ART TECHNOLOGY GROUP INC
Form 10-Q
May 10, 2006

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended March 31, 2006
OR

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

For the Transition Period from to
Commission file number 000-26679

ART TECHNOLOGY GROUP, INC.
(Exact name of registrant as specified in its charter)

Delaware	**04-3141918**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

25 First Street, Cambridge, Massachusetts
(Address of principal executive offices)
02141
(Zip Code)
(617) 386-1000
(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Sections 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 þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check One):

Large accelerated filer o Accelerated filer þ Non accelerated filer o

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

As of May 5, 2006 there were 111,422,894 shares of the Registrant s common stock outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

ART TECHNOLOGY GROUP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share data)
(UNAUDITED)

	March 31 2006	December 31 2005
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 28,854	$ 24,060
Marketable securities	7,301	9,509
Accounts receivable, net of reserves of $532 ($778 in 2005)	20,425	21,459
Prepaid expenses and other current assets	1,618	1,130
Total current assets	58,198	56,158
Property and equipment, net	3,458	2,995
Goodwill	27,347	27,347
Intangible assets, net	4,346	4,859
Other assets	1,274	1,406
	$ 94,623	$ 92,765
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities:		
Accounts payable	$ 3,210	$ 2,719
Accrued expenses	11,279	13,359
Capital lease obligations, current portion	56	56
Notes payable	182	198
Deferred revenue	21,549	21,113
Accrued restructuring, current portion	2,113	3,012
Total current liabilities	38,389	40,457
Capital lease obligations, less current portion	42	63
Accrued restructuring, less current portion	1,938	2,085
Commitments and contingencies		
Stockholders equity:		
Preferred stock, $0.01 par value: Authorized 10,000,000 shares; Issued and outstanding no shares		
Common stock, $0.01 par value: Authorized 200,000,000 shares;	1,114	1,106

Issued and outstanding 111,383,361 shares and 110,637,606 shares at March 31, 2006 and December 31, 2005, respectively		
Additional paid-in capital	252,903	251,454
Accumulated deficit	(196,825)	(199,466)
Accumulated other comprehensive loss	(2,938)	(2,934)
Total stockholders equity	54,254	50,160
	$ 94,623	$ 92,765

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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ART TECHNOLOGY GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(UNAUDITED)

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005
Revenues:		
Product licenses	$ 8,100	$ 7,383
Services	15,856	14,611
Total revenues	23,956	21,994
Cost of Revenues:		
Product licenses	498	593
Services	6,665	5,411
Total cost of revenues	7,163	6,004
Gross Profit	16,793	15,990
Operating Expenses:		
Research and development	4,827	4,589
Sales and marketing	6,923	6,799
General and administrative	2,680	2,988
Restructuring charge		204
Total operating expenses	14,430	14,580
Income from operations	2,363	1,410
Interest and other income, net	278	11
Income before provision for income taxes	2,641	1,421
Provision for income taxes		13
Net income	$ 2,641	$ 1,408
Basic net income per share	$ 0.02	$ 0.01
Diluted net income per share	$ 0.02	$ 0.01

Basic weighted average common shares outstanding	110,928	108,685
Diluted weighted average common shares outstanding	115,774	110,866

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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ART TECHNOLOGY GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(UNAUDITED)

	Three Months Ended March 31,	
	2006	**2005**
Cash Flows from Operating Activities:		
Net income	$ 2,641	$ 1,408
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,050	1,090
Non-cash stock-based compensation expense	594	
Changes in current assets and liabilities:		
Accounts receivable, net	1,034	3,696
Prepaid expenses and other current assets	(488)	(860)
Deferred rent	141	242
Accounts payable	491	(2,187)
Accrued expenses	(2,080)	(1,265)
Deferred revenues	436	(3,011)
Accrued restructuring	(1,046)	(1,857)
Net cash provided by (used in) operating activities	2,773	(2,744)
Cash Flows from Investing Activities:		
Purchases of marketable securities	(3,643)	(992)
Maturities of marketable securities	5,851	1,523
Purchases of property and equipment	(1,001)	(96)
Payment of acquisition costs		(1,010)
Decrease in other assets	(9)	204
Net cash provided by (used in) investing activities	1,198	(371)
Cash Flows from Financing Activities:		
Proceeds from exercise of stock options	713	579
Proceeds from employee stock purchase plan	150	182
Principal payments on notes payable	(16)	(324)
Payments on capital leases	(21)	(13)
Net cash provided by financing activities	826	424
Effect of Foreign Exchange Rate Changes on Cash and Cash Equivalents	(3)	64

Net Increase (Decrease) in Cash and Cash Equivalents		4,794		(2,627)
Cash and Cash Equivalents, Beginning of Period		24,060		21,310
Cash and Cash Equivalents, End of Period	$	28,854	$	18,683

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

ART TECHNOLOGY GROUP, INC.
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(1) Organization, Business and Summary of Significant Accounting Policies

Art Technology Group, Inc. (ATG or the Company) offers an integrated suite of Internet online marketing, sales and service applications, as well as related application development, integration and support services. The Company was incorporated in 1991 in the State of Delaware and has been a publicly traded corporation since 1999.

ATG delivers software solutions to help consumer-facing organizations create an interactive experience for their customers and partners via the Internet and other channels. The Company s software helps its clients market, sell and provide self-service opportunities to their customers and partners, which can enhance clients revenues, reduce their costs and improve their customers satisfaction. The Company also offers related services, including support and maintenance, education, professional services and application hosting services.

(a) Principles of Consolidation

The accompanying consolidated financial statements include the accounts of ATG and its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

(b) Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(c) Revenue Recognition

ATG earns product license revenues from licensing the rights to use its software to end-users. ATG also generates service revenues from integrating its software with its customers operating environments, the sale of support and maintenance services, the sale of certain other consulting and development services and hosting services. ATG has separate agreements with its customers that govern the terms and conditions of its software licenses, consulting, hosting and support and maintenance services. These separate agreements, along with ATG s business practices regarding pricing and of selling services separately, provide the basis for establishing vendor-specific objective evidence of fair value. This allows ATG to allocate revenue to the undelivered elements in a multiple element arrangement and apply the residual method under Statement of Position (SOP) No. 97-2 (SOP 97-2)*, Software Revenue Recognition* and SOP No. 98-9, *Modification of SOP 97-2, Software Revenue Recognition, with Respect to Certain Transactions.*

ATG recognizes revenue in accordance with SOP 97-2 and SOP 98-9. Revenues from software license agreements are recognized upon execution of a license agreement and delivery of the software, provided that the fee is fixed or determinable and deemed collectible by management. If conditions for acceptance are required subsequent to delivery, revenues are recognized upon customer acceptance if such acceptance is not deemed to be perfunctory. In multiple element arrangements, ATG uses the residual value method in accordance with SOP 97-2 and SOP 98-9. Revenue earned on software arrangements involving multiple elements that qualify for separate element accounting treatment is allocated to each undelivered element using the relative fair values of those elements based on vendor-specific objective evidence with the remaining value assigned to the delivered element, the software license. Many of the Company s software arrangements include consulting implementation services sold separately under consulting engagement contracts. Consulting revenues from these arrangements are generally accounted for separately from software licenses because the arrangements qualify as service transactions as defined in SOP 97-2. The more significant factors considered in determining whether the revenue should be accounted for separately include the nature of services (i.e., consideration of whether the services are essential to the functionality of the licensed product), degree of risk, availability of services from other vendors, timing of payments and impact of milestones or acceptance criteria on the realizability of the software license fee. Consequently, product license revenue is generally recognized when the product is shipped. Revenues from software support and maintenance or application hosting agreements are recognized ratably over the term of the support and maintenance or application hosting period, which for application hosting and support and maintenance is typically one year or two years. The Company accounts for these transactions

in accordance with Emerging Issues Task Force (EITF) 00-3, *Application of AICPA Statement of Position 97-2, Software Revenue Recognition, to Arrangements That Include the Right to Use Software Stored on Another Entity s Hardware*, and generally recognizes the product license fee upon delivery of the software license because the Company has established the fair value of vendor specific objective evidence of hosting services, the customer has the contractual right to take possession of the software at any time during the hosting period without significant penalties, and it is feasible for the customer to run the software on its own hardware or contract with another party to host the software. ATG enters into reseller arrangements that typically provide for sublicense fees payable to ATG based upon a percentage of ATG s list price. Revenues are recognized under reseller agreements based upon actual sales to the resellers. ATG does not grant its resellers the right of return or price protection.

Revenues from professional service arrangements are recognized on either a time-and-materials, proportional performance method or percentage-of-completion basis as the services are performed, provided that amounts due from customers are fixed or determinable and deemed collectible by management. From time to time the Company enters into fixed price service arrangements. In those

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circumstances in which services are essential to the functionality of the software, the Company applies the percentage-of-completion method, and in those situations when only professional services are provided, the Company applies the proportional performance method. Both of these methods require that the Company track the effort expended and the effort expected to complete a project. Amounts collected or billed prior to satisfying the above revenue recognition criteria are reflected as deferred revenue. Deferred revenue primarily consists of advance payments related to support and maintenance, service agreements and deferred product license revenues.

(d) Net Income Per Share

Basic net income per share is computed by dividing net income by the weighted average number of shares of common stock outstanding during the period. Diluted net income per share is computed by dividing net income by the weighted average number of shares of common stock outstanding plus the dilutive effect of common stock equivalents using the treasury stock method. Common stock equivalents consist of stock options.

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

	Three Months Ended March 31,	
	2006	**2005**
Net Income	$ 2,641	$ 1,408
Weighted average common shares outstanding used in computing basic net income per share	110,928	108,685
Weighted average common equivalent shares outstanding: Dilutive employee common stock options	4,846	2,181
Total weighted average common and common equivalent shares outstanding used in computing diluted net income per share	115,774	110,866
Basic net income per share	$ 0.02	$ 0.01
Diluted net income per share	$ 0.02	$ 0.01
Anti-dilutive common stock options	3,148	9,401

(e) Cash, Cash Equivalents and Marketable Securities

ATG accounts for investments in marketable securities under Statement of Financial Accounting Standards (SFAS) No. 115, *Accounting for Certain Investments in Debt and Equity Securities.* Under SFAS 115, investments consisting of cash equivalents and marketable securities, for which ATG has the positive intent and the ability to hold to maturity, are reported at amortized cost, which approximates fair market value. Cash equivalents are highly liquid investments with maturities at the date of acquisition of less than 90 days. Marketable securities are investment grade debt securities with maturities at the date of acquisition of greater than 90 days. At March 31, 2006 and December 31, 2005, all of ATG s marketable securities were classified as held-to-maturity. The average maturity of ATG s marketable securities was approximately 3.3 months and 3.2 months at March 31, 2006 and December 31, 2005, respectively. At March 31, 2006 and December 31, 2005, the difference between the carrying value and market value

of ATG s marketable securities were unrealized losses of approximately $11,000 and $18,000, respectively. At March 31, 2006 and December 31, 2005, ATG s cash, cash equivalents and marketable securities consisted of the following (in thousands):

	March 31, 2006	December 31, 2005
Cash and cash equivalents:		
Cash	$ 17,832	$ 15,473
Money market accounts	4,635	5,253
U.S. Treasury and U.S. Government Agency securities	1,489	1,323
Commercial paper	4,898	2,011
Total cash and cash equivalents	$ 28,854	$ 24,060
Marketable securities:		
U.S. Treasury and U.S. Government Agency securities	$ 394	$ 389
Certificate of Deposit	874	450
Commercial paper	1,288	2,011
Corporate debt securities	4,745	6,659
Total marketable securities	$ 7,301	$ 9,509

(f) Income Taxes

ATG expects to have no Federal and minimal foreign income taxes in 2006 due to its projection of taxable losses in domestic and certain foreign locations in 2006 and the use of net operating loss carryforwards. Accordingly, no taxes have been recorded for the three months ended March 31, 2006. Taxes recorded for the three months ended March 31, 2005 were for foreign locations. As a result of historical net operating losses incurred, and after evaluating its anticipated performance over its normal planning horizon, the Company has provided a full valuation allowance for its net operating loss carryforwards, research credit carryforwards and other net deferred tax assets.

(g) Stock Based Compensation

On December 16, 2004, the Financial Accounting Standards Board (FASB) issued SFAS 123 (revised 2004), *Share-Based Payment* (SFAS 123R). SFAS 123R supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and amends SFAS No. 95, *Statement of Cash Flows*. Generally, the approach in SFAS 123R is similar to the approach described in SFAS 123. However, SFAS 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values at the date of grant. Pro forma disclosure is no longer an alternative. On January 1, 2006 (the first day of its 2006 fiscal year), the Company adopted SFAS 123R using the modified prospective method as permitted under SFAS 123R. Under this transition method, compensation cost recognized in the first quarter of fiscal 2006 includes:
(a) compensation cost for all share-based payments granted prior to but not yet vested as of December 31, 2005, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123, and (b) compensation cost for all share-based payments granted subsequent to December 31, 2005, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R. In accordance with the modified prospective method of adoption, the Company s results of operations and financial position for prior periods have not been restated.

Equity Compensation Plans

The Company currently grants stock options under the following equity compensation plans:

1996 Stock Option Plan

In April 1996, the 1996 Stock Option Plan (the 1996 Plan) was approved by ATG s Board of Directors and stockholders. The purpose of the 1996 Plan is to reward employees, officers and directors and consultants and advisors to ATG who are expected to contribute to the growth and success of ATG. The 1996 Plan provides for the award of options to purchase shares of ATG s common stock. Stock options granted under the 1996 Plan may be either incentive stock options or nonqualified stock options. In 2004, shareholders approved resolutions to amend and restate the 1996 Plan to allow for the grant of restricted stock awards, performance share awards and other forms of equity based compensation that were not previously provided for in the plan and to extend the term of the 1996 Plan to December 31, 2013. The 1996 Plan is administered by the Board of Directors, which has the authority to designate participants, determine the number and type of awards to be granted, the time at which awards are exercisable, the method of payment

and any other terms or conditions of the awards. While the Board determines the prices at which options may be exercised under the 1996 Plan, the exercise price of an incentive stock option shall be at least 100% (110% for incentive stock options granted to a 10% stockholder) of the fair market value of ATG s common stock on the date of grant. As of March 31, 2006, there are 25,600,000 shares authorized under the 1996 Plan.

1999 Outside Director Stock Option Plan

The 1999 Outside Director Stock Option Plan (Director Plan) was adopted by ATG s Board of Directors and approved by stockholders in May 1999. Under the terms of the Director Plan, non-employee directors of ATG receive nonqualified options to purchase shares of ATG s common stock. In 2004, shareholders approved resolutions to amend and restate the Director Plan to allow for the grant of restricted stock awards, performance share awards and other forms of equity based compensation that were not previously provided for in the plan and to extend the term of the Director Plan to December 31, 2013. A total of 800,000 shares of common stock have been reserved under the Director Plan. On April 4, 2006, the Company amended its Non-Employee Director Compensation Plan. The changes to the plan provide that (i) the vesting of the annual stock option awards to the Company s non-employee directors under the plan change from quarterly vesting over one year to quarterly vesting over two years, with full acceleration of vesting upon a change of control of the Company; and (ii) the amount of the Company s annual restricted stock awards to the Company s non-employee directors under the plan increase from shares of the Company s common stock valued at $2,500 to shares of our common stock valued at $4,500.

Primus Stock Option Plans

In connection with the acquisition of Primus Knowledge Solutions, Inc., the Company assumed certain options, as defined in the merger agreement, issued under the Primus Solutions 1999 Stock Incentive Compensation Plan (the Primus 1999 Plan) and the Primus Solutions 1999 Non-Officer Employee Stock Compensation Plan (Primus 1999 NESC Plan) (together the Primus Stock Option Plans) subject to the same terms and conditions as set forth in the Primus Stock Option Plans, adjusted to give effect to the conversion under the terms of the merger agreement. All options assumed by the Company pursuant to the Primus Stock Option Plans were fully vested upon the closing of the acquisition and converted to options to acquire ATG common stock. Options granted under the Primus Stock Option Plans typically vest over four years and remain exercisable for a period not to exceed ten years. At March 31, 2006, there were 1,920,000 shares available for grant under the Primus 1999 Plan. No additional options will be granted under the Primus 1999 NESC Plan.

While the Company may grant to employees options that become exercisable at different times or within different periods, the Company has generally granted to employees options that vest and become exercisable in an annual installment of 25% on each of the first anniversary of the date of grant and then vest and become exercisable in installments of 6.25% per quarter over the next three years. The maximum contractual term of all options is ten years.

1999 Employee Stock Purchase Plan

The 1999 Employee Stock Purchase Plan (the Stock Purchase Plan) was adopted by ATG s Board of Directors and approved by stockholders in May 1999. The Stock Purchase Plan, as amended, authorizes the issuance of up to a total of 5,000,000 shares of ATG s common stock to participating employees. All ATG employees, including directors who are employees, are eligible to participate in the Stock Purchase Plan. The purchase price is 85% of the closing market price of ATG s common stock on either: (1) the first business day of the offering period or (2) the last business day of the offering period, whichever is lower. The Stock Purchase Plan offering period is quarterly. As such, the first day of each quarter is the beginning of each offering period and is the grant date for the purposes of recognizing the stock-based compensation expense. Under APB Opinion No. 25, the Company was not required to recognize stock-based compensation expense for the cost of stock options or shares issued under the Company s Stock Purchase Plan. Upon adoption of SFAS 123R, the Company began recording stock-based compensation expense related to the Stock Purchase Plan.

Grant-Date Fair Value

The Company uses the Black-Scholes option pricing model to calculate the grant-date fair value of an award. The fair value of options granted during the first quarter of fiscal 2006 and the first quarter of fiscal 2005 were calculated using the following estimated weighted average assumptions:

Stock Options	Three Months Ended March 31, 2006	March 31, 2005
Options granted (in thousands)	2,307	2,818
Weighted-average exercise price	$ 2.90	$ 1.25
Weighted-average grant date fair-value	$ 2.51	$ 0.82
Assumptions:		
Expected volatility	115%	93.7%
Expected term (in years)	6.25	4.0
Risk-free interest rate	4.55%	3.62%
Expected dividend yield	0%	0.0%

Expected volatility The Company has determined that the historical volatility of its common stock is the best indicator of the future volatility of the Company s stock. As such, the Company uses historical volatility to estimate the grant-date fair value of stock options. The historical volatility is calculated for the period that is commensurate with the

option s expected term.

Expected term in the first quarter of fiscal 2006, the Company was unable to use historical employee exercise and option expiration data to estimate the expected term assumption for the Black-Scholes grant-date valuation. The Company has utilized the safe harbor provision in Staff Accounting Bulletin No. 107 to determine the expected term of its stock options. With respect to options granted on or before December 31, 2005, the Company was able to use employee exercise and option expiration data to estimate the expected term assumption for the Black-Scholes grant-date valuation.

Risk-free interest rate the yield on zero-coupon U.S. Treasury securities for a period that is commensurate with the expected term is used as the risk-free interest rate.

Expected dividend yield the Company s Board of Directors did not declare a dividend for the first quarter 2006 and historically has not declared dividends nor expects to issue dividends. As such, the Company uses a 0% expected dividend yield.

Expense

The Company uses and has historically used the straight-line attribution method to recognize expense for stock options.

The amount of stock-based compensation recognized during a period is based on the value of the portion of the awards that are ultimately expected to vest. SFAS 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The term forfeitures is distinct from cancellations or expirations and represents only the unvested portion of the surrendered option. The Company has applied an annual forfeiture rate of 7.7% to all unvested options as of March 31, 2006. This analysis will be re-evaluated quarterly and the forfeiture rate will be adjusted as necessary. Ultimately, the actual expense recognized over the vesting period will only be for those shares that vest.

The adoption of SFAS 123R on January 1, 2006 had the following impact on the first quarter of fiscal 2006 results: operating profit before tax and net income were reduced by $594,000, and basic and diluted EPS were reduced by $0.01.

The following table details the effect on net income and earnings per share had stock-based compensation expense been recorded for the first three months of fiscal 2005 based on the fair-value method under SFAS 123, *Accounting for Stock-Based Compensation.* The reported and pro forma net income and earnings per share for the first quarter of fiscal 2006 are the same, since stock-based compensation expense was calculated under the provisions of SFAS 123R.

	Three Months Ended March 31, 2005 (in thousands, except per share amounts)	
Net income, as reported	$	1,408
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects		
Deduct: Total stock-based compensation expense determined under the fair value based method for all awards, net of related tax effects		(1,458)
Pro forma net loss	$	(50)
Earnings (loss) per share:		
Basic as reported	$	0.01
Basic pro forma	$	(0.00)
Diluted as reported	$	0.01
Diluted pro forma	$	(0.00)

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Option Activity

A summary of the activity under the Company s stock option plans as of March 31, 2006 and changes during the three-month period then ended, is presented below (in thousands, except per share amounts):

	Options Outstanding	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term in Years	Aggregate Intrinsic Value
Options outstanding at December 31, 2005	13,244	$ 2.33		
Options granted	2,307	2.90		
Options exercised	(651)	1.10		
Options forfeited	(193)	1.30		
Options expired	(191)	4.34		
Options outstanding at March 31, 2006	14,516	$ 2.46	7.8	$ 23,457
Options exercisable at March 31, 2006	7,075	$ 3.22	6.9	$ 9,395
Options vested or expected to vest at March 31, 2006 (1)	13,449	$ 2.47	8.1	$ 22,044

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

During the three months ended March 31, 2006, the total intrinsic value of options exercised (i.e. the difference between the market price at exercise and the price paid by the employee to exercise the options) was $1.2 million and the total amount of cash received from exercise of these options was $714,000.

As of March 31, 2006, there was $8.7 million of total unrecognized compensation cost related to unvested share-based awards. That cost is expected to be recognized over a weighted-average period of 2.9 years.

(h) Comprehensive Income

SFAS No. 130, *Reporting Comprehensive Income*, requires financial statements to include the reporting of comprehensive income, which includes net income and certain transactions that have generally been reported in the statement of stockholders equity. Comprehensive income consists of net income and foreign currency translation adjustments.

	Three Months Ended March 31, (in thousands)	
	2006	**2005**
Net income	$2,641	$1,408
Foreign currency translation adjustment	(4)	53
Comprehensive income	$2,637	$1,461

(i) Concentrations of Credit Risk and Major Customers

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of marketable securities and accounts receivable. ATG maintains cash, cash equivalents and marketable securities with high credit quality financial institutions. To reduce its concentration of credit risk with respect to accounts receivable, the Company routinely assesses the financial strength of its customers through continuing credit evaluations. The Company generally does not require collateral.

At March 31, 2006 one customer balance, comprising product and services invoices, accounted for 10% of accounts receivable. At December 31, 2005 another customer balance, comprising product and services invoices, accounted for 21% of accounts receivable. One customer in the three-month period ended March 31, 2006 accounted for 10% of total revenues. A different customer accounted for more than 10% of the Company s revenues for the three months ended March 31, 2005.

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(2) Disclosures About Segments of an Enterprise

SFAS No. 131, *Disclosures About Segments of an Enterprise and Related Information*, establishes standards for reporting information regarding operating segments in annual financial statements. SFAS No. 131 also requires related disclosures about products and services and geographic areas. Operating segments are identified as components of an enterprise about which separate discrete financial information is available for evaluation by the chief operating decision-maker or decision-making group in making decisions on how to allocate resources and assess performance. The Company s chief operating decision-maker is its executive management team. To date, the Company has viewed its operations and manages its business as principally one segment with two product offerings: software licenses and services. The Company evaluates these product offerings based on their respective gross margins. As a result, the financial information disclosed in the consolidated financial statements represents all of the material financial information related to the Company s principal operating segment.

Revenues from sources outside of the United States were approximately $4.0 million and $5.9 million for the three months ended March 31, 2006 and March 31, 2005, respectively. ATG s revenues from international sources were primarily generated from customers located in Europe and the UK region. All of ATG s product sales for the months ended March 31, 2006 and March 31, 2005, were delivered from its headquarters located in the United States.

The following table represents the percentage of total revenues by geographic region for the three months ended March 31, 2006 and March 31, 2005:

	Three Months Ended March 31,	
	2006	**2005**
United States	81%	73%
Europe, Middle East and Africa (excluding UK)	11%	13%
United Kingdom (UK)	5%	12%
Asia Pacific	0%	1%
Other	3%	1%
	100%	100%

(3) Credit Facility and Notes Payable

Credit Facility

Effective June 13, 2002, ATG entered into a $15 million revolving line of credit with Silicon Valley Bank (the Bank) which provided for borrowings of up to the lesser of $15 million or 80% of eligible accounts receivable. Effective December 24, 2002 the revolving line of credit increased to $20 million.

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The line of credit is secured by all of the Company s tangible and intangible personal property and is subject to financial covenants including liquidity coverage and profitability.

During the fourth quarter of 2005, the Company extended the line of credit through February 7, 2006. In February 2006, the Company entered into the Ninth Loan Modification Agreement (the Ninth Amendment) with the Bank, which amended the Amended and Restated Loan and Security Agreement dated as of June 13, 2002. Under the Ninth Amendment, the revolving line of credit was extended to January 31, 2008 and the profitability covenant was revised to require net income of at least $1.00 for the quarter ending March 31, 2006 and net income of at least $500,000 for the quarter ending June 30, 2006 and each quarter thereafter. The Company is required to maintain unrestricted and unencumbered cash, which includes cash equivalents and marketable securities, of greater than $20 million at the end of each month through the duration of the credit facility.

To avoid additional bank fees and expenses, the Company is required to maintain unrestricted cash, which includes cash equivalents and marketable securities, at the Bank in an amount equal to two times the amount of obligations outstanding, which includes letters of credit that have been issued but not drawn upon, under the loan agreement. In the event the Company s cash balances at the Bank fall below this amount, the Company will be required to pay fees and expenses to compensate the Bank for lost income. At March 31, 2006, the Company was in compliance with all related financial covenants. In the event that ATG does not comply with the financial covenants within the line of credit or defaults on any of its provisions, the Bank s significant remedies include: (1) declaring all obligations immediately due and payable, which could include requiring ATG to cash collateralize its outstanding Letters of Credit (LC s); (2) ceasing to advance money or extend credit for the Company s benefit; (3) applying to the obligations any balances and deposits held by the Company or any amount held by the Bank owing to or for the credit or the account of ATG; and, (4) putting a hold on any deposit account held as collateral. If the agreement expires, or is not extended, the Bank will require outstanding LC s at that time to be cash secured on terms acceptable to the Bank.

While there were no outstanding borrowings under the facility at March 31, 2006, the Bank had issued LC s totaling $4.6 million on ATG s behalf, which are supported by this facility. The LC s have been issued in favor of various landlords to secure obligations under ATG s facility leases pursuant to leases expiring through January 2009. The line of credit bears interest at the Bank s prime rate (7.75% at March 31, 2006). As of March 31, 2006, approximately $15.4 million was available under the facility.

On May 9, 2006, the Company entered into a new real estate lease that requires a $738,000 letter of credit which will be issued under this credit facility.

(4) Acquisitions

Acquisition of Primus Knowledge Solutions, Inc.

In connection with the Company s acquisition of Primus Knowledge Solutions, Inc. (Primus) in November 2004, the Company commenced integration activities which resulted in involuntary terminations and lease and contract terminations. The liability for involuntary termination benefits was for 49 employees, primarily in general and administrative and research and development functions. The following summarizes the obligations recognized in connection with the Primus acquisition and activity to date (in thousands):

	Involuntary Termination Benefits	Facilities Related Costs	Total
Obligation	$ 1,682	$ 376	$ 2,058
Payments	(464)	(97)	(561)
Balance December 31, 2004	1,218	279	1,497
Payments	(891)	(279)	(1,170)
Balance December 31, 2005	$ 327	$	$ 327

Payments			
Balance March 31, 2006	$ 327	$	$ 327

Intangible assets are being amortized based on the pattern in which the economic benefits of the intangible assets are being utilized or on a straight-line basis, if greater. Intangible assets consist of the following (in thousands):

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	March 31, 2006			December 31, 2005		
	Gross Carrying Amount	Accumulated Amortization	Net Book Value	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Purchased technology	$ 3,600	$ (1,462)	$ 2,138	$ 3,600	$ (1,258)	$ 2,342
Customer relationships	4,200	(2,203)	1,997	4,200	(1,927)	2,273
Non-compete agreements	400	(189)	211	400	(156)	244
Total intangible assets	$ 8,200	$ (3,854)	$ 4,346	$ 8,200	$ (3,341)	$ 4,859

Amortization expense from intangible assets was $513,000 and $579,000 for the three months ended March 31, 2006 and 2005, respectively. As of March 31, 2006, amortization expense on intangible assets for the next four years is as follows (in thousands):

Remainder of 2006	$ 1,542
2007	1,740
2008	848
2009	216
Total	$ 4,346

(5) Commitments and Contingencies

Indemnifications

The Company frequently has agreed to indemnification provisions in software license agreements with customers and in its real estate leases in the ordinary course of its business.

With respect to software license agreements, these indemnifications generally include provisions indemnifying the customer against losses, expenses, and liabilities from damages that may be awarded against the customer in the event the Company s software is found to infringe upon the intellectual property of others. The software license agreements generally limit the scope of and remedies for such indemnification obligations in a variety of industry-standard respects. The Company relies on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect its intellectual property rights. The Company believes such laws and practices, along with its internal development processes and other policies and practices limit its exposure related to the indemnification provisions of the software license agreements. However, in recent years there has been significant litigation in the United States involving patents and other intellectual property rights. Companies providing Internet-related products and services are increasingly bringing and becoming subject to suits alleging infringement of proprietary rights, particularly patent rights. From time to time, the Company s customers have been subject to third party patent claims and the Company has agreed to indemnify such customers from claims to the extent the claims relate to the Company s products.

With respect to real estate lease agreements or settlement agreements with landlords, these indemnifications typically apply to claims asserted against the landlord relating to personal injury and property damage at the leased premises or to certain breaches of the Company s contractual obligations or representations and warranties included in the settlement agreements. These indemnification provisions generally survive the termination of the respective agreements, although the provision generally has the most relevance during the contract term and for a short period of time thereafter. The maximum potential amount of future payments that the Company could be required to make under these indemnification provisions is unlimited. The Company has purchased insurance that reduces its monetary exposure for landlord indemnifications.

(6) Restructuring

During the years ended 2005, 2004, 2003, 2002 and 2001, the Company recorded net restructuring charges/(benefits) of $0.9 million, $3.6 million, $(10.5) million, $19.0 million and $75.6 million, respectively, primarily as a result of the global slowdown in information technology spending. The significant drop in demand in 2001 for technology oriented products, particularly internet related technologies, caused management to significantly scale back the Company s prior growth plans, resulting in a significant reduction in the Company s workforce and consolidation of the Company s facilities in 2001. Throughout 2002, the continued softness of demand for technology products, as well as near term revenue projections, caused management to further evaluate the Company s marketing, sales and service resource capabilities as well as its overall general and administrative cost structure, which resulted in additional restructuring actions being taken in 2002. These actions resulted in a further reduction in headcount and consolidation of additional facilities. In 2003, as the Company continued to refine its business strategy and to consider future revenue opportunities, the Company took further restructuring actions to reduce costs, including product development costs, to help move the Company towards profitability. In 2004, the Company s restructuring activities were undertaken to align the Company s headcount more closely with management s revenue projections and changing staff requirements as a result of strategic product realignments and the Company s acquisition of Primus, and to eliminate facilities that were not needed to efficiently run the Company s operations. In 2005, the Company restructuring was to align workforce and facilities needs. The charges referred to above primarily pertain to the closure and consolidation of excess facilities, impairment of assets, employee severance benefits, and the settlement of certain contractual obligations. The 2005, 2004 and 2003 charges were recorded in accordance with SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities,* SFAS No. 88, *Employers Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits* and Staff Accounting Bulletin (SAB) No. 100, *Restructuring and Impairment Charges.* The 2002 and 2001 charges were recorded in accordance with Emerging Issues Task Force Issue No. 94-3, *Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring)*, SFAS 88 and SAB 100.

As of March 31, 2006, the Company had an accrued restructuring liability of $4.1 million related to facility related costs. The long-term portion of the accrued restructuring liability was $1.9 million.

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A summary of the Company s charges and activity of restructuring accruals is as follows:

	Restructuring Charge (Benefit)					
	2005	2004	2003	2002	2001	Total
	(In thousands)					
Facility-related costs and impairments	$ 1,817	$ 1,488	$ 1,464	$ 14,634	$ 59,418	$ 78,821
Employee severance and benefits costs		2,461	1,236	3,553	7,938	15,188
Asset impairments					4,205	4,205
Exchangeable share settlement					1,263	1,263
Marketing costs					851	851
Legal and accounting					405	405
Restructuring Charges	1,817	3,949	2,700	18,187	74,080	100,733
Adjustments to 2001 action, net	(792)	(60)	(8,468)	818	1,500	(7,002)
Adjustments to 2002 action, net	43	(242)	(5,118)			(5,317)
Adjustments to 2003 action, net	74	(77)	410			407
Adjustments to 2004 action, net	(257)					(257)
Total adjustments of prior actions, net	(932)	(379)	(13,176)	818	1,500	(12,169)
Restructuring charge (benefit)	$ 885	$ 3,570	$ (10,476)	$ 19,005	$ 75,580	$ 88,564
Restructuring charges for the year ended December 31, 2001					$ 74,080	$ 74,080
Changes in estimates resulting in additional charges					9,700	9,700
Changes in estimates reducing accruals					(8,200)	(8,200)
Write-offs					(16,219)	(16,219)
Facility related payments					(6,308)	(6,308)
Employee related payments					(6,748)	(6,748)
Legal and accounting payments					(232)	(232)
Balance December 31, 2001					$ 46,073	$ 46,073
				$ 18,187		$ 18,187

Restructuring charges for the year ended December 31, 2002						
Changes in estimates resulting in additional charges					2,207	2,207
Changes in estimates reducing accruals					(1,389)	(1,389)
Write-offs				(2,613)		(2,613)
Facility related payments					(9,016)	(9,016)
Employee related payments					(920)	(920)
Legal and accounting payments					(173)	(173)
Balance December 31, 2002				$ 15,574	$ 36,782	$ 52,356
Restructuring charges for the year ended December 31, 2003			$ 2,700			$ 2,700
Changes in estimates resulting in additional charges			494	4,421	2,998	7,913
Changes in estimates reducing accruals			(84)	(7,321)	(11,466)	(18,871)
Write-offs			(371)		536	165
Facility related payments			(70)	(2,993)	(18,143)	(21,206)
Employee related payments			(994)	(3,794)	(270)	(5,058)
Balance December 31, 2003			$ 1,675	$ 5,887	$ 10,437	$ 17,999
Restructuring charges for the year ended December 31, 2004		$ 3,949				$ 3,949
Changes in estimates resulting in additional charges					112	112
Changes in estimates reducing accruals			(77)	(242)	(172)	(491)
Write-offs		(667)				(667)
Facility related payments		(71)	(179)	(4,490)	(4,066)	(8,806)
Employee related payments		(892)	(46)			(938)
Balance December 31, 2004		$ 2,319	$ 1,373	$ 1,155	$ 6,311	$ 11,158
Restructuring charges for the year ended December 31, 2005	$ 1,817					$ 1,817
Changes in estimates resulting in additional charges		200	98	91		389
		(457)	(24)	(48)	(792)	(1,321)

Changes in estimates reducing accruals						
Write-offs	(1,167)					(1,167)
Facility related payments	(264)	(317)	(428)	(548)	(2,676)	(4,233)
Employee related payments		(1,546)				(1,546)
Balance December 31, 2005	$ 386	$ 199	$ 1,019	$ 650	$ 2,843	$ 5,097
Facility related payments	$ (66)	$ (35)	$ (221)	$ (14)	$ (658)	$ (994)
Employee related payments		(52)				(52)
Balance March 31, 2006	$ 320	$ 112	$ 798	$ 636	$ 2,185	$ 4,051

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2001 Actions

Actions taken by the Company in 2001 included the consolidation and closure of excess facilities, a worldwide workforce reduction, the write-off of certain unrealizable assets and settling certain obligations that had no future benefit. In the second quarter of 2001, the Company recorded a restructuring charge of $44.2 million, and in the fourth quarter of 2001, the Company recorded a restructuring charge of $31.4 million. In connection with these actions, the Company also recorded in cost of product licenses an impairment charge for purchased software of $1.4 million. Total restructuring charges for 2001 totaled $75.6 million.

Facilities-Related Costs and Impairments

During 2001, the Company recorded facilities-related charges of $59.4 million of which $38.1 million was recorded in the second quarter and $21.3 million was recorded in the fourth quarter. The facilities-related charges comprised excess rental space for offices worldwide, net of estimates for vacancy periods and sublease income based on the then-current real estate market data, and related write-offs of abandoned leasehold improvements and fixed assets of $7.7 million and $2.2 million, respectively, which were directly related to excess office facilities. The estimated sublease income was $25.9 million based on then current rental rates and estimated vacancy periods. During the fourth quarter of 2001, the Company recorded an adjustment to increase the facilities-related costs for a change in estimate of the lease obligations for two leases by $9.7 million as a result of a market analysis indicating lower sublease rates and longer vacancy periods due to the continued weakening of the real estate market. In addition, the Company reduced its lease accruals by $8.2 million for a lease settlement in consideration of a buy-out totaling $9.3 million, which was paid ratably over 4.5 years.

The leasehold improvements, which will continue to be in use, are related to the facilities the Company vacated and is subleasing or attempting to sublease, and were written down to their estimated fair value of zero because the estimated cash flows to be generated by sublease income at those locations are not and will not be sufficient to recover the carrying value of the assets. Furniture and fixtures were written down to their fair value based on the expected discounted cash flows they will generate over their remaining economic life. Because these assets ceased being used as of the end of the period in which the write-downs were recorded, the fair value of these assets was estimated to be zero. The assets were abandoned and disposed of at the time of the charge.

During 2002, the Company recorded an adjustment to increase the facilities-related portion of the 2001 charge by an additional $2.2 million for changes to sublease and vacancy assumptions due to the continued weakening in the real estate market. In addition, during 2002, the Company executed sublease agreements for two locations and recorded a reduction to its lease accruals of $853,000 due to favorable sublease terms compared to the Company s original estimates.

During 2003, the Company settled future lease obligations for five leases for aggregate payments of $17.1 million, resulting in an aggregate reduction to its lease accruals relating to its 2001 restructuring of $11.5 million, net of sublease and vacancy assumptions. The Company also recorded an additional charge of $2.8 million for facilities-related costs comprising $2.3 million for updated management assumptions of probable settlement outcomes based on the then-current negotiations and $450,000 for updated sublease assumptions based on current real estate market conditions extending the estimated vacancy period.

During 2004, the Company made adjustments in cost estimates related to space vacated in 2001. These adjustments resulted in an increase to the restructuring charge of $112,000.

During 2005, the Company recorded an adjustment to its estimates of sublease costs related to the 2001 actions, resulting in a credit to the restructuring charge of $792,000. The change in estimate was primarily due to the Company s continued evaluation of the financial condition of its subtenants and their ability to meet their financial obligations to the Company.

Employee Severance, Benefits and Related Costs and Exchangeable Shares

As part of the 2001 restructuring actions, the Company recorded charges of $7.9 million for employee severance. The Company terminated the employment of 530 employees, or 46% of the Company s workforce, of which 249 were from sales and marketing, 117 from services, 101 from general and administrative and 63 from research and development. None of these employees remained employed as of September 30, 2002. In addition, the Company settled 11,762 exchangeable shares with an employee, who was terminated in connection with the restructuring action,

and recorded $1.3 million as a charge to restructuring for this settlement. During 2003, the Company recorded additional charges of $229,000 for severance related to an employee terminated as part of the 2001 restructuring action. During 2004, the Company reached a final settlement with this employee, resulting in a reduction to the restructuring charge of $172,000.

Asset Impairments

The asset impairment charges included the write-off of approximately $4.0 million of the remaining unamortized goodwill related to the two professional service organizations acquired in 2000. The Company had closed these operations and terminated the employees as part of the 2001 restructuring action, and as a result, the unamortized goodwill was impaired and had no future value. In addition, the Company recorded an impairment charge of approximately $1.4 million in cost of product license revenues related to purchased software to record the software at its net realizable value of zero due to the Company abandoning a certain product development strategy. The purchased software had no future use to the Company.

Marketing Costs and Legal and Accounting

The Company recorded charges of $851,000 to write off certain prepaid costs for future marketing services to their fair value of

zero due to changes in the Company s product development strategy, as a result of which, the prepaid marketing cost had no future utility to the Company. During 2002, the Company unexpectedly was able to recoup $536,000 and recorded a credit for the amount received. During 2001, the Company also recorded $405,000 for legal and accounting services incurred in connection with the 2001 restructuring action.

The 2001 actions were substantially completed by February 28, 2002.

2002 Actions

Actions taken by the Company in 2002 included the consolidation and closure of excess facilities, a worldwide workforce reduction and the write-off of certain idle assets. In the fourth quarter of 2002, the Company recorded a restructuring charge of $18.2 million.

Facilities-Related Costs and Impairments

During 2002, the Company recorded facilities-related charges of $14.6 million, which included $12.0 million for operating lease obligations, net of assumptions for vacancy periods and sublease income based on the then-current real estate market data, related to office space that was either idle or vacated during the first quarter of 2003. This action was completed by January 31, 2003. This charge also included write-offs of leasehold improvements and furniture and fixtures associated with these facilities of $948,000 and $507,000, respectively, and computer equipment and software of $1.2 million. The lease charge was for office space the Company vacated and intends to sublease. The estimated sublease income was $4.8 million based on then current rental rates and estimated vacancy periods.

As a result of this action and the actions taken in 2001, the Company wrote off certain computer equipment and software, aggregating $1.2 million, and furniture and fixtures, aggregating $507,000, which was no longer being used due to the reduction in personnel and office locations. These assets were abandoned and written down to their fair value based on the expected discounted cash flows they would generate over their remaining economic life. Due to the short remaining economic life and current market conditions for such assets, the fair value of these assets was estimated to be zero. These assets ceased being used either as of December 31, 2002 or in the first quarter of 2003 and were disposed of in the quarter ended March 31, 2003. In addition, the Company wrote off leasehold improvements, which will continue to be in use and are related to the facilities it is attempting to sublease, to their fair value of zero because the estimated cash flows to be generated by sublease income at those locations will not be sufficient to recover the carrying value of the assets.

During 2003, the Company recorded an adjustment of $1.9 million primarily to increase its lease obligation accrual at two locations because of changes in assumptions as to the vacancy period and sublease income. These changes resulted in an estimated reduction of sublease income of $1.8 million. In addition, principally due to a favorable lease settlement relating to its 2002 restructuring activities, the Company reduced its lease obligations by $7.2 million. The settlement resulted in the Company terminating a future lease obligation for an aggregate payment of $3.3 million, which was paid in January 2004. As a result of this transaction, the Company recorded prepaid rent of $2.2 million, increasing the accrual adjustments in 2003 to $4.1 million.

During 2004, the Company recorded an adjustment to its estimates related to the 2002 actions, resulting in a credit to the restructuring charge of $242,000.

During 2005, the Company recorded reversals of $48,000 to reduce accruals primarily due to executing a sub-lease agreement. Offsetting this reversal, the Company recorded additional charges of $91,000 due to changes in its sublease assumptions at one location.

Employee Severance, Benefits and Related Costs

As part of the 2002 restructuring action, the Company recorded a charge of $3.6 million for severance and benefit costs related to cost reduction actions taken across the worldwide employee base. The severance and benefit costs were for 125 employees, or 23% of the Company s workforce. Of the 125 employees, 53 of the employees were from sales and marketing, 45 from services, 19 from general and administrative and 8 from research and development. The Company accrued employee benefits pursuant to ongoing benefits plans and statutory minimum requirements in foreign locations. The Company began the termination process on January 6, 2003 and all employees had been terminated by June 30, 2003. During the second quarter of 2003, the Company recorded an adjustment to increase the severance accrual by $327,000 based on final severance settlements with certain employees at its foreign locations. During the fourth quarter of 2003, the Company reduced certain severance accruals by $86,000, primarily at its

foreign locations, due to amounts being settled at less than the amount recorded as a result of foreign currency exchange movements.

2003 Actions

As a result of several reorganization decisions, the Company undertook plans to restructure operations in the second and third quarters of 2003. Actions taken by the Company included the closure of excess facilities, a worldwide workforce reduction and the write-off of certain idle assets.

Second Quarter 2003 Actions

During the quarter ended June 30, 2003, the Company recorded a restructuring charge of $2.0 million. The Company also recorded an impairment charge in cost of product licenses of $169,000 related to certain purchased software.

Facilities-Related Costs and Impairments

During the second quarter of 2003, the Company recorded facilities-related charges of $1.1 million comprising $866,000 for an operating lease related to idle office space, $144,000 of leasehold improvements and fixed assets written down to their fair value, and $61,000 for various office equipment leases. The lease charge was for office space the Company vacated and intends to sublease. The amount of the operating lease charge was based on assumptions from current real estate market data for sublease income rates and vacancy rates at the location. The estimated sublease income was $500,000, based on then current rental rates and an estimated vacancy period. In the fourth quarter of 2003, as result of updated market conditions, the estimated sublet rental rate was lowered and the vacancy period was extended resulting in an additional charge of $227,000. In accordance with SFAS 146, the Company recorded the present value of the net lease obligation.

As a result of a reduction of employees and closure of an office location, the Company wrote off computer and office equipment to their fair value based on the expected discounted cash flows they would generate over their remaining economic life. Due to the short remaining economic life and current market conditions for such assets, the fair value of these assets was estimated to be zero. These assets ceased being used by June 30, 2003 and were disposed of by September 30, 2003. In addition, the Company wrote off leasehold improvements, which continue to be in use and are related to the facility it is attempting to sublease, to their fair value of zero because the estimated cash flows to be generated from that location will not be sufficient to recover the carrying value of the assets.

Employee Severance, Benefits and Related Costs

As part of the second quarter 2003 restructuring action, the Company recorded a charge of $927,000 for severance and benefit costs related to cost reduction actions taken across the worldwide employee base. The severance and benefit costs were for 32 employees, or 7.4% of the Company s workforce, consisting of 11 employees from sales and marketing, 3 from services, 3 from general and administrative and 15 from research and development. The Company accrued employee benefits pursuant to its ongoing benefit plans for domestic locations and under statutory minimum requirements in foreign locations. All employees were notified of their termination as of June 30, 2003. The termination process was completed during the fourth quarter of 2003. During the third quarter of 2003, the Company accrued an additional $69,000 for employees at its foreign locations based on management s best estimate of the final payments for severance. During the fourth quarter of 2003, the Company reduced certain severance accruals by $84,000 at its international locations as a result of final settlements.

Asset Impairments

The Company recorded a charge in cost of product license revenues of $169,000 to reduce the carrying value of third-party software embedded into one of its products, which was a minor component of its suite of products, to its net realizable value of $210,000 based on management s best estimate of future net cash flows to be generated from the sale of the software to customers. The Company discontinued marketing of this software and ceased future development work specifically related to this third-party software. However, the Company has not changed its overall product strategy for the purpose for which the software was acquired.

Third Quarter 2003 Actions

During the third quarter of 2003, the Company recorded a restructuring charge of approximately $771,000.

Facilities-Related Costs and Impairments

The Company recorded facilities-related charges of $393,000 comprising $227,000 for an operating lease related to idle office space and $166,000 of leasehold improvements and fixed assets written down to their fair value. The lease charge was for office space the Company vacated and intends to sublease. The amount of the operating lease charge was based on assumptions from current real estate market data for sublease income rates and vacancy rates at the location. The estimated sublease income was $216,000 based on then current rental rates and an estimated vacancy period. During the fourth quarter, as a result of updated market conditions, the Company determined that it was unlikely it would sublet this space before its lease expires, resulting in an additional charge of $198,000. In accordance with SFAS 146, the Company recorded the present value of the net lease obligation.

As a result of a reduction of employees and the closure of one office location, the Company wrote off computer and office equipment to their fair value based on the expected discounted cash flows they would generate over their remaining economic life. Due to the short remaining economic life and current market conditions for such assets, the

fair value of these assets was estimated to be zero. These assets ceased being used prior to September 30, 2003 and were disposed of by December 31, 2003. In addition, the Company wrote down leasehold improvements to their fair value of zero because the estimated cash flows to be generated from that location would not be sufficient to recover the carrying value of the assets.

In the fourth quarter of 2005 the Company recorded an adjustment in estimates of sublease income resulting in additional charges of $98,000.

Employee Severance, Benefits and Related Costs

The Company recorded a charge of $309,000 for severance and benefit costs related to cost reduction actions taken across the worldwide employee base. The severance and benefit costs were for 16 employees, or 4.3% of the Company s workforce, consisting of 7 employees from sales and marketing, 4 from services and 5 from research and development. The Company accrued employee benefits pursuant to its ongoing benefit plans. All employees were notified of their termination as of September 30, 2003. The termination process was completed during the fourth quarter of 2003. During 2004, the Company made adjustments in cost estimates

related to space vacated in 2003 and employee severance estimates related to 2003 actions. These adjustments resulted in a net reduction to the restructuring charge of $77,000. During 2005, the Company recorded an adjustment to its cost estimates related to the 2003 actions, resulting in a credit to the restructuring charge of $24,000.

2004 Actions

During 2004, the Company recorded a restructuring charge of $3.6 million, comprised of costs related to new actions of $3.9 million and net credits resulting from changes in estimates related to prior actions of $379,000.

Facilities-Related Costs and Impairments

During the fourth quarter of 2004, the Company recorded facilities-related charges of $1.5 million primarily comprised of $800,000 for an operating lease related to idle office space net of assumptions for vacancy period and sublease income based on the then current real estate market data, $200,000 of leasehold improvements written down to their fair value and $500,000 of prepaid rent related to the abandoned space, which was recorded as part of prior lease settlements. The lease charge was for office space the Company vacated before December 31, 2004 and intended to sublease. The estimated sublease income was $350,000 based on then current rental rates and an estimated vacancy period. In accordance with SFAS 146, the Company recorded the present value of the net lease obligation.

As a result of a reduction of employees and the closure of office space, the Company wrote off $200,000 of leasehold improvements related to the vacated space to their estimated fair value of zero because the estimated cash flows to be generated from that location will not be sufficient to recover the carrying value of the assets.

During 2005, the Company recorded a net reversal of $267,000 primarily due to adjusting its estimates of net sublease obligations as a result of executing a sublease agreement.

Employee Severance, Benefits and Related Costs

As part of the fourth quarter 2004 restructuring action, the Company recorded a charge of $2.5 million for severance and benefit costs related to cost reduction actions taken across the worldwide employee base. The severance and benefit costs were for 56 employees, or 14% of the Company s workforce, consisting of 27 employees from sales and marketing, 8 from services, 6 from general and administrative and 15 from research and development. The Company accrued employee benefits pursuant to its ongoing benefit plans for domestic locations and under statutory minimum requirements in foreign locations. All employees were notified of their termination as of December 31, 2004 which was completed during 2005.

During the first quarter of 2005, the Company recorded a restructuring charge of $200,000, resulting from adjustments to estimates made in 2004 for employee severance benefits payable in international geographies. Offsetting this charge were reversals of $190,000 due to final settlements.

2005 Actions

During 2005, the Company recorded net restructuring charges of $885,000, comprised of costs related to new actions of $1.8 million and net credits resulting from changes in estimates related to prior actions of $0.9 million.

Facilities-Related Costs and Impairments

During the second quarter of 2005, the Company relocated its San Francisco office and reduced the amount of space it occupies in San Francisco. As a result of this action and other minor facilities charges, the Company recorded facilities-related charges of $1.8 million primarily comprised of $1.0 million of deferred rent related to the abandoned space, $118,000 of leasehold improvements written down to their fair value, and $557,000 for an operating lease related to idle office space vacated, net of assumptions for sublease income based on an executed sublease agreement. In accordance with SFAS 146, the Company recorded the net present value of the net lease obligation.

Abandoned Facilities Obligations

At March 31, 2006, the Company had lease arrangements related to seven abandoned facilities. One of these leases is the subject of a lease settlement arrangement under which the Company is obligated to make payments through 2006. The lease agreements with respect to the other six facilities are ongoing. Of these locations, the restructuring accrual for the Reading, UK location is net of assumed sub-lease income, as no sub-lease agreement had been executed by March 31, 2006. The restructuring accrual for all other locations is either net of the contractual amounts due under an executed sub-lease agreement, or there is no assumed sub-lease income included in the accrual. All locations for which the Company has recorded restructuring charges have been exited, and thus the Company s plans with respect to these leases have been completed. A summary of the remaining facility locations and the timing of the

remaining cash payments are as follows (in thousands):

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Lease Locations	2006 (Remaining)	2007	2008	2009	Total
Cambridge, MA*	$ 345				$ 345
Cambridge, MA	57				57
Cambridge, MA	300				300
Waltham, MA	1,096	1,452	1,452	364	4,364
Chicago, IL	265				265
San Francisco, CA	384	512			896
Reading, UK	426	538	538		