SERENA SOFTWARE INC
Form 10-Q
December 15, 2011
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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 OCTOBER 31, 2011

OR

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NO. 000-25285

SERENA SOFTWARE, INC.

(Exact name of registrant as specified in its charter)

DELAWARE	**94-2669809**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

1900 SEAPORT BOULEVARD, REDWOOD CITY, CALIFORNIA 94063-5587

(Address of principal executive offices, including zip code)

650-481-3400

(Registrant s telephone number, including area code)

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

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

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

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer x	(Do not check if a smaller reporting company)	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 November 30, 2011, 98,392,478 shares of the registrant s common stock, $0.01 par value per share, were outstanding.

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SERENA SOFTWARE, INC.

Condensed Consolidated Balance Sheets

(In thousands, except share data)

(Unaudited)

	October 31, 2011	January 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	$ 79,100	$ 126,374
Accounts receivable, net of allowance of $1,038 and $1,095 at October 31, 2011 and January 31, 2011, respectively	24,911	22,903
Deferred taxes, net	4,462	4,456
Prepaid expenses and other current assets	5,321	6,152
Total current assets	113,794	159,885
Property and equipment, net	5,003	3,602
Goodwill	462,400	462,400
Other intangible assets, net	86,590	118,249
Other assets	3,904	3,901
TOTAL ASSETS	$ 671,691	$ 748,037
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Short-term debt and current portion of long-term debt	$	$ 7,500
Accounts payable	1,378	2,438
Income taxes payable	5,003	6,284
Accrued expenses	17,600	22,291
Accrued interest on term loan and subordinated notes	5,190	8,241
Deferred revenue	56,232	68,946
Total current liabilities	85,403	115,700
Deferred revenue, less current portion	7,689	10,246
Long-term liabilities	4,397	4,036
Deferred taxes	24,516	36,714
Term loans	308,500	308,500
Revolving credit facilities		35,000
Senior subordinated notes	134,265	134,265
Total liabilities	564,770	644,461
Commitments and contingencies		
Stockholders equity:		

Preferred stock, $0.01 par value; 10,000,000 shares authorized and no shares issued and outstanding at October 31, 2011 and January 31, 2011		
Series A Preferred stock, $0.01 par value; 1 share authorized, issued and outstanding at October 31, 2011 and January 31, 2011		
Common stock, $0.01 par value; 200,000,000 shares authorized; 98,392,478 and 98,389,625 shares issued and outstanding at 31, 2011 and January 31, 2011, respectively	984	984
Additional paid-in capital	516,071	515,182
Accumulated other comprehensive loss	(1,350)	(900)
Accumulated deficit	(408,784)	(411,690)
Total stockholders equity	106,921	103,576
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 671,691	$ 748,037

See accompanying notes to condensed consolidated financial statements.

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SERENA SOFTWARE, INC.

Condensed Consolidated Statements of Operations

For the Three Months and Nine Months Ended October 31, 2011 and 2010

(In thousands)

(Unaudited)

	Three Months Ended October 31, 2011	Three Months Ended October 31, 2010	Nine Months Ended October 31, 2011	Nine Months Ended October 31, 2010
Revenue:				
Software licenses	$ 14,637	$ 11,464	$ 38,347	$ 32,926
Maintenance	35,163	36,596	106,179	107,787
Professional services	5,858	4,832	17,483	14,068
Total revenue	55,658	52,892	162,009	154,781
Cost of revenue:				
Software licenses	1,006	432	1,803	965
Maintenance	2,949	2,895	8,662	8,585
Professional services	5,263	4,772	16,425	13,112
Amortization of acquired technology	21	8,333	3,672	25,362
Total cost of revenue	9,239	16,432	30,562	48,024
Gross profit	46,419	36,460	131,447	106,757
Operating expenses:				
Sales and marketing	15,446	13,393	45,646	39,544
Research and development	6,757	7,839	20,296	23,791
General and administrative	3,406	3,896	10,573	12,157
Amortization of intangible assets	9,198	9,203	27,599	27,609
Restructuring, acquisition and other charges	662	910	2,331	3,532
Goodwill impairment				1,433
Total operating expenses	35,469	35,241	106,445	108,066
Operating income (loss)	10,950	1,219	25,002	(1,309)
Other income (expense):				
Interest income	34	53	105	143
Loss on early extinguishment of debt		(243)		(243)
Interest expense	(6,464)	(5,825)	(19,181)	(19,018)
Change in the fair value of derivative instrument				1,616
Amortization and write-off of debt issuance costs	(366)	(546)	(1,041)	(1,415)
Amend and extend transaction fees			(1,487)	
Total other income (expense)	(6,796)	(6,561)	(21,604)	(18,917)

Income (loss) before income taxes	4,154	(5,342)	3,398	(20,226)
Income tax expense (benefit)	952	(4,628)	492	(11,855)
Net income (loss)	$ 3,202	$ (714)	$ 2,906	$ (8,371)

See accompanying notes to condensed consolidated financial statements.

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SERENA SOFTWARE, INC.

Condensed Consolidated Statements of Cash Flows

For the Nine Months Ended October 31, 2011 and 2010

(In thousands)

(Unaudited)

	Nine Months Ended October 31,	
	2011	2010
Cash flows from operating activities:		
Net income (loss)	$ 2,906	$ (8,371)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization of acquired technology and other intangibles	33,441	55,236
Deferred income taxes	(12,205)	(20,112)
Loss on early extinguishment of debt		243
Interest paid in excess of interest accrued	(3,004)	(4,109)
Fair market value adjustment on the interest rate swap		(1,616)
Amortization and write off of debt issuance costs	2,528	1,415
Stock-based compensation	888	2,852
Restructuring, acquisition and other charges		(380)
Goodwill impairment		1,433
Changes in operating assets and liabilities:		
Accounts receivable	(2,008)	609
Prepaid expenses and other assets	258	(585)
Accounts payable	(944)	290
Income taxes payable	(1,218)	304
Accrued expenses and other liabilities	(4,357)	(5,444)
Deferred revenue	(15,271)	(18,896)
Net cash provided by operating activities	1,014	2,869
Cash flows used in investing activities:		
Capital expenditures	(3,077)	(1,837)
Capital expenditures for internal use software	(305)	(349)
Net cash used in investing activities	(3,382)	(2,186)
Cash flows used in financing activities:		
Amend and extend transaction fees	(1,958)	
Common stock repurchased under stock repurchase plans and other plans		(347)
Repurchase of option rights under employee stock option plan	(2)	(63)
Exercise of stock options under employee stock option plan	4	24
Principal payments and early extinguishments under the term credit facility and senior subordinated notes	(42,500)	(40,930)
Net cash used in financing activities	(44,456)	(41,316)
Effect of exchange rate changes on cash and cash equivalents	(450)	(651)
Net decrease in cash and cash equivalents	(47,274)	(41,284)

Cash and cash equivalents at beginning of period	126,374	124,996
Cash and cash equivalents at end of period	$ 79,100	$ 83,712
Supplemental disclosures of cash flow information:		
Income taxes paid, net of refunds	$ 14,161	$ 7,292
Interest expense paid	$ 22,185	$ 23,127

See accompanying notes to condensed consolidated financial statements.

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(1) Description of Business and Summary of Significant Accounting Policies

(a) Description of Business

SERENA Software, Inc. (SERENA or the Company) is the largest global independent software company in terms of revenue solely focused on managing change and processes across information technology, or IT, environments. The Company s products and services primarily address the complexity of application lifecycle management, or ALM, and are used by customers to manage the development of, and control change in, mission critical applications within both mainframe and distributed systems environments. In addition, the Company provides products and services to enable customers to rapidly address IT service management, or ITSM, and business process challenges through the use of visually designed process workflows. The Company s products and services allow customers to orchestrate and manage their application development, IT and business processes by automating and integrating disparate ALM and ITSM products and processes, improving process visibility and consistency, enhancing software integrity, mitigating application development risks, supporting auditability and regulatory compliance, and boosting productivity. The Company s revenue is generated by software licenses, maintenance contracts and professional services. The Company s software products are typically installed within customer IT environments and generally accompanied by renewable annual maintenance contracts.

(b) Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation. The Company has prepared the accompanying unaudited condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America.

(c) Significant Accounting Policies

The Company s significant accounting policies are described in the notes to the Company s consolidated financial statements, included in the Company s Annual Report on Form 10-K for the fiscal year ended January 31, 2011 filed with the Securities and Exchange Commission (SEC) on May 2, 2011. There have been no changes to the Company s significant accounting policies.

(d) Spyglass Merger Corp.

On March 10, 2006, Spyglass Merger Corp., an affiliate of Silver Lake, a private equity firm, merged with and into us, a transaction we refer to in this report as the merger. As a result of the merger, our common stock ceased to be traded on the NASDAQ National Market and we became a privately-held company, with approximately 56.5% of our common stock at the time of the merger on a fully diluted basis owned by investment funds affiliated with Silver Lake.

(2) Stock-Based Compensation

Stock-based compensation cost is typically measured at the grant date based on the fair value of the award. The Company has elected the graded-vesting attribution method for recognizing stock-based compensation expense over the requisite service period for each separately vesting tranche of awards as though the awards were, in substance, multiple awards.

SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

2006 Stock Incentive Plan

Following the completion of the Merger on March 10, 2006, the Company established a new stock incentive plan, the 2006 Stock Incentive Plan (the 2006 Plan), governing, among other things, the grant of options, restricted stock bonuses, and other forms of share-based payments covering shares of the Company s common stock to our employees (including officers), directors and consultants. The Company s common stock representing 12% of outstanding common stock on a fully diluted basis as of the date of the Merger was reserved for issuance under the 2006 Plan. Stock options granted under the 2006 Plan are either time options that vest and become exercisable over a four-year period or time and performance options that vest based on the achievement of certain performance targets over a five-year period following the date of grant. All options granted under the 2006 Plan will expire not later than ten years from the date of grant, but generally will terminate earlier upon termination of employment. In the event of a sale of substantially all of the assets of the Company, or a merger or acquisition of the Company, the Board of Directors may provide that awards granted under the 2006 Plan will be cashed out, continued, replaced with new awards that substantially preserve the terms of the original awards, or terminated, with acceleration of vesting of the original awards determined at the discretion of the Board of Directors.

In the quarter ended October 31, 2009, the Company completed a tender offer permitting all eligible employees and its independent directors to exchange, on a one-for-one basis, stock options granted under the 2006 Plan for new stock options granted under Serena s Amended and Restated 2006 Stock Incentive Plan (the Amended 2006 Plan) having a lower exercise price and different vesting terms. Eligible optionholders exchanged part or all of their time-based options for new time-based options having a vesting period, generally, of three years and an exercise price of $3.00 per share, the fair market value of Serena s common stock after the closing of the tender offer. Eligible employees who were not executive officers or officers of the Company exchanged part or all of their performance-based options for new time-based options having a vesting period of three years. Executive officers and officers of the Company exchanged part or all of their performance-based options for new performance-based options having a vesting period of three years and six months, with vesting based on the achievement of EBITA targets established by Serena s board of directors.

Roll Over Options

In connection with the Merger, the management participants were permitted to elect to have the surviving company in the merger assume some or all of the Serena stock options that they held immediately prior to the merger and that had an exercise price of less than $24.00 per share. The number of shares subject to these roll over options was adjusted to be the number of shares equal to the product of (1) the difference between $24.00 and the exercise price of the option and (2) the quotient of the total number of shares of Serena s common stock subject to such option, divided by $3.75. The exercise price of these roll over options was adjusted to $1.25 per share. The roll over options are subject to terms of the original option agreements with Serena, except that in the event of a change in control of Serena (as defined in the 2006 Plan), the treatment of the roll over options upon such transaction will be determined in accordance with the terms of the 2006 Plan.

The Amended 2006 Plan does not include an evergreen provision to provide for automatic increases in the number of shares available for grant. Any increase in the number of shares available for grant under the Amended 2006 Plan would require approval from the Company s Board of Directors.

As of October 31, 2011, a total of 12,597,813 shares of common stock were reserved for issuance upon the exercise of stock options and for the future grant of stock options or awards under the Amended 2006 Plan.

SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

The fair value of each stock option grant under the stock option plans is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants in the three months and nine months ended October 31, 2011 and 2010.

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2011	2010	2011	2010
Expected life (in years)	3.0	2.4 to 3.0	3.0	2.4 to 3.0
Risk-free interest rate	0.1% to 0.4%	0.2% to 0.8%	0.1% to 1.2%	0.2% to 1.5%
Volatility	24% to 34%	16% to 33%	19% to 34%	16% to 38%

The Black-Scholes option-pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option-pricing models require the input of highly subjective assumptions including the expected stock price volatility.

With respect to the amounts set forth above, the Company s expected volatility is based on the combination of historical volatility of the Company s common stock and the Company s peer group s common stock over the period commensurate with the expected life of the options. To assist management in determining the estimated fair value of the Company s common stock, the Company engages a third-party valuation specialist to perform a valuation on a semi-annual basis as of January 31 and July 31. In estimating the fair value of the Company s common stock, the external valuation firm employs a two-step approach that first estimates the fair value of the Company as a whole, and then allocates the enterprise value to the Company s common stock. The risk-free interest rates are derived from the average U.S. Treasury constant maturity rates during the period and approximate the rate in effect at the time of grant for the respective expected term. The expected terms are based on the observed and expected time to post-vesting exercise or cancellation of options. The Company does not anticipate paying any cash dividends in the foreseeable future and therefore uses an expected dividend yield of zero. The Company estimates forfeitures at the time of grant and revises those estimates in subsequent periods if actual forfeitures differ from those estimates. The Company uses forecasted projections to estimate pre-vesting option forfeitures and records stock-based compensation expense only for those awards that are expected to vest.

General Stock Option Information

The following table sets forth the summary of option activity under our stock option programs for the nine months ended October 31, 2011:

	Options Available for Grant	Number of Options Outstanding	Weighted Average Exercise Price
Balances as of January 31, 2011	882,171	11,046,652	$ 2.79
Granted	(677,500)	677,500	$ 3.56
Exercised		(3,882)	$ 1.25
Cancelled(1)		(77,128)	$ 1.25
Cancelled	3,055,161	(3,055,161)	$ 3.02
Restricted stock units granted, net of cancellations(2)	750,000		
Balances as of October 31, 2011(3)	4,009,832	8,587,981	$ 2.78

(1) Represents cancelled Roll Over options which are not returned to the available-for-grant stock option pool.

SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(2) Restricted stock units are granted from the stock option pool. In the nine months ended October 31, 2011, a total of 750,000 units were cancelled and returned to the available-for-grant stock option pool. There were no units granted in the nine months ended October 31, 2011. See *Restricted Stock Units* below for further details.

(3) The number of options vested and expected to vest, net of estimated forfeitures, as of October 31, 2011 was 5,586,587 and has a weighted average exercise price of $2.63.

Information regarding the stock options outstanding at October 31, 2011 is summarized as follows:

Range of Exercise Price	Number Outstanding(1)(2)	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable(1)(2)	Weighted Average Exercise Price
$1.25	1,389,456	1.66 years	$ 1.25	1,389,456	$ 1.25
$3.00	5,191,027	7.86 years	$ 3.00	2,166,198	$ 3.00
$3.08	813,332	8.13 years	$ 3.08	213,186	$ 3.08
$3.19	541,666	8.66 years	$ 3.19	155,407	$ 3.19
$3.54	362,500	9.87 years	$ 3.54		
$3.58	290,000	9.32 years	$ 3.58	44,436	$ 3.58
	8,587,981	7.07 years	$ 2.78	3,968,683	$ 2.41

(1) The table shows options without consideration of expected forfeitures. The Company estimates its forfeiture rate to be approximately 2% per year.

(2) Total stock options outstanding at October 31, 2011 consist of 3,922,384 time-based options, 3,276,141 performance-based options and 1,389,456 roll over options. The Company presently does not record compensation expense associated with performance-based options because management believes their vesting is not probable.

The aggregate intrinsic value for options outstanding and options exercisable as of October 31, 2011 was $6.5 million and $4.5 million, respectively.

Restricted Stock Units

The Company has entered into restricted stock agreements with certain of its employees. These units are unvested and subject to each employee s continued employment with the Company for a period of three years from the date of issuance. In addition, if the Company is subject to a change in control or an initial public offering (as defined in these agreements) while the employee remains an employee of the Company, his or her remaining unvested restricted stock units will immediately vest in part or in full depending on the price per share at the time of such event.

The following table sets forth the summary of restricted stock units activity under our restricted stock purchase agreements for the nine months ended October 31, 2011:

	Non-Vested Shares	Weighted Average Grant Date

		Fair Value
Balances as of January 31, 2011	2,020,000	$ 3.01
Granted		
Cancelled	(750,000)	$ 3.00
Balances as of October 31, 2011	1,270,000	$ 3.02

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

The aggregate intrinsic value for restricted stock units outstanding as of October 31, 2011 was $4.5 million. There were no restricted stock units exercisable as of October 31, 2011.

As of October 31, 2011, total unrecognized compensation costs related to unvested stock options and restricted stock was $4.4 million. Costs related to unvested stock options are expected to be recognized over a period of 3 to 3.5 years and costs related to the restricted stock are expected to be recognized over a period of 3 to 4 years from grant date.

Stock-based compensation expense for the three and nine months ended October 31, 2011 and 2010 is categorized as follows (in thousands):

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2011	2010	2011	2010
Cost of maintenance	$ 16	$ 19	$ 46	$ 72
Cost of professional services	1	5	54	35
Stock-based compensation expense in cost of revenue	17	24	100	107
Sales and marketing	48	149	414	470
Research and development	66	193	(181)	616
General and administrative	265	493	554	1,659
Stock-based compensation expense in operating expense	379	835	787	2,745
Total stock-based compensation expense	396	859	887	2,852
Income tax benefit	(154)	(334)	(344)	(1,108)
Total stock-based compensation expense, net of tax	$ 242	$ 525	$ 543	$ 1,744

(3) Restructuring Charges and Accruals

In February 2011, in response to a decline in the Company s license revenue, the Company announced and began to execute plans to reduce its workforce by approximately 5%, or 28 positions, affecting all parts of the organization. The Company has realized and expects to continue to realize cost savings going forward as a result of this restructuring and other cost saving initiatives. This restructuring is substantially complete, and in connection with these actions, the Company recorded restructuring charges in the three months and nine months ended October 31, 2011 related to a facility closure totaling $0.0 million and $0.2 million, respectively. The nature of the restructuring charges and the amounts paid and accrued as of October 31, 2011 are summarized as follows (in thousands):

	Severance, payroll taxes and other employee benefits(1)	Facilities closures, legal and other miscellaneous(2)	Total restructuring charges and accruals

Balances as of January 31, 2011	$ 1,347	$ 463	$ 1,810
Accrued		163	163
Paid	(1,347)	(461)	(1,808)
Balances as of October 31, 2011	$	$ 165	$ 165

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(1) The February 2011 reduction in workforce plan was substantially in place and committed to by management prior to the beginning of the first fiscal quarter ended April 30, 2011. Accordingly, severance, payroll taxes and other employee benefits associated with this plan totaling $1.3 million were accrued in the fourth fiscal quarter ended January 31, 2011.

(2) As of October 31, 2011, contract termination costs accrued related to abandoned facility leases totaled $0.2 million and will be paid out over the remaining lease terms ranging from 4 months to 9 months.

Restructuring accruals are reflected in accrued expenses in the Company s unaudited condensed consolidated balance sheets.

The agreements underlying the Company s senior subordinated notes and the credit facility include financial covenants based on Adjusted EBITDA and restructuring, acquisition and other charges are a component of that computation. These charges have been included as a separate line within operating expenses in the Company s unaudited condensed consolidated statements of operations and are categorized as follows for the three months and nine months ended October 31, 2011 and 2010 (in thousands):

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2011	2010	2011	2010
Sponsor fees, administration fees and other costs related to the Merger and the issuance of debt	$ 309	$ 309	$ 931	$ 929
Restructuring charges consisting principally of severance, payroll taxes and other employee benefits, facilities closures and legal and other miscellaneous costs			163	925
Other redundancy costs not related to our restructuring plans including severance and other employee related costs, costs to establish or liquidate entities, and other miscellaneous costs not part of ongoing operations	353	601	1,237	1,678
Total restructuring, acquisition and other charges	$ 662	$ 910	$ 2,331	$ 3,532

(4) Goodwill and Other Intangible Assets

(a) Goodwill:

Goodwill is not amortized but instead is periodically tested for impairment. The required annual impairment test is performed in the fourth fiscal quarter each year. The Company has concluded that there were no indicators of impairment of goodwill as of October 31, 2011.

There were no changes in the carrying amount of goodwill during the three months and nine months ended October 31, 2011.

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(b) Other Intangible Assets:

Other intangible assets are comprised of the following (in thousands):

	As of October 31, 2011		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Amortizing intangible assets:			
Acquired technology	$ 178,699	$ (178,699)	$
Customer relationships	278,900	(197,276)	81,624
Trademark/Trade name portfolio	14,300	(10,115)	4,185
Capitalized software	6,654	(5,873)	781
Total	$ 478,553	$ (391,963)	$ 86,590

	As of January 31, 2011		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Amortizing intangible assets:			
Acquired technology	$ 178,699	$ (175,027)	$ 3,672
Customer relationships	278,900	(171,014)	107,886
Trademark/Trade name portfolio	14,300	(8,779)	5,521
Capitalized software	6,346	(5,176)	1,170
Total	$ 478,245	$ (359,996)	$ 118,249

Estimated amortization expense:	
For remaining three months of year ending January 31, 2012	$ 9,263
For year ending January 31, 2013	36,669
For year ending January 31, 2014	36,560
For year ending January 31, 2015	4,098
Total	$ 86,590

As of October 31, 2011, the weighted average remaining amortization periods for trademark/trade name portfolio, customer relationships and capitalized software are 28 months, 28 months and 18 months, respectively. The total weighted average remaining amortization period for all identifiable intangible assets is 17 months. The aggregate amortization expense of acquired technology and other intangible assets was $9.2 million and $31.3 million in the three months and nine months ended October 31, 2011, respectively, as compared to $17.5 million and $53.0 million in the same three months and nine months, respectively, a year ago.

The Company tests its long-lived assets for recoverability whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. A long-lived asset is not recoverable, and therefore subject to an impairment charge, if its carrying amount exceeds the

undiscounted cash flows associated with it. There were no impairment charges in the three month and nine month periods ended October 31, 2011 and 2010.

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(5) Comprehensive Loss

The Company reports components of comprehensive loss in its annual consolidated statements of shareholders equity. Comprehensive loss consists of net loss and foreign currency translation adjustments. Total comprehensive loss for the three months and nine months ended October 31, 2011 and 2010 is as follows (in thousands):

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2011	**2010**	**2011**	**2010**
Comprehensive loss:				
Net income (loss)	$ 3,202	$ (714)	$ 2,906	$ (8,371)
Other comprehensive loss foreign currency translation adjustments	(422)	(570)	(450)	(651)
Total comprehensive income (loss)	$ 2,780	$ (1,284)	$ 2,456	$ (9,022)

(6) Recent Accounting Pronouncements

In January 2010, the FASB issued an amendment regarding improving disclosures about fair value measurements. This new guidance requires some new disclosures and clarifies some existing disclosure requirements about fair value measurement. The new disclosures and clarifications of existing disclosures are effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. The Company s adoption of this guidance did not have any material impact on its consolidated financial position or results of operations.

In October 2009, the FASB issued Accounting Standards Update (ASU) No. 2009 13, *Multiple Deliverable Revenue Arrangements,* (ASU 2009 13). ASU 2009 13 amends existing revenue recognition accounting pronouncements that are currently within the scope of FASB ASC Subtopic 605-25. The new standard provides accounting principles and application guidance on whether certain non-software multiple deliverables exist, how the arrangement should be separated, and the consideration allocated. This guidance eliminates the requirement to establish the fair value of undelivered products and services and also eliminates the residual method of allocating arrangement consideration. The new guidance provides for separate revenue recognition based upon management s estimate of the selling price for an undelivered item when there is no other means to determine the fair value of that undelivered item. Under the previous guidance, if the fair value of all of the undelivered elements in the arrangement was not determinable, then revenue was generally deferred until all of the items were delivered or fair value was determined. This new approach is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. The Company s adoption of this guidance on February 1, 2011 did not have any material impact on its consolidated financial position or results of operations.

SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(7) Debt

Debt as of October 31, 2011 and January 31, 2011 consisted of the following (in thousands):

	October 31, 2011	January 31, 2011
Term loan, due March 10, 2013, three-month LIBOR plus 2.00%	$ 117,399	$ 316,000
Term loan, due March 10, 2016, three-month LIBOR plus 4.00%	191,101	
Revolving credit facility, due March 10, 2012, three-month LIBOR plus 1.75%		35,000
Senior subordinated notes, due March 15, 2016, 10.375%	134,265	134,265
Total long-term debt	442,765	485,265
Less current portion		7,500
Total long-term debt, less current portion	$ 442,765	$ 477,765

Senior Secured Credit Agreement

In connection with the consummation of the Merger, the Company entered into a senior secured credit agreement pursuant to a debt commitment that we obtained from affiliates of the initial purchasers of our senior subordinated notes (the credit facility).

General. The borrower under the credit facility initially was Spyglass Merger Corp. and immediately following completion of the Merger became Serena. The credit facility originally provided for (1) a seven-year term loan in the amount of $400.0 million amortizing at a rate of 1.00% per year on a quarterly basis for the first six and three-quarters years after the closing date of the Merger, with the balance paid at maturity, and (2) a six-year revolving credit facility that permits loans in an aggregate amount of up to $75.0 million, including a letter of credit facility and a swing line facility. In addition, subject to certain terms and conditions, the credit facility provides for one or more uncommitted incremental term loan or revolving credit facilities in an aggregate amount not to exceed $150.0 million. Proceeds of the term loan on the initial borrowing date were used to partially finance the Merger, to refinance certain indebtedness of Serena and to pay fees and expenses incurred in connection with the Merger. Proceeds of the revolving credit facility have been and any incremental facilities will be used for working capital and general corporate purposes of the Company and its restricted subsidiaries.

In the quarters ended July 31, 2006, April 30, 2007 and January 31, 2008, the Company made principal payments on the original $400 million term loan totaling $25 million, $30 million and $25 million, respectively.

In the quarters ended April 30, 2009, 2010 and 2011, the Company made mandatory principal payments totaling $2.0 million, $2.0 million and $7.5 million, respectively, on the original $400 million term loan.

In the quarter ended April 30, 2010, the Company made a voluntary principal payment totaling $30 million on the revolving credit facility.

In the quarter ended October 31, 2011, the Company made voluntary principal payments on the non-extended 2012 revolving credit facility and the extended 2015 revolving credit facility totaling $25.7 million and $9.3 million, respectively.

The revolving credit facility bears an annual commitment fee on the undrawn portion of that facility commencing on the date of execution and delivery of the senior secured credit agreement. As a result of the

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Company borrowing $65.0 million under the revolving credit facility in the fiscal quarter ended October 31, 2008 and Lehman Commercial Paper, Inc. (LCPI) becoming a defaulting lender due to its failure to fund its loan commitment, the annual commitment fee of 0.5% was not payable pursuant to the terms of the senior secured credit agreement until April 2010, when a $30 million portion of the loans under the revolving Credit Facility was repaid. In connection with the amendment of the Company s senior secured credit agreement in March 2011, Barclays Bank PLC assumed LCPI s revolving credit commitment of $10.0 million, reviving the applicable revolving credit commitment and resulting in total non-extended and extended revolving credit commitments of $75.0 million. Effective February 1, 2011, the annual commitment fee was 0.375% per annum.

In the quarter ended October 31, 2011, the Company cancelled the non-extended 2012 revolving credit commitment totaling $55.0 million. Effective with the cancellation, the Company s annual commitment fee is limited to the extended 2015 revolving credit commitment totaling $20.0 million.

Amended and Restated Senior Secured Credit Agreement. On March 2, 2011 the Company entered into an amendment to our senior secured credit agreement to extend the final maturity date for the repayment of a portion of outstanding term loans, extend the commitment termination date of the commitments for a portion of the revolving credit facility and provide for additional flexibility in the financial covenants under the senior secured credit agreement (the amend and extend transaction). As a result of the amendment, $191.1 million of the existing term loans were extended and will mature on March 10, 2016 (the extended term loans), and $20.0 million of the existing revolving credit commitments were extended and will terminate on March 10, 2015 (the extended revolving credit commitments). The $124.9 million of the existing term loans that were not extended (the non-extended term loans), and the $55.0 million of the existing revolving credit commitments that were not extended (the non-extended revolving credit commitments) will continue to mature on March 10, 2013 and March 10, 2012, respectively. The Company refers to the extended term loans and extended revolving credit commitments collectively as the extended facilities, and the non-extended term loans and non-extended revolving credit commitments collectively as the non-extended facilities. As a result of the amendment, the interest rate margins were increased by 200 basis points for the extended facilities. In addition, the maximum total leverage ratio stepped up to 5.50x beginning with the fiscal quarter ended April 30, 2011 and through the test periods ending on July 31, 2012 and will step down to 5.00x thereafter for both the extended facilities and non-extended facilities. After giving effect to the amendment, the aggregate principal amount outstanding under the senior secured credit agreement did not change, and the principal amount of the extended and non-extended term loans will continue to amortize at a rate of 1.00% per year on a quarterly basis. In connection with the amendment, Lehman Commercial Paper Inc. resigned as administrative agent, collateral agent, swingline lender and letter of credit issuer under the senior secured credit agreement and was replaced by Barclays Bank PLC.

Senior Subordinated Notes

The Company has outstanding $134.3 million principal amount of senior subordinated notes, which bear interest at a rate of 10.375%, payable semi-annually on March 15 and September 15, and which mature on March 15, 2016. Each of our domestic subsidiaries that guarantees the obligations under the Company s senior secured credit agreement will jointly, severally and unconditionally guarantee the notes on an unsecured senior subordinated basis. The Company does not have any domestic subsidiaries and, accordingly, there are no guarantors. The notes are the Company s unsecured, senior subordinated obligations, and the guarantees, if any, will be unsecured, senior subordinated obligations of the guarantors. The notes are subject to redemption at the Company s option under terms and conditions specified in the indenture related to the notes, and may be redeemed at the option of the holders at 101% of their face amount, plus accrued and unpaid interest, upon certain change of control events.

SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

In the fiscal year ended January 31, 2009, the Company repurchased, in eight separate privately negotiated transactions, an aggregate of $32.6 million of principal amount of its original outstanding $200.0 million senior subordinated notes. The repurchases resulted in a gain of $8.7 million from the extinguishment of debt in the fiscal year ended January 31, 2009.

In the fiscal year ended January 31, 2010, the Company repurchased, in six separate privately negotiated transactions, an aggregate of $24.4 million of principal amount of its original outstanding $200.0 million senior subordinated notes. The repurchases resulted in a gain of $4.6 million from the extinguishment of debt in the fiscal year ended January 31, 2010.

In the fiscal year ended January 31, 2011, the Company repurchased, in two separate privately negotiated transactions, an aggregate of $8.7 million of principal amount of its original outstanding $200.0 million senior subordinated notes. The repurchases resulted in a loss of $0.2 million from the extinguishment of debt in the fiscal year ended January 31, 2011.

The Company may from time to time repurchase the senior subordinated notes in open market or privately negotiated purchases or otherwise, or redeem the senior subordinated notes pursuant to the terms of the indenture dated March 10, 2006.

Debt Covenants

The senior subordinated notes and the credit facility contain various covenants including limitations on additional indebtedness, capital expenditures, restricted payments, the incurrence of liens, transactions with affiliates and sales of assets. In addition, the credit facility requires the Company to comply with certain financial covenants, including leverage and interest coverage ratios and capital expenditure limitations. The Company was in compliance with all of the covenants of the credit facility as of October 31, 2011.

The Company s senior secured credit agreement requires the Company to maintain a rolling twelve-month consolidated Adjusted EBITDA to consolidated Interest Expense ratio of a minimum of 2.00x at the end of each quarter beginning with the fiscal year ending January 31, 2010. Consolidated Interest Expense is defined in the senior secured credit agreement as consolidated cash interest expense less cash interest income and is further adjusted for certain non-cash interest expenses and other items. The Company is also required to maintain a rolling twelve-month consolidated Total Debt to consolidated Adjusted EBITDA ratio of a maximum of 5.00x at the end of each quarter beginning with the fiscal year ending January 31, 2011. Under the terms of the Amended and Restated Senior Secured Credit Agreement, the maximum total leverage ratio stepped up to 5.50x beginning with the fiscal quarter ending April 30, 2011 and through the test period ending on July 31, 2012 and will step down to 5.00x thereafter. Consolidated Total Debt is defined in the senior secured credit agreement as total debt other than certain indebtedness and is reduced by the amount of cash and cash equivalents on our consolidated balance sheet in excess of $5.0 million. As of October 31, 2011, our consolidated Total Debt was $368.7 million, consisting of total debt other than certain indebtedness totaling $442.8 million, net of cash and cash equivalents in excess of $5.0 million totaling $74.1 million. Failure to satisfy these ratio requirements would constitute a default under the senior secured credit agreement. If the Company s lenders failed to waive any such default, our repayment obligations under the senior secured credit agreement could be accelerated, which would also constitute a default under the indenture governing the senior subordinated notes.

The Company s ability to incur additional debt and make certain restricted payments under the indenture governing the senior subordinated notes, subject to specified exceptions, is tied to an Adjusted EBITDA to fixed charges ratio of at least 2.0x, except that we may incur certain debt and make certain restricted payments and

SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

certain permitted investments without regard to the ratio, such as the Company s ability to incur up to an aggregate principal amount of $625.0 million under our senior secured credit agreement (subject to reduction for mandatory prepayments under our senior secured credit agreement and inclusive of amounts outstanding under our senior secured credit agreement from time to time; as of October 31, 2011, we had $308.5 million outstanding under our term loan and $0.0 million under our revolving credit facility), to acquire persons engaged in a similar business that become restricted subsidiaries and to make other investments equal to the greater of $25.0 million or 2% of our consolidated assets. Fixed charges is defined in the indenture governing the senior subordinated notes as consolidated Interest Expense less interest income, adjusted for acquisitions, and further adjusted for non-cash interest expense.

(8) Income Taxes

Income tax expense was $1.0 million and $0.5 million in the three months and nine months ended October 31, 2011, respectively, as compared to an income tax benefit of $4.6 million and $11.9 million in the same three months and nine months, respectively, a year ago. The Company s projected effective income tax rate for fiscal year 2012 is 15%. The Company s effective income tax benefit rate for fiscal year 2011 was 57%. The Company s effective income tax rate differs from the federal statutory rate of 35% primarily due to the impacts of permanently reinvested foreign earnings, the domestic production deduction, the United States research and experimentation tax credit, and state taxes. During periods where the Company experiences losses, these items will generally increase the effective income tax rate above the statutory rate, whereas, they will reduce the effective income tax rate below the statutory rate during periods where the Company has income.

At January 31, 2011, the Company had total federal, state and foreign unrecognized tax benefits of $3.9 million, including interest of $0.9 million. During the nine months ended October 31, 2011 there were no material changes to the total unrecognized tax benefit, and the Company accrued immaterial amounts in interest.

The Company files tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. The statute of limitations on our federal and major state tax return filings remains open for the years ended January 31, 2006 through January 31, 2011. The statute of limitations on U.K. income tax filings remains open for the years ended January 31, 1999 through January 31, 2010. Over the next twelve months, we expect a decrease of $0.4 million in our unrecognized tax benefits primarily as a result of expiring statutes of limitation.

(9) Fair Value Measurement

Fair Value Hierarchy

FASB ASC Topic 820 *Fair Value Measurements and Disclosures* specifies a hierarchy of valuation techniques based upon whether the inputs to those valuation techniques reflect assumptions other market participants would use based upon market data obtained from independent sources (observable inputs) or reflect the Company s own assumptions of market participant valuation (unobservable inputs). In accordance with FASB ASC Topic 820, these two types of inputs have created the following fair value hierarchy:

Level 1 Quoted prices in active markets that are unadjusted and accessible at the measurement date for identical, unrestricted assets or liabilities;

Level 2 Quoted prices for identical assets and liabilities in markets that are not active, quoted prices for similar assets and liabilities in active markets or financial instruments for which significant inputs are observable, either directly or indirectly;

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Level 3 Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable. FASB ASC Topic 820 requires the use of observable market data if such data is available without undue cost and effort.

Items Measured at Fair Value on a Recurring Basis

The following table presents the Company s assets and liabilities that are measured at fair value on a recurring basis at October 31, 2011 consistent with the fair value hierarchy provisions of FASB ASC Topic 820 (in thousands):

		Fair Value Measurement at Reporting Date Using		
Description	**Estimated Fair Value at October 31, 2011**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Assets:				
Money market funds	$ 62,652	$ 62,652	$	$
Total Assets	$ 62,652	$ 62,652	$	$
Total Liabilities	$	$	$	$

At October 31, 2011, the Company did not have any assets or liabilities measured at fair value on a recurring basis using significant other observable inputs (Level 2) or significant unobservable inputs (Level 3).

Fair Value of Financial Instruments

The carrying amount of the Company s financial instruments including cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities approximate their respective fair values because of the relatively short period of time between origination of the instruments and their expected realization. The fair value of the Company s revolving credit facility approximates its respective carrying amount because this instrument includes LIBOR-based interest rates that are variable and fluctuate based on market conditions.

The estimated fair values of certain of the Company s long-term debt obligations, based on quoted market prices, as of October 31, 2011 and January 31, 2011 are as follows:

	Carrying Amount	**Fair Value**
	(In thousands)	
As of October 31, 3011:		
2.33561% Term Loan due 2013	$ 117,399	$ 114,758
4.33561% Term Loan due 2016	$ 191,101	$ 181,546
10.375% Senior Subordinated Notes due 2016	$ 134,265	$ 136,615
As of January 31, 2011:		
2.30344% Term Loan due 2013	$ 316,000	$ 306,520

10.375% Senior Subordinated Notes due 2016	$ 134,265	$ 137,622

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Financial instruments that potentially subject us to credit risk consist of cash and cash equivalents, and trade accounts receivable. The Company maintains the majority of its cash and cash equivalents balances with recognized financial institutions that follow the Company s investment policy. The Company has not experienced any significant losses on these investments to date. One of the most significant credit risks is the ultimate realization of accounts receivable. This risk is mitigated by (i) ongoing credit evaluation of our customers, and (ii) frequent contact with our customers, especially our most significant customers, thus enabling the Company to monitor current changes in business operations and to respond accordingly. The Company generally does not require collateral for sales on credit. The Company considers these concentrations of credit risks in establishing our allowance for doubtful accounts.

(10) Litigation

The Company is involved in various legal proceedings that have arisen during the ordinary course of its business. The reasonably possible or probable range of loss from the final resolution of these matters, individually or in the aggregate, is not expected to be material.

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

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that are subject to safe harbors under the Securities Act of 1933 and the Securities Exchange Act of 1934. These forward-looking statements include, but are not limited to, statements about financial projections, operational plans and objectives, future economic performance and other projections and estimates contained in this report. When used in this report, the words expects, anticipates, intends, plans, believes, seeks, estimates and similar expressions identify forward-looking statements. Because these forward-looking statements involve risks and uncertainties, they are subject to important factors that could cause actual results to differ materially from those expressed or implied by the forward-looking statements, including those risk factors discussed in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended January 31, 2011. We assume no obligation to update any forward-looking statements contained in this report. It is important that the discussion below be read together with the attached unaudited condensed consolidated financial statements and notes thereto and the risk factors discussed in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended January 31, 2011.

Overview

We are the largest global independent software company in terms of revenue focused solely on managing change and processes across information technology, or IT, environments. Our products and services primarily address the complexity of application lifecycle management, or ALM, and are used by our customers to manage the development of and control change in mission critical applications within both mainframe and distributed systems environments. In addition, we provide products and services to enable customers to rapidly address IT service management, or ITSM, and business process challenges through the use of visually designed process workflows. Our products and services allow customers to orchestrate and manage their application development, IT and business processes by automating and integrating disparate ALM and ITSM products and processes, improving process visibility and consistency, enhancing software integrity, mitigating application development risks, supporting auditability and regulatory compliance, and boosting productivity. Our revenue is generated by software licenses, maintenance contracts and professional services. Our software products are typically installed within customer IT environments and generally accompanied by renewable annual maintenance contracts.

In connection with our merger with Spyglass Merger Corp., an affiliate of Silver Lake, in March 2006 (the merger), we entered into a senior secured credit agreement, issued senior subordinated notes, and entered into other related transactions, which we refer to collectively as the acquisition transactions. After consummation of the acquisition transactions, we are highly leveraged. As of October 31, 2011 we had outstanding $442.8 million in aggregate indebtedness. Our liquidity requirements are significant, primarily due to debt service requirements.

On March 2, 2011 we entered into an amendment to our senior secured credit agreement to extend the final maturity date for the repayment of a portion of outstanding term loans, extend the commitment termination date of the commitments for a portion of the revolving credit facility and provide for additional flexibility in the financial covenants under the senior secured credit agreement. As a result of the amendment, $191.1 million of the existing term loans were extended and will mature on March 10, 2016, and $20.0 million of the existing revolving credit commitments were extended and will terminate on March 10, 2015. The $124.9 million of the existing term loans that were not extended, and the $55.0 million of the existing revolving credit commitments that were not extended will continue to mature on March 10, 2013 and March 10, 2012, respectively. As a result of the amendment, the interest rate margins were increased by 200 basis points for the extended facilities. In addition, the maximum total leverage ratio stepped up to 5.50x effective with the fiscal quarter ended April 30, 2011 through the test periods ending on July 31, 2012 and will step down to 5.00x thereafter for both the extended facilities and non-extended facilities. For additional information regarding the amended and restated senior secured credit agreement, see *Liquidity and Capital Resources Senior Secured Credit Agreement* below.

In the quarter ended October 31, 2011, we made voluntary principal payments on the non-extended 2012 revolving credit facility and the extended 2015 revolving credit facility totaling $25.7 million and $9.3 million,

respectively, and cancelled the non-extended 2012 revolving credit commitment totaling $55.0 million. Effective with the cancellation, our annual commitment fee is limited to the extended 2015 revolving credit commitment totaling $20.0 million.

We derive our revenue from software licenses, maintenance and professional services. Our distributed systems products are licensed on a per user seat basis. Customers typically purchase mainframe products under million instructions per second, or MIPS-based, perpetual licenses. Mainframe software products and applications are generally priced based on hardware computing capacity the higher the mainframe computer s MIPS capacity, the higher the cost of the software license.

We also provide ongoing maintenance, which includes technical support, version upgrades and enhancements, for an annual fee of approximately 21% of the discounted list price of the licensed product for our distributed systems products and approximately 17% to 18% of the discounted list price of the licensed product for our mainframe products. We recognize maintenance revenue over the term of the maintenance contract on a straight-line basis.

Professional services revenue is derived from technical consulting and educational services. Our professional services are typically billed on a time and materials basis and revenue is recognized as the related services are performed. Maintenance revenue and professional services revenue have lower gross profit margins than software license revenue as a result of the costs inherent in operating our customer support and professional services organizations.

In the quarter ended October 31, 2011, when compared to the same quarter a year ago, total revenues increased 5%, as total revenues were $55.7 million in the current quarter versus $52.9 million in the same quarter a year ago. In the nine months ended October 31, 2011, when compared to the same nine months a year ago, total revenues increased 5%, as total revenues were $162.0 million in the current nine months versus $154.8 million in the same nine months a year ago. The increase in total revenues in the quarter ended October 31, 2011, when compared to the same quarter a year ago, was primarily the result of increases in software license revenue and professional services revenue driven by several large transactions involving our Serena Release Management products (including *Serena Release Control, Serena Release Vault* and *Serena Release Automation*), sales of our *Serena Service Manager (SSM)* product and professional services engagements performed in the current quarter that related to solution-oriented sales from prior quarters. The increase in total revenues in the nine months ended October 31, 2011, when compared to the same nine months a year ago, was primarily the result of increases in software license revenue and professional services revenue driven by sales of our *ChangeMan ZMF* product, several large transactions involving our Serena Release Management products and professional services engagements relating to solution-oriented sales. In the quarter and nine months ended October 31, 2011, 75% and 60%, respectively, of our total software license revenue was derived from our distributed systems products, as compared to 59% and 62% in the same quarter and nine months, respectively, a year ago. In the quarter and nine months ended October 31, 2011, 25% and 40%, respectively, of our total software license revenue was derived from our mainframe products, as compared to 41% and 38% in the same quarter and nine months, respectively, a year ago.

Historically, our revenue has been generally attributable to sales in North America, Europe and to a lesser extent Asia Pacific. Revenue attributable to sales in North America accounted for approximately 65% of our total revenue in both the quarter and nine months ended October 31, 2011, as compared to 66% and 67% in the same quarter and nine months, respectively, a year ago.

Our international revenue is attributable principally to our European operations. International revenue accounted for approximately 35% of our total revenue in both the quarter and nine months ended October 31, 2011, as compared to 34% and 33% in the same quarter and nine months, respectively, a year ago.

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Critical Accounting Policies and Estimates

This discussion is based upon our consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosures of contingent assets and liabilities. In many instances, we could have reasonably used different accounting estimates, and in other instances changes in the accounting estimates are reasonably likely to occur from period to period. Accordingly, actual results could differ significantly from the estimates made by us. If actual results differ significantly from these estimates, the resulting changes could have a material adverse effect on our future reported financial results.

On an ongoing basis, management evaluates its estimates and judgments, including those related to revenue recognition, trade accounts receivable and allowance for doubtful accounts, impairment or disposal of long-lived assets, accounting for income taxes, projections used in purchase accounting, impairment of goodwill, valuation of our common stock, and assumptions related to valuation of our options and restricted stock, among other things. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources.

We believe the following are critical accounting policies and estimates used in the preparation of our consolidated financial statements.

- Revenue recognition,
- Stock-based compensation,
- Valuation of long-lived assets, including goodwill, and
- Accounting for income taxes

In the third quarter of fiscal year 2012, there has been no change in the above critical accounting policies or the underlying assumptions and estimates used in their application. See our Annual Report on Form 10-K for the fiscal year ended January 31, 2011 filed with the SEC on May 2, 2011 for further information regarding our critical accounting policies and estimates.

Recent Accounting Pronouncements

For a description of recent accounting pronouncements and their anticipated effect on our consolidated financial statements, see Note 6 of notes to our unaudited condensed consolidated financial statements.

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Historical Results of Operations

The following table sets forth our results of operations expressed as a percentage of total revenue. These operating results for the periods presented are not necessarily indicative of the results for the full fiscal year or any other period.

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2011	2010	2011	2010
Revenue:				
Software licenses	26%	22%	24%	21%
Maintenance	63%	69%	65%	70%
Professional services	11%	9%	11%	9%
Total revenue	100%	100%	100%	100%
Cost of revenue:				
Software licenses	2%	1%	1%	1%
Maintenance	5%	5%	6%	6%
Professional services	10%	9%	10%	8%
Amortization of acquired technology		16%	2%	16%
Total cost of revenue	17%	31%	19%	31%
Gross profit	83%	69%	81%	69%
Operating expenses:				
Sales and marketing	28%	25%	28%	26%
Research and development	12%	15%	13%	15%
General and administrative	6%	7%	7%	8%
Amortization of intangible assets	16%	18%	17%	18%
Restructuring, acquisition and other charges	1%	2%	1%	2%
Goodwill impairment				1%
Total operating expenses	63%	67%	66%	70%
Operating income (loss)	20%	2%	15%	(1)%
Other income (expense):				
Interest income				
Loss on early extinguishment of debt				
Interest expense	(12)%	(11)%	(12)%	(12)%
Change in the fair value of derivative instrument				1%
Amortization and write-off of debt issuance costs	(1)%	(1)%		(1)%
Amend and extend transaction fees			(1)%	
Total other income (expense)	(13)%	(12)%	(13)%	(12)%
Income (loss) before income taxes	7%	(10)%	2%	(13)%
Income tax expense (benefit)	1%	(9)%		(8)%
Net income (loss)	6%	(1)%	2%	(5)%

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Revenue

We derive revenue from software licenses, maintenance and professional services. Our total revenue increased $2.8 million, or 5%, to $55.7 million in the quarter ended October 31, 2011 from $52.9 million in the same quarter a year ago. For the nine months ended October 31, 2011, total revenues increased $7.2 million, or 5%, to $162.0 million from $154.8 million in the same nine months a year ago. The increase in total revenues in the quarter ended October 31, 2011, when compared to the same quarter a year ago, was primarily the result of increases in software license revenue and professional services revenue driven by several large transactions involving our Serena Release Management products (including *Serena Release Control, Serena Release Vault* and *Serena Release Automation*), sales of our *Serena Service Manager (SSM)* product and professional services engagements performed in the current quarter that related to solution-oriented sales from prior quarters. The increase in total revenues in the nine months ended October 31, 2011, when compared to the same nine months a year ago, was primarily the result of increases in software license revenue and professional services revenue driven by sales of our *ChangeMan ZMF* product, several large transactions involving our Serena Release Management products and professional services engagements relating to solution-oriented sales.

The following table summarizes software licenses, maintenance and professional services revenues for the periods indicated (in thousands, except percentages):

	Three Months Ended October 31,				Nine Months Ended October 31,			
			Increase (Decrease)				Increase (Decrease)	
	2011	2010	In Dollars	In %	2011	2010	In Dollars	In %
Revenue:								
Software licenses	$ 14,637	$ 11,464	$ 3,173	28%	$ 38,347	$ 32,926	$ 5,421	16%
Maintenance	35,163	36,596	(1,433)	(4)%	106,179	107,787	(1,608)	(1)%
Professional services	5,858	4,832	1,026	21%	17,483	14,068	3,415	24%
Total revenue	$ 55,658	$ 52,892	$ 2,766	5%	$ 162,009	$ 154,781	$ 7,228	5%

Software Licenses. Software licenses revenue as a percentage of total revenue was 26% and 24% in the quarter and nine months ended October 31, 2011, respectively, as compared to 22% and 21% in the same quarter and nine months, respectively, a year ago. The increase in software licenses revenue in the quarter ended October 31, 2011, when compared to the same quarter a year ago, was primarily driven by several large transactions involving our Serena Release Management products and sales of our *Serena Service Manager (SSM)* product. The increase in total revenues in the nine months ended October 31, 2011, when compared to the same nine months a year ago, was primarily driven by sales of our *ChangeMan ZMF* product, several large transactions involving our Serena Release Management products and sales of our *SSM* product. Our core ALM products, which include *Dimensions*, *ChangeMan ZMF* and our Serena Release Management products, continue to make up a significant portion of our total software license revenue. Combined, our core ALM products accounted for $13.8 million, or 95%, and $35.1 million, or 92%, of total software licenses revenue in the quarter and nine months ended October 31, 2011, respectively, as compared to $10.6 million, or 93%, and $31.0 million, or 94%, in the same quarter and nine months, respectively, a year ago. Distributed systems products accounted for $11.0 million, or 75%, and $23.2 million, or 60%, of total software licenses revenue in the quarter and nine months ended October 31, 2011, respectively, as compared to $6.8 million, or 59%, and $20.4 million, or 62%, in the same quarter and nine months, respectively, a year ago. We expect that our *Dimensions, ChangeMan ZMF* and *SBM* and *SSM* family of products will continue to account for a substantial portion of software license revenue in the future. We expect our software license revenue for the fiscal quarter ending January 31, 2012 to increase over the same quarter last year.

Maintenance. Maintenance revenue as a percentage of total revenue was 63% and 65% in the quarter and nine months ended October 31, 2011, respectively, as compared to 69% and 70% in the same quarter and nine months, respectively, a year ago. For the current quarter and nine months, when compared to the same quarter and nine months a year ago, the decrease in maintenance revenue in both absolute dollars and as a percentage of

total revenue, is primarily due to pricing pressures on maintenance renewals as a result of the weak global economy and several small maintenance contract cancellations. We expect maintenance revenue to remain generally flat in the near term as maintenance contracts continue to renew at consistent rates and we continue to sell software licenses, offset by pricing pressure caused by the prolonged adverse worldwide economic conditions.

Professional Services. Professional services revenue as a percentage of total revenue was 11% in both the quarter and nine months ended October 31, 2011, respectively, as compared to 9% in both the same quarter and nine months a year ago. For the current quarter and nine months, when compared to the same quarter and nine months a year ago, the increase in both absolute dollars and as a percentage of total revenue is predominantly due to an increase in the number of consulting engagements resulting from our focus on solution-oriented sales and expanded professional services organization. In general, professional services revenue is attributable to consulting opportunities in our installed customer base and expanding our consulting service capabilities. We expect professional services revenue to remain generally flat or slightly increase in the near term as we maintain our focus on selling solution-oriented offerings based on our ALM products and *SBM* and *SSM* family of products.

Cost of Revenue

Cost of revenue, consisting of cost of software licenses, cost of maintenance, cost of professional services and amortization of acquired technology, was 17% and 19% of total revenue in the quarter and nine months ended October 31, 2011, respectively, as compared to 31% in both the same quarter and nine months a year ago.

The following table summarizes cost of revenue for the periods indicated (in thousands, except percentages):

	Three Months Ended October 31,				Nine Months Ended October 31,			
			Increase (Decrease)				Increase (Decrease)	
	2011	2010	In Dollars	In %	2011	2010	In Dollars	In %
Cost of revenue:								
Software licenses	$ 1,006	$ 432	$ 574	133%	$ 1,803	$ 965	$ 838	87%
Maintenance	2,949	2,895	54	2%	8,662	8,585	77	1%
Professional services	5,263	4,772	491	10%	16,425	13,112	3,313	25%
Amortization of acquired technology	21	8,333	(8,312)	(100)%	3,672	25,362	(21,690)	(86)%
Total cost of revenue	$ 9,239	$ 16,432	$ (7,193)	(44)%	$ 30,562	$ 48,024	$ (17,462)	(36)%
Percentage of total revenue	17%	31%			19%	31%		

Software Licenses. Cost of software licenses consists principally of fees associated with integrating third party technology into our *Release Automation, PVCS* and *Dimensions* distributed systems products and, to a lesser extent, salaries, bonuses and other costs associated with our product release organization. Cost of software licenses as a percentage of total software licenses revenue was 7% and 5% in the quarter and nine months ended October 31, 2011, respectively, as compared to 4% and 3% in the same quarter and nine months, respectively, a year ago. The increase in both absolute dollars and as a percentage of total software licenses revenue in both the quarter and nine months ended October 31, 2011, when compared to the same quarter and nine months a year ago, was primarily due to increases in certain distributed systems products sales that have fees associated with distributing a third party product and integrating third party technology into our products.

Maintenance. Cost of maintenance consists primarily of salaries, bonuses and other costs associated with our customer support organization. Cost of maintenance as a percentage of total maintenance revenue was 8% in

both the current quarter and nine months ended October 31, 2011, as well as 8% in both the same quarter and nine months a year ago. For the current quarter and nine months, when compared to the same quarter and nine months a year ago, cost of maintenance remained generally flat in both absolute dollars and as a percentage of maintenance revenue as general cost increases associated with our customer support organization were offset by decreases in expenses associated with our prior restructuring and other cost cutting initiatives.

Professional Services. Cost of professional services consists of salaries, bonuses and other costs associated with supporting and growing our professional services organization. Cost of professional services as a percentage of total professional services revenue was 90% and 94% in the quarter and nine months ended October 31, 2011, respectively, as compared to 99% and 93% in the same quarter and nine months, respectively, a year ago. For both the current quarter and nine months, when compared to the same quarter and nine months a year ago, the increase in the cost of professional services in absolute dollars was predominantly due to increases in headcount to support higher professional services revenue.

Amortization of Acquired Technology. In connection with our merger in March 2006, and to a lesser extent small technology acquisitions in March 2006, October 2006 and September 2008, we have recorded $178.7 million in acquired technology. The acquired technology associated with our merger in March 2006 became fully amortized in the fiscal quarter ended April 30, 2011. Amortization expense was predominantly due to the acquired technology recorded in connection with the merger.

Operating Expenses

The following table summarizes operating expenses for the periods indicated (in thousands, except percentages):

	Three Months Ended October 31,				Nine Months Ended October 31,			
			Increase (Decrease)				Increase (Decrease)	
	2011	2010	In Dollars	In %	2011	2010	In Dollars	In %
Operating expenses:								
Sales and marketing	$ 15,446	$ 13,393	$ 2,053	15%	$ 45,646	$ 39,544	$ 6,102	15%