CHORDIANT SOFTWARE INC
Form 10-Q
January 28, 2010

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended December 31, 2009

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 Number 001-34179

Chordiant Software, Inc.
(Exact name of registrant as specified in its charter)

Delaware	93-1051328
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

20400 Stevens Creek Boulevard, Suite 400
Cupertino, CA 95014
(Address of principal executive offices) (Zip Code)

(408) 517-6100
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files): Yes No

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

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

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

As of January 15, 2010, there were 30,363,187 shares of the registrant's common stock outstanding.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited).

CHORDIANT SOFTWARE, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)
(Unaudited)

	December 31, 2009	September 30, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 50,613	$ 49,863
Marketable securities	1,716	—
Accounts receivable, net	22,021	16,708
Prepaid expenses and other current assets	3,453	4,006
Total current assets	77,803	70,577
Property and equipment, net	1,638	1,850
Goodwill	22,608	22,608
Intangible assets, net	—	303
Deferred tax assets—non-current	3,224	3,480
Other assets	2,378	2,491
Total assets	$ 107,651	$ 101,309
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 4,534	$ 3,809
Accrued expenses	9,242	6,334
Deferred revenue	32,157	28,704
Total current liabilities	45,933	38,847
Deferred revenue—long-term	8,786	9,257
Other liabilities—non-current	1,151	1,069
Restructuring costs, net of current portion	21	123
Total liabilities	55,891	49,296
Commitments and contingencies (Notes 7, 8 and 9)		
Stockholders' equity:		
Preferred stock, $0.001 par value; 51,000 shares authorized (500 shares designated as Series A Junior Participating Preferred Stock); none issued and outstanding at December 31, 2009 and September 30, 2009	—	—
Common stock, $0.001 par value; 300,000 shares authorized; 30,362 and 30,208 shares issued and outstanding at December 31, 2009 and September 30, 2009, respectively	30	30

Additional paid-in capital		286,583		285,666
Accumulated deficit		(237,586)		(236,614)
Accumulated other comprehensive income		2,733		2,931
Total stockholders’ equity		51,760		52,013
Total liabilities and stockholders’ equity	$	107,651	$	101,309

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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CHORDIANT SOFTWARE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	Three Months Ended December 31, 2009	2008
Revenues:		
License	$ 7,432	$ 7,941
Service	14,792	15,436
Total revenues	22,224	23,377
Cost of revenues:		
License	134	98
Service	5,545	6,686
Amortization of intangible assets	303	303
Total cost of revenues	5,982	7,087
Gross profit	16,242	16,290
Operating expenses:		
Sales and marketing	6,657	7,780
Research and development	5,354	5,259
General and administrative	4,504	4,402
Restructuring expense	144	784
Total operating expenses	16,659	18,225
Loss from operations	(417)	(1,935)
Interest income, net	29	292
Other income (expense), net	(90)	685
Loss before income taxes	(478)	(958)
Provision for income taxes	494	1,711
Net loss	$ (972)	$ (2,669)
Net loss per share:		
Basic and diluted	$ (0.03)	$ (0.09)
Weighted average shares used in computing net loss per share:		
Basic and diluted	30,180	30,008

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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CHORDIANT SOFTWARE, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Three Months Ended December 31, 2009	2008
Cash flows from operating activities:		
Net loss	$ (972)	$ (2,669)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	347	456
Amortization of intangibles and capitalized software	380	363
Non-cash stock-based compensation expense	889	965
Provision for doubtful accounts	(27)	202
Non-cash provision for income taxes	503	1,263
Changes in assets and liabilities:		
Accounts receivable	(5,524)	2,736
Prepaid expenses and other current assets	318	1,203
Other assets	29	(44)
Accounts payable	751	(2,443)
Accrued expenses, other liabilities—non-current and restructuring	2,938	(256)
Deferred revenue	3,170	864
Net cash provided by operating activities	2,802	2,640
Cash flows from investing activities:		
Property and equipment purchases	(131)	(180)
Capitalized product development costs	(11)	(13)
Increase in restricted cash	—	(1)
Purchases of marketable securities	(1,709)	—
Net cash used for investing activities	(1,851)	(194)
Cash flows from financing activities:		
Proceeds from exercise of stock options	27	11
Net cash provided by financing activities	27	11
Effect of exchange rate changes	(228)	(4,198)
Net increase (decrease) in cash and cash equivalents	750	(1,741)
Cash and cash equivalents at beginning of period	49,863	55,516
Cash and cash equivalents at end of period	$ 50,613	$ 53,775

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 1—THE COMPANY

Chordiant Software, Inc. or the Company, or Chordiant, is an enterprise software vendor that offers software solutions for global business-to-consumer companies that seek to improve the quality of their customer interactions and to reduce costs through increased employee productivity and process efficiencies. The Company concentrates on serving global customers in insurance, healthcare, telecommunications, financial services and other consumer direct industries.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The accompanying Condensed Consolidated Financial Statements have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission, or SEC. Certain information and footnote disclosures normally included in financial statements prepared in accordance with Generally Accepted Accounting Principles, or GAAP, in the United States have been condensed or omitted pursuant to such rules and regulations. The September 30, 2009 Condensed Consolidated Balance Sheet was derived from audited financial statements, but does not include all disclosures required by GAAP in the United States. However, the Company believes that the disclosures are adequate to make the information presented not misleading. These unaudited Condensed Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements and related Notes included in the Company’s Annual Report on Form 10-K for the year ended September 30, 2009, or 2009 Form 10-K, filed with the SEC.

All adjustments, consisting of only normal recurring adjustments, which in the opinion of management, are necessary to state fairly the financial position, results of operations and cash flows for the interim periods presented, have been made. The results of operations for interim periods are not necessarily indicative of the results expected for the full fiscal year or for any future period.

Principles of consolidation

The accompanying unaudited Condensed Consolidated Financial Statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany transactions and balances have been eliminated in consolidation.

Use of estimates

The preparation of Condensed Consolidated Financial Statements in conformity with GAAP in the United States requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods.

On an on-going basis, the Company evaluates the estimates, including those related to the allowance for doubtful accounts, the valuation of stock-based compensation, the valuation of goodwill and intangible assets, the valuation of deferred tax assets, restructuring expenses, contingencies, Vendor Specific Objective Evidence, or VSOE, of fair

value in multiple element arrangements and the estimates associated with the percentage-of-completion method of accounting for certain of its revenue contracts. The Company bases these estimates on historical experience and on various other assumptions believed to be reasonable. Actual results may differ from these estimates under different assumptions or conditions.

Revenue recognition

The Company derives revenue from licensing software and related services, which include assistance in implementation, customization and integration, post-contract customer support or PCS, training and consulting. All revenue amounts are presented net of sales taxes in the Company's Condensed Consolidated Statements of Operations. The amount and timing of revenue is difficult to predict and any shortfall in revenue or delay in recognizing revenue could cause operating results to vary significantly from period to period and could result in operating losses. The accounting rules related to revenue recognition are complex and are affected by the interpretation of the rules and an understanding of industry practices, both of which are subject to change. Consequently, the revenue recognition accounting rules require management to make significant estimates based on judgment.

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For arrangements with multiple elements, the Company recognizes revenue for services and PCS based upon the fair value VSOE of the respective elements. The fair value VSOE of the services element is based upon the standard hourly rates charged for the services when such services are sold separately. The fair value VSOE for annual PCS is generally established with the contractual future renewal rates included in the contracts, when the renewal rate is substantive and consistent with the fees when support services are sold separately. When contracts contain multiple elements and fair value VSOE exists for all undelivered elements, the Company accounts for the delivered elements, principally the license portion, based upon the "residual method" as prescribed by relevant accounting guidance on software recognition. In multiple element transactions where VSOE is not established for an undelivered element, revenue is recognized upon the establishment of VSOE for that element or when the element is delivered.

At the time a transaction is entered into, the Company assesses whether any services included within the arrangement relate to significant implementation or customization that is essential to the functionality of our products. For contracts for products that do not involve significant implementation or customization essential to the product functionality, the Company recognizes license revenue when there is persuasive evidence of an arrangement, the fee is fixed or determinable, collection of the fee is probable and delivery has occurred as prescribed by relevant accounting guidance on revenue recognition. For contracts that involve significant implementation or customization services essential to the functionality of the products, the license and professional consulting services revenue is recognized using either the percentage-of-completion method or the completed contract method.

The percentage-of-completion method is applied when the Company has the ability to make reasonably dependable estimates of the total effort required for completion using labor hours incurred as the measure of progress towards completion. The progress toward completion is measured based on the "go-live" date. The "go-live" date is defined as the date the essential product functionality has been delivered, or the application enters into a production environment or the point at which no significant additional Chordiant supplied professional service resources are required. Estimates are subject to revisions as the contract progresses to completion and these changes are accounted for as changes in accounting estimates when the information becomes known. Information impacting estimates obtained after the balance sheet date but before the issuance of the financial statements is used to update the estimates. Provisions for estimated contract losses, if any, are recognized in the period in which the loss becomes probable and can be reasonably estimated. When additional licenses are sold related to the original licensing agreement, revenue is recognized upon delivery if the project has reached the go-live date, or if the project has not reached the go-live date, revenue is recognized under the percentage-of-completion method. Revenue from these arrangements is classified as license and service revenue based upon the estimated fair value of each element using the residual method.

The completed contract method is applied when the Company is unable to obtain reasonably dependable estimates of the total effort required for completion. Under the completed contract method, all revenue and related costs of revenue are deferred and recognized upon completion.

For product co-development arrangements relating to software products in development prior to the consummation of the individual arrangements, where the Company retains the intellectual property being developed, and intends to sell the resulting products to other customers, license revenue is deferred until the delivery of the final product, provided all other requirements of the guidance on software revenue recognition are met. Expenses associated with these co-development arrangements are normally expensed as incurred as they are considered to be research and development costs that do not qualify for capitalization or deferral. There have been no such arrangements during the periods presented.

Revenue from subscription or term license agreements, which include software and rights to unspecified future products or maintenance, is recognized ratably over the term of the subscription period. Revenue from subscription or term license agreements, which include software, but exclude rights to unspecified future products and maintenance, is recognized upon delivery of the software if all conditions of recognizing revenue have been met, including that the related agreement is non-cancelable, non-refundable and provided on an unsupported basis.

For transactions involving extended payment terms, the Company deems these fees not to be fixed or determinable for revenue recognition purposes and revenue is deferred until the fees become due and payable.

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For arrangements with multiple elements where the Company determines it can account for the elements separately and the fees are not fixed or determinable due to extended payment terms, revenue is recognized in the following manner. If the undelivered element is PCS, or other services, an amount equal to the estimated value of the services to be rendered prior to the next payment becoming due is allocated to the undelivered services. The residual of the payment is allocated to the delivered elements of the arrangement.

For arrangements with multiple elements where the Company determines it can account for the elements separately and the fees are not fixed or determinable due to extended payment terms, revenue is recognized in the following manner. Amounts are first allocated to the undelivered elements included in the arrangement, as payments become due or are received, and the residual is allocated to the delivered elements.

Revenue for PCS is recognized ratably over the support period which ranges from one to five years.

Training and consulting services revenue is recognized as such services are performed on an hourly or daily basis for time and material contracts. For consulting services arrangements with a fixed fee, revenue is recognized on a percentage-of-completion basis.

For all sales, either a signed license agreement or a binding purchase order with an underlying master license agreement is used as evidence of an arrangement. Sales through third party systems integrators are evidenced by a master agreement governing the relationship together with binding purchase orders or order forms on a transaction-by-transaction basis. Revenues from reseller arrangements are recognized on the “sell-through” method, when the reseller reports to the Company the sale of software products to end-users. The Company’s agreements with customers and resellers do not contain product return rights.

Collectability is assessed based on a number of factors, including past transaction history with the customer and the credit-worthiness of the customer. Collateral is generally not requested from customers. If it is determined that the collection of a fee is not probable, the revenue is recognized at the time the collection becomes probable, which is generally upon the receipt of cash.

Cash and Cash Equivalents

Cash equivalents consist of highly liquid instruments purchased with an original maturity of three months or less. The Company invests primarily in money market funds as these investments have historically been subject to minimal credit and market risks.

Marketable Securities

Historically the Company’s marketable securities have been classified as available-for-sale. Available-for-sale securities are carried at fair value with unrealized gains and losses included as a separate component of Stockholder’s Equity, net of any tax effect. Realized gains and losses and declines in value determined by management to be other than temporary on these investments are included in Other income (expense), net when held. The Company periodically evaluates these investments for other-than-temporary impairment. For the purposes of computing realized gains and losses, cost is identified on a specific identification basis. See Note 3 for marketable securities at each balance sheet date.

Restricted cash

At December 31, 2009 and September 30, 2009, interest bearing certificates of deposit were classified as restricted cash. These restricted cash balances serve as collateral for letters of credit securing certain lease obligations. These restricted cash balances are classified in Other Assets in the Condensed Consolidated Balance Sheets. See Note 4 for restricted cash balances at each balance sheet date.

Concentrations of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist of cash, cash equivalents, restricted cash, and accounts receivable. To date, the Company has invested excess funds in money market

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CHORDIANT SOFTWARE, INC.
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(UNAUDITED)

accounts, commercial paper, corporate bonds, and certificates-of-deposit. The Company has cash and cash equivalents with various large banks and institutions domestically and internationally.

The Company's accounts receivable are derived from sales to customers located in North America, Europe, and elsewhere in the world. The Company performs ongoing credit evaluations of customers' financial condition and, generally, requires no collateral from customers. The Company maintains an allowance for doubtful accounts when deemed necessary. The Company estimates its allowance for doubtful accounts by analyzing accounts receivable for specific risk accounts as well as providing for a general allowance amount based on historical bad debt and billing dispute percentages. The estimate considers historical bad debts, customer concentrations, customer credit-worthiness and current economic trends. Based upon current economic conditions, the Company reviewed accounts receivable and has recorded allowances as deemed necessary.

Some of the Company's current or prospective customers have recently been facing financial difficulties. Customers that have accounted for significant revenues in the past may not generate revenues in any future period, causing any failure to obtain new significant customers or additional orders from existing customers to materially affect operating results. The following table summarizes the revenues from customers that accounted for 10% or more of total revenues:

	Three Months Ended December 31,	
	2009	2008
Royal Bank of Scotland plc	22%	*
Lloyds TSB Bank	11%	*
Citicorp Credit Services, Inc.	*	13%
Vodafone Group Services Limited and affiliated companies	*	25%

* Represents less than 10% of total revenues.

At December 31, 2009, Royal Bank of Scotland plc and Deutsche Angestellten Krankenkasse accounted for approximately 20% and 11%, respectively, of accounts receivable. At September 30, 2009, General Motors Corporation, the Royal Bank of Scotland plc, and Turkiye Is Bankasi, A.S. accounted for approximately 17%, 14% and 11%, respectively, of accounts receivable.

Research and Development

Software development costs are expensed as incurred until technological feasibility of the underlying software product is achieved. After technological feasibility is established, software development costs are capitalized until general availability of the product. Capitalized costs are then amortized at the greater of a straight line basis over the estimated product life, or the ratio of current revenue to total projected product revenue.

During fiscal years 2008 and 2009 and the quarter ended December 31, 2009, technological feasibility to port existing products to new platforms was established through the completion of detailed program designs. Costs aggregating $0.6 million associated with these products have been capitalized and included in Other Assets as of December 31, 2009. As the porting of these products are completed, the capitalized costs are being amortized using the straight-line method over the estimated economic life of the product which is 36 months. For the three months ended December 31,

2009 and 2008, amortization expense, included in cost of revenue for licenses related to these products was less than $0.1 million for both periods. As of December 31, 2009 and 2008, the unamortized expense was approximately $0.4 million.

During the quarter ended September 30, 2006, technological feasibility to port an existing product to a new platform was established through the completion of a detailed program design. Costs aggregating $0.5 million associated with this product were capitalized and included in Other Assets as of September 30, 2007. This product was completed and became available for general release in July 2007, accordingly, the capitalized costs are being amortized using the straight-line method over the remaining estimated economic life of the product which is 36 months. For the three months ended December 31, 2009 and 2008, amortization expense, included in cost of revenue for license related to this product was less than $0.1 million for both periods. As of December 31, 2009, the unamortized expense was $0.1 million. As of December 31, 2008, the unamortized expense was $0.3 million.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Subsequent Events

The Company has evaluated subsequent events for recognition and disclosure through the time that these financial statements were filed in Form 10-Q Report with the SEC on January 28, 2010.

Income Taxes

Income taxes are accounted for using an asset and liability approach, which requires the recognition of taxes payable or refundable for the current period and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in the Company’s financial statements or tax returns. The measurement of current and deferred tax liabilities and assets is based on provisions of the enacted tax law; the effects of future changes in tax laws or rates are not anticipated. The measurement of deferred tax assets is reduced, if necessary, by the amount of any tax benefits that, based on available evidence, are not expected to be realized.

Net income (loss) per share

Basic net income (loss) per share is computed by dividing the net income (loss) by the weighted average number of common shares outstanding during the period. Diluted net income (loss) per share is computed by dividing the net income (loss) for the period by the weighted average number of common and potentially dilutive shares outstanding during the period. Potentially dilutive shares, which consist of incremental shares issuable upon the exercise of stock options, unvested restricted stock awards (using the treasury stock method), and unvested restricted stock units (using the treasury stock method), are included in the calculation of diluted net income per share, in periods in which net income is reported, to the extent such shares are dilutive. The calculation of diluted net loss per share excludes potential common shares as their effect is anti-dilutive for the three months ended December 31, 2009 and 2008.

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

	Three Months Ended December 31,	
	2009	2008
Net loss attributable to common stockholders	$ (972)	$ (2,669)
Denominator:		
Weighted average common stock outstanding for basic and diluted calculations	30,180	30,008
Net loss per share—basic and diluted	$ (0.03)	$ (0.09)

The following table sets forth the potential total common shares that are excluded from the calculation of diluted net loss per share as their effect is anti-dilutive as of the dates indicated (in thousands):

	December 31, 2009	December 31, 2008

Employee stock options	4,276	4,212
Restricted stock awards (RSAs)	90	71
Restricted stock units (RSUs)	987	520
	5,353	4,803

CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Recent Accounting Pronouncements

In October 2009, the Financial Accounting Standards Board (FASB) issued an Accounting Standard Update, or ASU, that that removes tangible products containing software components and non-software components that function together to deliver the product's essential functionality from the scope of industry-specific revenue accounting guidance for software and software related transactions. The ASU will be effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010 and early adoption will be permitted. The Company has evaluated the ASU and has determined that it will not have a significant impact on the determination or reporting of our financial results.

In October 2009, the FASB issued an ASU that addresses criteria for separating the consideration in multiple-element arrangements. The ASU will require companies to allocate the overall consideration to each deliverable by using a best estimate of the selling price of individual deliverables in the arrangement, in the absence of VSOE or other third-party evidence of the selling price. The ASU will be effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010 and early adoption will be permitted. The Company has evaluated the ASU and has determined that it will not have a significant impact on the determination or reporting of our financial results.

NOTE 3—FINANCIAL INSTRUMENTS AND FAIR VALUE

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The Company's investments are valued under a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

Level 1 – Valuations based on quoted prices in active markets for identical assets that the Company has the ability to access.
Level 2 – Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly.
Level 3 – Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

The following table represents information about the Company's investments measured at fair value on a recurring basis (in thousands).

		Fair value of investments as of December 31, 2009		
	Total	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)

Money Market Funds	$ 33,930	$ 33,930	$ —	$ —
Marketable securities	1,716	1,716	—	—
Total	$ 35,646	$ 35,646	$ —	$ —

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CHORDIANT SOFTWARE, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

	Fair value of investments as of September 30, 2009			
	Total	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Money Market Funds	$ 39,497	$ 39,497	$ —	$ —

The Company had the following available for sale securities as of December 31, 2009 (in thousands):

	December 31, 2009			
	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Fair Value
Marketable securities	$ 1,709	$ 7	$ —	$ 1,716

The Company had no marketable securities as of September 30, 2009. For the three months ended December 31, 2009 and September 30, 2009, no gains or losses were realized on the sale of marketable securities. The marketable securities represent common shares of SWK Holding Corporation (formerly Kana Software, Inc.), a publicly-traded company. These purchases were associated with the attempted, but unsuccessful, acquisition of the Company. As of December 31, 2009, due to the nature of these marketable securities, the Company has classified these marketable securities as available for sale and intends to hold these for less than one year.

NOTE 4—BALANCE SHEET COMPONENTS

Accounts receivable, net

Accounts receivable, net, consists of the following (in thousands):

	December 31, 2009	September 30, 2009
Accounts receivable, net:		
Accounts receivable	$ 22,213	$ 17,017
Less: allowance for doubtful accounts	(192)	(309)
	$ 22,021	$ 16,708

Prepaid expenses and other current assets

Prepaid expenses and other current assets consist of the following (in thousands):

	December 31, 2009	September 30, 2009
Prepaid expenses and other current assets:		
Prepaid commissions and royalties	$ 689	$ 582
Deferred tax assets	1,449	1,684
Other prepaid expenses and current assets	1,315	1,740
	$ 3,453	$ 4,006

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(UNAUDITED)

Property and equipment, net

Property and equipment, net, consists of the following (in thousands):

	December 31, 2009	September 30, 2009
Property and equipment, net:		
Computer hardware (useful lives of 3 years)	$ 4,667	$ 4,580
Purchased internal-use software (useful lives of 3 years)	3,414	3,381
Furniture and equipment (useful lives of 3 to 7 years)	743	739
Leasehold improvements (shorter of 7 years or the term of the lease)	2,738	2,741
	11,562	11,441
Accumulated depreciation and amortization	(9,924)	(9,591)
	$ 1,638	$ 1,850

Intangible assets, net

Intangible assets, net, consist of the following (in thousands):

	December 31, 2009			September 30, 2009		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Intangible assets:						
Developed technologies	$ 6,904	$ (6,904)	$ —	$ 6,904	$ (6,661)	$ 243
Customer list and trade-names	2,731	(2,731)	—	2,731	(2,671)	60
	$ 9,635	$ (9,635)	$ —	$ 9,635	$ (9,332)	$ 303

All of the Company’s acquired intangible assets are subject to amortization and are carried at cost less accumulated amortization. Amortization is computed on a straight line basis over the estimated useful lives which are as follows: Developed technologies—one and one half to five years; trade-names—three to five years; customer list—three to five years. Aggregate amortization expense for intangible assets totaled $0.3 million for each of the three month periods ended December 31, 2009 and 2008, respectively. As of December 31, 2009, the intangible assets are fully amortized.

Other assets

Other assets consist of the following (in thousands):

		December 31, 2009		September 30, 2009
Other assets:				
Long-term accounts receivable	$	930	$	930
Long-term restricted cash		88		90
Other assets		1,360		1,471
	$	2,378	$	2,491

The long-term account receivable balance represents a receivable from a single customer related to a multiple year maintenance renewal that occurred during the quarter ended March 31, 2009. This amount represents a payment which is due in the quarter ending March 31, 2011. All revenue associated with this receivable has been deferred and will be recognized as revenue over the term of the services performed. As of December 31, 2009, an allowance has not been provided for this receivable based on the Company’s assessment of the underlying customer’s credit worthiness.

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Accrued expenses

Accrued expenses consist of the following (in thousands):

	December 31, 2009	September 30, 2009
Accrued expenses:		
Accrued payroll, payroll taxes and related expenses	$ 4,248	$ 2,509
Accrued restructuring expenses, current portion (Note 5)	519	408
Accrued third party consulting fees	505	505
Accrued income, sales and other taxes	2,684	1,786
Other accrued liabilities	1,286	1,126
	$ 9,242	$ 6,334

Deferred Revenue

Deferred revenue consists of the following (in thousands):

	December 31, 2009	September 30, 2009
Deferred revenue:		
License	$ 7,635	$ 7,314
Support and maintenance	32,219	29,959
Other	1,089	688
	40,943	37,961
Less: current portion	(32,157)	(28,704)
Long-term deferred revenue	$ 8,786	$ 9,257

NOTE 5—RESTRUCTURING

Restructuring Costs

Through December 31, 2009, the Company approved certain restructuring plans to, among other things, reduce its workforce, terminate contracts and consolidate facilities. Restructuring and asset impairment expenses have been recorded to align the Company's cost structure with changing market conditions and to create a more efficient organization. The Company's restructuring expenses have been comprised primarily of: (i) severance and termination benefit costs related to the reduction of our workforce; (ii) lease termination costs and costs associated with permanently vacating certain facilities, and (iii) contract termination costs.

Accruals for facilities restructured prior to 2003 do not reflect any adjustments relating to the estimated net present value of cash flows associated with the facilities.

For each of the periods presented herein, restructuring expenses consist solely of:

- Severance and Termination Benefits—These costs represent severance and payroll taxes related to restructuring plans.

- Excess Facilities Costs—These costs represent future minimum lease payments related to excess and abandoned office space under leases, and the disposal of property and equipment including facility leasehold improvements, net of estimated sublease income.

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- Termination Costs—These costs represent contract termination costs related to the restructuring plan.

As of December 31, 2009, the total restructuring accrual consisted of the following (in thousands):

	Current	Non-Current	Total
Severance and termination benefits	$ 87	$ —	$ 87
Excess facilities	432	21	453
Total	$ 519	$ 21	$ 540

As of December 31, 2009 and September 30, 2009, $0.5 million and $0.4 million, respectively, of the restructuring reserve are included in the Accrued Expenses line item on the Condensed Consolidated Balance Sheets. The allocation between current portion and long term portion is based on the current lease agreements or the anticipated settlement dates.

The Company expects to pay the excess facilities amounts related to the restructured or vacated leased office space as follows (in thousands):

Fiscal Year Ended September 30,	Total Net Future Minimum Lease Payments
2010 (nine months remaining)	$ 331
2011	122
Total	$ 453

Included in the future minimum lease payments schedule above is an offset of $0.3 million of contractually committed sublease rental income.

Fiscal Year 2010 Restructuring

In the quarter-ended December 31, 2009, the Company initiated a restructuring plan, the 2010 Restructuring, intended to consolidate and reduce the size of our management team. This resulted in a reduction of headcount. As a result of the cost-cutting measure, the Company recorded a pre-tax cash restructuring charge in the first quarter of fiscal year 2010, of approximately $0.1 million for severance costs. The following table summarizes the activity related to the 2010 Restructuring (in thousands):

	Severance and Termination Benefits
Provision	$ 144
Cash paid	(57)
Reserve balance as of December 31, 2009	$ 87

Fiscal Year 2009 Restructuring

In October 2008, the Company initiated a restructuring plan, the 2009 Restructuring, intended to align its resources and cost structure with expected future revenues. The 2009 Restructuring plan includes reductions in headcount and third party consultants across all functional areas in both North America and Europe. The 2009 Restructuring plan includes a reduction of approximately 13% of the Company's permanent workforce. A significant portion of the positions eliminated were in North America.

As a result of the cost-cutting measures, the Company recorded a pre-tax cash restructuring charge in the first quarter of fiscal year 2009, of approximately $0.9 million, including $ 0.8 million for severance costs and $0.1 million for other contract termination costs. As of December 31, 2008, all payments had been made.

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	Severance and Benefits	Contract Termination Costs	Total
Provision	$ 758	$ 130	$ 888
Cash paid	(758)	(130)	(888)
Reserve balance as of December 31, 2008	$ —	$ —	$ —

Fiscal Year 2005 Restructuring

In May 2005, the Company undertook an approximate 10% reduction in our workforce. In connection with this action, the Company incurred a one-time cash expense of approximately $1.1 million in the fourth quarter ended September 30, 2005 for severance benefits. During the quarter ended March 31, 2007, the Company incurred an additional charge of less than $0.1 million for additional severance expense for an employee located in France. During the quarter ended December 31, 2008, the Company reversed the charge as we were not ultimately required to pay the severance expense to the employee.

The following table summarizes the activity related to the 2005 Restructuring (in thousands):

	Severance and Termination Benefits
Reserve balance as of September 30, 2008	$ 123
Provision adjustment	(104)
Non-cash	(19)
Cash paid	—
Reserve balance as of December 31, 2008	$ —

Prior Restructurings

During fiscal year 2002, based upon the Company's continued evaluation of economic conditions in the information technology industry and our expectations regarding revenue levels, the Company restructured several areas so as to reduce expenses and improve revenue per employee, or the 2002 Restructuring. As part of the 2002 Restructuring, the Company recorded a total workforce reduction expense relating to severance and termination benefits of approximately $2.0 million and $3.8 million for years ended December 31, 2003 and 2002, respectively. In addition to these costs, the Company accrued lease costs related to excess facilities of $0.2 million and $2.8 million during the years ended December 31, 2003 and 2002, respectively, pertaining to the consolidation of excess facilities relating to lease terminations and non-cancelable lease costs. This expense is net of estimated sublease income based on then current comparable rates for leases in the respective markets.

During the year ended September 30, 2007, the Company entered into a new sublease for the last remaining facility lease associated with the 2002 Restructuring. As a result of this sublease, rental income was lower than previously estimated as part of the restructure facility reserve, and the Company recorded an additional $0.4 million of

restructuring expense during the year ended September 30, 2007. The sublease term is through the entire remaining term of the Company's lease obligation for the facility.

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The following table summarizes the activity related to the 2002 Restructuring (in thousands):

	Excess Facilities
Reserve balance as of September 30, 2009	$ 531
Cash paid	(78)
Reserve balance as of December 31, 2009	$ 453

NOTE 6—COMPREHENSIVE INCOME (LOSS)

The components of comprehensive income (loss) are as follows (in thousands):

	Three Months Ended December 31,	
	2009	2008
Net loss	$ (972)	$ (2,669)
Other comprehensive loss:		
Change in foreign currency translation	(205)	(3,494)
Net change in unrealized gain from investments	7	—
Comprehensive loss	$ (1,170)	$ (6,163)

NOTE 7—BORROWINGS

Revolving Line of Credit

The Company’s revolving line of credit with Comerica Bank expires on June 7, 2010. The terms of the agreement include a $5.0 million line of credit, available on a non-formula basis, and requires the Company to (i) maintain at least a $5.0 million cash balance in Comerica Bank accounts, (ii) maintain a minimum quick ratio of 2 to 1, (iii) maintain a liquidity ratio of at least 1 to 1 at all times, and (iv) subordinate any debt issuances subsequent to the effective date of the agreement, and certain other covenants. All assets of the Company have been pledged as collateral on the credit facility. As of December 31, 2009, the Company is in compliance with all covenants of the revolving line of credit.

The revolving line of credit contains a provision for a sub-limit of up to $5.0 million for issuances of standby commercial letters of credit. As of December 31, 2009, the Company had utilized $0.1 million of the standby commercial letters of credit limit which serves as collateral for a leased facility. The revolving line of credit also contains a provision for a sub-limit of up to $3.0 million for issuances of foreign exchange forward contracts. As of December 31, 2009, the Company had not entered into any foreign exchange forward contracts. The Company is required to secure the standby commercial letters of credit and foreign exchange forward contracts through June 7, 2010. If these have not been secured to Comerica Bank’s satisfaction, the Company’s cash and cash equivalent balances held by Comerica Bank automatically secure such obligations to the extent of the then continuing or outstanding and undrawn letters of credit or foreign exchange contracts.

Borrowings under the revolving line of credit bear interest at the lending bank's prime rate. Except for the standby commercial letters of credit, as of December 31, 2009, there were no outstanding balances on the revolving line of credit.

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NOTE 8—COMMITMENTS AND CONTINGENCIES

Lease Commitments

The Company leases its facilities and certain equipment under non-cancelable operating leases that expire on various dates through 2014. Rent expense is recognized on a straight line basis over the lease term.

Future minimum lease payments as of December 31, 2009 are as follows (in thousands):

	Operating Leases	Operating Sublease Income	Net Operating Leases
Fiscal year ended September 30:			
2010 (remaining nine months)	$ 2,684	$ (196)	$ 2,488
2011	2,994	(86)	2,908
2012	2,201	—	2,201
2013	2,031	—	2,031
2014	351	—	351
Total minimum payments	$ 10,261	$ (282)	$ 9,979

Operating lease payments in the table above include approximately $0.7 million for our Boston, Massachusetts facility operating lease commitment included in Restructuring accrual. As of December 31, 2009, the Company has $0.3 million in sublease income contractually committed for future periods relating to this facility. See Note 5 for further discussions.

Asset Retirement Obligations

The Company recorded an Asset Retirement Obligation (ARO) of approximately $0.3 million and a corresponding increase in leasehold improvements in the fiscal year 2007. The FASB guidance requires the recognition of a liability for the fair value of a legally required conditional ARO when incurred, if the liability's fair value can be reasonability estimated. The fair value of the liability is added to the carrying amount of the associated asset and this additional carrying amount is amortized over the life of the asset.

The Company's ARO is associated with commitments to return property subject to operating leases to original condition upon lease termination. As of December 31, 2009, the Company estimated that gross expected cash flows of approximately $0.3 million will be required to fulfill these obligations.

ARO payments as of December 31, 2009 are included in Other Long-term Liabilities in the Condensed Consolidated Balance Sheets and are estimated as follows (in thousands):

	Payments
Fiscal year ended September 30:	
2010	$ —
2011	145

2012		172
Total	$	317

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Other Obligations

In 2003, the Company entered into an agreement with Ness Technologies Inc., Ness USA, Inc. (formerly Ness Global Services, Inc.) and Ness Technologies India, Ltd. (collectively, "Ness") and in January 2009, the Company and Ness extended the Ness agreement through December 31, 2011. Pursuant to the Ness agreement, Ness provides the Company's customers with technical product support through a worldwide help desk facility, a sustaining engineering function that serves as the interface between technical product support and internal engineering organization, product testing services, product development services and certain other identified technical and consulting services (collectively, the "Services"). Under the terms of the Ness agreement, the Company pays for services rendered on a monthly fee basis and reimbursement of approved out-of-pocket expenses. If the Company had terminated the Ness agreement for convenience prior to December 31, 2009, it would have been required to pay a termination fee no greater than $0.5 million, however this cancellation penalty lapsed at December 31, 2009. The Company also had guaranteed certain equipment lease obligations of Ness for equipment acquired by Ness to be used in performance of the Services, either through leasing arrangements or direct cash purchases, for which the Company was obligated under the agreement to reimburse Ness. In 2006, Ness entered into a 36 month equipment lease agreement with IBM India and, in connection with the lease agreement the Company had an outstanding standby letter of credit to guarantee Ness' financial commitments under the lease. During the quarter ended June 30, 2009, the lease expired and the Company no longer has an obligation to reimburse Ness.

Indemnification

As permitted under Delaware law, the Company enters into indemnification agreements pursuant to which the Company is obligated to indemnify certain of its officers, directors and employees for certain events or occurrences while the officer, director or employee is, or was, serving at the Company's request in such capacity. The Company's Bylaws similarly provide for indemnification of its officers, directors and employees under certain circumstances to the maximum extent permitted under Delaware law. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements and arrangements is unlimited; however, the Company has a Director and Officer insurance policy that limits the Company's exposure and may enable the Company to recover a portion of any future amounts paid. As a result of insurance policy coverage, the Company believes the estimated fair value of these indemnification agreements and arrangements is minimal. Accordingly, the Company has no liabilities recorded for these agreements or arrangements as of December 31, 2009.

The Company enters into standard agreements with indemnification provisions in its ordinary course of business. Pursuant to these agreements, the Company agrees to indemnify, defend, hold harmless, and/or reimburse the indemnified party for losses suffered or incurred by the indemnified party, generally the Company's customers or business partners, in connection with any patent, copyright or other intellectual property infringement claim by any third party with respect to the Company's products. The term of these agreements is generally perpetual after execution of the agreement. The maximum potential amount of future payments the Company could be required to make under these agreements is unlimited. The Company has not incurred significant costs to defend lawsuits or settle claims related to these agreements. The Company believes the estimated fair value of these agreements is minimal. Accordingly, the Company has no liabilities recorded for these agreements as of December 31, 2009.

The Company may, at its discretion and in the ordinary course of business, enter into arrangements, generally with the Company's customers or business partners, whereby the Company agrees to indemnify them for certain acts, such as

personal property damage, by the Company. The Company may also enter into arrangements with the Company's business partners whereby the business partners agree to provide services as subcontractors for the Company's implementations. Accordingly, the Company enters into standard agreements with its customers whereby the Company agrees to indemnify them for certain acts, such as personal property damage, by subcontractors. The maximum potential amount of future payments the Company could be required to make under these agreements is unlimited; however, the Company has general and umbrella insurance policies that may enable the Company to recover a portion of any amounts paid. The Company has not incurred significant costs to defend lawsuits or settle claims related to these agreements. As a result, the Company believes the estimated fair value of these agreements is minimal. Accordingly, the Company has no liabilities recorded for these agreements as of December 31, 2009.

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When, as part of an acquisition, the Company acquires all of the stock or all of the assets and liabilities of a company, the Company may assume the liability for certain events or occurrences that took place prior to the date of acquisition. The maximum potential amount of future payments, if any, the Company could be required to make for such obligations is undeterminable at this time. Accordingly, the Company has no amounts recorded for these contingent liabilities as of December 31, 2009.

The Company warrants that its software products will perform in all material respects in accordance with standard published specifications and documentation in effect at the time of delivery of the licensed products to the customer for a specified period of time. Additionally, the Company warrants that maintenance and consulting services will be performed consistent with generally accepted industry standards. If necessary, the Company would account for the estimated cost of product and service warranties based on specific warranty claims and claim history, however, the Company has not incurred significant expense under product or services warranties to date. As a result, the Company believes the estimated fair value of these warranties is minimal. Accordingly, the Company has no amounts recorded for these contingent liabilities as of December 31, 2009.

NOTE 9—LITIGATION

IPO Laddering

Beginning in July 2001, the Company and certain of its officers and directors (“Individuals”) were named as defendants in a series of class action stockholder complaints filed in the United States District Court for the Southern District of New York, now consolidated under the caption “In re Chordiant Software, Inc. Initial Public Offering Securities Litigation, Case No. 01-CV-6222.” In the amended complaint, filed in April 2002, the plaintiffs allege that the Company, the Individuals, and the underwriters of the Company’s initial public offering (“IPO”), violated Section 11 of the Securities Act of 1933, as amended (“Securities Act”), and Section 10(b) of the Securities Exchange Act of 1934, as amended (“Exchange Act”), based on allegations that the Company’s registration statement and prospectus failed to disclose material facts regarding the compensation to be received by, and the stock allocation practices of, the Company’s IPO underwriters. The complaint also contains claims against the Individuals for control person liability under Securities Act Section 15 and Exchange Act Section 20. The plaintiffs seek unspecified monetary damages and other relief. Similar complaints were filed in the same court against hundreds of other public companies that conducted IPO’s of their common stock in the late 1990’s or in the year 2000 (collectively, the “IPO Lawsuits”).

On February 25, 2009, liaison counsel for plaintiffs informed the district court that a settlement of the IPO Lawsuits had been agreed to in principle, subject to formal approval by the parties and preliminary and final approval by the court. On April 2, 2009, the parties submitted a tentative settlement agreement to the court and moved for preliminary approval thereof.

On June 11, 2009, the Court granted preliminary approval of the tentative settlement, ordered that Notice of the settlement be published and mailed, and set a Final Fairness Hearing for September 10, 2009. On October 6, 2009, the District Court certified the settlement class in each IPO Case and granted final approval of the settlement. On or about October 23, 2009, three shareholders filed a Petition for Permission To Appeal Class Certification Order, challenging the District Court’s certification of the settlement classes. Beginning on October 29, 2009, a number of shareholders filed direct appeals, objecting to final approval of the settlement. If the settlement is affirmed on appeal, the settlement will result in the dismissal of all claims against the Company and its officers and directors with

prejudice, and the Company's pro rata share of the settlement fund will be fully funded by insurance.

Yue vs. Chordiant Software, Inc.

On January 2, 2008, the Company and certain of its officers and one other employee were named in a complaint filed in the United States District Court for the Northern District of California by Dongxiao Yue under the caption "Dongxiao Yue v. Chordiant Software, Inc. et al. Case No. CV 08-0019 (N.D. Cal.)". The complaint alleged that the Company's Marketing Director ("CMD") software product infringed copyrights in certain software referred to as the "PowerRPC software," copyrights that had been owned by Netbula LLC and assigned to Mr. Yue, the owner of Netbula. On July 23, 2008, the Court issued an order that granted one employee's motion to dismiss for lack of personal jurisdiction, with prejudice, and granted, with leave to amend, the Company's motion to dismiss, ruling that Mr. Yue's company, Netbula LLC, is the real party in interest and must appear through counsel.

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On September 9, 2008, plaintiffs Yue and Netbula LLC filed a First Amended Complaint asserting four causes of action relating to the Company's alleged unauthorized use and distribution of plaintiffs' PowerRPC software: claims for copyright infringement, unfair competition, and "accession and confusion of property" against the Company, and a claim for vicarious copyright infringement against the Company's Chief Executive Officer and its former Vice President, General Counsel and Secretary (the "individual defendants"). On September 20, 2008, the parties filed a stipulation allowing plaintiffs to file a Second Amended Complaint dropping the unfair competition and accession and confusion claims. On November 10, 2008, the Company answered the Second Amended Complaint and asserted various affirmative defenses, including that the plaintiffs' claims are barred by the existence of an express or implied license from the plaintiffs. Also on November 10, 2008, the individual defendants filed a motion to dismiss, which the Court granted with leave to amend on March 20, 2009. Plaintiffs filed a Third Amended Complaint on April 6, 2009.

On May 29, 2009, as stipulated by the parties, the Court allowed plaintiffs to file a Fourth Amended Complaint to include allegations about the Company's use in CMD of a different, additional Netbula product—JavaRPC—an implementation of ONC RPC for Java. Plaintiffs filed the Fourth Amended Complaint on May 29, 2009, and the Company and the individual defendants answered on June 15, 2009. The Fourth Amended Complaint alleges that the Company infringed Plaintiffs' copyrights by using PowerRPC and JavaRPC in the development and distribution of CMD, without the required licenses from Netbula. The Fourth Amended Complaint seeks monetary damages, an accounting of profits, and injunctive relief according to proof.

On July 9, 2009, the Court found triable issues about whether the Company held a license in PowerRPC, and accordingly denied the Company's motion for summary judgment as to that issue.

On October 30, 2009, both fact and expert discovery closed.

On November 9, 2009, as stipulated by the parties, the Court ordered the dismissal of the Company's Chief Executive Officer from the case, leaving only one remaining individual defendant, the Company's former general counsel, Mr. Derek Witte. On December 21, 2009, the Court granted Mr. Witte's motion for summary judgment, finding that he was not vicariously liable for the Company's alleged infringement.

Also on December 21, 2009 the court granted the Company's Motion for Summary Judgment as to Statutory Damages and Plaintiffs' Attorneys' Fees, ruling that Defendants are not entitled to recover statutory damages or attorneys' fees under the Copyright Act. In addition, the court granted the Company's motion for summary adjudication regarding the Company's status as a reseller, declaring that the Company, as a reseller for Chordiant Software International, Ltd., has the same distribution rights as its subsidiary under Netbula's licenses. Plaintiffs have moved for reconsideration of that ruling. In that same Order, the Court also denied plaintiffs' motion for summary judgment as to infringement of the copyrights in JavaRPC, finding triable issues of fact as to whether plaintiffs' copyrights are valid, and as to whether Chordiant held a license to JavaRPC.

The Court has set a final pretrial conference for March 22, 2010. Trial is scheduled for April 2010, with Jury selection set for April 6, 2010, trial sessions set for April 7-9 and April 13-16, closing arguments set for April 20, 2010, and jury deliberation set for April 21-23, 2010.

The Company cannot predict the outcome or provide an estimate of any possible losses. The Company will continue to vigorously defend itself against the claims in these actions.

This action may divert the efforts and attention of our management and, if determined adversely to us, could have a material impact on our business, results of operations, financial condition or cash flows.

The Company, from time to time, is also subject to various other claims and legal actions arising in the ordinary course of business. The ultimate disposition of these various other claims and legal actions is not expected to have a material effect on our business, financial condition, results of operations or cash flows. However, litigation is subject to inherent uncertainties.

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NOTE 10—INCOME TAXES

The Company's provision for income taxes was $0.5 million and $1.7 million for the quarter ended December 31, 2009 and 2008, respectively. The $1.2 million decrease in income taxes is primarily due to a decrease in non-cash tax expense in our UK subsidiary and a decrease in unrecoverable withholding tax payments related to sales transactions in India and Turkey compared to quarter ended December 31 2008.

Of the total $0.5 million of provision recognized in quarter ended December 31, 2009, a significant portion was related to a non-cash deferred tax expense for the recognition of taxable income in the United Kingdom. The remainder of the Company's provision is attributable to taxes on earnings from the Company's foreign subsidiaries, unrecoverable withholding taxes related to sales transactions that occurred in India and Turkey and a federal and research development tax refund benefit.

At September 30, 2009, the Company had $1.0 million of unrecognized tax benefits related to tax positions taken in prior periods, $0.5 million of which would affect the Company's effective tax rate if recognized. As of December 31, 2009, the Company had gross unrecognized tax benefits of $1.1 million.

The Company recognizes accrued interest and penalties related to unrecognized tax benefits in the Provision for Income Taxes. The Company had less than $0.1 million accrued for interest and penalties as of December 31, 2009.

The Company files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. With few exceptions, all U.S. federal, state and United Kingdom tax years between 1995 and 2008 remain open to examination due to net operating loss carryforwards and credit carryforwards. Tax years 2003 and later remain open to examination in Canada and years 2004 and later remain open to examination in Germany.

At December 31, 2009, the Company has $74.3 million in gross deferred tax assets (DTAs) attributable principally to net operating losses (NOLs) and to a lesser extent temporary differences relating to deferred revenue. Historically, the Company maintained a 100% valuation allowance on DTAs because it previously was unable to conclude that it is more-likely-than-not that it will realize the tax benefits of these DTAs. Based on recent operating results and the reorganization of the Company's intellectual property into the U.S., current projections of disaggregated future taxable income has enabled the Company to conclude that it is more-likely-than-not that it will have future taxable income sufficient to realize $4.7 million of tax benefits from its deferred tax assets, which consist of that portion of net deferred tax assets attributable to net operating losses (NOLs) residing in the United Kingdom. On September 30, 2008, the Company had released (eliminated) $10.0 million of the valuation allowance on its DTAs related to the United Kingdom, of which $9.5 million was recognized as an offsetting reduction to goodwill (representing pre-acquisition NOLs) and $0.5 million was recognized as a credit (reduction) to the provision for income taxes. In future periods, the Company expects to incur tax expense related to the United Kingdom which will result in an increase in overall expense; however, to the extent that such tax expense is offset by the utilization of NOLs and capital allowances, the recognition of this additional tax expense will be a non-cash item.

The remaining balance of gross deferred tax assets was generated in the U.S. With respect to U.S. generated deferred tax assets, the Company recorded a full valuation allowance as the future realization of the tax benefit is not considered by management to be more likely than not. The Company's estimate of future taxable income considers available positive and negative evidence regarding current and future operations, including projections of income in

various states and foreign jurisdictions. The Company believes the estimate of future taxable income is reasonable; however, it is inherently uncertain, and if future operations generate taxable income greater than projected, further adjustments to reduce the valuation allowance are possible. Conversely, if the Company realizes unforeseen material losses in the future, or the ability to generate future taxable income necessary to realize a portion of the net deferred tax asset is materially reduced, additions to the valuation allowance could be recorded. At December 31, 2009 and September 30, 2009, the balance of deferred tax valuation allowance was approximately $69.6 million.

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Under the Tax Reform Act of 1986, the amounts of, and the benefit from, net operating losses that can be carried forward may be impaired or limited in certain circumstances. Under Section 382 of the Internal Revenue Code (IRC), as amended, a cumulative stock ownership change of more than 50% over a three-year period can cause such limitations. The Company has analyzed its historical ownership changes and removed any net operating loss carryforwards that will expire unutilized from its deferred tax balances as a result of an IRC 382 limitation. On September 30, 2009, the Company had federal research and development tax credit carryforwards of approximately $3.8 million. Due to Section 382 ownership changes under IRC Section 383, $2.1 million of the federal research tax credit carryforwards were subject to annual limitations and is expected to expire unutilized.

On September 30, 2009, the Company had net operating loss carryforwards for federal and state income tax purposes of approximately $144.3 million and $36.2 million, respectively. Approximately $18.1 million of the federal net operating loss carryforwards represent net operating loss carryforwards related to the acquisition of Prime Response in 2001. In addition to the federal and state net operating loss carryforwards, the Company has approximately $13.6 million of net operating loss carryforwards that are generated in the United Kingdom, none of which will expire. Approximately $4.3 million of additional net operating loss carryforwards are related to stock option deductions which, if utilized, will be accounted for as an addition to equity rather than as a reduction of the provision for income taxes. These carryforwards are available to offset future federal and state taxable income and expire in fiscal years 2011 through 2029 and 2010 through 2029, respectively. At September 30, 2009, there were approximately $1.8 million of federal research and development credits that expire in 2025 through 2029. For the year-ended September 30, 2009, there were also California state credits of approximately $4.0 million of which $3.9 million do not expire.

On September 23, 2008, the state of California enacted tax legislation on the utilization of net operating losses and credit limitations. Effective fiscal year 2009, any California net operating losses that the Company generates will have a 20 year carryforward period and effective for fiscal year ended 2012, will have a two year carryback period. In addition, for fiscal year 2009 through fiscal year 2010, the Company will be unable to utilize California net operating losses as they are being temporarily disallowed as a result of this legislation. This may give rise to tax expense for any such taxable income rising out of the disallowable 2 year period. Any disallowed California net operating losses that cannot be utilized during the disallowed period will be extended by two years. For fiscal year 2012, the carryback amount cannot exceed 50% of the net operating loss, for fiscal year 2013, the carryback cannot exceed 75% of the net operating loss, and for fiscal year 2014, the carryback cannot exceed 100% of the net operating loss. For the year ended September 30, 2009, the Company generated $3.7 million of additional net operating losses in California which will expire in 2029.

Effective fiscal year 2009, California business tax credits will be limited to 50% of the Company’s tax liability. The carryover period for disallowed credit will be extended by the number of tax years that the credit was disallowed.

At September 30, 2009, the Company has not provided for U.S. federal and state income taxes on foreign earnings which are expected to be invested outside of the U.S. indefinitely. Upon distribution of those earnings, the Company will be subject to U.S. income taxes (subject to a reduction of the foreign tax credit) and withholding taxes payable to the foreign countries where the foreign operations are located, if any.

NOTE 11—EMPLOYEE BENEFIT PLANS AND STOCK-BASED COMPENSATION

2005 Equity Incentive Plan

As of December 31, 2009, there were approximately 1.8 million shares available for future grant and approximately 4.8 million options and RSUs that are outstanding under the 2005 Equity Incentive Plan or 2005 Plan.

2000 Nonstatutory Equity Incentive Plan

As of December 31, 2009, there were approximately 0.3 million options that are outstanding under the 2000 Nonstatutory Equity Incentive Plan.

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1999 Non-Employee Directors' Option Plan

As of December 31, 2009, there were approximately 0.1 million shares of common stock are available for future grant and 0.2 million options that are outstanding under the 1999 Non-Employee Directors' Option Plan or Directors' Plan. In the quarter ended December 31, 2009, the Board amended the Directors' Plan to increase the number of shares reserved for future issuance by 0.1 million shares. This amendment was approved by the stockholders at the 2010 Annual Meeting of Stockholders held on January 27, 2010.

Shareholder Rights Plan

On July 7, 2008, the Board of Directors adopted the Shareholder Rights Plan. See Note 12 to the 2008 Form 10-K filed with the SEC for more detailed information. In conjunction with the adoption of the Shareholder Rights Plan, the Company submitted a non-binding proposal to the Company's stockholders to approve that plan, to be voted upon at the 2009 Annual Meeting of Stockholders. On January 28, 2009, at the 2009 Annual Meeting of Stockholders, the stockholders did not approve the non-binding proposal. As discussed in the Company's 2008 Proxy Statement, if the Company's stockholders did not support the non-binding proposal, the Board committed to reconsider whether to terminate the Shareholders Rights Plan and redeem the rights issued thereunder.

On November 18, 2009, the Board, after deliberations spanning over multiple Board meetings since the 2009 Annual Meeting of Stockholders, and with the input of its outside legal and financial advisors, determined not to terminate the Shareholder Rights Plan, or redeem the rights issued thereunder, at this time. The Shareholder Rights Plan (and the rights issued thereunder) is scheduled to expire on July 21, 2011. The Board considered the non-binding stockholder vote and the current environment relating to shareholder rights plans generally and balanced those factors against the short life of the Company's Shareholder Rights Plan, the current increase in unsolicited and unfavorable acquisition proposals in the marketplace, particularly at a time when stock prices continue to experience downward pressure, increased hostile activity, and the overall effectiveness of such plans in requiring a potential acquirer to negotiate in good faith with the board so that the board may use its business judgment and exercise its fiduciary duties to its stockholders to obtain the highest possible price for the company. The Board also considered that shareholder rights plans do not prevent legitimate offers from being made. The Board has and will continue to use its business judgment and to exercise its fiduciary duties, and continue to consider all reasonable acquisition proposals.

Finally, the members of the Board made this decision with the knowledge that in doing so, certain corporate governance organizations would recommend "withhold" votes on them when they stood for reelection.

Stock Option Activity

The following table summarizes stock option activity under our stock option plans (in thousands, except per share data):

		Outstanding		
	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual	Aggregate Intrinsic Value Closing

				Life (Years)		Price at 12/31/2009 of $2.76
Balance at September 30, 2009	3,694	$	6.82			
Granted	690		2.87			
Options exercised	(14)		1.98			
Options cancelled/forfeited	(94)		6.75			
Balance at December 31, 2009	4,276	$	6.20	6.06	$	314
Vested and expected to vest at December 31, 2009	3,974	$	6.36	5.97	$	301
Exercisable at December 31, 2009	2,610	$	7.12	5.54	$	181

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The following table summarizes information about stock options outstanding and exercisable at December 31, 2009 (in thousands, except exercise prices and contractual life data):

	Options Outstanding				Options Exercisable		
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Aggregate Intrinsic Value Closing Price at 12/31/2009 of $2.76	Number Exercisable	Weighted Average Exercise Price	Aggregate Intrinsic Value Closing Price at 12/31/2009 of $2.76
$0.35 – 2.32	653	3.71	$ 2.30	$ 299	353	$ 2.29	$ 166
2.50 – 2.87	745	6.89	2.83	15	75	2.57	15
2.98 – 4.90	517	6.13	4.17	—	322	4.21	—
4.95 – 7.65	430	5.33	6.72	—	375	6.81	—
7.68 – 8.13	423	5.87	7.97	—	406	7.97	—
8.25 – 8.28	547	7.05	8.25	—	423	8.25	—
8.35 – 9.25	613	7.49	9.13	—	368	9.06	—
9.26 – 45.00	348	5.66	12.56	—	288	12.53	—
$0.35 – 45.00	4,276	6.06	$ 6.20	$ 314	2,610	$ 7.12	$ 181

The aggregate intrinsic value in the preceding table represents the total intrinsic value, based on the Company's closing stock price of $2.76 as of December 31, 2009, which would have been received by the option holders had all option holders exercised their options as of that date. The total intrinsic value of options exercised during the three months ended December 31, 2009 and 2008 was less than $0.1 million for both periods. As of December 31, 2009, total unrecognized compensation costs related to non-vested stock options was $3.0 million, which is expected to be recognized as expense over a weighted-average period of approximately 2.4 years. As of December 31, 2008, total unrecognized compensation costs related to non-vested stock options was $5.9 million, which is expected to be recognized as expense over a weighted-average period of approximately 2.3 years.

Stock Award Activity

Non-vested stock awards are comprised of restricted stock awards and restricted stock units. The following table summarizes the stock award activity (in thousands, except per share data):

Non-vested Stock Awards	RSAs	RSUs	Total Number of Shares Underlying Awards	Weighted Average Grant Date Fair Value
Non-vested balance at September 30, 2009	90	588	678	$ 2.48
Awarded	—	455	455	2.87
Vested/Released	—	(140)*	(140)*	2.32

Forfeited	—	(56)	(56)	2.38
Non-vested balance at December 31, 2009	90	847	937	$ 2.70

*The RSUs released to employees require a two year holding period.

The aggregate intrinsic value of unvested RSAs based upon the Company's closing price of $2.76 as of December 31, 2009 was $0.2 million. As of December 31, 2009, total unrecognized compensation costs related to unvested RSAs was less $0.1 million which is expected to be recognized as expense over a weighted average period of approximately 1 month.

On January 27, 2010, the Company's Board members were granted 90,000 shares of RSAs for their annual service awarded under the Directors' Plan. These grants are excluded from the preceding table.

The aggregate intrinsic value of RSUs based upon the Company's closing price of $2.76 as of December 31, 2009 was $2.3 million. As of December 31, 2009, total unrecognized compensation costs related to unvested RSUs was $1.5 million which is expected to be recognized as expense over a weighted average period of approximately 3.0 years.

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The Company settles stock option exercises, RSAs and RSUs with newly issued common shares.

Valuation and Expense Information under SFAS 123(R)

On October 1, 2005, the Company adopted a FASB standard, which requires the measurement and recognition of compensation expense for all share-based payment awards made to the Company's employees and directors including employee stock options, RSAs, and RSUs based on estimated fair values. The following table summarizes stock-based compensation expense related to employee stock options, RSAs, and RSUs for the three months ended December 31, 2009 and 2008, respectively, which was allocated as follows (in thousands):

	Three Months Ended December 31,	
	2009	2008
Stock-based compensation expense:		
Cost of revenues	$ 162	$ 134
Sales and marketing	162	256
Research and development	90	109
General and administrative	475	466
Total stock-based compensation expense	$ 889	$ 965

The weighted-average estimated fair value of stock options granted during the three months ended December 31, 2009 and 2008 was $1.44 and $1.18 per share, respectively, using the Black-Scholes model with the following weighted-average assumptions:

	Three Months Ended December 31,	
	2009	2008
Expected lives in years	3.8	2.8
Risk free interest rates	1.6%	1.6%
Volatility	68%	62%
Dividend yield	0%	0%

The fair value of each option award is estimated on the date of grant using the Black-Scholes option valuation model with the weighted-average assumptions for volatility, expected term, and risk free interest rate. The Company used the trinomial lattice valuation technique to determine the assumptions used in the Black-Scholes model. The trinomial lattice valuation technique was used to provide a better estimate of fair values and meet the fair value objectives of the FASB standard. The expected term of options granted is derived from historical data on employee exercises and post-vesting employment termination behavior. The risk-free rate is based on the U.S. Treasury rates in effect during the corresponding period of grant. The expected volatility rate is based on the historical volatility of our stock price.

Stock-based compensation expense recognized in the Condensed Consolidated Statement of Operations for the three months ended December 31, 2009 and 2008 is based on awards ultimately expected to vest and has been reduced for estimated forfeitures. The FASB standard requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Our estimated forfeiture rate for the three months ended December 31, 2009 and 2008 was based on our historical forfeiture experience.

Accuracy of Fair Value Estimates

The Company uses available information including third-party analyses to assist in developing the fair value assumptions based on a trinomial lattice valuation technique used in the Black-Scholes model. The Company is responsible for determining the assumptions used in estimating the fair value of share-based payment awards.

Our determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by the Company’s stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to the Company’s expected stock price volatility over the term of the

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awards, and actual and projected employee stock option exercise behaviors. Because the Company's stock options have certain characteristics that are significantly different from traded options, and because changes in the subjective assumptions can materially affect the estimated value, in management's opinion, the existing valuation models may not provide an accurate measure of the fair value of the Company's stock options, RSAs, and RSUs. Although the fair value of stock options, RSAs, and RSUs is determined in accordance with a FASB and an SEC Staff Accounting Bulletin standard using an option-pricing model, that value may not be indicative of the fair value observed in a willing buyer/willing seller market transaction.

NOTE 12—SEGMENT INFORMATION

Our chief operating decision maker reviews financial information presented on a consolidated basis, accompanied by desegregated information about revenues by geographic regions for purposes of making operating decisions and assessing financial performance. Accordingly, the Company has concluded that the Company has one reportable segment.

The following table summarizes license revenue by product emphasis (in thousands):

	Three Months Ended December 31,	
	2009	2008
License revenue:		
Enterprise Foundation solutions	$ 2,808	$ 1,544
Marketing Director solutions	332	2,381
Decision Management solutions	4,292	4,016
Total	$ 7,432	$ 7,941

The following table summarizes service revenue consisting of consulting implementation and integration, consulting customization, training, PCS, and certain reimbursable out-of-pocket expenses by product emphasis (in thousands):

	Three Months Ended December 31,	
	2009	2008
Service revenue:		
Enterprise Foundation solutions	$ 8,471	$ 9,662
Marketing Director solutions	2,254	2,951
Decision Management solutions	4,067	2,823
Total	$ 14,792	$ 15,436

Foreign revenues are based on the country in which the customer order is generated. The following is a summary of total revenues by geographic area (in thousands):

	Three Months Ended December 31,	
	2009	2008
United States	$ 7,077	$ 8,083
EMEA:		

United Kingdom	11,697	6,132
Germany	2,473	3,636
Other EMEA	977	5,526
Total EMEA	15,147	15,294
Total	$ 22,224	$ 23,377

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Net property and equipment information is based on the physical location of the assets. The following is a summary of property and equipment by geographic area (in thousands):

	December 31 2009	September 30, 2009
United States	$ 1,164	$ 1,313
EMEA:		
United Kingdom	308	343
Other EMEA	166	194
Total EMEA	474	537
Total	$ 1,638	$ 1,850

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

This discussion and analysis should be read in conjunction with our Condensed Consolidated Financial Statements and accompanying Notes included in this report and the 2009 Audited Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the year ended September 30, 2009 filed with the SEC. Operating results are not necessarily indicative of results that may occur in future periods.

The following discussion and analysis contains forward-looking statements. These statements are based on our current expectations, assumptions, estimates and projections about our business and our industry, and involve known and unknown risks, uncertainties and other factors that may cause our or our industry's results, levels of activity, performance or achievement to be materially different from any future results, levels of activity, performance or achievements expressed or implied in or contemplated by the forward-looking statements. Words such as "believe," "anticipate," "expect," "intend," "plan," "will," "may," "should," "estimate," "predict," "guidance," "potential," "continue" or such terms or other similar expressions, identify forward-looking statements. Our actual results and the timing of events may differ significantly from those discussed in the forward-looking statements as a result of various factors, including but not limited to, those discussed under the subheading "Risk Factors" and those discussed elsewhere in this report, in our other SEC filings and under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our 2009 Form 10-K. Chordiant undertakes no obligation to update any forward-looking statement to reflect events after the date of this report.

Overview

We generate substantially all of our revenues from the insurance, healthcare, telecommunications, financial services and retail markets. Our customers typically fund purchases of our software and services out of their lines of business and information technology budgets. As a result, our revenues are heavily influenced by our customers' long-term business outlook and willingness to invest in new enterprise information systems and business applications.

Our business, like other businesses, has been impacted and continues to be impacted by the global economic recession. Unprecedented market conditions include illiquid credit markets, volatile equity markets, and dramatic fluctuations in foreign currency rates and economic recession, all of which have adversely impacted our business.

Our operations and performance depend on our customers having adequate resources to purchase our products and services. The unprecedented turmoil in the credit markets and the global economic downturn generally adversely impacts our customers and potential customers. These economic conditions have not shown significant improvement despite government intervention globally, and may remain volatile and uncertain for the foreseeable future. Customers may alter their purchasing activities in response to a lack of credit, economic uncertainty and concern about the stability of markets in general, and these customers may reduce, delay or terminate purchases of our products and services or other sales activities that affect purchases of our products and services. If we are unable to adequately respond to changes in demand resulting from unfavorable economic conditions, our financial condition and operating results may be materially and adversely affected.

Several of our current and prior customers have recently merged with others, been forced to raise significant levels of new capital, or received funds and/or equity infusions from regulators or governmental entities. This list of companies is extensive and includes Wachovia Corporation, AIG, Halifax Bank of Scotland, Royal Bank of Scotland, Barclays, and Lloyds. The impact of these transactions on our near term business is uncertain. Customers who have recently reorganized, merged or face new regulations may delay or terminate their software purchasing decisions, and an acquired or merged entity may lose the ability to make such purchasing decisions, resulting in declines in our bookings, revenues and cash flows. Alternatively, merged customers may expand the use of our software across the

larger entity resulting in opportunities for us to sell additional software and services.

For the three months ended December 31, 2009, we recorded revenue of $22.2 million, a decrease of $1.2 million or 5% from the three months ended December 31, 2008. We incurred a net loss of $1.0 million and ended the quarter with over $52.3 million in cash, cash equivalents, and marketable securities as compared to $49.9 million at September 30, 2009. We generated cash from operating activities of $2.8 million.

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Total revenue for the three months ended December 31, 2009 increased $7.0 million or 46% from the three months ended September 30, 2009. The increase in license revenue was $5.4 million, as we had a higher number of transactions at a higher average price than for the comparable period. Service revenue increased $1.6 million for the three months ended December 31, 2009 as compared to the three months ended September 31, 2009. The increase in service revenue was primarily composed of increases of $1.3 million in consulting revenue, $0.1 million in training revenue, and $0.3 million in support and maintenance revenue offset by a decrease of less than $0.1 million in expense reimbursement revenue.

Software Industry Consolidation and Possible Increased Competition

Our business strategy includes pursuing opportunities to grow our business, both through internal growth and through merger, acquisition and technology and other asset transactions. To implement this strategy, we may be involved in merger and acquisition activity and additional technology and asset purchase transactions of other software companies. During the quarter ended December 31, 2009, we purchased 1.95 million shares of SWK Holding Corporation (formerly Kana Software, Inc.) for approximately $1.7 million. These purchases were associated with the attempted, but unsuccessful, acquisition of the Company.

The enterprise software industry continues to undergo consolidation in sectors of the software industry in which we operate. IBM, SAP, Oracle and Sun Microsystems have made numerous acquisitions in the industry and Oracle has entered into an agreement to acquire Sun Microsystems, subject to certain regulatory approvals. While we do not believe that the companies acquired by IBM, SAP and Oracle have been significant competitors of Chordiant in the past, these acquisitions may indicate that we may face increased competition from larger and more established entities in the future.

Financial Trends

Backlog. As of December 31, 2009 and 2008, we had approximately $44.1 million and $55.6 million in backlog, respectively, which we define as contractual commitments made by our customers through purchase orders or contracts. Backlog is comprised of:

- software license orders for which the delivered products have yet not been accepted by customers or have not otherwise met all of the required criteria for revenue recognition. This component includes billed amounts classified as deferred revenue;

- contractual commitments received from customers through purchase orders or contracts that have yet to be delivered;

- deferred revenue from customer support contracts; and

- consulting service orders representing the unbilled remaining balances of consulting contracts not yet completed or delivered, plus deferred consulting revenue where we have not otherwise met all of the required criteria for revenue recognition. Consulting service orders that have expired are excluded from backlog.

The $11.5 million decline in total backlog over the past fiscal year is due to declines of approximately $7.1 million, $0.2 million and $4.2 million in the areas of software licenses, customer support contracts and professional services consulting contracts, respectively. Backlog declined sequentially for six of the past eight fiscal quarters but has increased in the two most recent quarters. The declines in backlog are due to revenue on previously signed transactions being recognized at a faster pace than new transactions are being consummated. Each category of backlog

has also been impacted by recent foreign exchange rate changes, as significant portions of the underlying balances are denominated in Euros or in Pounds Sterling.

The year over year decline in backlog and the associated deferred revenue balances will adversely affect revenues in future periods and our ability to forecast future revenues will be diminished. Because our backlog has declined, the financial results of future periods will be more dependent upon the signing of new transactions. Accordingly, the level of future revenues will be less predictable. If average quarterly aggregate bookings remain at the $16.0 million levels achieved during the past twelve months, future losses will be incurred unless operating expenses are further reduced.

With respect to the year over year decline in the backlog of professional service consulting contracts, as some customers recently delayed or canceled projects, statements of work for professional services either expired unutilized or were canceled. For the three months ended December 31, 2009 these items aggregated $0.2 million and were removed from backlog at the date of the expiration or cancellation. While additional significant cancelations are not contemplated, such events could cause further declines.

Backlog is not necessarily indicative of revenues to be recognized in a specified future period. There are many factors that would impact Chordiant's conversion of backlog as recognizable revenue, such as Chordiant's progress in completing projects for its customers, Chordiant's customers' meeting anticipated schedules for customer-dependent deliverables and customers increasing the scope or duration of a contract causing license revenue to be deferred for a longer period of time.

A significant portion of our revenues have been derived from large customer transactions. For some of these transactions, the associated professional services provided to the customer can span over a period greater than one year. If the services delivery period is over a prolonged period of time, it will cause the associated backlog of services to be recognized as revenue over a similar period of time. Chordiant provides no assurances that any portion of its backlog will be recognized as revenue during any fiscal year or at all, or that its backlog will be recognized as revenues in any given period. In addition, it is possible that customers from whom we expect to derive revenue from backlog will default and, as a result, we may not be able to recognize expected revenue from backlog.

Implementation by Third Parties. Over time, as our Enterprise Foundation products mature and system integrators become more familiar with our products, our involvement with implementations has diminished on some projects. If this trend continues to evolve, certain agreements with customers may transition from a contract accounting model to a more traditional revenue model whereby revenues are recorded upon delivery.

Service Revenues. Service revenues as a percentage of total revenues were 67% and 66% for the three months ended December 31, 2009 and 2008, respectively. We have shifted our sales force focus more towards our Decisioning Management solutions rather than our Enterprise Foundation solutions due to the current economic climate. The magnitude of professional services required to implement Decisioning Management solutions is much lower and performed in a shorter period of time than our Enterprise Foundation solutions, and as such, we expect our professional service revenue to decrease as we sell more of our Decisioning Management solutions. While the composition of revenue will continue to fluctuate on a quarterly basis, we expect that service revenues will represent between 60% and 75% of our total annual revenues in the foreseeable future.

Revenues from International Customers versus North America. For all periods presented, revenues were principally derived from customer accounts in North America and Europe. For the three months ended December 31, 2009 and 2008, international revenues were $15.1 million and $15.3 million, or approximately 68% and 65% of our total revenues, respectively. In future periods, we plan to pursue revenue opportunities in several emerging markets that may include Eastern Europe, Russia, China, and India. We believe that international revenue may represent a larger portion of our total revenues if our expansion into emerging markets is successful.

For the three months ended December 31, 2009 and 2008, North America revenues were $7.1 million and $8.1 million, or approximately 32% and 35%, respectively of our total revenues. We believe North America revenues will continue to represent a significant portion of our total revenues in the foreseeable future.

Gross Margins. Management focuses on license and service gross margin in evaluating our financial condition and operating performance. Gross margins on license revenues were 98% and 99% for the three months ended December

31, 2009 and 2008, respectively. We expect license gross margin on current products to range from 96% to 98% in the foreseeable future. The margin will fluctuate with the mix of products sold. Historically, the Enterprise Foundation products have higher associated third party royalty expense than the Marketing Director and Decision Management products.

Gross margins on service revenues were 63% and 57% for the three months ended December 31, 2009 and 2008, respectively. Generally gross margins improve as support and maintenance revenues represent a higher proportion of total services revenues. We expect that gross margins on service revenues will range between 50% and 65% in the foreseeable future.

Reductions in Workforce. In October 2009, we initiated a restructuring plan, the 2010 Restructuring, intended to consolidate and reduce the size of our management team. This resulted in a reduction of headcount. As a result of the cost-cutting measure, we recorded a pre-tax cash restructuring charge in the first quarter of fiscal year 2010, of approximately $0.1 million for severance costs.

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In October 2008, we initiated a restructuring plan, the 2009 Restructuring, intended to align our resources and cost structure with expected future revenues. The 2009 Restructuring plan includes reductions in headcount and third party consultants across all functional areas in both North America and Europe. The 2009 Restructuring plan includes a reduction of approximately 13% of our permanent workforce. A significant portion of the positions eliminated were in North America.

As a result of the cost-cutting measures, we recorded a pre-tax cash restructuring charge in the first quarter of fiscal year 2009, of approximately $0.9 million, including $ 0.8 million for severance costs and $0.1 million for other contract termination costs. As of December 31, 2008, all payments had been made.

In May 2005, we undertook an approximate 10% reduction in our workforce. In connection with this action, we incurred a one-time cash expense of approximately $1.1 million in the fourth quarter ended September 30, 2005 for severance benefits. During the quarter ended March 31, 2007, we incurred an additional charge of less than $0.1 million for additional severance expense for an employee located in France. During the quarter ended December 31, 2008, we reversed the charge as we were not ultimately required to pay the severance expense to the employee.

During fiscal year 2002, we restructured several areas of the Company to reduce expenses and improve revenues. As part of this restructuring, we closed an office facility in Boston, Massachusetts and recorded an expense associated with the long-term lease which expires in January 2011. In 2007, we entered into a sublease with a sub-lessee for the remaining term of our lease at a rate lower than that which was forecasted when the original restructuring expense was recorded in 2002. This change in estimate resulted in a $0.4 million restructuring expense for the fiscal year ended September 30, 2007. If the sub-lessee of the facility were to default on their payments to us, further adjustments to restructuring expense might be required.

Income Taxes. During the period ended December 31, 2009, we recognized $0.5 million of non-cash deferred tax expense related to taxable income in the United Kingdom. It is expected that we will recognize a total of approximately $1.7 million of non-cash deferred tax expense during fiscal year 2010. We expect the deferred tax expense to be reduced in future years.

Past Results may not be Indicative of Future Performance. We believe that period-to-period comparisons of our operating results should not be relied upon as indicative of future performance. Our prospects must be considered given the risks, expenses and difficulties frequently encountered by companies in new and rapidly evolving businesses. There can be no assurance we will be successful in addressing these risks and difficulties. Moreover, we may not achieve or maintain profitability in the future.

Critical Accounting Estimates and Assumptions

Our discussion and analysis of our financial condition and results of operations are based upon our Condensed Consolidated Financial Statements, which have been prepared in accordance with Generally Accepted Accounting Principles, or GAAP, in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities.

On an on-going basis, we evaluate the estimates, including those related to our allowance for doubtful accounts, valuation of stock-based compensation, valuation of goodwill and intangible assets, valuation of deferred tax assets, restructuring expenses, contingencies, vendor specific objective evidence, or VSOE, of fair value in multiple element arrangements and the estimates associated with the percentage-of-completion method of accounting for certain of our

revenue contracts. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities and the recognition of revenue and expenses that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following critical accounting judgments and estimates are used in the preparation of our Condensed Consolidated Financial Statements:

- Revenue recognition, including estimating the total estimated time required to complete sales arrangements involving significant implementation or customization essential to the functionality of our products;
- Estimating valuation allowances and accrued liabilities, specifically the allowance for doubtful accounts, and assessment of the probability of the outcome of our current litigation;

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- Stock-based compensation expense;
- Accounting for income taxes;
- Valuation of long-lived and intangible assets and goodwill;
- Restructuring expenses; and
- Determining functional currencies for the purposes of consolidating our international operations.

Revenue Recognition. We derive revenues from licenses of our software and related services, which include assistance in implementation, customization and integration, post-contract customer support or PCS, training and consulting. The amount and timing of our revenue is difficult to predict and any shortfall in revenue or delay in recognizing revenue could cause our operating results to vary significantly from quarter to quarter and could result in operating losses. The accounting rules related to revenue recognition are complex and are affected by interpretation of the rules and an understanding of industry practices, both of which are subject to change. Consequently, the revenue recognition accounting rules require management to make significant estimates based on judgment.

For arrangements with multiple elements, we recognize revenue for services and PCS based upon the fair value VSOE of the respective elements. The fair value VSOE of the services element is based upon the standard hourly rates we charge for the services when such services are sold separately. The fair value VSOE for annual PCS is generally established with the contractual future renewal rates included in the contracts, when the renewal rate is substantive and consistent with the fees when support services are sold separately. When contracts contain multiple elements and fair value VSOE exists for all undelivered elements, we account for the delivered elements, principally the license portion, based upon the “residual method” as prescribed by relevant accounting guidance on software revenue recognition. In multiple element transactions where VSOE is not established for an undelivered element, we recognize revenue upon the establishment of VSOE for that element or when the element is delivered.

At the time we enter into a transaction, we assess whether any services included within the arrangement related to significant implementation or customization essential to the functionality of our products. For contracts for products that do not involve significant implementation or customization essential to the product functionality, we recognize license revenues when there is persuasive evidence of an arrangement, the fee is fixed or determinable, collection of the fee is probable and delivery has occurred as prescribed by relevant accounting guidance on software revenue recognition. For contracts that involve significant implementation or customization essential to the functionality of our products, we recognize the license and professional consulting services revenue using either the percentage-of-completion method or the completed contract method.

The percentage-of-completion method is applied when we have the ability to make reasonably dependable estimates of the total effort required for completion using labor hours incurred as the measure of progress towards completion. The progress toward completion is measured based on the “go-live” date. We define the “go-live” date as the date the essential product functionality has been delivered or the application enters into a production environment or the point at which no significant additional Chordiant supplied professional service resources are required. Estimates are subject to revisions as the contract progresses to completion. We account for the changes as changes in accounting estimates when the information becomes known. Information impacting estimates obtained after the balance sheet date but before the issuance of the financial statements is used to update the estimates. Provisions for estimated contract losses, if any, are recognized in the period in which the loss becomes probable and can be reasonably estimated. When we sell additional licenses related to the original licensing agreement, revenue is recognized upon delivery if the project

has reached the go-live date, or if the project has not reached the go-live date, revenue is recognized under the percentage-of-completion method. We classify revenues from these arrangements as license and service revenue based upon the estimated fair value of each element using the residual method.

The completed contract method is applied when we are unable to obtain reasonably dependable estimates of the total effort required for completion. Under the completed contract method, all revenue and related costs of revenue are deferred and recognized upon completion.

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For product co-development arrangements relating to software products in development prior to the consummation of the individual arrangements where we retain the intellectual property being developed and intend to sell the resulting products to other customers, license revenue is deferred until the delivery of the final product, provided all other requirements of the guidance on software revenue recognition are met. Expenses associated with these co-development arrangements are normally expensed as incurred as they are considered to be research and development costs that do not qualify for capitalization or deferral. There have been no such arrangements during the periods presented.

Revenue from subscription or term license agreements, which include software and rights to unspecified future products or maintenance, is recognized ratably over the term of the subscription period. Revenue from subscription or term license agreements, which include software, but exclude rights to unspecified future products and maintenance, is recognized upon delivery of the software if all conditions of recognizing revenue have been met including that the related agreement is non-cancelable, non-refundable and provided on an unsupported basis.

For transactions involving extended payment terms, we deem these fees not to be fixed or determinable for revenue recognition purposes and revenue is deferred until the fees become payable and due.

For arrangements with multiple elements where we determine we can account for the elements separately and the fees are not fixed or determinable due to extended payment terms, revenue is recognized in the following manner. If the undelivered element is PCS, or other services, an amount equal to the estimated value of the services to be rendered prior to the next payment becoming due is allocated to the undelivered services. The residual of the payment is allocated to the delivered elements of the arrangement.

For arrangements with multiple elements where we determine we can account for the elements separately and the fees are not fixed or determinable due to extended payment terms, revenue is recognized in the following manner. Amounts are first allocated to the undelivered elements included in the arrangement, as payments become due or are received, and the residual is allocated to the delivered elements.

We recognize revenue for PCS ratably over the support period which ranges from one to five years.

Our training and consulting services revenues are recognized as such services are performed on an hourly or daily basis for time and material contracts. For consulting services arrangements with a fixed fee, we recognize revenue on a percentage-of-completion method.

For all sales we use either a signed license agreement or a binding purchase order where we have a master license agreement as evidence of an arrangement. Sales through our third party systems integrators are evidenced by a master agreement governing the relationship together with binding purchase orders or order forms on a transaction-by-transaction basis. Revenues from reseller arrangements are recognized on the “sell-through” method, when the reseller reports to us the sale of our software products to end-users. Our agreements with customers and resellers do not contain product return rights.

We assess collectability based on a number of factors, including past transaction history with the customer and the credit-worthiness of the customer. We generally do not request collateral from our customers. If we determine that the collection of a fee is not probable, we recognize revenue at the time collection becomes probable, which is generally upon the receipt of cash.

Allowance for Doubtful Accounts. We must make estimates of the uncollectability of our accounts receivables. We specifically analyze accounts receivable and analyze historical bad debts, customer concentrations, customer credit-worthiness and current economic trends when evaluating the adequacy of the allowance for doubtful accounts. Generally, we require no collateral from our customers. Our gross accounts receivable balance was $23.1 million (including long-term accounts receivable of $0.9 million) with an allowance for doubtful accounts of $0.2 million as of December 31, 2009. Our gross accounts receivable balance was $21.1 million with an allowance for doubtful accounts of $0.8 million as of December 31, 2008. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances would be required. Based upon current economic conditions, we have reviewed accounts receivable and have recorded allowances as deemed necessary.

Probability of the outcome of our current litigation. As discussed in Note 9, “Litigation” in Notes to Condensed Consolidated Financial Statements, the Company is subject to various legal proceedings and claims that arise in the ordinary course of business. In accordance with GAAP, we record a liability when it is probable that a loss has been incurred and the

amount is reasonably estimable. There is significant judgment required in both the probability determination and as to whether an exposure can be reasonably estimated. In management's opinion, we do not have a potential liability related to any current legal proceedings and claims that would individually or in the aggregate materially adversely affect its financial condition or operating results. However, the outcomes of legal proceedings and claims brought against us are subject to significant uncertainty. Should we fail to prevail in any of these legal matters or should several of these legal matters be resolved against us in the same reporting period, the operating results of a particular reporting period could be materially adversely affected.

Stock-based Compensation Expense. We estimate the fair value of share-based payment awards on the date of grant using the Black-Scholes model. The determination of the fair value of shared-based payment awards on the date of grant using an option-pricing model is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to the expected stock price volatility over the term of the awards, and actual and projected employee stock option exercise behaviors.

We used the trinomial lattice valuation technique to determine the assumptions used in the Black-Scholes model. The trinomial lattice valuation technique was used to provide better estimates of fair values and meet the fair value objectives of the FASB standard on stock compensation. The expected term of options granted is derived from historical data on employee exercises and post-vesting employment termination behavior. The expected volatility is based on the historical volatility of our stock.

As stock-based compensation expense recognized in the Condensed Consolidated Statement of Operations is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. The standard on stock compensation requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Forfeitures were estimated based on historical experience.

If factors change and we employ different assumptions in future periods, the compensation expense that we record may differ significantly from what we have recorded in the current period. The estimated value of a stock option is most sensitive to the volatility assumption. Based on the December 31, 2009 variables, it is estimated that a change of 10% in either the volatility, expected life or interest rate assumption would result in a corresponding 8%, 4% and less than 1% change, respectively, in the estimated value of the option being valued using the Black-Scholes model. See Note 11 to the Condensed Consolidated Financial Statements for detailed information about stock-based compensation.

Accounting for Income Taxes. As part of the process of preparing our Condensed Consolidated Financial Statements we estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items, such as deferred revenue, for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our Condensed Consolidated Balance Sheets. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income and to the extent we believe that recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase this allowance in a period, we must include an expense within the tax provision in the Consolidated Statement of Operations.

At December 31, 2009, we have $74.3 million in gross deferred tax assets (DTAs) attributable principally to our net operating losses (NOLs) and to a lesser extent temporary differences relating to deferred revenue. Historically, we maintained a 100% valuation allowance on our DTAs because we have previously been unable to conclude that it is more-likely-than-not that we will realize the tax benefits of these DTAs. Based on recent operating results and the reorganization of our intellectual property into the U.S., our current projections of disaggregated future taxable

income have enabled us to conclude that it is more-likely-than-not that we will have future taxable income sufficient to realize $4.7 million of tax benefits from our deferred tax assets, which consist of that portion of our net deferred tax assets attributable to our NOLs residing in the United Kingdom. On September 30, 2008, we released (eliminated) $10.0 million of the valuation allowance on our DTAs related to the United Kingdom, of which $9.5 million was recognized as an offsetting reduction to goodwill (representing pre-acquisition NOLs) and $0.5 million was recognized as a credit (reduction) to the provision for income taxes. In future periods, we expect to incur tax expense related to the United Kingdom which will result in an increase in overall expense; however, to the extent that such tax expense is offset by the utilization of NOLs and capital allowances, the recognition of this additional tax expense will be a non-cash item.

The remaining balance of gross deferred tax assets was generated in the U.S. With respect to our U.S. generated deferred tax assets, we have recorded a full valuation allowance as the future realization of the tax benefit is not considered

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by management to be more likely than not. Our estimate of future taxable income considers available positive and negative evidence regarding our current and future operations, including projections of income in various states and foreign jurisdictions. We believe our estimate of future taxable income is reasonable; however, it is inherently uncertain, and if our future operations generate taxable income greater than projected, further adjustments to reduce the valuation allowance are possible. Conversely, if we realize unforeseen material losses in the future, or our ability to generate future taxable income necessary to realize a portion of the net deferred tax asset is materially reduced, additions to the valuation allowance could be recorded. At December 31, 2009 and September 30, 2009, the balance of the deferred tax valuation allowance was approximately $69.6 million.

Valuation of Long-lived and Intangible Assets and Goodwill. We assess the impairment of identifiable intangibles and long-lived assets whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Furthermore, we assess the impairment of goodwill annually. Factors we consider important which could trigger an impairment review include the following:

- Significant underperformance relative to expected historical or projected future operating results;
- Significant changes in the manner of our use of the acquired assets or the strategy for our overall business;
- Significant negative industry or economic trends;
- Significant decline in our stock price for a sustained period;
- Market capitalization declines relative to net book value; and
- A current expectation that, more likely than not, a long-lived asset will be sold or otherwise disposed of significantly before the end of its previously estimated useful life.

When one or more of the above indicators of impairment occurs, we estimate the value of long-lived assets and intangible assets to determine whether there is impairment. We measure any impairment based on the projected discounted cash flow method, which requires us to make several estimates including the estimated cash flows associated with the asset, the period over which these cash flows will be generated and a discount rate commensurate with the risk inherent in our current business model. These estimates are subjective and if we made different estimates, it could materially impact the estimated fair value of these assets and the conclusions we reached regarding impairment. Recently, due to the decline of our stock price, our market capitalization, and the general economic climate we have assessed our long-lived assets and intangible assets and determined that no impairment charge was necessary. At December 31, 2009, the market capitalization of the Company exceeded the book value of the Company.

We are required to perform an impairment review of our goodwill balance on at least an annual basis. This impairment review involves a two-step process as follows:

Step 1—We compare the fair value of our reporting units to the carrying value, including goodwill, of each of those units. For each reporting unit where the carrying value, including goodwill, exceeds the unit’s fair value, we proceed on to Step 2. If a unit’s fair value exceeds the carrying value, no further work is performed and no impairment charge is necessary.

Step 2—We perform an allocation of the fair value of the reporting unit to our identifiable tangible and non-goodwill intangible assets and liabilities. This derives an implied fair value for the reporting unit’s goodwill. We then compare

the implied fair value of the reporting unit's goodwill with the carrying amount of the reporting unit's goodwill. If the carrying amount of the reporting unit's goodwill is greater than the implied fair value of its goodwill, an impairment charge would be recognized for the excess.

We determined that we have one reporting unit. We completed a goodwill impairment review for the period ended September 30, 2009 and performed Step 1 of the goodwill impairment analysis required by a FASB standard on "Goodwill and Other Intangible Assets", and concluded that goodwill was not impaired as of September 30, 2009 using the methodology described above. Accordingly, Step 2 was not performed. We will continue to test for impairment on an annual basis and on an interim basis if an event occurs or circumstances change that would more likely than not reduce the fair value of our reporting units below their carrying amount.

Restructuring Expenses. In the past several years, we have implemented cost-reduction plans as part of our continued effort to streamline our operations to reduce ongoing operating expenses. These plans resulted in restructuring expenses

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related to, among others, the consolidation of excess facilities. These charges relate to facilities and portions of facilities we no longer utilize and either seek to terminate early or sublease. Cost to terminate contracts represents contract termination costs related to the restructuring plan. Lease termination costs and brokerage fees for the abandoned facilities were estimated for the remaining lease obligations and were offset by estimated sublease income. Estimates related to sublease costs and income are based on assumptions regarding the period required to locate and contract with suitable sub-lessees and sublease rates which can be achieved using market trend information analyses provided by a commercial real estate brokerage retained by us. Each reporting period we review these estimates and to the extent that these assumptions change due to new agreements with landlords, new subleases with tenants, potential defaults on existing subleases, or changes in the market, the ultimate restructuring expenses for these abandoned facilities could vary by material amounts. See Note 5 to the Condensed Consolidated Financial Statement for detailed information regarding restructuring expense.

Determining Functional Currencies for the Purpose of Consolidation. We have several foreign subsidiaries that together account for a significant portion of our revenues, expenses, assets and liabilities.

In preparing our Condensed Consolidated Financial Statements, we are required to translate the financial statements of the foreign subsidiaries from the currency in which they keep their accounting records, generally the local currency, into United States dollars. This process results in exchange gains and losses which are either included within the Condensed Consolidated Statement of Operations or as a separate part of our net equity under the caption “Accumulated Other Comprehensive Income.” The treatment of these translation gains or losses is dependent upon our management’s determination of the functional currency of each subsidiary. The functional currency is determined based on management’s judgment and involves consideration of all relevant economic facts and circumstances affecting the subsidiary. Generally, the currency in which the subsidiary conducts a majority of its transactions, including billings, financing, payroll and other expenditures would be considered the functional currency, but any dependency upon the parent and the nature of the subsidiary’s operations must also be considered.

If any subsidiary’s functional currency were deemed to be the local currency, then any gain or loss associated with the translation of that subsidiary’s financial statements would be included in cumulative translation adjustments. However, if the functional currency were deemed to be the United States dollar then any gain or loss associated with the translation of these financial statements would be included within our Condensed Consolidated Statement of Operations. If we dispose of any of our subsidiaries, any cumulative translation gains or losses would be recognized in our Condensed Consolidated Statement of Operations. If we determine that there has been a change in the functional currency of a subsidiary to the United States dollar, any translation gains or losses arising after the date of change would be included within our Condensed Consolidated Statement of Operations.

Based on our assessment of the factors discussed above, we consider the relevant subsidiary’s local currency to be the functional currency for each of our international subsidiaries. Accordingly, foreign currency translation gains and losses are included as part of Accumulated Other Comprehensive Income within our Condensed Consolidated Balance Sheets for all periods presented.

The magnitude of foreign currency gains or losses is dependent upon movements in the exchange rates of the foreign currencies in which we transact business against the United States dollar. These currencies include the United Kingdom Pound Sterling, the Euro, the Canadian Dollar, and the Chinese Yuan. Any future translation gains or losses could be significantly larger or smaller than those reported in previous periods. At December 31, 2009, approximately $21.2 million of our cash and cash equivalents were held by our subsidiaries outside of the United States as compared to $36.6 million at December 31, 2008.

Recent Accounting Pronouncements

See Note 2 to the Condensed Consolidated Financial Statements for detailed information regarding status of new accounting standards.

IFRS

International Financial Reporting Standards (IFRS) is a comprehensive series of accounting standards published by the International Accounting Standards Board (IASB). In November 2008, the SEC issued for comment a proposed roadmap outlining several milestones that, if achieved, could lead to mandatory adoption of IFRS by U.S. issuers starting in 2014. Implementation of IFRS reporting would be in staged transition periods based upon our filing status. Based upon the current filing status, we would begin IFRS filing for the fiscal year ending September 30, 2017. The SEC is expected to make a determination in 2011 regarding the mandatory adoption of IFRS. We are currently assessing the impact that this potential change would have on our Condensed Consolidated Financial Statements, and we will continue to monitor the development of the potential implementation of IFRS.

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Results of Operations

The following table sets forth, in dollars (in thousands) and as a percentage of total revenues, unaudited Condensed Consolidated Statements of Operations data for the periods indicated. This information has been derived from the Condensed Consolidated Financial Statements included elsewhere in this Quarterly Report.

	Three Months Ended December 31,			
	2009		2008	
Statements of Operations Data:				
Revenues:				
License	$ 7,432	33%	$ 7,941	34%
Service	14,792	67	15,436	66
Total revenues	22,224	100	23,377	100
Cost of revenues:				
License	134	1	98	—
Service	5,545	25	6,686	29
Amortization of intangible assets	303	1	303	1
Total cost of revenues	5,982	27	7,087	30
Gross profit	16,242	73	16,290	70
Operating expenses:				
Sales and marketing	6,657	30	7,780	33
Research and development	5,354	24	5,259	23
General and administrative	4,504	20	4,402	19
Restructuring expense	144	1	784	3
Total operating expenses	16,659	75	18,225	78
Loss from operations	(417)	(2)	(1,935)	(8)
Interest income, net	29	—	292	1
Other income (expense) , net	(90)	—	685	3
Loss before income taxes	(478)	(2)	(958)	(4)
Provision for income taxes	494	2	1,711	7
Net loss	$ (972)	(4)%	$ (2,669)	(11)%

Comparison of the Three Months Ended December 31, 2009 and 2008 (Unaudited)

Revenues

The following summarizes the components of our total revenues:

License Revenue

The increase or decrease of license revenue occurring within our three different product emphases is dependent on the timing of when a sales transaction is completed and whether a license transaction was sold with essential consulting services. License revenue sold with essential consulting services is generally recognized under the percentage-of-completion method of accounting. The timing and amount of revenue for those transactions being recognized under the percentage-of-completion is influenced by the progress of work performed relative to the project length of customer contracts and the dollar value of such contracts. The following table sets forth our license revenue by product emphasis for the three months ended December 31, 2009 and 2008 (in thousands, except percentages):

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	Three Months Ended December 31,			
License Revenue:	2009	2008	Change	%
Enterprise Foundation solutions	$ 2,808	$ 1,544	$ 1,264	82%
Marketing Director solutions	332	2,381	(2,049)	(86)
Decision Management solutions	4,292	4,016	276	7
Total license revenue	$ 7,432	$ 7,941	$ (509)	(6)%

Total license revenue decreased by $0.5 million or 6% for the three months ended December 31, 2009 as compared to the same period of the prior year. We had a similar number of transactions in the comparable periods. Due to the current economic climate, we have shifted our near term focus of our sales staff towards Decision Management solutions rather than Enterprise Foundation solutions. However, our Decision Management solutions generally generate smaller revenue per transaction than our Enterprise Foundation solutions. Included in license revenue for the three months ended December 31, 2009 were $1.6 million of revenues associated with additional seat orders placed by an existing Enterprise Foundation customer. Included in license revenue for the three months ended December 31, 2008 is $4.2 million of revenue related to Vodafone. These Vodafone revenues were associated with the Marketing Director and Decision Management solutions. License revenue as a percentage of total revenue was 33% and 34% for the three months ended December 31, 2009 and 2008, respectively.

Service Revenue

Service revenue is primarily composed of consulting implementation and integration, consulting customization, training, PCS, and certain reimbursable out-of-pocket expenses. The increase or decrease of service revenue within our three different product emphases is primarily due to the timing of when license transactions are completed, whether or not the license was sold with essential consulting services, the sophistication of the customer's application, and the expertise of the customer's internal development team. For non-essential service transactions, service revenue will lag in timing compared to the period of when the license revenue is recognized. The following table sets forth our service revenue by product emphasis for the three months ended December 31, 2009 and 2008 (in thousands, except percentages):

	Three Months Ended December 31,			
Service Revenue:	2009	2008	Change	%
Enterprise Foundation solutions	$ 8,471	$ 9,662	$ (1,191)	(12)%
Marketing Director solutions	2,254	2,951	(697)	(24)
Decision Management solutions	4,067	2,823	1,244	44
Total service revenue	$ 14,792	$ 15,436	$ (644)	(4)%

Total service revenue decreased $0.6 million or 4% for the three months ended December 31, 2009 as compared to the same period of the prior year. The change in service revenue was primarily composed of decreases of $0.8 million in consulting revenue and $0.4 million in expense reimbursement revenue, offset by increases of $0.5 million in support and maintenance revenue and $0.1 million in training revenue. The decrease in consulting revenue is directly related to the decrease in license revenues in previous periods, since the majority of our customers use some form of our consulting services in connection with their projects. The timing of recognizing service revenue can vary from quarter to quarter depending on the project. We derived more of our license revenues from Decision Management solutions rather than Enterprise Foundation solutions due to our shift in focus of our sales staff. This has resulted in an increase of service revenue for our Decision Management solutions. Service revenue as percentage of total revenue was 67% and 66% for the three months ended December 31, 2009 and 2008, respectively.

See the Overview and Financial Trend section for further analysis of revenues.

Cost of Revenues

License

Cost of license revenue includes third-party software royalties and amortization of capitalized software development costs. Royalty expenses can vary depending upon the mix of products sold within the period. In addition, not all license

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products have associated royalty expense. Capitalized software development costs pertain to third party costs associated with the porting of existing products to new platforms. The following table sets forth our cost of license revenues for the three months ended December 31, 2009 and 2008 (in thousands, except percentages):

	Three Months Ended December 31,			
	2009	2008	Change	%
Cost of license revenue	$ 134	$ 98	$ 36	37%
Percentage of total revenue	1%	—%		

Cost of license revenue increased by less than $0.1 million or 37% for the three months ended December 31, 2009 as compared to the same period of the prior year. The change is from increase in our royalty expense and the amortization of our porting capitalized software costs.

Service

Cost of service revenues consists primarily of personnel, third party consulting, facility, and travel costs incurred to provide consulting implementation and integration, consulting customization, training, and PCS. The following table sets forth our cost of service revenues for the three months ended December 31, 2009 and 2008 (in thousands, except percentages):

	Three Months Ended December 31,			
	2009	2008	Change	%
Cost of service revenue	$ 5,545	$ 6,686	$ (1,141)	(17)%
Percentage of total revenue	25%	29%		

Cost of service revenue decreased $1.1 million or 17% for the three months ended December 31, 2009 as compared to the same period of the prior year. The change was primarily due to decreases of $0.5 million in consulting cost, $0.2 million in sales and marketing programs, and $0.4 million in travel expense. We utilized fewer third party consultants because of the decrease in service revenue.

Gross Margins

See the Financial Trend section for our analysis of gross margins.

Amortization of Intangible Assets

Amortization of intangible assets cost consists of the amortization of amounts paid for developed technologies, customer lists and trade-names resulting from business acquisitions. The following table sets forth our costs associated with amortization of intangible assets for the three months ended December 31, 2009 and 2008 (in thousands, except percentages):

	Three Months Ended December 31,			
	2009	2008	Change	%
Amortization of intangible assets	$ 303	$ 303	$ —	—%
Percentage of total revenues	1%	1%		

These costs are solely related to the $6.1 million of intangible assets associated with the acquisition of KiQ in December 2004. As of December 31, 2009, the intangible assets have been fully amortized.

Operating Expenses

Sales and Marketing

Sales and marketing expense is attributed to activities associated with selling, promoting and advertising our products, product demonstrations and customer sales calls. These costs consist primarily of employee compensation and benefits, commissions and bonuses, facilities, travel expenses and promotional and advertising expenses. The following table sets forth our sales and marketing expenses for the three months ended December 31, 2009 and 2008 (in thousands, except percentages):

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	Three Months Ended December 31,			
	2009	2008	Change	%
Sales and marketing expense	$ 6,657	$ 7,780	$ (1,123)	(14)%
Percentage of total revenues	30%	33%		

Sales and marketing expense decreased by $1.1 million or 14% for the three months ended December 31, 2009 as compared to the same period of the prior year. The change was primarily from decreases of $0.6 million in employee related costs, $0.1 million in recruiting expense, $0.3 million in consultant expense, and $0.2 million in travel expense offset by an increase of $0.1 million in sales and marketing programs. The decrease in employee related costs is primarily from a 21% reduction in average headcount for each quarter. See Note 5 to the Condensed Consolidated Financial Statements for more details regarding the reduction in headcount.

Research and Development

Research and development expense results from the activities associated with the development of new products, enhancements of existing products and quality assurance activities. These costs consist primarily of employee compensation and benefits, facilities, the cost of software and development tools, equipment and consulting costs, including costs for offshore consultants. The following table sets forth our research and development expenses for the three months ended December 31, 2009 and 2008 (in thousands, except percentages):

	Three Months Ended December 31,			
	2009	2008	Change	%
Research and development expense	$ 5,354	$ 5,259	$ 95	2%
Percentage of total revenues	24%	23%		

Research and development expense increased by $0.1 million or 2% for the three months ended December 31, 2009 as compared to the same period of the prior year. The change was primarily from increases of $0.3 million in employee related costs, $0.1 million in facility expense, and $0.1 million in travel expense offset by decreases of $0.3 million in consultant costs and $0.1 million in recruiting expense. We continue to reduce the use of consultants for our research and development.

General and Administrative

General and administrative expense is composed primarily of costs associated with our executive and administrative personnel (e.g. the office of the CEO, legal, human resources and finance personnel). These costs consist primarily of employee compensation and benefits, bonuses, stock compensation expense, facilities, consulting, legal and audit costs, including costs for Sarbanes-Oxley Act of 2002 (SOX) compliance. The following table sets forth our general and administrative expenses for the three months ended December 31, 2009 and 2008 (in thousands, except percentages):

	Three Months Ended December 31,			
	2009	2008	Change	%
General and administrative expense	$ 4,504	$ 4,402	$ 102	2%
Percentage of total revenues	20%	19%		

General and administrative expense increased by $0.1 million or 2% for the three months ended December 31, 2009 as compared to the same period of the prior year. The change was primarily from increases of $0.3 million in

professional services offset by decrease of $0.2 million in bad debt expense. The increase in professional services is primarily due to accounting, tax, legal and outside service costs associated with our various merger and acquisition activities. The decrease in bad debt is primarily due to the resolution of a disputed receivable with one of our customers.

Restructuring Expense

In October 2009, we initiated a restructuring plan, the 2010 Restructuring, intended to consolidate and reduce the size of our management team. This resulted in a reduction of headcount. As a result of the cost-cutting measure, we recorded a pre-tax cash restructuring charge in the first quarter of fiscal year 2010, of approximately $0.1 million for severance costs.

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In October 2008, we initiated a restructuring plan, the 2009 Restructuring, intended to align our resources and cost structure with expected future revenues. The 2009 Restructuring plan includes reductions in headcount and third party consultants across all functional areas in both North America and Europe. The 2009 Restructuring plan includes a reduction of approximately 13% of our permanent workforce. A significant portion of the positions eliminated were in North America.

As a result of the cost-cutting measures, we recorded a pre-tax cash restructuring charge in the first quarter of fiscal year 2009, of approximately $0.9 million, including $ 0.8 million for severance costs and $0.1 million for other contract termination costs. As of December 31, 2008, all payments had been made.

In May 2005, we undertook an approximate 10% reduction in our workforce. In connection with this action, we incurred a one-time cash expense of approximately $1.1 million in the fourth quarter ended September 30, 2005 for severance benefits. During the quarter ended March 31, 2007, we incurred an additional charge of less than $0.1 million for additional severance expense for an employee located in France. During the quarter ended December 31, 2008, we reversed the charge as we were not ultimately required to pay the severance expense to the employee.

Stock-based Compensation (included in Individual Operating Expense and Cost of Revenue categories)

The following table sets forth our stock-based compensation expense and functional breakdown for the three months ended December 31, 2009 and 2008 (in thousands):

	Three Months Ended December 31,	
	2009	2008
Cost of revenues - service	$ 162	$ 134
Operating expenses:		
Sales and marketing	162	256
Research and development	90	109
General and administrative	475	466
Total operating expenses	727	831
Total stock-based compensation expense	$ 889	$ 965

For the three months ended December 31, 2009, the aggregate stock-based compensation cost included in cost of revenues and in operating expenses was $0.9 million and primarily related to $0.7 million associated with employee stock options, $0.1 million associated with restricted stock awards and $0.1 million associated with restricted stock units.

For the three months ended December 31, 2008, the aggregate stock-based compensation cost included in cost of revenues and in operating expenses was $1.0 million and primarily related to $0.8 million associated with employee stock options, $0.2 million associated with restricted stock awards, and less than $0.1 million associated with restricted stock units.

Interest Income, Net

Interest income, net, consists primarily of interest income generated from our cash, cash equivalents, restricted cash and marketable securities, offset by interest expense incurred in connection with letters of credit and interest charges imputed under FASB guidance for restructuring accruals. The following table sets forth our interest income, net for the three months ended December 31, 2009 and 2008 (in thousands, except percentages):

	Three Months Ended December 31,			
	2009	2008	Change	%
Interest income, net	$ 29	$ 292	$ (263)	(90)%
Percentage of total revenues	—%	1%		

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Interest income, net decreased by $0.3 million or 90% for the three months ended December 31, 2009 as compared to the same period of the prior year. The change is primarily from the decrease of interest income earned at our foreign entities.

Other Income (Expense), Net

Other income (expense), net is primarily attributed to foreign currency transaction gains or losses and re-measurement of our short-term intercompany balances between the U.S. and our foreign denominated subsidiaries. The following table sets forth our other income, net for the three months ended December 31, 2009 and 2008 (in thousands, except percentages):

	Three Months Ended December 31,			
	2009	2008	Change	%
Other income (expense), net	$ (90)	$ 685	$ (775)	(113)%
Percentage of total revenues	—%	3%		

Other income decreased by $0.8 million or 113% for the three months ended December 31, 2009 as compared to the same period of the prior year. The change is primarily due to the re-measurement of our short-term intercompany balances resulting from changes in foreign exchange rates.

Provision for Income Taxes

Our provision for income taxes was $0.5 million and $1.7 million for the three months ended December 31, 2009 and 2008, respectively. The $1.2 million decrease in income taxes is primarily due to a decrease in non-cash tax expense in our UK subsidiary and a decrease in unrecoverable withholding tax payments related to sales transactions in India and Turkey compared to three months ended December 31 2008.

At December 31, 2009, we have $74.3 million in gross deferred tax assets (DTAs) attributable principally to our net operating losses (NOLs) and to a lesser extent temporary differences relating to deferred revenue. Historically, we maintained a 100% valuation allowance on our DTAs because we have previously been unable to conclude that it is more-likely-than-not that we will realize the tax benefits of these DTAs. Based on recent operating results and the reorganization of our intellectual property into the U.S., our current projections of disaggregated future taxable income have enabled us to conclude that it is more-likely-than-not that we will have future taxable income sufficient to realize $4.7 million of tax benefits from our deferred tax assets, which consist of that portion of our net deferred tax assets attributable to our net operating losses (NOLs) residing in the United Kingdom. On September 30, 2008, we had released (eliminated) $10.0 million of the valuation allowance on our DTAs related to the United Kingdom, of which $9.5 million was recognized as an offsetting reduction to goodwill (representing pre-acquisition NOLs) and $0.5 million was recognized as a credit (reduction) to the provision for income taxes. In future periods, we expect to incur tax expense related to the United Kingdom which will result in an increase in overall expense; however, to the extent that such tax expense is offset by the utilization of NOLs and capital allowances, the recognition of this additional tax expense will be a non-cash item.

The remaining balance of gross deferred tax assets was generated in the U.S. With respect to our U.S. generated deferred tax assets, we have recorded a full valuation allowance as the future realization of the tax benefit is not considered by management to be more likely than not. Our estimate of future taxable income considers available positive and negative evidence regarding our current and future operations, including projections of income in various states and foreign jurisdictions. We believe our estimate of future taxable income is reasonable; however, it is

inherently uncertain, and if our future operations generate taxable income greater than projected, further adjustments to reduce the valuation allowance are possible. Conversely, if we realize unforeseen material losses in the future, or our ability to generate future taxable income necessary to realize a portion of the net deferred tax asset is materially reduced, additions to the valuation allowance could be recorded. At December 31, 2009 and September 30, 2009, the balance of the deferred tax valuation allowance was approximately $69.6 million.

Liquidity and Capital Resources

Prior to fiscal year 2007, we had not been profitable and we periodically generated cash through the issuance of our common stock.

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For the three months ended December 31, 2009, we used approximately $1.7 million to purchase 1.95 million shares of SWK Holding Corporation (formerly Kana Software, Inc.). While these shares are publicly traded, the trading volumes are low and our ability to liquidate the shares may be unpredictable. Additionally, we incurred professional service costs associated with our various merger and acquisition related activities in the quarter ended December 31, 2009.

We generated cash from operating and financing activities and used cash in investing activities. It is anticipated that our current cash balances are adequate to fund operations for the next twelve months, however in the event we are not profitable, we would anticipate a decrease in cash and cash equivalents in the near term.

Due to the current global economic recession, maintaining our cash balances at their current levels will be highly dependent upon our ability to enter into new license and service agreements with customers and the payment terms associated with these agreements. Historically we have been able to negotiate payment terms that were favorable to us. In the current economic environment we may not be as successful in negotiating payments terms that are as favorable as in the past. If bookings do not meet our expectations, or we are not able to negotiate favorable payment terms, we would anticipate a decrease in cash and cash equivalents in the near term.

We believe that the effects of our strategic actions implemented to improve revenue as well as to control costs will be adequate to reduce the near term level of cash used by operations, which, when considered with existing cash balances, will be sufficient to meet our working capital and operating resource expenditure requirements for the near term. If the global economy weakens further, additional declines in cash balances could occur.

We anticipate that operating expenses will continue to be a material use of our cash resources. We may utilize cash resources to fund acquisitions, purchase minority ownership interests in other companies, or fund investments in other businesses, technologies or product lines. In the long-term, we may require additional funds to support our working capital and operating expense requirements or for other purposes, and may seek to raise these additional funds through public or private debt or equity financings. There can be no assurance that this additional financing will be available, or if available, will be on reasonable terms. Failure to generate sufficient revenues or to control spending could adversely affect our ability to achieve our business objectives.

Operating Activities

Cash provided by operating activities was $2.8 million during the three months ended December 31, 2009, which consisted primarily of our net loss of $1.0 million adjusted for non-cash items (primarily depreciation and amortization, non-cash stock-based compensation expense, non-cash provision for income taxes , and the provision for doubtful accounts) aggregating approximately $2.1 million and the net cash change in assets and liabilities of approximately $1.7 million. This net cash change in account balances is primarily from deferred revenue of $3.2 million, accrued expenses, other liabilities—non-current and restructuring accruals of $2.9 million, accounts payable of $0.8 million, prepaid expenses and other current assets of $0.3 million, and other assets of less than $0.1 million offset by the change of $5.5 million in accounts receivable. The change in accounts receivable and deferred revenue is primarily due to the billing of customers near the end of the period for maintenance renewals for future periods.

Cash provided by operating activities was $2.6 million during the three months ended December 31, 2008, which consisted primarily of our net loss of $2.7 million adjusted for non-cash items (primarily depreciation and amortization, non-cash stock-based compensation expense, non-cash provision for income taxes , and the provision for doubtful accounts) aggregating approximately $3.2 million and the net cash change in assets and liabilities of approximately $2.1 million. This net cash change in account balances is primarily from deferred revenue of $0.9

million, accounts receivable of $2.7 million, and prepaid expenses and other current assets of $1.2 million, offset by net cash changes in account balance in other assets of $0.1 million, accounts payable of $2.4 million, and $0.2 million in accrued expenses, other liabilities—non-current and restructuring. The change in accounts receivable is primarily due to receivables collected at a slower rate than billed. The change in accounts payable is primarily due to our program to cut expenses.

Investing Activities

Cash used for investing activities was $1.8 million during the three months ended December 31, 2009. The cash used was primarily from the purchase of $1.7 million in marketable securities of SWK Holding Corporation (formerly Kana Software, Inc.), which are classified as available for sale, the purchase of $0.1 million of property and equipment and the capitalization of less than $0.1 million of software development costs associated with the porting of an existing product to a new platform. The property and equipment purchases were primarily computer equipment and software used in day-to-day operations. As computer equipment continues to age, we expect that we will need to increase equipment

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purchases in some future period. Additionally, we may use cash to fund acquisitions, purchase minority ownership interests in other companies, or fund investments in other businesses, technologies, or product lines.

Cash used for investing activities was $0.2 million during the three months ended December 31, 2008. The cash used was primarily from the purchase of $0.2 million of property and equipment and the capitalization of less than $0.1 million of software development costs associated with the porting of an existing product to a new platform. The property and equipment purchases were primarily computer equipment and software used in day-to-day operations.

We have no material commitments for capital expenditures. Expenditures in the next 24 months may increase as the average age of laptops and servers has increased.

Financing Activities

Cash provided by financing activities was less than $0.1 million during the three months ended December 31, 2009. The cash provided was related to proceeds from stock option exercises. The majority of stock options outstanding have strike prices that exceed the current market value, accordingly we do not anticipate significant proceeds from stock option exercises in the near term.

Cash provided by financing activities was less than $0.1 million during the three months ended December 31, 2008. The cash provided was related to proceeds from stock option exercises. As long as the market value of the Company’s common stock remains below the exercise price for the majority of the outstanding exercise price for the majority of outstanding stock options, significant proceeds from stock option exercised are not expected.

Revolving Line of Credit

See Note 7 to the Condensed Consolidated Financial Statements for detailed information regarding our existing revolving line of credit. We may consider other bank borrowing options which we believe are commercially available to us. Such facilities generally allow for higher borrowing limits based on a percentage of annual recurring revenues.

Contractual Obligations

Ness

In 2003, we entered into an agreement with Ness Technologies Inc., Ness USA, Inc. (formerly Ness Global Services, Inc.) and Ness Technologies India, Ltd. (collectively, “Ness”) and in January 2009, we extended the Ness agreement through December 31, 2011. Pursuant to the Ness agreement, Ness provides our customers with technical product support through a worldwide help desk facility, a sustaining engineering function that serves as the interface between technical product support and internal engineering organization, product testing services, product development services and certain other identified technical and consulting services (collectively, the “Services”). Under the terms of the Ness agreement, we pay for services rendered on a monthly fee basis and reimbursement of approved out of-pocket expenses. If we had terminated the Ness agreement for convenience prior to December 31, 2009, we would have been required to pay a termination fee no greater than $0.5 million, however, this cancellation penalty lapsed at December 31, 2009. We also had guaranteed certain equipment lease obligations of Ness for equipment acquired by Ness to be used in performance of the Services, either through leasing arrangements or direct cash purchases, for which we were obligated under the agreement to reimburse Ness. In 2006, Ness entered into a 36 month equipment lease agreement with IBM India and, in connection with the lease agreement we had an outstanding standby letter of credit to guarantee Ness’ financial commitments under the lease. During the quarter ended June 30, 2009, the lease expired and we no longer have an obligation to reimburse Ness.

Leases

Operating lease obligations in the table below include approximately $0.7 million for our Boston, Massachusetts facility operating lease commitment that is included in Restructuring Expense. As of December 31, 2009, we had $0.3 million in sublease income contractually committed for future periods relating to this facility. See Notes 5 and 8 to the Condensed Consolidated Financial Statements for further discussion.

We have asset retirement obligations, associated with commitments to return property subject to operating leases to original condition upon lease termination. As of December 31, 2009, we estimate that approximately $0.3 million will be required to fulfill these obligations.

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The following table presents certain payments due under contractual obligations as of December 31, 2009 based on fiscal years (in thousands):

	Payments Due By Period			
	Total	Due in 2010	Due in 2011-2012	Due in 2013-2014
Operating lease obligations	$ 10,261	$ 2,684	$ 5,195	$ 2,382
Asset retirement obligations	317	—	317	—
Total	$ 10,578	$ 2,684	$ 5,512	$ 2,382

As of December 31, 2009, we had $1.1 million of gross unrecognized tax benefits. As of December 31, 2009, we cannot make a reasonably reliable estimate of the period in which these liabilities may be settled with the respective tax authorities, as such they are excluded from the above table. See Note 10 to the Condensed Consolidated Financial Statements for additional information.

Indemnification

See Note 8 to the Condensed Consolidated Financial Statements for detailed information regarding our indemnifications.

Off Balance Sheet Arrangements

None.

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Item 3. Quantitative and Qualitative Disclosures about Market Risk.

We are exposed to the impact of interest rate changes, equity volatility and foreign currency fluctuations.

Interest Rate Risk. The primary objective of our investment activities is to preserve principal while at the same time maximizing yields without significantly increasing risk. To achieve this objective, we primarily invested in money market accounts and short-term certificates of deposit. Due to the nature of these investments, the Company did not have a material interest rate risk at September 30, 2009 and December 31, 2009.

Equity Price Risk. We are exposed to equity price risk as we hold marketable securities, which had an estimated fair value of $1.7 million. These marketable securities may be subject to significant fluctuations in fair value due to the volatility of the stock market. Using a hypothetical reduction of 10 percent in the stock price of these marketable securities, the fair value of our marketable securities would decrease by approximately $0.2 million as of December 31, 2009.

Foreign Currency Risk. International revenues accounted for approximately 68% of total revenues for three months ended December 31, 2009. International revenues accounted for approximately 65% of total revenues for the year ended December 31, 2008. The Company's international operations have increased our exposure to foreign currency fluctuations. Revenues and related expense generated from our international subsidiaries are generally denominated in the functional currencies of the local countries. Primary currencies include the United Kingdom Pound Sterling, the Euro, the Canadian Dollar, and the Chinese Yuan. The Consolidated Statement of Operations is translated into United States Dollars at the average exchange rates in each applicable period. To the extent the United States Dollar strengthens against foreign currencies, the translation of these foreign currency denominated transactions results in reduced revenues, operating expense, and net income for our international operations. Similarly, our revenues, operating expenses, and net income will increase for our international operations, if the United States Dollar weakens against foreign currencies. We do not hedge our exposure to foreign currency fluctuations.

We are also exposed to foreign exchange rate fluctuations as we convert the financial statements of our foreign subsidiaries and our investments in equity interests into United States dollars in consolidation. If there is a change in foreign currency exchange rates, the conversion of the foreign subsidiaries' financial statements into United States dollars will lead to a translation gain or loss which is recorded as a component of accumulated other comprehensive income which is a component of Stockholders' Equity. In addition, we have certain assets and liabilities that are denominated in currencies other than the relevant entity's functional currency. Changes in the functional currency value of these assets and liabilities create fluctuations that will lead to a transaction gain or loss. For the three months ended December 31, 2009 and the fiscal year ended September 30, 2009, we recorded net foreign currency transaction loss of $0.1 million and less than $0.1 million, respectively.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including the President and Chief Executive Officer and the Chief Financial Officer, we have evaluated the effectiveness of our disclosure controls and procedures as required by Exchange Act of 1934, as amended, Rule 13a-15(e) and 15d-15(e) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that these disclosure controls and procedures are effective in alerting them in a timely manner to material information required to be disclosed in our periodic reports filed with the SEC.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

See Note 9 to the Condensed Consolidated Financial Statements in Part 1, Item 1 of this Form 10-Q for a description of our legal proceedings.

Item 1A.

RISK FACTORS

The Company has marked with an asterisk (*) those risk factors that reflect substantive changes from the risk factors included in the Company's Form 10-K filed with the Securities and Exchange Commission for the fiscal year ended September 30, 2009.

We may experience a shortfall in bookings, revenue, earnings, cash flow or other financial metrics, or otherwise fail to meet public market expectations, which could materially and adversely affect our business and the market price of our common stock.

Our revenues and operating results may fluctuate significantly because of a number of factors, many of which are outside of our control. Some of these factors may include:

- Additional deterioration and changes in domestic and foreign markets and economies, including those impacted by the turmoil in the financial services, mortgage and credit markets;
- Our ability to close new license transactions;
- Size and timing of individual license transactions;
- Delay, deferral or termination of customer implementations of our products;
- Lengthening of our sales cycle;
- Efficiently utilizing our global services organization, direct sales force and indirect distribution channels;
- Our ability to develop and market new products;
- Timing of new product introductions and product enhancements;
- Mix of products licensed and services sold;
- Activities of and acquisitions by our competitors;
- Product and price competition; and
- Our ability to control our costs.

One or more of the foregoing factors may cause our operating expenses to be disproportionately high during any given period or may cause our bookings, revenues and operating results to fluctuate significantly. Based upon the preceding

factors, we may experience a shortfall in bookings, revenues and earnings or otherwise fail to meet public market expectations, which could materially and adversely affect our business, financial condition, results of operations and the market price of our common stock.

*Our backlog has declined over the past two years, which will adversely affect revenues and could result in losses in future periods, and our known backlog of business may not result in revenue.

We define backlog as contractual commitments by our customers through purchase orders or contracts. Backlog includes software license orders for which the delivered products have not been accepted by customers or have not otherwise met all of the required criteria for revenue recognition, deferred revenue from customer support contracts, and deferred consulting and education orders for services not yet completed or delivered.

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Prior to the most recent two fiscal quarters, when backlog increased, backlog had declined sequentially over each of the prior six fiscal quarters due to lower than expected bookings. In the aggregate, backlog declined significantly over the past fiscal year. The decline in backlog is primarily due to revenue on previously signed transactions being recognized at a faster pace than new transactions were being consummated. Each category of backlog has also been unfavorably impacted by recent foreign exchange rate changes, as significant portions of the underlying balances are denominated in Euros or Pounds Sterling.

The decline in backlog and the associated deferred revenue balances will adversely affect revenues in future periods, and our ability to forecast future revenues will be diminished. Because our backlog has declined, the financial results of future periods will be more dependent upon the signing of new transactions. Accordingly, the level of future revenues will be less predictable. If average quarterly aggregate bookings remain at the $16.0 million levels achieved during the past twelve months, future losses would be incurred unless operating expenses are reduced.

Backlog is not necessarily indicative of revenues to be recognized in a specified future period. There are many factors that would impact the Company’s filling of backlog, such as the Company’s progress in completing projects for its customers and Chordiant’s customers’ meeting anticipated schedules for customer-dependent deliverables. The Company provides no assurances that any portion of its backlog will be filled during any fiscal year or at all, or that its backlog will be recognized as revenues in any given period or at all. In addition, it is possible that customers from whom we expect to derive revenue from backlog will default, and as a result we may not be able to recognize expected revenue from backlog. The risk that customers will reduce the scope of, delay or terminate projects, thus delaying or eliminating our ability to recognize backlog as revenue, is exacerbated in the current economic environment. For the three months ended December 31, 2009 these items defaulted aggregated $0.2 million and were removed from backlog at the date of the expiration or cancellation

Geopolitical concerns could make the closing of license transactions with new and existing customers difficult.

Our revenues may further decrease in fiscal year 2010 or beyond if we are unable to enter into new large value license transactions with new and existing customers. The current state of the global financial markets and the global economic decline generally have left many customers reluctant to enter into new large value license transactions without some expectation that the economy both in the customer’s home country and globally will stabilize. Geopolitical instability will continue to make closing large license transactions difficult. In addition, we cannot predict what effect the U.S. military presence overseas or potential or actual political or military conflict have had or are continuing to have on our existing and prospective customers’ decision-making process with respect to licensing or implementing enterprise-level products such as ours. Our ability to enter into new large value license transactions also directly affects our ability to create additional consulting service and maintenance revenue opportunities, on which we also depend.

Recent worldwide market turmoil may adversely affect our customers which directly impacts our business and results of operations.

The Company’s operations and performance depend on our customers having adequate resources to purchase our products and services. The unprecedented turmoil in the global markets and the global economic downturn generally continues to adversely impact our customers and potential customers. These market and economic conditions have continued to deteriorate despite government intervention globally, and may remain volatile and uncertain for the foreseeable future. Customers have altered and may continue to alter their purchasing and payment activities in response to deterioration in their businesses, lack of credit, economic uncertainty and concern about the stability of markets in general, and these customers may reduce, delay or terminate purchases of, and payment for, our products

and services. Recently, a number of our current and prospective customers have merged with others, been forced to raise significant amounts of capital, or received loans or equity investments from the government, which actions may result in less demand for our products and services. If we are unable to adequately respond to changes in demand resulting from deteriorating market and economic conditions, our financial condition and operating results may be materially and adversely affected.

Our primary products have a long sales and implementation cycle, which makes it difficult to predict our quarterly and annual results and may cause our operating results to vary significantly from period to period.

The period between the initial contact with a prospective customer and the sale of our products is unpredictable and often lengthy, typically ranging from three to eighteen months. Thus, revenue and cash receipts could vary significantly from quarter to quarter. Any delays in the implementation of our products could cause reductions in our revenues. The licensing of our products is often an enterprise-wide decision that generally requires us to provide a significant level of education to

prospective customers about the use and benefits of our products. The implementation of our products involves a significant commitment of technical and financial resources that may be provided by us, by the customer or by third-party systems integrators. If we underestimate the resources required to meet the expectations we have set with a customer when we set prices, then we may experience a net loss on that customer engagement. If this happens with a large customer engagement, then this could have a material adverse effect on our financial results. Customers generally consider a wide range of issues before committing to purchase our products, including product benefits, ability to operate with existing and future computer systems, vendor financial stability and longevity, ability to accommodate increased transaction volume and product reliability. Certain of our customers have become more cautious regarding their technology purchases given the current economic conditions and specifically the issues that continue to impact the financial and credit markets. The result is that our sales cycles may have lengthened in some instances, requiring more time to finalize transactions. In particular, in each of the past several quarters, transactions that we expected to close before the end of the quarter were delayed or suspended.

*Because a small number of customers account for a substantial portion of our revenues, the loss of a significant customer could cause a substantial decline in our revenues.

We derive a significant portion of our license and service revenue from a limited number of customers. The loss of a major customer could cause a decrease in revenues and net income. For the three months ended December 31, 2009, Royal Bank of Scotland plc and Lloyds TSB Bank accounted for 22% and 11% of our total revenue, respectively. For the three months ended December 31, 2008, Citicorp Credit Services, Inc. and Vodafone Group Services Limited and affiliated companies accounted for 13% and 25%, respectively, of our total revenue. While our customer concentration has fluctuated, we expect that a limited number of customers will continue to account for a substantial portion of our revenues in any given period. As a result, if we lose a major customer, or if a contract is delayed or cancelled or we do not contract with new major customers, our revenues and net income would be adversely affected. In addition, customers that have accounted for significant revenues in the past may not generate revenues in any future period, which may materially affect our operating results. For example, Vodafone Group Services Limited and affiliated companies, which had purchase commitments through the quarter ended June 30, 2009, may not purchase additional products or services with us. The deteriorating economic environment has resulted in failures of financial institutions and significant consolidation within the financial services industry from which we derive a significant portion of our customers and revenues. Accordingly, the risk that we could lose a significant customer is exacerbated in the current economic environment.

Given that our stock price is near its historical low, we may be subject to takeover overtures that will divert the attention of our management and Board, and require us to incur expenses for outside advisors.

Given that our stock price is near its historical low, we may be subject to takeover overtures. Evaluating and addressing these overtures would require the time and attention of our management and Board, divert them from their focus on our business, and require us to incur additional expenses on outside legal, financial and other advisors, all of which could materially and adversely affect our business, financial condition and results of operations.

In periods of worsening economic conditions, our exposure to credit risk and payment delinquencies on our accounts receivable significantly increases.

Our outstanding accounts receivables are generally not secured by any form of collateral. In addition, our standard terms and conditions permit payment within a specified number of days following the receipt of our product. While we have procedures to monitor and limit exposure to credit risk on our receivables, there can be no assurance such procedures will effectively limit our credit risk and avoid losses. As economic conditions deteriorate, certain of our customers have faced and may face liquidity concerns and have delayed and may delay or may be unable to satisfy

their payment obligations, which would have a material adverse effect on our financial condition and operating results.

Our cash and cash equivalents could be adversely affected if the financial institutions in which we hold our cash and cash equivalents fail.

Our cash and cash equivalents are highly liquid investments with original maturities of three months or less at the time of purchase. We maintain the cash and cash equivalents with reputable major financial institutions. Deposits with these banks exceed the Federal Deposit Insurance Corporation ("FDIC") insurance limits or similar limits in foreign jurisdictions. While we frequently monitor the cash balances in the operating accounts and adjust the balances as appropriate, these balances could be impacted if one or more of the financial institutions with which we deposit fails or is subject to other adverse conditions in the financial or credit markets. To date we have experienced no loss or lack of access to our invested cash or cash equivalents; however, we can provide no assurance that access to our invested cash and cash equivalents will not be impacted by adverse conditions in the financial and credit markets.

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*Our marketable securities could be adversely affected if the companies underlying the investments are not successful or if the stock market remains volatile.

Our marketable securities represent investments in common stock that could decline or fluctuate in value based upon the results of the investee companies, or a deterioration of general market conditions. Additionally, trading volumes can fluctuate and impact our ability to sell shares at favorable prices. To date we have experienced no losses associated with these possible events; however, we can provide no assurance that our investment in marketable securities will not be impacted by future results or adverse market conditions.

*To date, our sales have been concentrated in the insurance, healthcare, telecommunications and financial services markets, and if we are unable to continue sales in these markets or successfully penetrate new markets, our revenues may decline.

Sales of our products and services in several large markets—insurance, healthcare, telecommunications and financial services, accounted for approximately 87% and 82% of our total revenues for the three months ended December 31, 2009 and 2008, respectively. We expect that revenues from these markets will continue to account for a substantial portion of our total revenues for the foreseeable future. However, we are seeking to opportunistically expand in other markets. If we are unable to successfully increase penetration of our existing markets or achieve sales in additional markets, or if the overall economic conditions in our target markets further deteriorates, our revenues may decline. Some of our current and prospective customers, especially those in the financial services and insurance industries, have faced and may continue to face severe financial difficulties given their exposure to deteriorating financial and credit markets, as well as the mortgage and homebuilder sectors of the economy. This may cause our current and prospective customers to reduce, delay or terminate their spending on technology, which in turn would have an adverse impact on our bookings and revenues.

Historically, some of our products and services have assisted companies in attracting and retaining customers. To the extent financial institutions and other large companies shrink the size of their customer base, the demand for these products may be reduced.

Some of our customers have used our products to aggressively expand the size of their customer base. Our marketing, decisioning and enterprise solutions have been used to varying degrees on projects intended to manage leads, personalize marketing campaigns and deliver highly effective sales messages. Due to the current economic climate, many large financial institutions have been forced to deleverage, sell parts of their businesses, or otherwise reduce the size of their organizations. In these situations it is possible that the demand for our products has been, and may continue to be, reduced, resulting in lower revenues in the future.

Over the near term, we have shifted the focus of our sales staff towards Decisioning Management products and have reduced the marketing focus on Enterprise Foundation products to reflect market conditions. This change in focus may not be successful and may result in lower revenues.

Sales of Enterprise Foundation solutions generally have a much higher cost to a customer than Decisioning Management solutions. The magnitude of the professional services required to implement Enterprise Foundation projects is also much higher and often can take long periods of time to complete. Decisioning products are generally faster to implement and can produce a positive return on investment in a shorter period of time. Due to the current economic climate, our customers are focusing on those projects that are smaller and faster to complete. Accordingly, we have shifted our sales force to increase the marketing of these types of solutions. This plan may not be successful and, as a result, revenues may not meet our expectations. Further, license and services fees associated with our

Decisioning Management solutions generate smaller sales and, as a result, may result in lower revenues.

*Given current economic and market conditions, we may be forced to make additional reductions to our workforce.

In July 2005, October 2006, May 2008, October 2008 and first fiscal quarter of 2010, we reduced our workforce, in the case of the reductions in 2005, 2006 and 2008 by approximately 10% to 15% and in the case of the reduction in the first quarter of 2010 by approximately less than 1%. Given the current economic and market conditions, we may be forced to further reduce our workforce, which could materially and adversely affect our business, financial condition and results of operations.

*Fluctuations in the value of the U.S. dollar relative to foreign currencies could negatively affect our operating results and cash flows.

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A significant portion of our sales and operating expenses result from transactions outside of the U.S., often denominated in foreign currencies. These currencies include the United Kingdom Pound Sterling, the Euro, the Canadian Dollar, and the Chinese Yuan. Our international sales comprised 68 % and 65% of our total sales for the three months ended December 31, 2009 and 2008, respectively. Our future operating results, as well as our cash and deferred revenue balances, will continue to be subject to fluctuations in foreign currency rates, especially if international sales increase as a percentage of our total sales, and we may be negatively impacted by fluctuations in foreign currency rates in the future. For the three months ended December 31, 2009, we had a foreign currency transaction loss of $0.1 million. See Item 3, Quantitative and Qualitative Disclosures about Market Risk, for further discussions.

*Low gross margin in services revenues could adversely impact our overall gross margin and income.

Our services revenues have had lower gross margins than our license revenues. Service revenues comprised 67% and 66% of our total revenues for the three months ended December 31, 2009 and 2008, respectively. Gross margin on service revenues was 63% and 57% for the three months ended December 31, 2009 and 2008, respectively. License revenues comprised 33% and 34% of our total revenues for the three months ended December 31, 2009 and 2008, respectively. Gross margins on license revenues were 98% and 99% for the three months ended December 31, 2009 and 2008, respectively. As a result, an increase in the percentage of total revenues represented by services revenues, or an unexpected decrease in license revenues, could have a detrimental impact on our overall gross margins. To increase services revenues, we may expand our services organization, requiring us to successfully recruit and train a sufficient number of qualified services personnel, enter into new implementation projects and obtain renewals of current maintenance contracts by our customers. This expansion could further reduce gross margins in our services revenues. In addition, given the current economic environment, customers and potential customers have sought and may seek discounts on our services, or services at no charge, which has and would further reduce our services gross margins and materially and adversely affect our business, financial condition and results of operations.

*Our revenues decreased in fiscal year 2009 as compared to fiscal year 2008, in fiscal year 2008 as compared to fiscal year 2007, and in fiscal year 2009 we were not profitable, which may raise vendor viability concerns about us and thereby make it more difficult to consummate license transactions with new and existing customers.

Our revenues decreased materially in fiscal year 2009 as compared to fiscal year 2008 and in fiscal year 2008 as compared to fiscal year 2007. In addition, we were not profitable in the three months ended December 31, 2009, fiscal year 2009, or the fiscal years prior to September 30, 2007. As of December 31, 2009, we had an accumulated deficit of $237.6 million. We may incur losses in the future and cannot be certain that we can generate sufficient revenues to achieve profitability. Continued losses or decreased revenues may make many customers reluctant to enter into new large value license transactions without some assurance that we will operate profitably. If we fail to enter into new large value license transactions due to profitability and/or viability concerns by our vendors, our revenues could decline, which could further adversely affect our operating results.

Competition in our markets is intense and could reduce our sales and prevent us from achieving profitability.

Increased competition in our markets could result in price reductions for our products and services, reduced gross margins and loss of market share, any one of which could reduce our future revenues. The market for our products is intensely competitive, evolving and subject to rapid technological change. Historically, our primary competition has been from internal development, custom systems integration projects and application software competitors, each of whom we expect will continue to be a significant source of competition. In particular, we compete with:

- Internal information technology departments: in-house information technology departments of potential customers have developed or may develop systems that provide some or all of the functionality of our products.

- Custom systems integration projects: we compete with large systems integrators who may develop custom solutions for specific companies which may reduce the likelihood that they would purchase our products and services.

- Application software vendors: we compete with providers of stand-alone point solutions for web-based customer relationship management as well as traditional client/server-based, call-center service customer and sales-force automation solution providers, many of whom offer broad suites of application and other software.

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The enterprise software industry continues to undergo consolidation in sectors of the software industry in which we operate. IBM, SAP, Oracle and Sun Microsystems have made numerous acquisitions in the industry and Oracle has entered into an agreement to acquire Sun Microsystems, which transaction is subject to certain regulatory approvals. While we do not believe that the companies acquired by IBM, SAP and Oracle have been significant competitors of Chordiant in the past, these acquisitions may indicate that we may face increased competition from larger and more established entities in the future.

Many of our competitors have greater resources, broader customer relationships and broader product and service offerings than we do. In addition, many of these competitors have extensive knowledge of our industry. Current and potential competitors have established, or may further establish, cooperative relationships among themselves or with third parties to offer a single solution and to increase the ability of their products to address customer needs.

Our operating results and cash flows fluctuate significantly and delays in delivery or implementation of our products or changes in the payment terms with customers may cause unanticipated declines in revenues or cash flow, which could disappoint investors and result in a decline in our stock price.

A portion of our quarterly revenues depends primarily upon product implementation by our customers. We have historically recognized a significant portion of our license and services revenue through the percentage-of-completion accounting method, using labor hours incurred as the measure of progress towards completion of implementation of our products, and we expect this practice to continue. The percentage-of-completion accounting method requires ongoing estimates of progress of complicated and frequently changing technology projects. Documenting the measure of progress towards completion of implementation is subject to potential errors and changes in estimates. As a result, even minor errors or minor changes in estimates may lead to significant changes in accounting results which may be revised in later quarters due to subsequent information and events. Thus, delays or changes in customer business goals or direction when implementing our software may adversely impact our quarterly revenue. Additionally, we may increasingly enter into term, subscription or transaction-based licensing transactions that would cause us to recognize license revenue for such transactions over a longer period of time than we have historically experienced for our perpetual licenses. In addition, a significant portion of new customer orders have been booked in the third month of each calendar quarter, with many of these bookings occurring in the last two weeks of the third month. We expect this trend to continue, and therefore any failure or delay in bookings would decrease our quarterly revenue and cash flows. The terms and conditions of individual license agreements with customers vary from transaction to transaction. Historically, the Company has been able to obtain prepayments for product in some cases, but more recently we have entered into large transactions with payments from customers due over one or more years. Other transactions link payment to the delivery or acceptance of products. If we are unable to negotiate prepayments of fees our cash flows and financial ratios with respect to accounts receivable would be adversely impacted. If our revenues, operating margins or cash flows are below the expectations of the investment community, our stock price is likely to decline.

If we fail to introduce new versions and releases of functional and scalable products in a timely manner, customers may license competing products and our revenues may decline.

If we are unable to ship or implement enhancements to our products when planned, or fail to achieve timely market acceptance of these enhancements, we may suffer lost sales and could fail to achieve anticipated revenues. If our competitors release new products that are superior to our products in performance or price, or if we fail to enhance our products or introduce new products, features and functionality in a timely manner, demand for our products may decline. We have in the past experienced delays in the planned release dates of new products or new versions of our software products and upgrades. New versions of our products may not be released on schedule or may contain defects when released.

*If we are not able to successfully manage our partner operations in India, our operations and financial results may be adversely affected.

Since 2003, we have contracted with Ness Technologies Inc., Ness USA, Inc. (formerly Ness Global Services, Inc.) and Ness Technologies India, Ltd. (collectively, “Ness”) to attract, train, assimilate and retain sufficient highly qualified personnel to provide staffing for our consulting projects, technical support, product testing and certain sustaining engineering functions. As of December 31, 2009, we use the services of approximately 128 consultants through Ness, down from the 144 consultants used at December 31, 2008. In addition, as a result of the reductions in our workforce in recent years, we continue to have a significant dependence on Ness. This agreement is an important component of our strategy to address the business needs of our customers and manage our expenses. The success of this operation will depend on our ability and Ness’s ability to attract, train, assimilate and retain highly qualified personnel in the required periods. A disruption or termination of our relationship with Ness could adversely affect our operations. Failure to effectively manage the organization and operations will harm our business and financial results.

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If we become subject to intellectual property infringement claims, including copyright or patent infringement claims, these claims could be costly and time-consuming to defend, divert management's attention, cause product delays and have an adverse effect on our revenues and net income.

We expect that software product developers and providers of software in markets similar to our target markets will increasingly be subject to infringement claims as the number of products and competitors in our industry grows and the functionality of products overlap. Additionally, we are seeing copyright infringement claims being asserted by certain third party software developers. Any claims, with or without merit, could be costly and time-consuming to defend, divert our management's attention or cause product delays. If any of our products were found to infringe a third party's proprietary rights, we could be required to pay damages and/or enter into royalty or licensing agreements to be able to sell our products, if at all. Royalty and licensing agreements, if required, may not be available on terms acceptable to us or at all. A patent or copyright infringement claim could have a material adverse effect on our business, operating results and financial condition.

We are the subject of a suit by a person and related entity claiming that certain of our products infringe their copyrights. Such litigation is costly. If any of our products were found to infringe such copyrights, we could be required to pay damages. If we were to settle such claim, it could be costly.

*If we fail to adequately address the difficulties of managing our international operations, our revenues and operating expenses will be adversely affected.

For the three months ended December 31, 2009, international revenues were $15.1 million or approximately 68% of our total revenues. For the three months ended December 31, 2008, international revenues were $15.3 million or approximately 65% of our total revenues. We expect that international revenues will continue to represent a significant portion of our total revenues in future periods. We have faced, and will continue to face, difficulties in managing international operations, which include:

- Difficulties in hiring qualified local personnel;
- Seasonal fluctuations in customer orders;
- Longer accounts receivable collection cycles;
- Expenses associated with licensing products and servicing customers in foreign markets;
- Economic downturns and political uncertainty in international economies;
- Income tax withholding issues in countries in which we do not have a physical presence, resulting in non-recoverable tax payments;
- Complex transfer pricing arrangements between legal entities;
- Doing business and licensing our software to customers in countries with weaker intellectual property protection laws and enforcement capabilities; and
- Difficulties in commencing new operations in countries where the Company has not previously conducted business, including those associated with corporate and tax laws, banking relationships, product registrations, employment

laws, government regulation, product warranty laws and adopting to local customs and culture;

Any of these factors could have a significant impact on our ability to license products and provide services on a competitive and timely basis and could adversely affect our operating expenses and net income.

Because competition for qualified personnel is intense, we may not be able to retain or recruit personnel, which could impact the development and sales of our products.

If we are unable to hire or retain qualified personnel, or if newly hired personnel fail to develop the necessary skills or fail to reach expected levels of productivity, our ability to develop and market our products will be weakened. Our success depends largely on the continued contributions of our key management, finance, engineering, sales, marketing and

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professional services personnel. In particular, in prior years we have had significant turnover of our executives as well as in our sales, marketing and engineering organizations, and several key positions are held by people who have less than two years of experience in their roles with the Company. If these people are not well suited to their new roles, then this could result in the Company having problems in executing its strategy or in developing and marketing new products. Because of the dependency on a small number of large deals, we are uniquely dependent upon the talents and relationships of a few executives and have no guarantee of their retention. Changes in key sales management could affect our ability to maintain existing customer relationships or to close pending transactions. Further, particularly in the current economic environment, employees or potential employees may choose to work for larger, more profitable companies.

The application of percentage-of-completion and completed contract accounting to our business is complex and may result in delays in the reporting of our financial results and revenue not being recognized as we expect.

Although we attempt to use standardized license agreements designed to meet current revenue recognition criteria under generally accepted accounting principles, we must often negotiate and revise terms and conditions of these standardized agreements, particularly in multi-product transactions. At the time of entering into a transaction, we assess whether any services included within the arrangement require us to perform significant implementation or customization essential to the functionality of our products. For contracts involving significant implementation or customization essential to the functionality of our products, we recognize the license and professional consulting services revenues using the percentage-of-completion accounting method using labor hours incurred as the measure of progress towards completion. The application of the percentage-of-completion method of accounting is complex and involves judgments and estimates, which may change significantly based on customer requirements. This complexity combined with changing customer requirements could result in delays in the proper determination of our percentage-of-completion estimates and revenue not being recognized as we expect.

In the past we have also entered into co-development projects with our customers to jointly develop new applications, often over the course of a year or longer. In such cases we may only be able to recognize revenue upon delivery of the new application. The accounting treatment for these co-development projects could result in delays in the recognition of revenue. If we were to enter into similar transactions, the failure to successfully complete these projects to the satisfaction of the customer could have a material adverse effect on our business, operating results and financial condition.

If our products do not operate effectively in a company-wide environment, we may lose sales and suffer decreased revenues.

If existing customers have difficulty deploying our products or choose not to fully deploy our products, it could damage our reputation and reduce revenues. Our success requires that our products be highly scalable and able to accommodate substantial increases in the number of users. Our products are expected to be deployed on a variety of computer software and hardware platforms and to be used in connection with a number of third-party software applications by personnel who may not have previously used application software systems or our products. These deployments present very significant technical challenges, which are difficult or impossible to predict. If these deployments do not succeed, we may lose future sales opportunities and suffer decreased revenues. If we underestimate the resources required to meet the expectations we have set with a customer when we set prices, then we may experience a net loss on that customer engagement. If this happens with a large customer engagement then this could have a material adverse effect on our financial results.

Defects in our products could diminish demand for our products and result in decreased revenues, decreased market acceptance and injury to our reputation.

Errors may be found from time-to-time in our existing, new, acquired or enhanced products. Any significant software errors in our products may result in decreased revenues, decreased sales, and injury to our reputation and/or increased warranty and repair costs. Although we conduct extensive product testing during product development, we have in the past discovered and may in the future discover software errors in our products as well as in third-party products, and as a result have experienced and may in the future experience delays in the shipment of our new products.

If our products do not keep up with advancing technological requirements or operate with the hardware and software platforms used by our customers, our customers may license competing products and our revenues will decline.

If our products fail to satisfy advancing technological requirements of our customers and potential customers, the market acceptance of these products could be reduced. We currently serve a customer base with a wide variety of constantly

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changing hardware, software applications and networking platforms. Customer acceptance of our products depends on many factors, including our ability to integrate our products with multiple platforms and existing or legacy systems, and our ability to anticipate and support new standards, especially Internet and enterprise Java standards. If our products do not keep up with advancing technological requirements or operate with the hardware and software platforms used by our customers, our customers may license competing products and our revenues will decline.

If we fail to maintain and expand our relationships with systems integrators and other business partners, our ability to develop, market, sell and support our products may be adversely affected.

Our development, marketing and distribution strategies rely on our ability to form and maintain long-term strategic relationships with systems integrators, in particular, with our existing business alliance partners IBM, Ness, Electronic Data Systems, Tata Consultancy Services and HCL Technologies. These business relationships often consist of joint marketing programs, technology partnerships and resale and distribution arrangements. Although most aspects of these relationships are contractual in nature, many important aspects of these relationships depend on the continued cooperation between the parties. Divergence in strategy, change in focus, competitive product offerings or potential contract defaults may interfere with our ability to develop, market, sell or support our products, which in turn could harm our business. If any of IBM, Ness, Electronic Data Systems, Tata Consultancy Services or HCL Technologies were to terminate their agreements with us or our relationship were to deteriorate, it could have a material adverse effect on our business, financial condition and results of operations. In many cases, these parties have extensive relationships with our existing and potential customers and influence the decisions of these customers. A number of our competitors have stronger relationships with IBM, Ness, Electronic Data Systems, Tata Consultancy Services and HCL Technologies and, as a result, these systems integrators may be more likely to recommend competitors' products and services. Over the past several years, IBM has acquired a number of software companies. While we do not believe those companies were direct competitors of Chordiant in the past, IBM's acquisition of these companies may indicate that IBM will become a more significant competitor of ours in the future. While the Company currently has a good relationship with IBM, this relationship and the Company's strategic relationship agreement with IBM may be harmed if the Company increasingly finds itself competing with IBM. Our relationships with systems integrators and their willingness to recommend our products to their customers could be harmed if the Company were to be subject to a takeover attempt from a competitor of such systems integrators.

If systems integrators fail to properly implement our software, our business, reputation and financial results may be harmed.

We often rely on systems integrators to implement our products. As a result, we have less quality control over the implementation of our software with respect to these transactions and are more reliant on the ability of our systems integrators to correctly implement our software. If these systems integrators fail to properly implement our software, our business, reputation and financial results may be harmed.

Anti-takeover provisions could make it more difficult for a third-party to acquire us.

We have adopted a stockholder rights plan and initially declared a dividend distribution of one right for each outstanding share of common stock to stockholders of record as of July 21, 2008. Each right entitles the holder to purchase one one-hundredth of a share of our Series A Junior Participating Preferred Stock for $20. Under certain circumstances, if a person or group acquires 20 percent or more of our outstanding common stock, holders of the rights (other than the person or group triggering their exercise) will be able to purchase, in exchange for the $20 exercise price, shares of our common stock or of any company into which we are merged, having a value of $40. The rights expire on July 21, 2011, unless extended by our Board of Directors. Because the rights may substantially dilute the stock ownership of a person or group attempting to acquire us without the approval of our Board of Directors, our

rights plan could make it more difficult for a third-party to acquire us (or a significant percentage of our outstanding capital stock) without first negotiating with our Board of Directors regarding that acquisition.

In addition, our Board of Directors has the authority to issue up to 51 million shares of Preferred Stock (of which 500,000 shares have been designated as Series A Junior Participating Preferred Stock) and to fix the designations and the powers, preferences and rights, and the qualifications, limitations and restrictions thereof. The rights of the holders of our common stock may be subject to, and may be adversely affected by, the rights of the holders of any Preferred Stock that may be issued in the future. The issuance of Preferred Stock may have the effect of delaying, deterring or preventing a change of control of Chordiant without further action by the stockholders and may adversely affect the voting and other rights of the holders of our common stock.

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Further, certain provisions of our charter documents, including a provision limiting the ability of stockholders to raise matters at a meeting of stockholders without giving advance notice, may have the effect of delaying or preventing changes in control or management of Chordiant, which could have an adverse effect on the market price of our stock. In addition, our charter documents do not permit cumulative voting, which may make it more difficult for a third party to gain control of our Board of Directors. Similarly, we have a classified Board of Directors whereby approximately one-third of our Board members are elected annually to serve for three-year terms, which may also make it more difficult for a third party to gain control of our Board of Directors. Further, we are subject to the anti-takeover provisions of Section 203 of the Delaware General Corporation Law, which will prohibit us from engaging in a “business combination” with an “interested stockholder” for a period of three years after the date of the transaction in which the person became an interested stockholder, even if such combination is favored by a majority of stockholders, unless the business combination is approved in a prescribed manner. The application of Section 203 also could have the effect of delaying or preventing a change of control or management.

We may not have the workforce necessary to support our platform of products if demand for our products substantially increased, and, if we need to rebuild our workforce in the future, we may not be able to recruit personnel in a timely manner, which could negatively impact the development, sales and support of our products.

In recent years, we have, from time to time, reduced our workforce. In the event that demand for our products increases, we may need to rebuild our workforce or increase outsourced functions to companies based in foreign jurisdictions and we may be unable to hire, train or retain qualified personnel in a timely manner, which may weaken our ability to market our products in a timely manner, negatively impacting our operations. Our success depends largely on ensuring that we have adequate personnel to support our suite of products as well as the continued contributions of our key management, finance, engineering, sales, marketing and professional services personnel.

We depend on technology licensed to us by third parties, and the loss or inability to maintain these licenses could prevent or delay sales of our products.

We license from several software providers technologies that are incorporated into our products. We anticipate that we will continue to license technology from third parties in the future. This software may not continue to be available on commercially reasonable terms, if at all. While currently we are not materially dependent on any single third party for such licenses, the loss of the technology licenses could result in delays in the license of our products until equivalent technology is developed or identified, licensed and integrated into our products. Given the current economic environment, the risk that one or more of our suppliers or vendors may go out of business or be unable to meet their contractual obligations to us is exacerbated. Even if substitute technologies are available, there can be no guarantee that we will be able to license these technologies on commercially reasonable terms, if at all, which could have a material adverse effect on our business, operating results and financial condition.

Defects in third party products associated with our products could impair our products’ functionality and injure our reputation.

The effective implementation of our products depends upon the successful operation of third-party products in conjunction with our products. Any undetected defects in these third-party products could prevent the implementation or impair the functionality of our products, delay new product introductions or injure our reputation. In the past, while our business has not been materially harmed, product releases have been delayed as a result of errors in third-party software and we have incurred significant expenses fixing and investigating the cause of these errors.

Our customers and systems integration partners may have the ability to alter our source code and resulting inappropriate alterations could adversely affect the performance of our products, cause injury to our reputation and increase operating expenses.

Customers and systems integration partners may have access to the computer source code for certain elements of our products and may alter the source code. Alteration of our source code may lead to implementation, operation, technical support and upgrade problems for our customers. This could adversely affect the market acceptance of our products and our reputation, and any necessary investigative work and repairs could cause us to incur significant expenses and delays in implementation, which could have a material adverse effect on our business, operating results and financial condition.

Our failure to successfully acquire or integrate with future acquired or merged companies and technologies could prevent us from operating efficiently.

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Our business strategy includes pursuing opportunities to grow our business, both through internal growth and through mergers, acquisitions and technology and other asset transactions. To implement this strategy, we may be involved in various related discussions and activity. Such endeavors may involve significant risks and uncertainties, including that we may not consummate opportunities that we pursue. These endeavors could distract management from current operations that may adversely affect the Company's financial condition and operating results. Merger and acquisition transactions are motivated by many factors, including, among others, our desire to grow our business, obtain recurring support and maintenance revenue streams, acquire skilled personnel, obtain new technologies and expand and enhance our product offerings or markets. Mergers and acquisitions of high-technology companies are inherently risky, and the Company cannot be certain that any acquisition will be successful and will not materially harm the Company's business, operating results or financial condition. Generally, acquisitions involve numerous risks, including: (i) the benefits of the acquisition (such as cost savings and synergies) not materializing as planned or not materializing within the time periods or to the extent anticipated; (ii) the Company's ability to manage acquired entities' people and processes, particularly those that are headquartered in separate geographical locations from the Company's headquarters; (iii) the possibility that the Company will pay more than the value it derives from the acquisition; (iv) difficulties in integration of the operations, technologies, content and products of the acquired companies; (v) the assumption of certain known and unknown liabilities of the acquired companies; (vi) difficulties in retaining key relationships with customers, partners and suppliers of the acquired company; (vii) the risk of diverting management's attention from normal daily operations of the business; (viii) the Company's ability to issue new releases of the acquired company's products on existing or other platforms; (ix) negative impact to the Company's financial condition and results of operations and the potential write down of impaired goodwill and intangible assets resulting from combining the acquired company's financial condition and results of operations with our financial statements; (x) risks of entering markets in which the Company has no or limited direct prior experience; (xi) incurring significant legal and accounts costs to investigate and analyze potential merger opportunities which fail to be completed; and (xii) the potential loss of key employees of the acquired company. Realization of any of these risks in connection with any technology transaction or asset purchase we have entered into, or may enter into, could have a material adverse effect on our business, operating results and financial condition.

If we do not maintain effective internal controls over financial reporting, investors could lose confidence in our financial reporting and customers may delay purchasing decisions, which would harm our business and the market price of our common stock.

Effective internal controls are necessary for us to provide reliable financial reports. If we cannot provide reliable financial reports, our business could be harmed. We are a complex company with complex accounting issues and thus subject to related risks of errors in financial reporting which may cause problems in corporate governance, the costs of which may outweigh the costs of the underlying errors themselves.

If we are not successful in maintaining effective internal controls over financial reporting, customers may delay purchasing decisions or we may lose customers, create investor uncertainty, face litigation and the market price of our common stock may decline.

Changes in our revenue recognition model could result in short-term declines in revenue.

Historically, we have recognized revenue for a high percentage of our license transactions on the percentage-of-completion method of accounting or upon the delivery of product. If we were to enter into new types of transactions accounted for on a subscription or term basis, revenues might be recognized over a longer period of time. The impact of this change might make revenue recognition more predictable over the long term, but it might also result in a short-term reduction of revenue as the new transactions took effect.

We may encounter unexpected delays in maintaining the requisite internal controls over financial reporting and we expect to incur ongoing expenses and diversion of management's time as a result of performing future system and process evaluation, testing and remediation required to comply with future management assessment and auditor attestation requirements.

Management must report on, and our independent registered public accounting firm must attest to, our internal control over financial reporting as required by Section 404 of SOX, within the time frame required by Section 404. We may encounter unexpected delays in satisfying those requirements. Accordingly, we cannot be certain about the timely completion of our evaluation, testing and remediation actions or the impact that these activities will have on our operations. We also expect to incur ongoing expenses and diversion of management's time as a result of performing ongoing system and process

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evaluations and the testing and remediation required to comply with management's assessment and auditor attestation requirements. If we are not able to timely comply with the requirements set forth in Section 404 in future periods, we might be subject to sanctions or investigation by the regulatory authorities. Any such action could adversely affect our business or financial results.

We may experience additional volatility in our operating results as a result of our periodic evaluation of our goodwill and deferred tax assets.

We have recorded significant goodwill and deferred tax asset balances that are subject to either impairment or realizability evaluations under U.S. Generally Accepted Accounting Principles. Such evaluations are based on factors including our future profitability and market value. As a result, if we experience significant declines in those measurements, these assets could be subject to impairment or write-off, which would result in additional volatility to our operating results.

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Item 6. Exhibits.

The exhibits listed on the accompanying index to exhibits are filed or incorporated by reference (as stated therein) as part of this Quarterly Report on Form 10-Q.

Chordiant Software, Inc.

SIGNATURES

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

CHORDIANT SOFTWARE, INC.

By: /s/ PETER S. NORMAN
Peter S. Norman
Chief Financial Officer and
Principal Accounting Officer

Dated: January 28, 2010

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EXHIBIT INDEX

Exhibit Number	Description of Document	Form	Date	Filed Herewith
3.1	Amended and Restated Certificate of Incorporation of Chordiant Software, Inc.	Form 10-K	11/20/2008	
3.2	Certificate of Designation of Series A Junior Participating Preferred Stock	Form 8-K	7/11/2008	
3.3	Amended and Restated Bylaws of Chordiant Software, Inc.	Form 8-K	6/3/2008	
4.1	Specimen Common Stock Certificate	Form S-1 (No. 333-92187)	2/7/2000	
4.2	Rights Agreement dated as of July 10, 2008 by and between Chordiant Software, Inc. and American Stock Transfer & Trust Company, LLC	Form 8-K	7/11/2008	
4.3	Form of Rights Certificate	Form 8-K	7/11/2008	
10.31*	Separation Agreement by and between Chordiant Software, Inc. and Charles Altomare dated October 9, 2009.	Form 10-K	11/19/2009	
10.71 *	Form of Chordiant Software, Inc. 2005 Equity Incentive Plan Restricted Stock Unit Grant Notice and Chordiant Software, Inc. 2005 Equity Incentive Plan Restricted Stock Unit Agreement (No Holding Period)	Form 8-K	11/19/2009	
10.72 *	Form of Chordiant Software, Inc. 2005 Equity Incentive Plan Restricted Stock Unit Grant Notice for Non-U.S. Employees and Chordiant Software, Inc. 2005 Equity Incentive Plan Restricted Stock Unit Agreement for Non-U.S. Employees (No Holding Period)	Form 8-K	11/19/2009	
10.73*	A description of certain compensation arrangements between Chordiant Software, Inc. and its executive officers.	Form 8-K	11/19/2009	
10.74*	Amended and Restated 1999 Non-Employee Directors' Stock Option Plan	Schedule 14A	12/18/2009	
10.75 *†	Chordiant Software, Inc. Fiscal Year 2010 Executive Incentive Bonus Plan			X
10.76 *†	Chordiant Software, Inc. Fiscal Year 2010 Senior Vice President and General Manager Worldwide Client Services Incentive Bonus Plan			X
10.77 *†	Chordiant Software, Inc. Fiscal Year 2010 General Counsel Incentive Bonus Plan			X
21.1	Subsidiaries of Chordiant Software, Inc.			X
31.1				X

	Certification required by Rule 13a-14(a) or Rule 15d-14(a)	
31.2	Certification required by Rule 13a-14(a) or Rule 15d-14(a)	X
32.1#	Certification required by Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350)	

* Management contract or compensatory plan or arrangement.

\# The certification attached as Exhibit 32.1 is not deemed filed with the Securities and Exchange Commission and is not incorporated by reference into any filing of Chordiant Software, Inc., whether made before or after the date of this Form 10-Q irrespective of any general incorporation language contained in such filing.

† Confidential treatment has been requested with respect to certain portions of this exhibit. Omitted portions have been filed separately with the SEC pursuant to Rule 24b-2 of the Securities Exchange Act of 1934.