasing consulting services and renewing their annual maintenance and support contracts. If our existing customers fail to renew their maintenance and support agreements or fail to purchase new product enhancements or additional services from the Company at historical levels, the Company s revenues and results of operations could be materially impacted.**

Historically, approximately 50% to 60% of the Company s license revenues, 90% of the Company s maintenance revenues and a substantial portion of the Company s consulting revenues are generated from the Company s installed base of customers. Maintenance and support agreements with these customers are traditionally renewed on an annual basis at the customer s discretion, and there is normally no requirement that a customer so renew or that a customer pay new license or service fees to the Company following the initial purchase. As a result, if the Company s existing customers fail to renew their maintenance and support agreements or fail to purchase new

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product enhancements or additional services at historical levels, our revenues and results of operations could be materially impacted.

**Our increasingly complex software products may contain errors or defects, which could result in the rejection of our products and damage to our reputation as well as cause lost revenue, delays in collecting accounts receivable, diverted development resources and increased service costs and warranty claims.**

The Company s software products are made up of increasingly complex computer programs. Software products are complex and products offered by the Company often contain undetected errors or failures (commonly referred to as bugs) when first introduced to the market or as new updates or upgrades of such products are released to the market. Despite testing by the Company, and by current and potential customers, prior to general release to the market, the Company s products may still contain material errors after their initial commercial shipment. Such material errors may result in loss of or delay in market acceptance of the Company s products, damage to the Company s reputation and increased service and warranty costs. Ultimately, such errors could lead to a decline in the Company s revenues. The Company has from time to time been notified by some of its customers of errors in its various software products. Although it has not occurred to date, the possibility of the Company being unable to correct such errors in a timely manner could have a material adverse effect on the Company s results of operations and its cash flows. In addition, if material technical problems with the current release of the various database and technology platforms, on which the Company s products operate, including Progress, IBM, Microsoft SQL or Microsoft .NET, occur, such difficulties could also negatively impact sales of these products, which could in turn have a material adverse effect on the Company s results of operations.

**The market for new development tools, application products and consulting and education services continues to emerge, which could negatively affect our client/server and web-based products, and, if the Company fails to respond effectively to evolving requirements of these markets, the Company s business, financial condition, results of operations and cash flows could be materially and adversely affected.**

The Company s development tools, application products and consulting and education services generally help organizations build, customize or deploy solutions that operate in both client/server-computing and web-based environments. The Company believes that the environment for application software is continuing to change from client/server to a Web-based environment to facilitate commerce on the Internet. There can be no assurance that the market for client/server computing will continue to grow, or will not decrease, or that the Company will be able to continue to respond effectively to the evolving requirements of Web-based markets.

**The market for our software products and services is highly competitive. If we are unable to compete effectively with existing or new competitors our business could be negatively impacted.**

The business information systems industry in general and the manufacturing, distribution, retail, CRM and financial computer software industry specifically, in which the Company competes are very competitive and subject to rapid technological change, evolving standards, frequent product enhancements and introductions and changing customer requirements. Many of the Company s current and potential competitors have (i) longer operating histories, (ii) significantly greater financial, technical and marketing resources, (iii) greater name recognition, (iv) larger technical staffs and (v) a larger installed customer base than the Company. A number of companies offer products that are similar to the Company s products and target the same markets. In addition, any of these competitors may be able to respond more quickly to new or emerging technologies and changes in customer requirements (such as commerce on the Internet and Web-based application software), and to devote greater resources to the development, promotion and sale of their products than the Company. Furthermore, because there are relatively low barriers to entry in the software industry, the Company expects additional competition from other established and emerging companies. Such competitors may develop products and services that compete with those offered by the Company or may acquire companies, businesses and product lines that compete with the Company. It also is possible that competitors may create alliances and rapidly acquire significant market share, including in new and emerging markets. Accordingly, there can be no assurance that the Company s current or potential competitors will not develop or acquire products or services comparable or superior to those that the Company develops, combine or merge to form significant competitors or adapt more quickly than the Company to new technologies, evolving industry trends and changing customer requirements. Competition could cause price reductions, reduced margins or loss of market share for the Company s products and services, any of which could materially and adversely affect the Company s business, operating results and financial condition. There can be no assurance that the Company will be able to compete successfully against current and future competitors or that the competitive pressures that the Company may face will not materially adversely affect its business, operating results, cash flows and financial condition.

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**If we were to lose the services of the members of our senior management team, we may not be able to execute our business strategy.**

Our future success depends in a large part upon the continued service of key members of our senior management team. In particular, our executive officers and other senior members of our management team such as our chief marketing officer and senior vice presidents are critical to the overall management of Epicor as well as the development of our technology, our operations and our strategic direction. All of our executive officers and key employees are at-will employees, and we do not maintain any key-person life insurance policies. The loss of any members of our executive management team and the possible inability to attract qualified replacements in a timely manner could adversely affect our ability to compete effectively and seriously harm our business.

**We may not be able to maintain and expand our product offerings or business if we are not able to retain, hire and integrate sufficiently qualified personnel.**

The Company s success depends in large part on the continued service of key management personnel that are not subject to employment agreements, including, but not limited to, several of the key personnel employed as a result of the Company s recent acquisitions. In addition, the Company needs to expand its workforce to continue its growth, and the competition to attract, retain and motivate qualified technical, sales and software development personnel is intense. Additionally, the sudden unexpected loss of such technical personnel, such as developers can have a negative impact on the Company s ability to develop and introduce new products in a timely and effective manner. There is no assurance that the Company will retain its key personnel, including those who came to the Company as part of acquisitions, or attract sufficient numbers of qualified key personnel in the future. The failure to retain or attract such persons could have a material adverse effect on the Company s business, operating results, cash flows and financial condition.

**Our software products incorporate and rely upon third party software products for certain key functionality and our revenues, as well as our ability to develop and introduce new products, could be adversely affected by our inability to control or replace these third party products and operations.**

The Company s products incorporate and rely upon software products developed by several other third party entities such as Microsoft, IBM and Progress. Specifically, the Company s software products are built and depend upon several underlying and evolving relational database management system platforms including Microsoft SQL Server, Progress OpenEdge and IBM U2, and also are integrated with several other third party provider products for the purpose of providing or enhancing necessary functionality. In the event that these third party products were to become unavailable to the Company or to our customers, either directly from the third party manufacturers or through other resellers of such products, the Company could not readily replace these products with substitute products. As a result, the Company cannot provide assurance that these third parties will:

Remain in business;

Continue to support the Company s product lines;

Maintain viable product lines;

Make their product lines available to the Company on commercially acceptable terms and

Not make their products available to the Company s competitors on more favorable terms.

In the long term (i.e., a year or more), an interruption of supply from these vendors could potentially be overcome through migration to another third party supplier or development within the Company. However, any interruption in the short term could have a significant detrimental effect on the Company s ability to continue to market and sell those of its products relying on these specific third party products and could have a material adverse effect on the Company s business, results of operation, cash flows and financial condition.

**We may pursue strategic acquisitions, investments and relationships and may not be able to successfully manage our operations if we fail to successfully integrate such acquired businesses and technologies, which could adversely affect our operating results.**

As part of its business strategy, the Company may continue to expand its product offerings to include application software products and services that are complementary to its existing software applications, particularly in the areas of electronic commerce or commerce over the Internet, or may gain access to established customer bases into which

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the Company can sell its current products. The Company s acquisitions of Scala Business Solutions in 2004, CRS in 2005 and NSB in 2008 are typical of this ongoing strategy. However, while this strategy has historically and may in the future involve acquisitions, investments in other businesses that offer complementary products, joint development agreements or technology licensing agreements, the specific risks we commonly encounter in these types of transactions include the following:

- Difficulty in effectively integrating any acquired technologies or software products into our current products and technologies;
- Difficulty in predicting and responding to issues related to product transition such as development, distribution and customer support;
- The possible adverse impact of such acquisitions on existing relationships with third party partners and suppliers of technologies and services;
- The possibility that customers of the acquired company might not accept new ownership and may transition to different technologies or attempt to renegotiate contract terms or relationships, including maintenance or support agreements;
- The possibility that the due diligence process in any such acquisition may not completely identify material issues associated with product quality, product architecture, product development, intellectual property issues, key personnel issues or legal and financial contingencies;
- Difficulty in integrating acquired operations, including incorporating internal control structures, due to geographical distance, and language and cultural differences and
- Difficulty in retaining employees of the acquired company.

A failure to successfully integrate acquired businesses or technology for any of these reasons could have a material adverse effect on the Company s results of operations.

**Our future results could be harmed by economic, political, geographic, regulatory and other specific risks associated with our international operations.**

The Company believes that any future growth of the Company will be dependent, in part, upon the Company s ability to maintain and increase revenues in its existing and emerging international markets, including Asia and Latin America. During the three months ended June 30, 2008 and 2007, 33.7% and 38.2%, respectively, of total Company revenues were generated by the Company s international operations. During the six months ended June 30, 2008 and 2007, 34.5% and 39.8%, respectively, of total Company revenues were generated by the Company s international operations. There can be no assurance that the Company will maintain or expand its international sales. If the revenues that the Company generates from foreign activities are inadequate to offset the expense of maintaining foreign offices and activities, the Company s business, financial condition and results of operations could be materially and adversely affected. The international reach of the Company s businesses could also subject the Company and its results of operations to unexpected, uncontrollable and rapidly changing economic and political conditions. Specifically, our international sales and operations are subject to inherent risks, including:

- Differing intellectual property and labor laws;

Lack of experience in a particular geographic market;

Different and changing regulatory requirements in various countries and regions;

Tariffs and other barriers, including import and export requirements and taxes on subsidiary operations;

Fluctuating exchange rates and currency controls;

Difficulties in staffing and managing foreign sales and support operations;

Longer accounts receivable payment cycles;

Potentially adverse tax consequences, including repatriation of earnings;

Development and support of localized and translated products;

Lack of acceptance of localized products or the Company in foreign countries;

Shortage of skilled personnel required for local operations and

Perceived health risks, natural disasters or terrorist risks which impact a geographic region and business operations therein.

Any one of these factors or a combination of them could materially and adversely affect the Company s future international sales and, consequently, the Company s business, operating results, cash flows and financial condition. A portion of the Company s revenues from sales to foreign entities, including foreign governments, has been in the form of foreign currencies. While the Company does enter into hedges and other similar foreign currency contracts

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from time to time, there can be no assurance that such activities will effectively minimize the impact that fluctuations in the value of foreign currencies may have on the Company. Fluctuations in the value of foreign currencies could adversely impact the profitability of the Company s foreign operations.

**We rely, in part, on third parties to sell our products. Disruptions to these channels would adversely affect our ability to generate revenues from the sale of our products.**

The Company distributes products through a direct sales force as well as through an indirect distribution channel, which includes VARs and other distributors and authorized consultants, consisting primarily of professional firms. During the three months ended June 30, 2008 and 2007, 11% and 16%, respectively, of the Company s software license revenues were generated by VARs and distributors. During the six months ended June 30, 2008 and 2007, 12% and 13%, respectively, of the Company s software license revenues were generated by VARs and distributors. If the Company s VARs or authorized consultants cease distributing or recommending the Company s products or emphasize competing products, the Company s results of operations could be materially and adversely affected. The success of the Company s distributors depends in part upon their ability to attract and maintain qualified sales and consulting personnel. Additionally, the Company s distributors may generally terminate their agreements with the Company upon 30 days notice, while the Scala partners may generally terminate their agreements upon 30 days to several months notice. Almost all partners though may effectively terminate their agreements at any time by ceasing to promote or sell our products. If our VARs or other distributors are unable to maintain such qualified personnel or if several of the Company s VARs or other distributors were to cease doing business or terminate their agreements and the Company is unable to replace them in a timely fashion, such factors could negatively impact the Company s results of operations. Finally, there can be no assurance that having both a direct sales force and a distribution channel for the Company s products will not lead to conflicts between those two sales forces which could adversely impact the Company s ability to close sales transactions or could have a negative impact upon average selling prices, any of which may negatively impact the Company s operating revenues and results of operations.

**If third parties infringe upon our intellectual property, we may expend significant resources enforcing our rights or suffer competitive injury, which could adversely affect our operating results. In addition, we may be subject to claims that we infringe upon the intellectual property of others.**

The Company considers its proprietary software and the related intellectual property rights in such products to be among its most valuable assets. The Company relies on a combination of copyright, trademark and trade secret laws (domestically and internationally), employee and third-party nondisclosure agreements and other industry standard methods for protecting ownership of its proprietary software. However, the Company cannot assure you that in spite of these precautions, an unauthorized third party will not copy or reverse-engineer certain portions of the Company s products or obtain and use information that the Company regards as proprietary. From time to time, the Company has in the past taken legal action against third parties whom the Company believed were infringing upon the Company s intellectual property rights. However, there is no assurance that the mechanisms that the Company uses to protect its intellectual property will be adequate or that the Company s competitors will not independently develop products that are substantially equivalent or superior to the Company s products.

Moreover, the Company from time to time receives claims from third parties that the Company s software products infringe upon the intellectual property rights of others. The Company expects that as the number of software products in the United States and worldwide increases and the functionality of these products further overlaps, the number of these types of claims will increase. This risk is potentially heightened in such diverse international markets as Eastern Europe, Asia and the Middle East. Although it has not yet occurred to date, any such claim, with or without merit, could result in costly litigation and require the Company to enter into royalty or licensing arrangements. The terms of such royalty or license arrangements, if required, may not be favorable to the Company. In addition, in certain cases, the Company provides the source code for some of its application software under licenses to its customers and distributors to enable them to customize the software to meet their particular requirements or translate or localize the products for resale in foreign countries, as the case may be. Although the source code licenses contain confidentiality and nondisclosure provisions, the Company cannot be certain that such customers or distributors will take adequate precautions to protect the Company s source code or other confidential information. Moreover, regardless of contractual arrangements, the laws of some countries in which the Company does business or distributes its products do not offer the same level of protection to intellectual property, as do the laws of the United States.

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**Foreign currency fluctuations may negatively impact the financial results of the Company.**

The results of operations or financial condition of the Company may be negatively impacted by foreign currency fluctuations. The Company operates throughout the world through international sales subsidiaries, networks of exclusive third party distributors, and non-exclusive dealers. As a result, certain sales and related expenses are denominated in currencies other than the U.S. dollar. The Company s results of operations may fluctuate due to exchange rate fluctuation between the U.S. dollar and other currencies because our financial results are reported on a consolidated basis in U.S. dollars and through the use of foreign currency denominated loans available under the Company s credit facility. In an effort to minimize operation fluctuations due to currency movements, we may attempt to limit foreign exchange exposure through operational strategies (e.g. natural hedges, netting, leading and lagging of accounts payables and account receivables) to offset the effects of exchange rate changes. In addition, the Company may enter into forward currency contracts and purchased options contracts to mitigate unfavorable impacts to our non-operating income. The Company estimates the volume of sales transactions in various currencies. Our estimates of transaction volumes in these various currencies could be overstated or understated. If these estimates are overstated or understated during periods of currency volatility, the Company may experience material currency gains or losses.

**Our quarterly operating results are difficult to predict and subject to substantial fluctuation.**

The Company s quarterly operating results have fluctuated significantly in the past. For example, from the first quarter of 2006 through the second quarter of 2008, quarterly operating results have ranged from a loss of $9.0 million to income of $13.9 million. The Company s operating results may continue to fluctuate in the future as a result of many specific factors that include:

- The demand for the Company s products, including reduced demand related to changes in marketing focus for certain products, software market conditions or general economic conditions as they pertain to information technology (IT) spending;
- Fluctuations in the length of the Company s sales cycles which may vary depending on the complexity of our products as well as the complexity of the customer s specific software and service needs;
- The size and timing of orders for the Company s software products and services, which, because many orders are completed in the final days of each quarter, may be delayed to future quarters;
- The number, timing and significance of new software product announcements, both by the Company and its competitors;
- Customers unexpected postponement or termination of expected system upgrades or replacement due to a variety of factors including economic conditions, changes in IT strategies or management changes;
- Changes in accounting standards, including software revenue recognition standards;
- Currency fluctuations and
- Fluctuations in number of customers renewing maintenance.

In addition, the Company has historically realized a significant portion of its software license revenues in the final month of any quarter, with a concentration of such revenues recorded in the final ten business days of that month. Further, the Company generally realizes a significant portion of its annual software license revenues in the final quarter of the fiscal year.

Due to the above factors, among others, the Company s revenues are difficult to forecast. The Company, however, bases its expense levels, including operating expenses and hiring plans, in significant part, on its expectations of future revenue. As a result, the Company expects its

expense levels to be relatively fixed in the short term. The Company s failure to meet revenue expectations could adversely affect operating results. Further, an unanticipated decline in revenue for a particular quarter may disproportionately affect the Company s operating results in that quarter because the majority of the Company s expenses will be fixed in the short term. As a result, the Company believes that period-to-period comparisons of the Company s results of operations are not, and will not, necessarily be meaningful, and you should not rely upon them as an indication of future performance. Due to the foregoing factors, it is likely that, as in past quarters, in some future quarters the Company s operating results will be below the expectations of public market analysts and investors. As in those past quarters, such an event would likely have an adverse effect upon the price of the Company s outstanding securities.

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**Our operating cash flows are subject to fluctuation, primarily related to our ability to timely collect accounts receivable and to achieve anticipated revenues and expenses. Negative fluctuations in operating cash flows may require us to seek additional cash sources to fund our working capital requirements. If additional cash sources are not available to the Company, our operations could be adversely affected.**

From the first quarter of 2006 through the first quarter of 2008, the Company s quarterly operating cash flows have ranged from $0.1 million provided by operating activities to $34.8 million provided by operating activities. The Company s cash and cash equivalents have increased from $70.2 million at December 31, 2006 to $132.4 million at June 30, 2008. However, the Company has at times experienced decreasing revenues and, prior to the first quarter of 2003, continued operating losses. If, in the future, the Company is not successful in achieving its anticipated revenues and expenses or maintaining a positive cash flow, the Company may not have sufficient resources for planned growth and may be required to take actions to reduce its operating expenses, such as reductions in work force and/or seek additional sources of funding. Historically, the Company has also experienced fluctuations in the proportion of accounts receivable over 90 days old and days sales outstanding. These fluctuations have been due to various issues, including product and service quality, deteriorating financial condition of customers during the recent recession and lack of effectiveness of the Company s collection processes. During the past year, our days sales outstanding have decreased from 68 as of March 31, 2007 to 66 as of June 30, 2008, due in part to the recent acquisition of NSB. If the Company cannot successfully collect a significant portion of its net accounts receivable, the Company may be required to seek alternative financing sources. As of June 30, 2008, the Company had a $230.0 million obligation to holders of the Company s convertible bonds and $157.9 million in debt.

**The market for our stock is volatile and fluctuations in operating results, changes in the Company s guidance on revenues and earnings estimates and other factors could negatively impact our stock s price.**

During the three year period ended June 30, 2008, the price of the Company s common stock ranged from a low of $6.91 to a high of $15.75. For six months ended June 30, 2008, the stock price ranged from a low of $6.91 to a high of $12.62. As of August 1, 2008, the Company had 59,573,711 shares of Common Stock outstanding. The market prices for securities of technology companies, including the Company s, have historically been quite volatile. Quarter to quarter variations in operating results, changes in the Company s guidance on revenues and earnings estimates, announcements of technological innovations or new products by the Company or its competitors, announcements of major contract awards, announcements of industry acquisitions by us or our competitors, changes in accounting standards or regulatory requirements as promulgated by the FASB, SEC, NASDAQ or other regulatory entities, changes in management and other events or factors may have a significant impact on the market price of the Company s Common Stock. In addition, the securities of many technology companies have experienced extreme price and volume fluctuations, which have often been related more to changes in recommendations or financial estimates by securities analysts than to the companies actual operating performance. Any of these conditions may adversely affect the market price of the Company s Common Stock.

**If we are not able to successfully integrate NSB Retail Systems and its operations with those of CRS Retail Technology Group and the Company, our ability to achieve anticipated revenues and related profits, as well as sales for NSB products may be adversely impacted.**

The success of our acquisition of NSB will depend in large part upon our ability to continue to successfully integrate the NSB business with CRS and into the Company. As with most acquisitions, integration issues are complex, time-consuming and expensive and, without proper planning and implementation, could significantly disrupt the business of NSB and thus, the Company. The challenges involved in continuing to integrate NSB with the Company include:

Coordinating sales and marketing efforts to effectively communicate the combined company s capabilities;

Introducing and effectively selling and cross selling the NSB products into international (non-US) markets where they have not traditionally been offered;

Combining product offerings and technology;

Coordinating and combining domestic operations, relationships and facilities;

Coordinating and rationalizing research and development activities to enhance introduction of new products and technologies with reduced cost;

Coordinating NSB s research and development efforts here in the United States and Canada with the Company s R&D facilities in the U.S. as well as in Moscow, Russia and Monterrey, Mexico;

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Continuing to demonstrate to the existing NSB customers that the acquisitions will not result in adverse changes in client service standards or business focus and helping customers conduct business easily with the Company;

Preserving distribution, marketing or other important relationships of the Company and NSB and resolving potential conflicts that may arise;

Successfully integrating the business cultures of the Company and NSB, maintaining employee morale and retaining key employees and

Consolidating and rationalizing corporate information technology and administrative infrastructures.

The integration of the NSB business into the Company s business may not realize all of the anticipated benefits of the acquisition to the extent, or in the time frame, anticipated. The failure to fully integrate the NSB business operations successfully with those of CRS and the Company or to realize all of the anticipated benefits of the acquisitions could seriously hinder our plans for product development and business and market expansion.

**A variety of specific business interruptions could adversely affect our business.**

A number of particular types of business interruptions could greatly interfere with our ability to conduct business. For example, a substantial portion of our facilities, including our corporate headquarters and other critical business operations, are located near major earthquake faults. We do not carry earthquake insurance and do not fund for earthquake-related losses. In addition, our computer systems are susceptible to damage from fire, floods, earthquakes, power loss, telecommunications failures, and similar events. The Company continues to consider and implement its options and develop contingency plans to avoid and/or minimize potential disruptions to its telecommunication services.

**If open source software expands into enterprise software applications, our software license revenues may decline.**

Open source software includes a broad range of software applications and operating environments produced by companies, development organizations and individual software developers and typically licensed for use, distribution and modification at a nominal cost or often, free of charge. A notable example of open source software is the Linux operating system, which continues to gain in popularity. To the extent that the open source software models expand and non-commercial companies and software developers create and contribute competitive enterprise software applications to the open source community, we may have to adjust our pricing, maintenance and distribution strategies and models, which could adversely affect our revenue and operating margins.

**Future acquisitions of technologies or companies, which are paid for partially, or entirely through the issuance of stock or stock rights could prove dilutive to existing shareholders.**

Consistent with past experience, the Company expects that the consideration it might pay for any future acquisitions of companies or technologies could include stock, rights to purchase stock, cash or some combination of the foregoing. For example, the Company s acquisition of Scala Business Solutions in 2004 involved the issuance of approximately 4.25 million shares of the Company s Common Stock. If the Company issues stock or rights to purchase stock in connection with future acquisitions, earnings (loss) per share and then-existing holders of the Company s Common Stock may experience dilution.

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**Item 3 Quantitative and Qualitative Disclosures About Market Risk:**

*Interest Rate Risk.* The Company s exposure to market risk for changes in interest rates relates primarily to the Company s cash and cash equivalents and outstanding debt. At June 30, 2008, the Company had $132.4 million in cash and cash equivalents. Based on the investment interest rate and the balance as of June 30, 2008, a hypothetical 1% decrease in interest rates would decrease interest income by approximately $1.3 million on an annual basis, as well as increase the Company s net loss and decrease cash flows from operations. The Company places its investments with high credit quality issuers and, by policy, limits the amount of credit exposure to any one issuer. Deposits with its U.S. issuers may exceed the amounts of federal deposit insurance provided on such deposits, and deposits held outside the U.S. are not afforded such protection. The Company is averse to principal loss and ensures the safety and preservation of its invested funds by limiting default, market and reinvestment risk. The Company mitigates default risk by investing in only the safest and highest credit quality securities and by constantly positioning its portfolio to respond appropriately to a significant reduction in a credit rating of any investment issuer or guarantor. The Company has not experienced any losses on deposits of cash or cash equivalents.

The Company cannot predict market fluctuations in interest rates and their impact on its variable rate debt, nor can there be any assurance that fixed rate long-term debt will be available to the Company at favorable rates, if at all. Consequently, future results may differ materially from the estimated adverse changes discussed above. Changes in interest rates do not affect the amount of interest we pay on our fixed rate senior convertible notes, but do affect the fair value of the debt.

On April 18, 2008, the Company entered into interest rate swap arrangements that convert our portion of its floating rate interest rate exposure under the 2007 credit facility to a fixed rate basis. The interest rate swaps qualify for hedge accounting treatment pursuant to SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended. The changes in the fair value of the interest rate swaps will be reflected in the carrying value of the interest rate swap on the balance sheet. The differential to be paid or received on the interest rate swap agreements is accrued and recognized as an adjustment to interest expense as interest rates change.

*Foreign Currency Risk.* The Company did not have any foreign currency forward or option contracts open as of June 30, 2008. At June 30, 2008, the Company had foreign currency denominated LIBOR borrowings under its 2007 credit facility consisting of $10 million Australian dollars, $2 million Canadian dollars and 2 million Euro. International revenues represented 33.7% of the Company s total revenues for the three months ended June 30, 2008, and 28.1% of revenues were denominated in foreign currencies. International revenues represented 34.5% of the Company s total revenues for the six months ended June 30, 2008, and 28.5% of revenues were denominated in foreign currencies. The Company had an unrealized and realized transactional foreign currency gain for the three months ended June 30, 2008 of $121,000. The Company had an unrealized and realized transactional foreign currency loss for the six months ended June 30, 2008 of $569,000. For the three and six months ended June 30, 2008, the transactional gain/loss was primarily due to inter-company revenues and cost of sales and the settlement of the Company s option contracts. The Company sold the NSB acquisition call options during the first quarter 2008 back to the issuing institutions for $192,000, resulting in net foreign currency loss of $1,610,000. The year-to-date foreign currency transactional losses also include inter-company balances and non-functional currency cash balances. Given a hypothetical increase or decrease of 10% in the foreign exchange rate between the USD and other major currencies, the unrealized or realized transaction gain or (loss) would increase or decrease by approximately USD $1,265,000 for the six months ended June 30, 2008, and likewise increase or decrease the Company s earnings and cash flows for the respective periods.

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**Item 4 Controls and Procedures:**

*Evaluation of disclosure controls and procedures*

The Company s management evaluated, with the participation of the Chief Executive Officer and the Chief Financial Officer, the effectiveness of the Company s disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, the Company s principal executive officer and principal financial officer have concluded that the Company s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) (the Exchange Act) are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and is accumulated and communicated to our management, including the principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

*Changes in internal controls over financial reporting*

There was no change in the Company s internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, the Company s internal control over financial reporting.

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## PART II

## OTHER INFORMATION

**Item 1 Legal Proceedings:**

The Company is subject to legal proceedings and claims in the normal course of business. The Company is currently defending these proceedings and claims, and it is the opinion of management that it will be able to resolve these matters in a manner that will not have a material adverse effect on the Company s consolidated financial position, results of operations or cash flows. However, the results of legal proceedings cannot be predicted with certainty. Should the Company fail to prevail in any of these legal matters or should several of these legal matters be resolved against the Company in the same reporting period, the operating results of a particular reporting period could be materially adversely affected.

**Item 1a Risk Factors:**

A description of the risk factors associated with our business is included under Certain Factors That May Affect Future Results in Management s Discussion and Analysis of Financial Condition and Results of Operations, contained in Item 2 of Part I of this report.

**Item 2 Unregistered Sales of Equity Securities and Use of Proceeds:**

*Purchases of Equity Securities by the Issuer and Affiliated Purchasers*

| Dates | Total Number of Shares Purchased (a) | Average Price Paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Average Price Paid Per Share | Maximum Number (or Approximate Dollar Value) of Shares (or Units) that may Yet Be Purchased Under the Plans or Programs |
|---|---|---|---|---|---|
| April 1, 2008 to April 30, 2008 | 3,048 | $ 7.91 | | $ | N/A |
| May 1, 2008 to May 31, 2008 | 4,016 | $ 8.15 | 161,900 | $ 8.03 | N/A |
| June 1, 2008 to June 30, 2008 | | $ | | $ | N/A |
| **Total** | **7,064** | **$ 8.05(1)** | **161,900** | **$ 8.03(1)** | |

**(1)** Represents the weighted average price per share purchased during the quarter.
All shares of the Company s common stock purchased listed in column (a) were purchased through a plan or program not publicly announced and are shares repurchased under the Company s restricted stock programs as consideration for the payment of the required withholding taxes.

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**Item 4 Submission of Matters to a Vote of Security Holders**

On May 27, 2008, the Company held its annual meeting of stockholders. At this meeting 49,126,009 shares of Common Stock were available for voting.

At the meeting, L. George Klaus, Michael Kelly, Thomas F. Kelly, Robert H. Smith and Michael L. Hackworth were elected as directors of the Company by the Common stockholders. With respect to the election of directors, the following nominees received the votes by common stockholders as noted below:

| Name | Votes For | Withheld Authority |
|---|---|---|
| L. George Klaus | 43,200,421 | 5,925,588 |
| Michael Kelly | 45,906,994 | 3,219,015 |
| Thomas F. Kelly | 45,555,473 | 3,570,536 |
| Michael L. Hackworth | 45,997,799 | 3,128,210 |
| Robert H. Smith | 44,180,595 | 4,945,414 |

With respect to the proposal to ratify the appointment of McGladrey & Pullen, LLP as independent auditors for the fiscal year ended December 31, 2008, 48,309,014 shares of Common Stock voted in favor of this proposal, 791,669 shares of Common Stock voted against, and 25,325 shares of Common Stock abstained from voting.

**Item 6 Exhibits**

(a) Index to Exhibits.

The list of exhibits contained in the accompanying Index to Exhibits is herein incorporated by reference.
Items 3 and 5 of Part II are not applicable and have been omitted.

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**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

EPICOR SOFTWARE CORPORATION
(Registrant)

Date: August 8, 2008

/s/ *Thomas F. Kelly*
Thomas F. Kelly
President, Chief Executive Officer, Chief Financial Officer (Principal Executive Officer and Principal Financial Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

EPICOR SOFTWARE CORPORATION
(Registrant)

Date: August 8, 2008

/s/ *Russell C. Clark*
Russell C. Clark
Senior Vice President, Finance (Principal Accounting Officer)

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***Exhibit Index***

| Exhibit No. | Description | Location |
|---|---|---|
| 1.1 | Underwriting Agreement, dated as of May 2, 2007 between the Company, UBS Securities LLC and Lehman Brothers Inc. | (46) |
| 2.1 | Agreement and Plan of Reorganization and Merger dated as of June 27, 1997 among the Company, CSI Acquisition Corp., Clientele Software, Inc., Dale E. Yocum, Pamela Yocum, William L. Mulert. (Schedules not included pursuant to Rule 601(b)(2) of Reg. S-K) | (9) |
| 2.2 | Agreement and Plan of Reorganization dated as of November 4, 1997 by and among the Company, FS Acquisition Corp., FocusSoft, Inc., John Lococo, Michael Zimmerman and Joseph Brumleve. (Schedules not included pursuant to Rule 601(b)(2) of Reg. S-K). | (11) |
| 2.3 | Agreement and Plan of Reorganization by and among the Company, Zoo Acquisition Corp. and DataWorks Corporation, dated as of October 13, 1998, as amended as of October 30, 1998. (Schedules not included pursuant to Rule 601(b)(2) of Reg. S-K). | (14) |
| 2.4 | Merger Protocol by and between the Company and Scala Business Solutions N.V. dated as of November 14, 2003 | (40) |
| 2.5 | Stock Purchase Agreement dated as of December 6, 2005 by and among Epicor Software Corporation, Cougar Acquisition Corporation, CRS Retail Technology Group, Inc., certain principal stockholders of CRS Retail Technology Group, Inc., and certain other parties | (43) |
| 3.1 | Second Restated Certificate of Incorporation of the Company. | (1) |
| 3.2 | Certificate of Amendment to Second Restated Certificate of Incorporation. | (10) |
| 3.3 | Certificate of Amendment to Second Restated Certificate of Incorporation | (39) |
| 3.4 | Amended and Restated Bylaws of the Company, as currently in effect. | (10) |
| 3.6 | Specimen Certificate of Common Stock. | (2) |
| 3.7 | Certificate of Designation of Rights, Preferences and Privileges of Series A Junior Participating Preferred Stock. | (4) |
| 3.8 | Certificate of Designation of Preferences of Series C Preferred Stock. | (6) |
| 3.9 | Certificate of Designation of Preferences of Series D Preferred Stock. | (37) |
| 4.1 | First Supplemental Indenture between the Company and U.S. Bank National Association as trustee dated May 8, 2007 | (47) |
| 10.1* | Platinum Software Corporation Incentive Stock Option, Nonqualified Stock Option and Restricted Stock Purchase Plan - 1990 (the 1990 Plan ). | (2) |
| 10.2* | Form of Incentive Option Agreement pertaining to the 1990 Plan. | (2) |
| 10.3* | Form of Nonqualified Stock Option Agreement pertaining to the 1990 Plan. | (2) |
| 10.4* | Form of Restricted Share Agreement pertaining to the 1990 Plan. | (2) |
| 10.5 | Form of Indemnification Agreement for Officers and Directors of the Company. | (2) |
| 10.6* | Platinum Software Corporation Employee Stock Purchase Plan, as amended. | (2) |
| 10.10* | 1993 Nonqualified Stock Option Plan. | (3) |
| 10.11* | Form of Nonqualified Stock Option Agreement pertaining to the 1993 Nonqualified Stock Option Plan. | (3) |
| 10.12* | 1994 Incentive Stock Option, Non-qualified Stock Option and Restricted Stock Purchase Plan. | (31) |
| 10.13* | Form of Non-qualified Stock Option Agreement pertaining to the 1994 Plan. | (31) |
| 10.28 | Stock Purchase Agreement dated September 22, 1994 between the Company and the Series B Preferred Stock Investors. | (6) |
| 10.29 | Registration Rights Agreement dated September 22, 1994 between the Company and the Series B Preferred Stock Investors. | (6) |
| 10.30 | Amendment to Stock Purchase Agreement dated May 26, 1995 between the Company and the Series C Preferred Stock Investors. | (6) |
| 10.31 | Amendment to Registration Rights Agreement dated May 26, 1995 between the Company and the Series C Preferred Stock Investors. | (6) |
| 10.33* | Employment Offer letter with L. George Klaus dated February 7, 1996. | (7) |
| 10.34* | Restricted Stock Purchase Agreement between the Company and L. George Klaus dated as of February 7, 1996. | (7) |

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|---|---|---|
| 10.44* | 1996 Nonqualified Stock Option Plan and Form of Nonqualified Option Agreement. | (12) |
| 10.45* | Platinum Software Corporation Clientele Incentive Stock Plan. | (12) |
| 10.47* | 1997 Nonqualified Stock Option Plan. | (13) |
| 10.48* | Amended and Restated 1998 Nonqualified Stock Option Plan. | (15) |
| 10.49 | Software Distribution License Agreement with FRx Software Corporation, as amended to date. | (15) |
| 10.52* | DataWorks 1995 Equity Incentive Plan, as amended ( Equity Plan ). | (18) |
| 10.54* | DataWorks 1995 Non-Employee Directors Stock Option Plan, as amended | (18) |
| 10.55 | Sublease Agreement dated November 22, 1991 between DataWorks and Titan Corporation ( Sublease ). | (17) |
| 10.56 | First Amendment to Sublease dated December 1, 1994. | (17) |
| 10.57 | Lease Agreement dated January 16, 1997 between DataWorks and Whiop Real Estate Limited Partnership. | (19) |
| 10.58* | 1995 Stock Option Plan, as amended of Interactive (the Interactive Option Plan ). | (20) |
| 10.59 | Form of Incentive Stock Option Plan under the Interactive Option Plan. | (21) |
| 10.61 | Lease between James S. Hekiman and William Finard, as Trustees of the Burlington Woods Office Trust No. 11 under a declaration of trust dated September 10, 1980 and Interactive dated September 23, 1991. | (21) |
| 10.62* | 1997 Nonstatutory Stock Plan of Interactive. | (22) |
| 10.63 | Single Tenant lease between ADI Research Partners, LP and DataWorks, dated as of August 14, 1998. | (23) |
| 10.64 | 1999 Merger Transition Stock Option Plan. | (24) |
| 10.65 | Trademark License Agreement between the Company and Platinum Technology, Inc. dated as of January 14, 1999. | (24) |
| 10.66 | Value Added Reseller Agreement with Ardent Software. | (24) |
| 10.67* | 1999 Nonstatutory Stock Option Plan. | (25) |
| 10.68 | Bracknell Lease Agreement dated May 19, 1999. | (26) |
| 10.70* | Nonstatutory Stock Option Agreement with Richard L. Roll dated November 16, 1999. | (27) |
| 10.71* | Nonstatutory Stock Option Agreement with Richard L. Roll dated November 16, 1999. | (27) |
| 10.72 | Loan and Security Agreement by and among Epicor Software Corporation as borrower and Foothill Capital corporation as lender dated as of July 26, 2000. | (28) |
| 10.73 | Amendment to Loan and Security Agreement dated November 20, 2000. | (29) |
| 10.74 | Amendment to Loan and Security Agreement dated May 21, 2001. | (30) |
| 10.75* | Amendment to Note Secured by Stock Pledge Agreement dated February 7, 2001 by and between the Company and L. George Klaus. | (38) |
| 10.76* | Amendment to Unsecured Note dated February 7, 2001 by and between the Company and L. George Klaus. | (38) |
| 10.77* | Management Retention Agreement dated as of December 17, 2001 by and between the Company and L. George Klaus. | (38) |
| 10.78 | Amendment to Loan and Security Agreement dated June 25, 2002. | (34) |
| 10.79* | Epicor Software Corporation 2002 Employee Stock Purchase Plan. | (35) |
| 10.80 | Series D Preferred Stock Purchase Agreement dated as of February 11, 2003 by and among the Company and certain Purchasers. | (37) |
| 10.81* | Employment Offer Letter with Michael A. Piraino dated April 30, 2003 | (39) |
| 10.82 | Lease Agreement dated October 14, 2003 between Epicor Software Corporation and Koll Center Irvine Number Two, L.L.C. | (40) |
| 10.83* | Compromise Agreement with Andreas Kemi effective August 13, 2005 | (39) |
| 10.84* | Final Statement of Account under Employment Agreement with Andreas Kemi dated September 6, 2004 | (40) |
| 10.85* | Consulting Agreement dated October 18, 2004 between Epicor Software Corporation and CHB Management GmbH, a Swiss Corporation | (40) |
| 10.86 | Credit agreement by and among Epicor Software Corporation and KeyBank National Association dated March 29, 2005 | (41) |
| 10.87* | 2005 Stock Incentive Plan | (42) |
| 10.88* | Deferred Compensation Plan | (51) |

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|---|---|---|
| 10.89 | Credit agreement by and among Epicor Software Corporation and KeyBank National Association dated March 30, 2006 | (44) |
| 10.91* | Chairman and CEO retention agreement, dated May 26, 2006 | (45) |
| 10.92 | Form of Notice of Restricted Stock Award and Restricted Stock Purchase Agreement | (45) |
| 10.93* | Amended Management Retention Agreement | (48) |
| 10.94 | First Amendment to Credit Agreement, dated as of May 1, 2007, among the Company, the lenders party thereto, and KeyBank National Association, as Administrative Agent, Sole Book Manager and Letter of Credit Issuing Lender | (46) |
| 10.95 | 2007 Stock Incentive Plan | (49) |
| 10.96 | Form of Time-based restricted stock agreement | (50) |
| 10.97 | Form of Performance-based restricted stock agreement | (50) |
| 10.98 | Implementation Agreement between NSB Retail Systems Plc and Epicor Software Corporation, dated December 17, 2007 | (52) |
| 10.99 | Recommended Proposals for the Cash Acquisition of NSB Retail Systems Plc by Epicor Software Corporation, dated December 17, 2007 | (52) |
| 10.100 | Credit Agreement dated December 16, 2007 by and among Epicor Software Corporation, the Guarantors identified therein, the Lenders identified therein and Bank of America, N.A., as Administrative Agent | (53) |
| 10.101 | Security and Pledge Agreement dated December 16, 2007 by and between Epicor Software Corporation, the Obligors identified therein and Bank of America, N.A., as Administrative Agent | (53) |
| 10.102 | First Amendment dated February 11, 2008, to Credit Agreement dated December 16, 2007, by and among Epicor Software Corporation, the Guarantors identified therein, the Lenders identified therein and Bank of America, N.A., as Administrative Agent | (53) |
| 10.103 | Notice of Increase of Aggregate Revolving Commitment, dated February 11, 2008, pursuant to Credit Agreement dated December 16, 2007 | (53) |
| 10.104* | Management Retention Agreement between Epicor and Thomas Kelly, dated February 19, 2008 | (54) |
| 10.105* | Letter Agreement between Epicor and Mark Duffell, dated February 19, 2008 | (54) |
| 10.106 | Second Amendment dated April 11, 2008, to Credit Agreement dated December 16, 2007, by and among Epicor Software Corporation, the Guarantors identified therein, the Lenders identified therein and Bank of America, N.A., as Administrative Agent. | (55) |
| 10.107 | 2007 Equity Incentive Plan | |
| 10.108 | Form option agreement for 2007 Plan | |
| 31.1 | Certification by Chief Executive Officer and Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. | |
| 32.1 | Certification by the Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. | |

* Management contract or compensatory plan or arrangement.

(1) Incorporated by reference to the referenced exhibit number to the Company s Registration Statement on Form S-1, Reg. No. 33-57294.

(2) Incorporated by reference to the referenced exhibit number to the Company s Registration Statement on Form S-1, Reg. No. 33-51566.

(3) Incorporated by reference to the referenced exhibit to the Company s Annual Report on Form 10-K for the year ended June 30, 1993.

(4) Incorporated by reference to the Company s Registration Statement on Form 8-A, dated April 14, 1994.

(5) Incorporated by reference to the referenced exhibit to the Company s Amended Registration Statement on Form 8-A, filed November 21, 2001, Reg. No. 000-20740.

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(6) Incorporated by reference to the referenced exhibit to the Company s Annual Report on Form 10-K for the year ended June 30, 1995.
(7) Incorporated by reference to the referenced exhibit to the Company s Quarterly Report on Form 10-Q for the quarter ended March 31, 1996.
(8) Incorporated by reference to the referenced exhibit to the Company s Current Report on Form 8-K dated June 30, 1997.
(9) Incorporated by reference to the referenced exhibit to the Company s Quarterly Report on Form 10-Q for the quarter ended December 31, 1996.
(10) Incorporated by reference to Exhibit 2.2 to the Company s Current Report on Form 8-K dated November 14, 1997.
(11) Incorporated by reference to the referenced exhibit to the Company s Annual Report on Form 10-K for the year ended June 30, 1997.
(12) Incorporated by reference to the referenced exhibit to the Company s Quarterly Report on Form 10-Q for the quarter ended September 30, 1997.
(13) Incorporated by reference to Exhibit 1 to the Company s Schedule 13D filed with the SEC on October 23, 1998, as amended.
(14) Incorporated by reference to the referenced exhibit to the Company s Annual Report on Form 10-K for the year ended June 30, 1998, as amended.
(15) Incorporated by reference to Company s Registration Statement on Form S-4, Reg. No. 333-67577.
(16) Incorporated by reference to the DataWorks Registration Statement on Form S B-2 (No. 33-97022LA) or amendments thereto.
(17) Incorporated by reference to the referenced exhibit to the DataWorks Annual Report on Form 10-K for its fiscal year ended December 31, 1997.
(18) Incorporated by reference to the DataWorks Annual Report on Form 10-K for its fiscal year ended December 31, 1996.
(19) Incorporated by reference to the Interactive Group, Inc. Annual Report on Form 10-K for its fiscal year ended December 31, 1996.
(20) Incorporated by reference to the Interactive Group, Inc. Registration Statement on Form S-1 (Reg. No. 33-90816).
(21) Incorporated by reference to the Interactive Group, Inc. Registration Statement on Form S-8 (Reg. No. 333-30259).
(22) Incorporated by reference to the referenced exhibit to the Company s Transition Report on Form 10-K for the six months ended December 31, 1998.
(23) Incorporated by reference to the Company s Quarterly Report on Form 10-Q for the quarter ended March 31, 1999.
(24) Incorporated by reference to the Company s Registration Statement on Form S-8, Registration No. 333-85105.
(25) Incorporated by reference to the Company s Quarterly Report on Form 10-Q for the quarter ended June 30, 1999.

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(26) Incorporated by reference to the referenced exhibit to the Company s Annual Report on Form 10-K for the year ended December 31, 1999.
(27) Incorporated by reference to the referenced exhibit to the Company s Quarterly Report on Form 10-Q for the quarter ended September 30, 2000.
(28) Incorporated by reference to the referenced exhibit to the Company s Annual Report on Form 10-K for the year ended December 31, 2000.
(29) Incorporated by reference to the referenced exhibit to the Company s Quarterly Report on Form 10-Q for the quarter ended June 30, 2001.
(30) Incorporated by reference from the Company s Annual Report on Form 10-K for the year ended June 30, 1994.
(31) Incorporated by reference to the referenced exhibit to the Company s Amendment No. 1 to Annual Report on Form 10-K for the year ended December 31, 1999, filed March 31, 2000.
(32) Incorporated by reference to the referenced exhibit to the Company s Annual Report on Form 10-K for the year ended December 31, 2001.
(33) Incorporated by reference to the referenced exhibit to the Company s Quarterly Report on Form 10-Q for the quarter ended June 30, 2002.
(34) Incorporated by reference to the Company s Registration Statement on Form S-8, Reg. No. 333-97063.
(35) Incorporated by reference to the Company s Current Report on Form 8-K filed December 23, 2002.
(36) Incorporated by reference to the Company s Current Report on Form 8-K filed February 18, 2003.
(37) Incorporated by reference to the Company s Annual Report on Form 10-K for the year ended December 31, 2001.
(38) Incorporated by reference to the Company s Quarterly Report on Form 10-Q for the quarter ended June 30, 2003.
(39) Incorporated by reference to the Company s Quarterly Report on Form 10-Q for the quarter ended September 30, 2004.
(40) Incorporated by reference to the Company s Annual Report on Form 10-K for the year ended December 31, 2003.
(41) Incorporated by reference to the Company s Quarterly Report on Form 10-Q for the quarter ended March 31, 2005.
(42) Incorporated by reference to the Company s Quarterly Report on Form 10-Q for the quarter ended June 30, 2005.
(43) Incorporated by reference to the Company s Current Report on Form 8-K filed December 12, 2005.
(44) Incorporated by reference to the Company s Quarterly Report on Form 10-Q for the quarter ended March 31, 2006.
(45) Incorporated by reference to the Company s Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.
(46) Incorporated by reference to the Company s Current Report on Form 8-K/A filed May 8, 2007.
(47) Incorporated by reference to the Company s Current Report on Form 8-K filed May 14, 2007.

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(48) Incorporated by reference to the Company s Quarterly Report on Form 10-Q filed May 10, 2007.
(49) Incorporated by reference to the Company s Current Report on Form 8-K filed May 29, 2007.
(50) Incorporated by reference to the Company s Registration Statement on Form S-8 filed June 18, 2007.
(51) Incorporated by reference to the Company s Registration Statement on Form S-8 filed August 3, 2005.
(52) Incorporated by reference to the Company s Current Report on Form 8-K filed on February 13, 2008.
(53) Incorporated by reference to the Company s Current Report on Form 10-K filed on March 11, 2008.
(54) Incorporated by reference to the Company s Current Report on Form 8-K filed on February 22, 2008.
(55) Incorporated by reference to the Company s Quarterly Report on Form 10-Q filed May 9, 2008.