

# SECURITIES & EXCHANGE COMMISSION EDGAR FILING

## Support.com, Inc.

**Form: 10-Q**

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Quarterly Period Ended September 30, 2002

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. 000-30901

**SUPPORTSOFT, INC.**

(Exact Name of Registrant as Specified in Its Charter)  
(Zip Code)

Delaware

94-3282005

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(State or Other Jurisdiction of Incorporation or Organization)

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(I.R.S. Employer Identification No.)

575 Broadway  
Redwood City, CA 94063

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(Address of Principal Executive Offices)

**Registrant's Telephone Number, Including Area Code: (650) 556-9440**

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

On November 14, 2002, 33,697,384 shares of the Registrant's Common Stock, \$0.0001 par value, were outstanding.

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SUPPORTSOFT, INC.  
FORM 10-Q

QUARTERLY PERIOD ENDED SEPTEMBER 30, 2002

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## PART I. FINANCIAL INFORMATION

## ITEM 1: FINANCIAL STATEMENTS

## SUPPORTSOFT, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS  
(in thousands)

	September 30, 2002	December 31, 2001
	(unaudited)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 16,077	\$ 17,757
Short term investments	12,406	8,515
Accounts receivable, net	14,282	12,509
Other current assets	2,816	3,708
	<hr/>	<hr/>
Total current assets	45,581	42,489
Property and equipment, net	1,529	1,932
Purchased intangibles, net	—	1,794
Other assets	158	148
	<hr/>	<hr/>
	\$ 47,268	\$ 46,363
	<hr/>	<hr/>
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 1,064	\$ 1,331
Accrued compensation	1,371	1,867
Other accrued liabilities	1,684	1,793
Purchased technology obligation, current portion	1,546	1,449
Capital lease obligations, current portion	563	569
Deferred revenue	16,781	12,535
	<hr/>	<hr/>
Total current liabilities	23,009	19,544
Capital lease obligations, net of current portion	128	663
Other long term liabilities	—	927
Deferred revenue – long-term portion	2,023	932
Stockholders' equity:		
Common stock	3	3
Additional paid-in capital	108,049	108,031
Notes receivable from stockholders	—	(1,523)
Deferred stock compensation	—	(997)
Accumulated other comprehensive income (loss)	(41)	95
Accumulated deficit	(85,903)	(81,312)
	<hr/>	<hr/>
Stockholders' equity	22,108	24,297
	<hr/>	<hr/>
	\$ 47,268	\$ 46,363
	<hr/>	<hr/>

See accompanying notes.

## SUPPORTSOFT, INC.

**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(in thousands, except per share amounts; unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001
Revenue:				
License fees	\$ 8,562	\$ 5,069	\$ 22,148	\$ 15,997
Services	2,551	1,998	7,196	5,955
<b>Total revenue</b>	<b>11,113</b>	<b>7,067</b>	<b>29,344</b>	<b>21,952</b>
Costs and expenses:				
Cost of license fees	67	131	197	500
Cost of services	1,448	1,486	4,384	4,735
Amortization of purchased technology	385	598	1,581	2,214
Research and development	2,228	2,995	6,698	9,817
Sales and marketing	5,741	7,101	16,833	21,723
General and administrative	1,490	1,346	4,177	4,715
Amortization of deferred stock compensation	—	870	578	3,554
<b>Total costs and expenses</b>	<b>11,359</b>	<b>14,527</b>	<b>34,448</b>	<b>47,258</b>
Loss from operations	(246)	(7,460)	(5,104)	(25,306)
Interest and other income, net	283	255	513	1,367
<b>Net income (loss)</b>	<b>\$ 37</b>	<b>\$ (7,205)</b>	<b>\$ (4,591)</b>	<b>\$ (23,939)</b>
<b>Basic net income (loss) per share</b>	<b>\$ 0.00</b>	<b>\$ (0.23)</b>	<b>\$ (0.14)</b>	<b>\$ (0.77)</b>
Shares used in computing per share amounts	32,643	31,316	32,290	30,891
<b>Diluted net income (loss) per share</b>	<b>\$ 0.00</b>	<b>\$ (0.23)</b>	<b>\$ (0.14)</b>	<b>\$ (0.77)</b>
Shares used in computing per share amounts	34,074	31,316	32,290	30,891

See accompanying notes.

## SUPPORTSOFT, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(in thousands; unaudited)

	Nine Months Ended September 30,	
	2002	2001
Operating Activities		
Net loss	\$ (4,591)	\$ (23,939)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,583	1,790
Amortization of deferred stock compensation	578	3,554
Amortization of purchased technology	1,581	2,214
Provision for bad debts	(164)	379
Other	(102)	81
Changes in assets and liabilities:		
Accounts receivable	(1,609)	(586)
Prepays and other current assets	892	249
Accounts payable	(267)	749
Accrued compensation	(496)	(915)
Other accrued liabilities	(109)	(2,253)
Deferred revenue	5,337	(2,843)
Net cash provided by (used in) operating activities	2,633	(21,520)
Investing Activities		
Purchases of property and equipment	(1,180)	(1,601)
Other assets	(10)	(41)
Payments of purchased technology obligation	(618)	(304)
Purchases of short-term investments	(13,969)	(31,205)
Sales and maturities of short-term investments	10,045	58,914
Net cash provided by (used in) investing activities	(5,732)	25,763
Financing Activities		
Proceeds from issuance of common stock, net of repurchases	437	1,517
Repayment of notes receivable from stockholders	1,523	528
Principal payments under capital lease obligations	(541)	(460)
Net cash provided by financing activities	1,419	1,585
Net increase (decrease) in cash and cash equivalents	(1,680)	5,828
Cash and cash equivalents at beginning of period	17,757	11,756
Cash and cash equivalents at end of period	\$ 16,077	\$ 17,584

See accompanying notes.

**SUPPORTSOFT, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)**

**(1) Significant Accounting Policies:**

**Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements include the accounts of SupportSoft, Inc. (the “Company” or “SupportSoft”) (formerly known as Support.com, Inc.) and its wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation. The balance sheet at September 30, 2002 and the statements of operations for the three and nine months ended September 30, 2002 and 2001 and cash flows for the nine months ended September 30, 2002 and 2001 are unaudited. In the opinion of management, these financial statements reflect all adjustments (consisting of normal recurring adjustments) that are necessary for a fair presentation of the results for and as of the periods shown. The results of operations for such periods are not necessarily indicative of the results expected for the full fiscal year or for any future period. The condensed consolidated financial statement information as of December 31, 2001 is derived from audited financial statements as of that date. These financial statements should be read with the consolidated financial statements and related notes included in the Company’s Annual Report on Form 10-K, filed with the Securities and Exchange Commission on March 29, 2002. Certain prior period balances have been reclassified to conform to current period presentation.

**Financial Instruments**

Estimated fair values of financial instruments are based on quoted market prices. The following is a summary of available-for-sale securities (in thousands) at September 30, 2002:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Cash	\$ 3,301	\$ —	\$ —	\$ 3,301
Money market funds	10,777	—	—	10,777
Commercial paper	1,999	—	—	1,999
Federal agencies	8,346	14	—	8,360
Corporate bonds	1,043	3	—	1,046
Auction backed securities	3,000	—	—	3,000
	<u>\$ 28,466</u>	<u>\$ 17</u>	<u>\$ —</u>	<u>\$ 28,483</u>
Classified as:				
Cash and cash equivalents	\$ 16,077	—	—	\$ 16,077
Short-Term Investments	12,389	17	—	12,406
	<u>\$ 28,466</u>	<u>\$ 17</u>	<u>\$ —</u>	<u>\$ 28,483</u>

**Revenue Recognition**

SupportSoft has applied Statement of Position (“SOP”) 97-2, Software Revenue Recognition, as amended by SOP 98-4 and SOP 98-9, since its inception. License revenue is generally recognized when a customer agreement has been signed, the software product has been delivered, there are no uncertainties surrounding product acceptance, the fees are fixed or determinable, and collection is considered probable. License revenue is comprised of fees for term and perpetual licenses of SupportSoft’s software by corporate customers and resellers. Term licenses are sold with maintenance for which SupportSoft does not have vendor specific objective evidence (VSOE) to determine fair value. As a result, license revenue for term licenses is recognized ratably over the service period of the agreement and

includes maintenance for term licenses. We do not allocate maintenance revenue from term licenses to services revenue, as we do not believe there is an allocation methodology that provides a meaningful and supportable allocation between license and maintenance revenues. SupportSoft considers all arrangements with payment terms extending beyond twelve months and other arrangements with payment terms longer than normal not to be fixed or determinable. If the fee is determined not to be fixed or determinable, revenue is recognized as payments become due from the customer. License revenue from arrangements with resellers is recognized ratably over the term of the arrangement commencing when payments are made or become due limited by guaranteed minimum amounts due under the arrangement or sell through activity.

Services revenue is primarily comprised of revenue from professional services, such as consulting services, training, maintenance and support. Arrangements that include software services are evaluated to determine whether those services are essential to the functionality of other elements of the arrangement. For perpetual license arrangements, when software services are not considered essential, the revenue related to the software services is recognized as the services are performed. When non-essential software services are bundled in a term licensing arrangement, revenue from the software services is recognized ratably over the period associated with the initial payment. When software services are considered essential, revenue under the arrangement is recognized using contract accounting, typically using the percentage of completion method.

Perpetual license revenues are recognized using the residual method described in SOP 98-9 for arrangements in which licenses are sold with multiple elements. For perpetual licensing arrangements, maintenance revenue is deferred and recognized over the service period of the arrangement, which is typically one year. Our perpetual arrangements may contain certain elements, such as the requirement that the Company deliver unspecified additional products, which require revenue to be taken ratably (monthly) over the delivery period.

#### **Concentration of Credit Risk and Significant Customers**

SupportSoft performs ongoing evaluations of its customers' financial condition and generally does not require collateral. SupportSoft maintains reserves for credit losses, and such losses have been within management's expectations. If the financial condition of SupportSoft's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional reserves may be required. The Company had reserves for credit losses at September 30, 2002 and December 31, 2001 of \$664,000 and \$828,000, respectively. One customer accounted for 34% of our total revenue for the three months ended September 30, 2002 and 14% of our total revenue for the nine months ended September 30, 2002. No other customer individually accounted for 10% or more of our total revenue for either period.

#### **Net Income (Loss) Per Common Share**

Basic and diluted net income (loss) per share are presented in accordance with Statement of Financial Accounting Standards No. 128, "Earnings per Share" ("FAS 128"), for all periods presented.

SupportSoft computes basic income or loss per share using the weighted-average number of common shares outstanding during the period, less shares subject to repurchase. SupportSoft computes diluted income or loss per share using the weighted-average number of common and dilutive common equivalent shares outstanding during the period. In loss periods, basic and dilutive loss per share is identical since the impact of common equivalent shares is anti-dilutive.

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The following table sets forth the computation of basic and diluted net income (loss) per share (in thousands, except per share data):

	Three months ended September 30,		Nine months ended September 30,	
	2002	2001	2002	2001
Net income (loss)	\$ 37	\$ (7,205)	\$ (4,591)	\$ (23,939)
<b>Basic:</b>				
Weighted-average shares of common stock outstanding	33,575	33,417	33,477	33,344
Less: Weighted-average shares subject to repurchase	(932)	(2,101)	(1,187)	(2,453)
Shares used in computing basic net income (loss) per share	32,643	31,316	32,290	30,891
Basic net income (loss) per share	\$ 0.00	\$ (0.23)	\$ (0.14)	\$ (0.77)
<b>Diluted:</b>				
Weighted-average shares of common stock outstanding	33,575	33,417	33,477	33,344
Add: Common equivalent shares outstanding	499	—	—	—
Less: Weighted-average shares subject to repurchase	—	(2,101)	(1,187)	(2,453)
Shares used in computing diluted net income (loss) per share	34,074	31,316	32,290	30,891
Diluted net income (loss) per share	\$ 0.00	\$ (0.23)	\$ (0.14)	\$ (0.77)

### (2) Purchased Intangibles

On September 20, 2000, SupportSoft purchased source code and other related intellectual property rights from ePeople, Inc. (formerly known as NoWonder, Inc.) for \$6.8 million. The purchase price was recorded as purchased intangibles and included as an other asset in the Company's consolidated balance sheet. The Company paid \$5.3 million through September 30, 2002, and will pay an additional \$1.5 million through the quarter ended September 30, 2003. In addition to these payments, the Company's obligation was reduced by approximately \$200,000 in the quarter ended September 30, 2002 due to the final determination of the variable amount payable under the agreement. The purchased technology was being amortized on a straight-line basis over the past two years and as of September 30, 2002 the purchased technology has been fully amortized. Total amortization related to the purchased intangibles for the nine months ended September 30, 2002 was \$1.6 million.

### (3) Recently Issued Accounting Standards

In July 2001, the FASB issued SFAS 142, "Goodwill and Other Intangible Assets." SFAS 142 supersedes APB 17, "Intangible Assets," and requires the discontinuance of goodwill amortization. In addition, SFAS 142 includes provisions regarding the reclassification of certain existing recognized intangibles as goodwill, reassessment of useful lives of existing recognized intangibles, reclassification of certain intangibles out of previously reported goodwill and the testing for impairment of existing goodwill and other intangibles. SFAS 142 is required to be applied for fiscal years beginning after December 15, 2001, with certain early adoption permitted. The adoption of SFAS 142 during the quarter ended March 31, 2002 did not have an impact on our financial position or results of operations. Additionally, there was no material impact on any prior period results upon adoption of SFAS 142.

In October 2001, the FASB issued SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This statement addresses financial accounting and reporting for the impairment of long-lived assets. The adoption of SFAS 144 during the quarter ended March 31, 2002 did not have an impact on our financial position or results of operations.

In July 2002, the FASB approved SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 addresses the financial accounting and reporting for obligations associated with an exit activity, including restructuring, or with a

disposal of long-lived assets. Exit activities include, but are not limited to, eliminating or reducing product lines, terminating employees and contracts and relocating plant facilities or personnel. SFAS No. 146 specifies that a company will record a liability for a cost associated with an exit or disposal activity only when that liability is incurred and can be measured at fair value. Therefore, commitment to an exit plan

or a plan of disposal expresses only management's intended future actions and, therefore, does not meet the requirement for recognizing a liability and the related expense. SFAS No. 146 is effective prospectively for exit or disposal activities initiated after December 31, 2002, with earlier adoption encouraged. The Company does not anticipate that the adoption of SFAS No. 146 will have a material effect on its financial position or results of operations.

#### (4) Comprehensive Income (Loss)

Statement of Financial Accounting No. 130, "Reporting Comprehensive Income" ("SFAS 130") establishes standards for reporting and displaying comprehensive net income and its components in stockholders' equity. However, it has no impact on our net income as presented in our financial statements. SFAS 130 requires foreign currency translation adjustments and changes in the fair value of available-for-sale securities to be included in comprehensive income.

The following are the components of comprehensive income (loss): (in thousands)

	Three months ended September 30,		Nine months ended September 30,	
	2002	2001	2002	2001
Net income (loss)	\$ 37	\$ (7,205)	\$ (4,591)	\$ (23,939)
Net unrealized gain (loss) on available-for-sale securities	(16)	65	(45)	55
Translation adjustment gain (loss)	84	125	(91)	6
<b>Comprehensive income (loss)</b>	<b>\$ 105</b>	<b>\$ (7,015)</b>	<b>\$ (4,727)</b>	<b>\$ (23,878)</b>

The components of accumulated other comprehensive loss relate entirely to unrealized gains (losses) on available-for-sale securities and translation adjustment gains (losses) and are \$(41,000) at September 30, 2002 and \$138,000 at September 30, 2001.

#### (5) Legal Proceedings

On or about November 30, 2001, Dana [sic] Risley, on behalf of herself [sic] and other similarly situated, filed a lawsuit, styled as a class action, against us in the United States District Court for the Southern District of New York. The complaint alleges, inter alia, that our Registration Statement and Prospectus dated July 18, 2000 for the issuance and initial public offering of 4,250,000 shares of the Company's common stock contained material misrepresentations and/or omissions, related to alleged inflated commissions received by the underwriters of the offering. The lawsuit seeks unspecified damages as well as interest, fees and costs. The defendants named in the lawsuit are the Company, Radha Basu, Brian Beattie, Credit Suisse First Boston Corporation, Bear, Stearns & Co. Inc., and FleetBoston Robertson Stephens Inc. While it is too early to predict with certainty the outcome of the litigation, we believe that the claims against the Company and its management are without merit.

## ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Management's Discussion and Analysis of Financial Condition and Results of Operations should be read together with the unaudited condensed consolidated financial statements and related notes appearing in Item 1 of this report on Form 10-Q and the section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and related notes included in SupportSoft's Annual Report on Form 10-K for the year ended December 31, 2001.

This report on Form 10-Q contains forward-looking statements. These statements relate to our, and in some cases our customers', or alliance partners', future plans, objectives, expectations, intentions and financial performance, as well as statements as to the anticipated percentage of total revenue that term licensing arrangements may constitute in

future periods, expected net income or losses, expected cash flows, the adequacy of capital resources, growth in operations, the ability to compete and respond to technological change and the acceptance and performance of our products and services. In some cases, you can identify forward-looking statements because they use terms such as anticipates, believes, continue, could, estimates, expects, intends, may, plans, potential, predicts, should or will or the negative of those terms or other comparable words. These statements involve risks and uncertainties that may cause our actual results, activities or achievements to be materially different from those expressed or implied by these statements. These risks and uncertainties include those listed under Factors that May Affect Future Results and Management's Discussion and Analysis of Financial Condition and Results of Operations.

SupportSoft expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained in this report to conform these statements to actual results or changes in our expectations or in events, conditions or circumstances on which any such statement is based. You should not place undue reliance on these forward-looking statements, which apply only as of the date hereof.

## **Overview**

SupportSoft is a leading provider of service and support automation software. Our Web-based family of product solutions is designed to help corporations automate and personalize the service or support they provide their customers, subscribers, employees and partners. Our software is used both within office environments and the home. SupportSoft principally sells its software products to corporate enterprises, service providers, information technology outsourcers plus personal computer and device manufacturers.

SupportSoft's customers utilize its software platform to increase the efficiency and effectiveness of their service or support operations. For example, our corporate customers can use our software to better manage enterprise knowledge through automation, discover and meter information technology assets, or provide support to employees, including support for mobile devices, through mass healing or enabling employee self-service. Similarly, our customers that focus on service automation for their consumers can use our software to provide automated installation of a broadband connection, customer self-service or intelligent assisted service.

As a result of eliminating manual steps in either the service or support processes, we believe that our software reduces operational costs, contributes to improved user satisfaction and may accelerate business growth. These benefits are enabled through faster, more precise and automated resolution of difficulties associated with the use of operating systems, networks, software applications, business processes, broadband connectivity and other technologies. Our core products offer automated, personalized support designed to resolve problems through proactive mass healing, self-healing, user self-service and intelligent assisted support -- all delivered via the Internet.

As the diversity of computing systems and devices increases, the number and types of software applications proliferate, and the reliance on technology of all kinds intensifies at work and at home, we believe that service and support automation software will play an increasingly essential role in helping companies function and compete effectively. Customers which have purchased our products and services include corporate enterprises such as General Electric, Cisco Systems, Bank of America, and Procter & Gamble; broadband service providers such as Comcast Online Communications, SBC Communications, Cox Communications, and Charter Communications; personal computer manufacturers such as IBM and Sony; and support outsourcers such as Computer Sciences Corporation, IBM, and Perot Systems.

## RESULTS OF OPERATIONS

The following table sets forth the results of operations for the three and nine months ended September 30, 2002 and 2001 expressed as a percentage of total revenue.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2002	2001	2002	2001
Revenue:				
License fees	77%	72%	75%	73%
Services	23	28	25	27
Net revenue	100	100	100	100
Costs and expenses:				
Cost of license fees	1	2	1	12
Cost of services	13	21	15	22
Amortization of purchased intangibles	3	9	5	10
Research and development	20	42	23	45
Sales and marketing	52	101	57	99
General and administrative	13	19	14	21
Amortization of deferred stock compensation	—	12	2	16
Total costs and expenses	102	206	117	215
Loss from operations	(2)	(106)	(17)	(115)
Interest income and other income, net	2	4	1	6
Net income (loss)	0%	(102)%	(16)%	(109)%

### Three and Nine Months Ended September 30, 2002 and 2001

#### Revenue

License revenue is generally recognized when a customer agreement has been signed, the software product has been delivered, there are no uncertainties surrounding product acceptance, the fees are fixed or determinable, and collection is considered probable. License revenue is comprised of fees for term and perpetual licenses of SupportSoft's software by corporate customers and resellers. Term licenses are sold with maintenance for which SupportSoft does not have vendor specific objective evidence (VSOE) to determine fair value. As a result, license revenue for term licenses is recognized ratably over the service period of the agreement and includes maintenance for term licenses. We do not allocate maintenance revenue from term licenses to services revenue, as we do not believe there is an allocation methodology that provides a meaningful and supportable allocation between license and maintenance revenues. SupportSoft considers all arrangements with payment terms extending beyond twelve months and other arrangements with payment terms longer than normal not to be fixed or determinable. If the fee is determined not to be fixed or determinable, revenue is recognized as payments become due from the customer. License revenue from arrangements with resellers is recognized ratably over the term of the arrangement commencing when payments are made or become due limited by guaranteed minimum amounts due under the arrangement or sell through activity.

Services revenue is primarily comprised of revenue from professional services, such as consulting services, training, maintenance and support. Arrangements that include software services are evaluated to determine whether those services are essential to the functionality of other elements of the arrangement. For perpetual license arrangements, when software services are not considered essential, the revenue related to the software services is recognized as the services are performed. When non-essential software services are bundled in a term licensing arrangement, revenue from the software services is recognized ratably over the period associated with the initial payment. When software services are considered essential, revenue under the arrangement is recognized using contract accounting, typically using the percentage of completion method.

Perpetual license revenues are recognized using the residual method described in SOP 98-9 for arrangements in which licenses are sold with multiple elements. For perpetual licensing arrangements, maintenance revenue is deferred and recognized over the service period of the arrangement, which is typically one year. Our perpetual arrangements may contain certain elements, such as the

requirement that the Company deliver unspecified additional products, which require revenue to be taken ratably (monthly) over the delivery period.

The following is an example of our revenue recognition for a term license. If we receive an order from a customer for a 36-month term license in December of a year, we would recognize only one month of license fees for that year even if that customer prepaid 12 months of the 36-month term. Pursuant to this typical arrangement, we would record one year of fees in accounts receivable upon signing a new term license agreement, while recognizing only one month of revenue. As a result, our accounts receivable balance could represent a significant portion of our total revenue and increase our days sales outstanding (DSO) calculation.

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Total revenue increased 57% to \$11.1 million for the three months ended September 30, 2002 from \$7.1 million for the three months ended September 30, 2001. Total revenue increased 34% to \$29.3 million for the nine months ended September 30, 2002 as compared to \$22.0 million for the same period in 2001.

International revenue represented 6% and 13% of total revenue for the three and nine months ended September 30, 2002, compared with 19% and 21% for the three and nine months ended September 30, 2001.

One customer accounted for 34% of our total revenue for the three months ended September 30, 2002 and 14% of our total revenue for the nine months ended September 30, 2002. No other customer individually accounted for 10% or more of our total revenue for either period.

### *License revenue*

License revenue increased to \$8.6 million for the three months ended September 30, 2002 from \$5.1 million for the three months ended September 30, 2001 and to \$22.1 million for the nine months ended September 30, 2002 from \$16.0 million for the nine months ended September 30, 2001. The increase in license revenue was due primarily to greater demand for, and market acceptance of, our software products, expansion of our product line and an increase in the amount of revenue from perpetual licenses, where typically more revenue is recognized in the period when the license arrangements are signed than from term license arrangements. For the three months ended September 30, 2002 and 2001, ratable revenue from licenses as a percentage of total revenue was 41% and 55%. For the nine months ended September 30, 2002 and 2001, ratable revenue from licenses as a percentage of total revenue was 41% and 57%, respectively. Although the percentage of revenue we recognize from ratable licensing arrangements will vary from period to period, we currently anticipate that this revenue will represent approximately 35% to 45% of total revenue in future periods. The percentage of revenue we recognize from ratable arrangements may vary from period to period due to factors including: the acceptance of product deliverables, the timing of payments received from our customers, renewal of agreements and the financial condition of our customers which may restrict or eliminate their ability to continue to pay for our software.

### *Services revenue*

Service revenue increased to \$2.6 million for the three months ended September 30, 2002 from \$2.0 million for the three months ended September 30, 2001 and to \$7.2 million for the nine months ended September 30, 2002 from \$6.0 million for the nine months ended September 30, 2001. This increase was due primarily to increased implementation, training and consulting services and maintenance revenue from new licensing arrangements.

## **Cost of Revenue**

### *Cost of license fees*

Cost of license revenue consists primarily of costs related to license fees paid to third parties under technology license arrangements. Cost of license fees decreased to \$67,000 for the three months ended September 30, 2002 from \$131,000 for the three months ended September 30, 2001. Cost of license fees for the nine months ended September 30, 2002 decreased to \$197,000 from \$500,000 for the same period in 2001. The lower cost was due to the decrease in the resale of third party software sold with our products.

### *Cost of services fees*

Cost of services consists primarily of salaries, travel costs, related overhead expenses and payments made to third parties for consulting services. Cost of services revenue decreased to \$1.4 million for the three months ended September 30, 2002 from \$1.5 million for the three months ended September 30, 2001. This decrease was due primarily to a decrease in travel and consulting expenses offset by a smaller increase in salary and related expenses. Cost of services revenue for the nine months ended September 30, 2002 decreased to \$4.4 million compared to \$4.7 million for the same period in 2001. This decrease was primarily due to a decrease in traveling expenses.

### ***Amortization of Purchased Technology***

Amortization of purchased intangibles was \$385,000 and \$1.6 million for the three and nine months ended September 30, 2002 compared to \$598,000 and \$2.2 million for the three and nine months ended September 30, 2001. These decreases were attributable to a reduction in payments required to be made to a third party pursuant to a technology acquisition agreement. As of September 30, 2002, the purchased intangibles balance was fully amortized and therefore we do not anticipate future amortization expense as a result of prior arrangements.

### ***Research and Development Expense***

Research and development expense consists primarily of salary and related costs and consulting expenses for research and development personnel. Research and development expense decreased to \$2.2 million for the three months ended September 30, 2002 from \$3.0 million for the three months ended September 30, 2001. Research and development expense for the nine months ended September 30, 2002 decreased to \$6.7 million from \$9.8 million for the same period in 2001. These decreases were due primarily to a reduction in third party consulting services and salary expenses due to lower headcount.

### ***Sales and Marketing Expense***

Sales and marketing expense consists primarily of salary and commission costs as well as promotional expenses, including public relations, advertising and trade shows. Sales and marketing expense decreased to \$5.7 million for the three months ended September 30, 2002 from \$7.1 million for the three months ended September 30, 2001. Sales and marketing expense for the nine months ended September 30, 2002 decreased to \$16.8 million from \$21.7 million for the same period in 2001. These decreases were due primarily to a reduction in salary expenses due to lower headcount, recruiting expenses and promotional expenses, including public relations, advertising and trade shows.

### ***General and Administrative Expense***

General and administrative expense consists primarily of salary expense and related costs of administrative personnel and professional fees for legal, accounting and other professional services. General and administrative expense increased to \$1.5 million for the three months ended September 30, 2002 from \$1.3 million for the three months ended September 30, 2001. This increase was primarily due to an increase in salary and related expenses. General and administrative expense for the nine months ended September 30, 2002 decreased to \$4.2 million as compared to \$4.7 million for the same period in 2001. This decrease was due primarily to a reduction in fees for legal services, consulting fees and annual report costs.

### ***Amortization of Deferred Stock Compensation***

We amortized deferred compensation expense of zero and \$578,000 during the three and nine months ended September 30, 2002 as compared to \$870,000 and \$3.6 million during the same periods in 2001. This compensation expense relates to options awarded to individuals in all operating expense categories. As of June 30, 2002, all existing deferred stock compensation balances have been fully amortized.

### ***Interest and Other Income, Net***

Interest and other income, net, increased to \$283,000 for the three months ended September 30, 2002 from \$255,000 for the three months ended September 30, 2001. This increase was attributable primarily to a foreign currency translation gain and interest earned on the repayment of notes receivable from stockholders. Interest and other income, net, decreased to \$513,000 for the nine months ended September 30, 2002 as compared to \$1.4 million for the same period in 2001. The decrease was attributable primarily to a decrease in interest income due to lower cash, cash equivalents and short-term investment balances and to a lesser extent the rate of return on our invested cash balances.

## **LIQUIDITY AND CAPITAL RESOURCES**

Since our incorporation in December 1997, we have financed our operations primarily through our initial public offering, cash flows from operations and, to a lesser extent, from the private placement of our preferred and common stock, bank borrowings and capital equipment lease financing.

### ***Operating Activities***

Net cash generated by operating activities was \$2.6 million for the nine months ended September 30, 2002, an increase of \$24.1 million over the \$21.5 million used in operating activities for the nine months ended September 30, 2001. Amounts included in net loss, which do not require the use of cash, including amortization of deferred stock compensation, amortization of purchased intangibles, depreciation of fixed assets and the provision for bad debt, amounted to \$3.6 million for the nine months ended September 30, 2002 compared to \$7.9 million for the nine months ended September 30, 2001. Net cash generated by operating activities for the nine month period ended September 30, 2002 was also the result of an increase of \$5.3 million in deferred revenue and a decrease in other current assets of \$892,000, offset by a net loss of \$4.6 million and an increase in accounts receivable of \$1.6 million.

### ***Investing Activities***

Net cash used in investing activities was \$5.7 million for the nine months ended September 30, 2002, a decrease of \$31.5 million over the \$25.8 million provided by the investing activities for the comparable period ended September 30, 2001. Net cash used in investing activities for the nine months ended September 30, 2002, resulted from the purchase of \$14.0 million in short-term investments and \$1.2 million in property and equipment offset by the sale and maturity of \$10.0 million in short-term investments.

### ***Financing Activities***

Net cash provided by financing activities was \$1.4 million for the nine months ended September 30, 2002 and \$1.6 million for the nine months ended September 30, 2001. For the period ended September 30, 2002, cash provided by financing activities was attributable primarily to net proceeds from the repayment of notes receivable from stockholders and to a lesser extent the purchase of common stock under the Employee Stock Purchase Plan offset by principal repayments under capital lease obligations.

## Commitments

As of September 30, 2002, our principal commitments consisted of obligations outstanding under a technology acquisition agreement and capital and operating leases. We anticipate requiring minimal additional space in the next 12 months. The following summarizes our contractual obligations as of September 30, 2002 and the effect these contractual obligations are expected to have on our liquidity and cash flows in future periods (in thousands).

	Payments Due By Period			
	Total	1 Year or Less	1-3 Years	After 3 Years
Operating leases	\$ 1,723	\$ 932	\$ 791	\$ —
Purchased technology	1,546	1,546	—	—
Capital lease obligations	691	563	128	—
<b>Total</b>	<b>\$ 3,960</b>	<b>\$ 3,041</b>	<b>\$ 919</b>	<b>\$ —</b>

## Working Capital and Capital Expenditure Requirements

We believe that our existing cash balances will be sufficient to meet our working capital and capital expenditure requirements for at least the next 12 months. We evaluate potential acquisitions of other businesses, products and technologies and may in the future require additional equity or debt financings to accomplish any potential acquisitions.

If we require additional capital resources to grow our business internally or to acquire complementary technologies and businesses at any time in the future, we may seek to sell additional equity or debt securities. The sale of additional equity or debt securities could result in more dilution to our stockholders. Financing arrangements may not be available to us, or may not be available in amounts or on terms acceptable to us.

## Critical Accounting Policies and Estimates

The preparation of our consolidated financial statements in conformity with accounting principles generally accepted in the United States requires us to make estimates and assumptions that affect the amounts reported in our financial statements and accompanying notes. Our significant accounting policies are described in Note 1 to the consolidated financial statements. The items in our financial statements requiring significant estimates and judgments include revenue recognition and allowance for bad debt.

### Revenue Recognition

SupportSoft has applied Statement of Position (“SOP”) 97-2, Software Revenue Recognition, as amended by SOP 98-4 and SOP 98-9, since its inception. License revenue is generally recognized when a customer agreement has been signed, the software product has been delivered, there are no uncertainties surrounding product acceptance, the fees are fixed or determinable, and collection is considered probable. License revenue is comprised of fees for term and perpetual licenses of SupportSoft’s software by corporate customers and resellers. Term licenses are sold with maintenance for which SupportSoft does not have vendor specific objective evidence (VSOE) to determine fair value. As a result, license revenue for term licenses is recognized ratably over the service period of the agreement and license revenue includes maintenance for term licenses. We do not allocate maintenance revenue from term licenses to services revenue, as we do not believe there is an allocation methodology that provides a meaningful and supportable allocation between license and maintenance revenues. SupportSoft considers all arrangements with payment terms extending beyond twelve months and other arrangements with payment terms longer than normal not to be fixed or determinable. If the fee is determined not to be fixed or determinable, revenue is recognized as payments become due from the customer. License revenue from arrangements with resellers is recognized ratably over the term of the arrangement commencing when payments are made or become due limited by guaranteed minimum amounts due under the arrangement or sell through activity.

Services revenue is primarily comprised of revenue from professional services, such as consulting services, training, maintenance and support. Arrangements that include software services are evaluated to determine whether those services are essential to the functionality of other elements of the arrangement. For perpetual license arrangements, when software services are not considered essential, the revenue related to the software services is recognized as the services are performed. When non-essential software services are bundled in a term licensing arrangement, revenue from the software services is recognized ratably over the period associated with the initial payment. When the software services are considered essential, revenue under the arrangement is recognized using contract accounting, typically using the percentage of completion method.

Perpetual license revenues are recognized using the residual method described in SOP 98-9 for arrangements in which licenses are

sold with multiple elements. For perpetual licensing arrangements, maintenance revenue is deferred and recognized over the service period of the arrangement, which is typically one year. Our perpetual arrangements may contain certain elements, such as the requirement that the Company deliver unspecified additional products, which require revenue to be taken ratably (monthly) over the delivery period.

#### *Allowance for Bad Debt*

SupportSoft maintains reserves for estimated credit losses resulting from the inability of its customers to make required payments. A considerable amount of judgment is required when we assess the realization of receivables, including assessing the probability of collection and the current credit-worthiness of each customer. If the financial condition of SupportSoft's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional reserves may be required.

In July 2001, the FASB issued SFAS 142, "Goodwill and Other Intangible Assets." SFAS 142 supersedes APB 17, "Intangible Assets," and requires the discontinuance of goodwill amortization. In addition, SFAS 142 includes provisions regarding the reclassification of certain existing recognized intangibles as goodwill, reassessment of useful lives of existing recognized intangibles, reclassification of certain intangibles out of previously reported goodwill and the testing for impairment of existing goodwill and other intangibles. SFAS 142 is required to be applied for fiscal years beginning after December 15, 2001, with certain early adoption permitted. The adoption of SFAS 142 during the quarter ended March 31, 2002 did not have an impact on our financial position or results of operations. Additionally, there was no material impact on any prior period results upon adoption of SFAS 142.

In October 2001, the FASB issued SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This statement addresses financial accounting and reporting for the impairment of long-lived assets. The adoption of SFAS 144 during the quarter ended March 31, 2002 did not have an impact on our financial position or results of operations.

In July 2002, the FASB approved SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 addresses the financial accounting and reporting for obligations associated with an exit activity, including restructuring, or with a disposal of long-lived assets. Exit activities include, but are not limited to, eliminating or reducing product lines, terminating employees and contracts and relocating plant facilities or personnel. SFAS No. 146 specifies that a company will record a liability for a cost associated with an exit or disposal activity only when that liability is incurred and can be measured at fair value. Therefore, commitment to an exit plan or a plan of disposal expresses only management's intended future actions and, therefore, does not meet the requirement for recognizing a liability and the related expense. SFAS No. 146 is effective prospectively for exit or disposal activities initiated after December 31, 2002, with earlier adoption encouraged. The Company does not anticipate that the adoption of SFAS No. 146 will have a material effect on its financial position or results of operations.

## Chief Executive Officer and Chief Financial Officer Certifications

The certification by the Company's chief executive officer and chief financial officer of this report on Form 10-Q, as required by section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. § 1350), has been submitted to the Securities and Exchange Commission as additional correspondence.

## Factors that May Affect Future Results

**We have a history of losses and only recently became profitable. If we do not continue to be profitable, we may not be able to continue to operate.**

We incurred net losses of approximately \$85.9 million for the period from December 3, 1997 through June 30, 2002, and although we earned a profit of \$37,000 during the three month period ending September 30, 2002, we expect to incur a net loss for the full year 2002. If we do not maintain the net income or loss predicted or expected by securities analysts or investors, the market price of our stock will likely decline. If we incur net losses, we may not be able to increase our number of employees in sales, marketing and research and development programs or increase our investment capital equipment or otherwise execute our business plan. If we fail to sustain or increase profitability in the future, our business will suffer and we may not be able to continue to operate.

**Our quarterly results are difficult to predict and may fluctuate. If we do not meet quarterly financial expectations, our stock price would likely decline.**

Because of our limited operating history, our quarterly revenue and operating results are difficult to predict and may fluctuate from quarter to quarter. Our operating results in some quarters may fall below our predictions or the expectations of securities analysts or investors, which would likely cause the market price of our common stock to decline.

Several factors are likely to cause fluctuations in our operating results, including:

- demand for our service and support automation software;
- the price and mix of products and services we or our competitors offer;
- our ability to gain and retain customers;
- the amount and timing of operating costs and capital expenditures relating to expansion of our business, infrastructure and marketing activities;
- size and timing of customer orders and the timing of customer license payments; and
- our ability to recognize revenue in a given quarter.

**Our quarterly results depend on the size of a small number of orders, so the delay or loss of any single large order during a quarterly period, and especially an order for a perpetual license rather than a term license, could harm that quarter's results and cause our stock price to decline.**

Our operating results could suffer if any large orders are delayed or cancelled in any future period. Each quarter, we derive a significant portion of our license revenue from a small number of relatively large orders for the licensing of our service and support automation software. We license our service and support automation software under

perpetual and term licenses. Perpetual licenses typically result in our recognition of a larger amount of revenue in the quarter in which the license is granted as compared with term licenses. Revenue from a perpetual license is generally recognized upon delivery of a product. Revenue from a term license is recognized on a monthly basis over the agreement term, which is typically three years. We expect that we will continue to depend upon a small number of large orders for a significant portion of our license revenue.

**Because a small number of customers have historically accounted for and may in future periods account for substantial portions of our revenue, our revenue could decline because of delays of customer orders or the failure of existing customers to renew licenses.**

For the three months ended September 30, 2002, one customer accounted for 34% of our total revenue. Because we have a small number of customers and a few customers are likely to continue to account for a significant portion of our revenue, our revenue could decline because of the loss or delay of a single customer order or the failure of an existing customer to renew its term license. We may not obtain additional customers. The failure to obtain additional customers, the loss or delay of customer orders and the failure of existing customers to renew licenses or pay fees due will harm our operating results.

**Our sales cycle can be lengthy and if revenue forecasted for a particular quarter is not realized in that quarter, significant expenses incurred may not be offset by corresponding sales.**

Our sales cycle for our service and support automation software can range from three months to nine months or more and may vary substantially from customer to customer. While our customers are evaluating our products and services, we may incur substantial sales and marketing expenses and spend significant management effort. Any delay in completing sales in a particular quarter could cause our operating results to be below expectations.

**We must achieve broad adoption and acceptance of our service and support automation products and services or we will not increase our market share or grow our business.**

We must achieve broad market acceptance and adoption of our products and services or our business and operating results will suffer. Specifically, we must encourage our customers to transition from using traditional support methods. To accomplish this, we must:

- continually improve the performance, features and reliability of our products and services to address changing industry standards and customer needs; and
- develop integration with other support-related technologies.

**Our product innovations may not achieve the market penetration or price stability necessary for us to maintain profitability.**

If we fail to develop, in a timely manner, new or enhanced versions of our service and support automation software or to provide new products and services that achieve rapid and broad market acceptance or price stability, we may not maintain our profitability. We may fail to identify new product and service opportunities successfully. Our existing products will become obsolete if we fail to introduce new products or product enhancements that meet new customer demands, support new standards or integrate with new or upgraded versions of packaged applications. We may have little or no control over the factors that might influence market acceptance of our products and services. These factors include:

- the willingness of enterprises to transition to service and support automation solutions and
- acceptance of competitors' service and support automation solutions or other similar technologies.

**Our software may not operate with the hardware and software platforms that are used by our customers now or in the future, and as a result our business and operating results may suffer.**

We currently serve a customer base with a wide variety of constantly changing hardware, packaged software applications and networking platforms. If there is widespread adoption of other operating system environments, and if we fail to release versions of our service and support automation software that are compatible with these other operating systems, our business and operating results will suffer. Our future success also depends on:

- our ability to integrate our product with multiple platforms and to modify our product as new versions of packaged applications are introduced;
- the number of different operating systems and databases that our product can work with; and
- our management of software being developed by third parties for our customers or for use with our products.

**We rely on third-party technologies and our inability to use or integrate third-party technologies could delay product or service development.**

We intend to continue to license technologies from third parties, including applications used in our research and development activities and technologies, which are integrated into our products and services. Our inability to obtain or integrate any of these licenses could delay product and service development until equivalent technology can be identified, licensed and integrated. These technologies may not continue to be available to us on commercially reasonable terms or at all. We may fail to successfully integrate any licensed technology into our products or services. This would harm our business and operating results. Third-party licenses also expose us to increased risks that include:

- risks of product malfunction after new technology is integrated;
- the diversion of resources from the development of our own proprietary technology; and
- our inability to generate revenue from new technology sufficient to offset associated acquisition and maintenance costs.

**We may engage in future acquisitions or investments that could dilute our existing stockholders, or cause us to incur significant expenses.**

We may acquire or invest in complementary businesses, technologies or products. If we are unable to use or integrate any newly acquired entities or technologies effectively or profitably, our operating results could suffer. Acquisitions by us could also result in large and immediate write-offs, incurrence of debt and contingent liabilities or amortization of expenses related to goodwill and other intangibles, which could harm our operating results. Additional funds to finance any acquisitions may not be available on terms that are favorable to us, and, in the case of equity financings, may dilute our stockholders.

**We may lose the services of our key personnel, which in turn would harm the market's perception of our business and our ability to achieve our business goals.**

Our success will depend on the skills, experience and performance of our senior management, engineering, sales, marketing and other key personnel. The loss of the services of any of our senior management or other key personnel, including our chief executive officer, Radha R. Basu, our chief financial officer, Brian Beattie, our chief technical officer, Scott W. Dale, and our chief software officer, Cadir B. Lee, could harm the market's perception of our business and our ability to achieve our business goals.

**Our failure to establish and expand strategic alliances would harm our ability to achieve market acceptance of our service and support automation software.**

If we fail to maintain, establish or successfully implement strategic alliances, our ability to achieve market acceptance of our automation software will suffer and our business and operating results will be harmed. Specifically, we must establish and extend existing distribution alliances with specialized technology and services firms such as support outsourcers.

**Our products depend on and work with products containing complex software and if our products fail to perform properly due to errors or similar problems in the software, we may need to spend resources to correct the errors or compensate for losses from these errors and our reputation could be harmed.**

Our products depend on complex software, both internally developed and licensed from third parties. Also, our customers may use our products with other companies' products which also contain complex software. Complex software often contains errors. These errors could result in:

- delays in product shipments;
- unexpected expenses and diversion of resources to identify the source of errors or to correct errors;
- damage to our reputation;
- lost sales;
- product liability claims; and
- product returns.

**Our system security is important to our customers and we may need to spend significant resources to protect against or correct problems caused by security breaches.**

A fundamental requirement for online communications, transactions and support is the secure transmission of confidential information. Third parties may attempt to breach our security or that of our customers. We may be liable to our customers for any breach in security and any breach could harm our business and reputation. Also, computers are vulnerable to computer viruses, physical or electronic break-ins and similar disruptions, which could lead to interruptions, delays or loss of data. We may be required to expend significant capital and other resources to further protect against security breaches or to correct problems caused by any breach.

**We may face claims of invasion of privacy or inappropriate disclosure, use or loss of our customers' information and any liability imposed could harm our reputation and cause us to lose customers.**

Our software contains features which may allow us or our customers to control, monitor or collect information from computers running the software without notice to the computing users. Therefore we may face claims about invasion of privacy or inappropriate disclosure, use or loss of this information. Any imposition of liability could harm our operating results.

**We have limited experience in international operations and if our revenue from international operations does not exceed the expense of establishing and maintaining our international operations, our business could suffer.**

We intend to expand further into international markets. We have limited experience in international operations and may not be able to compete effectively in international markets. If we do not generate enough revenue from

international operations to offset the expense of these operations, our business could suffer. Risks we face in conducting business internationally include:

- difficulties and costs of staffing and managing international operations;
- differing technology standards;
- longer sales cycles and collection periods;
- changes in currency exchange rates and controls;
- dependence on local vendors; and
- the effects of the terrorist attacks in the United States and the effects of the war on terrorism and any related conflicts or similar events worldwide.

**Any system failure that causes an interruption in our customers' ability to use our products or services or a decrease in their performance could harm our relationships with our customers and result in reduced revenue.**

Our software may depend on the uninterrupted operation of our internal and outsourced communications and computer systems. These systems are vulnerable to damage or interruption from computer viruses, human error, natural disasters and intentional acts of vandalism and similar events. Our disaster recovery plan may not be adequate and business interruption insurance may not be enough to compensate us for losses that occur. These problems could interrupt our customers' ability to use our service and support automation products or services which could harm our reputation and cause us to lose customers and revenue.

**We may not obtain sufficient patent protection, and this could harm our competitive position and increase our expenses which would harm our business.**

Our success and ability to compete depend to a significant degree upon the protection of our software and other proprietary technology. It is possible that:

- our pending patent applications may not be issued;
- competitors may independently develop similar technologies or design around any of our patents;
- patents issued to us may not be broad enough to protect our proprietary rights; and
- our issued patents could be successfully challenged.

**We rely upon trademarks, copyrights and trade secrets to protect our proprietary rights and if these rights are not sufficiently protected, it could harm our ability to compete and to generate revenue.**

We also rely on a combination of laws, such as copyright, trademark and trade secret laws, and contractual restrictions, such as confidentiality agreements and licenses, to establish and protect our proprietary rights. Our ability to compete and grow our business could suffer if these rights are not adequately protected. Our proprietary rights may not be adequately protected because:

- laws and contractual restrictions may not prevent misappropriation of our technologies or deter others from developing similar technologies; and
- policing unauthorized use of our products and trademarks is difficult, expensive and time-consuming, and we may be unable to determine the extent of this unauthorized use.

Also, the laws of other countries in which we market our products may offer little or no protection of our proprietary technologies. Reverse engineering, unauthorized copying or other misappropriation of our proprietary technologies could enable third parties to benefit from our technologies without paying us for them, which would harm our competitive position and market share.

**We may face intellectual property infringement claims that could be costly to defend and result in our loss of significant rights.**

Other parties may assert intellectual property infringement claims against us and our products may infringe the intellectual property rights of third parties. Intellectual property litigation is expensive and time-consuming and could divert management's attention from our business. If there is a successful claim of infringement, we may be required to develop non-infringing technology or enter into royalty or license agreements which may not be available on acceptable terms, if at all. Our failure to develop non-infringing technologies or license the proprietary rights on a timely basis would harm our business. Our products may infringe issued patents that may relate to our products.

Also, patent applications may have been filed by third parties which relate to our software products. The adoption of the new trademark and corporate name SupportSoft increases the risk that a prior user could view the mark or name to be confusingly similar to the prior user's mark or name. Although we have conducted limited trademark and trade name searches, and do not believe the SupportSoft trademark and corporate name will infringe any known party's trademark rights, it is possible that a third party will claim our use of SupportSoft infringes its trademark.

**We must compete successfully in the service and support automation market or we will lose market share and our business will fail.**

The market for our products is intensely competitive, rapidly changing and significantly affected by new product introductions and other market activities of industry participants. Competitive pressures could reduce our market share or require us to reduce the price of products and services and therefore our gross margin, which could harm our business and operating results. Our integrated software solution competes against various vendors' software products designed to accomplish specific elements of a complete service and support automation solution. For example, in the market for automated delivery of support solutions, we compete with Motive Communications, Inc.

We may encounter competition from companies such as:

- customer communications software companies;
- question and answer companies;
- customer relationship management solution providers;
- consolidated service desk solution vendors;
- Internet infrastructure companies; and
- operating systems providers.

Our potential competitors may have longer operating histories, significantly greater financial, technical, and other resources or greater name recognition than we do. Our competitors may be able to respond more quickly to new or emerging technologies and changes in customer requirements. If we fail to compete effectively, we may lose or be unable to expand our market share and our business and operating results would suffer.

**Because our service and support automation software is designed to support businesses operating over the Internet, our success depends on the continued growth and levels of performance of Internet usage.**

Because a majority of our products are designed to support businesses operating over the Internet, the success of our business will depend on the continued improvement of the Internet as a convenient means of consumer interaction and commerce, as well as an efficient medium for the delivery and distribution of information by enterprises to their employees and extended enterprise. Because global commerce on the Internet and the online exchange of information is evolving, we cannot predict whether the Internet will continue to be a viable commercial marketplace.

**We may experience a decrease in market demand due to the slowing economy in the United States which has been further stymied by the recent concerns of terrorism, war and social and political instability.**

Economic growth has slowed significantly, and some analysts believe the United States economy is experiencing a recession. In addition, the terrorists attacks in the United States and turmoil in the Middle East have increased the uncertainty in the United States economy and may further add to the decline in the United States business environment. The war on terrorism, along with the effects of the terrorist attack and other similar events, could have contributed to the further slowdown of the already slumping market demand for goods and services, including service and support automation software. If the economy continues to decline as a result of the recent economic, political and social turmoil, or if there are further terrorist attacks in the United States or elsewhere, we may experience decreases in the demand for our products and services, which may harm our operating results.

**Governmental regulation and legal changes could impair the growth of the Internet and decrease demand for our products or increase our cost of doing business.**

The laws and regulations that govern our business change rapidly. Any change in laws and regulations could impair the growth of the Internet and could reduce demand for our products, subject us to liability or increase our cost of doing business. The United States government and the governments of states and foreign countries have attempted to regulate activities on the Internet and the distribution of software. Also, in 1998, Congress passed the Internet Freedom Act, which imposed a three-year moratorium on state and local taxes on Internet-based transactions. In late 2001, this moratorium was extended for two years. Failure to renew this moratorium would allow states to impose taxes on e-commerce. This might harm our business directly and indirectly by harming the businesses of our customers, potential customers and the parties to our business alliances. The applicability to the Internet of existing laws governing issues is uncertain and may take years to resolve. Evolving areas of law that are relevant to our business include privacy laws, intellectual property laws, proposed encryption laws, content regulation and sales and use tax laws and regulations.

**Our directors, executive officers, and principal stockholders own a substantial portion of our common stock and this concentration of ownership may allow them to elect most of our directors and could delay or prevent a change in control of SupportSoft.**

Our directors, executive officers, and stockholders who currently own over 5% of our common stock collectively beneficially own a substantial portion of our outstanding common stock. These stockholders, if they vote together, will be able to significantly influence all matters requiring stockholder approval. For example, they may be able to elect most of our directors, delay or prevent a transaction in which stockholders might receive a premium over the market price for their shares or prevent changes in control or management.

**Our stock price may be highly volatile and may decline significantly because of stock market fluctuations and other factors that affect the prices of technology stocks. A decline in our stock price could result in securities class action litigation against us. Securities class action litigation diverts management's attention and may harm our business.**

The stock market has experienced significant price and volume fluctuations that have adversely affected the market prices of common stock of technology companies. These broad market fluctuations may reduce the market price of our common stock. Other factors that may lead to high volatility or have an adverse affect on the market price of our common stock include:

- actual or anticipated fluctuations in our operating results;
- changes in or our failure to meet securities analysts' expectations; and
- sales of shares of our common stock by our affiliates or others.

In the past, securities class action litigation has often been brought against a company after periods of volatility in the market price of securities.

On or about November 30, 2001, Dana [sic] Risley, on behalf of herself [sic] and other similarly situated, filed a securities class action lawsuit against SupportSoft. We may again in the future be a target of similar litigation. Securities litigation could result in substantial costs and divert management's attention and resources, which could harm our ability to execute our business plan.

**We may need additional capital and if funds are not available on acceptable terms, we may not be able to hire and retain employees, fund our expansion or compete effectively.**

We believe that our existing capital resources will enable us to maintain our operations for at least the next 12 months. However, if our capital requirements vary materially from those currently planned, we may require additional financing sooner than anticipated. This financing may not be available in sufficient amounts or on terms acceptable to us and may be dilutive to existing stockholders. If adequate funds are not available or are not available on acceptable terms, our ability to hire, train or retain employees, to fund our expansion, take advantage of unanticipated opportunities, develop or enhance services or products, or respond to competitive pressures would be significantly limited.

### **ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

#### **Qualitative and Quantitative Disclosures about Market Risk**

We develop products in the United States and market and sell in North America, South American, Asia and Europe. As a result, our financial results could be affected by factors such as changes in foreign currency exchange rates or weak economic conditions in foreign markets. As most sales are currently made in U.S. dollars, a strengthening of the dollar could make our products less competitive in foreign markets. Our interest income is sensitive to changes in the general level of U.S. interest rates, particularly since the majority of our investments are in short-term instruments. Because of the nature of our short-term investments, we have concluded that there is no material market risk exposure.

Our investment policy requires us to invest funds in excess of operating requirements in:

- obligations of the U.S. government and its agencies;
- investment grade state and local government obligations;
- securities of U.S. corporations rated A1 or the equivalent for short-term ratings and A2 or the equivalent for long-term ratings by Standard and Poors or the Moody's equivalent; and
- money market funds or deposits issued or guaranteed by U.S. and non-U.S. commercial banks, meeting credit rating and net worth requirements with maturities of less than two years.

At September 30, 2002, our cash and cash equivalents consisted primarily of money market funds held by large institutions in the U.S. and our short-term investments were invested in government debt securities maturing in less than eighteen months.

#### **ITEM 4: CONTROLS AND PROCEDURES**

##### **Evaluation of Disclosure Controls and Procedures**

Within 90 days prior to the date of this report, we carried out an evaluation, under the supervision and with the participation of our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures are effective in alerting them timely to material information required to be included in our periodic SEC reports.

##### **Changes in Internal Controls**

There were no significant changes in our internal controls or, to our knowledge, in other factors that could significantly affect those controls subsequent to the date of their evaluation, and there were no significant deficiencies or material weaknesses in such controls requiring corrective actions.

**PART II: OTHER INFORMATION**

Not applicable.



## Certifications

I, Radha R. Basu, certify that:

1. I have reviewed this quarterly report on Form 10-Q of SupportSoft, Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 14, 2002

/s/ Radha R. Basu

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**Radha R. Basu**  
**Chief Executive Officer and President**

I, Brian M. Beattie, certify that:

1. I have reviewed this quarterly report on Form 10-Q of SupportSoft, Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 14, 2002

/s/ Brian M. Beattie

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**Brian M. Beattie**  
**Senior Vice President of Finance**  
**and Administration and Chief**  
**Financial Officer**