INTELLISYNC CORP
Form 10-Q
June 09, 2005

FORM 10-Q

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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

For the quarterly period ended April 30, 2005

OR

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

For the transition period from to

Commission File Number 0-21709

INTELLISYNC CORPORATION

(Exact name of Registrant as specified in its charter)

Delaware	**77-0349154**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

2550 North First Street, San Jose, California 95131

(Address of principal executive office and zip code)

(408) 321-7650

(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 ý No o

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).
Yes ý No o

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of June 6, 2005: 66,633,155

INTELLISYNC CORPORATION

10-Q REPORT

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INTELLISYNC CORPORATION

PART I - FINANCIAL INFORMATION

Item 1. Unaudited Condensed Consolidated Financial Statements

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

(Unaudited)

	April 30, 2005	July 31, 2004
Assets		
Current assets:		
Cash and cash equivalents	$ 23,910	$ 12,991
Short-term investments	23,235	40,657
Accounts receivable, net of allowance for doubtful accounts of $560 and $470	11,682	10,380
Inventories	33	69
Other current assets	2,435	2,485
Total current assets	61,295	66,582
Property and equipment, net	2,357	1,540
Goodwill	67,536	65,288
Other intangible assets, net	25,876	29,828
Restricted cash	3,979	4,032
Other assets	2,810	3,084
Total assets	$ 163,853	$ 170,354
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 2,337	$ 1,562
Accrued liabilities	6,675	7,482
Current portion of obligations under capital lease	149	51
Deferred revenue	6,093	5,794
Total current liabilities	15,254	14,889
Obligations under capital lease	250	144
Convertible senior notes	57,884	58,443
Other liabilities	2,674	2,487
Total liabilities	76,062	75,963
Commitments and contingencies (Note 8)		

Stockholders equity:				
Preferred stock, $0.001 par value; 2,000 shares authorized; none issued and outstanding at April 30, 2005 and July 31, 2004				
Common stock, $0.001 par value; 160,000 shares authorized; 66,630 and 65,592 shares issued and outstanding at April 30, 2005 and July 31, 2004		67		66
Additional paid-in capital		227,026		225,832
Accumulated deficit		(139,957)		(131,116)
Accumulated other comprehensive income (loss)		655		(391)
Total stockholders equity		87,791		94,391
Total liabilities and stockholders equity	$	163,853	$	170,354

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

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INTELLISYNC CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	Three Months Ended April 30, 2005	Three Months Ended April 30, 2004	Nine Months Ended April 30, 2005	Nine Months Ended April 30, 2004
Revenue				
License	$ 9,643	$ 7,512	$ 28,662	$ 20,336
Services	5,594	3,495	15,133	8,690
Total revenue	15,237	11,007	43,795	29,026
Cost and operating expenses:				
Cost of revenue (includes non-cash stock compensation of $2, $(94), $(19) and $8, respectively)	2,537	2,237	7,397	5,667
Amortization of developed and core technology	1,187	990	3,515	1,543
Research and development (includes non-cash stock compensation of $5, $(30), $1 and $37, respectively)	3,810	3,495	10,819	8,098
Sales and marketing (includes non-cash stock compensation of $43, $(206), $4 and $11, respectively)	8,209	4,612	20,055	11,463
General and administrative (includes non-cash stock compensation of $20, $(205), $5 and $673, respectively)	2,221	1,582	6,383	5,894
Amortization of other intangibles	1,074	679	3,176	1,003
In-process research and development		775		3,667
Other charges		253		929
Total cost and operating expenses	19,038	14,623	51,345	38,264
Operating loss	(3,801)	(3,616)	(7,550)	(9,238)
Other income (expense):				
Interest income	304	171	813	410
Interest expense	(389)	(99)	(907)	(99)
Other, net	(158)	(99)	(625)	(86)
Litigation settlement gain, net		1,576		1,576
Total other income (expense)	(243)	1,549	(719)	1,801
Loss before income taxes	(4,044)	(2,067)	(8,269)	(7,437)
Provision for income taxes	(317)	(117)	(572)	(260)
Net loss	$ (4,361)	$ (2,184)	$ (8,841)	$ (7,697)
Basic and diluted net loss per common share	$ (0.07)	$ (0.03)	$ (0.14)	$ (0.14)
Shares used in computing basic and diluted net loss per common share	66,523	63,859	65,451	55,575

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

INTELLISYNC CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Nine Months Ended April 30, 2005	Nine Months Ended April 30, 2004
Cash flows from operating activities:		
Net loss	$ (8,841)	$ (7,697)
Adjustments to reconcile net loss to net cash used in operating activities:		
In-process research and development		3,667
Allowance for doubtful accounts	90	193
Depreciation	898	753
Amortization	6,691	2,546
Amortization of debt issuance costs	495	92
Non-cash stock compensation (recovery)	(9)	729
Changes in operating assets and liabilities, net of business acquisitions:		
Accounts receivable	(1,081)	(1,628)
Inventories	36	(87)
Other current assets	276	(709)
Other assets	75	(294)
Accounts payable	775	(1,940)
Accrued liabilities	(1,553)	(3,430)
Deferred revenue	299	49
Net cash used in operating activities	(1,849)	(7,756)
Cash flows from investing activities:		
Purchase of property and equipment	(1,412)	(441)
Purchase of short term investments	(5,902)	(30,565)
Proceeds from the sales of short-term investments	17,347	5,100
Proceeds from the maturities of short-term investments	5,950	5,650
Increase in restricted cash	(61)	(3,709)
Acquisitions, net of cash acquired	(4,095)	(17,951)
Net cash provided by (used in) investing activities	11,827	(41,916)
Cash flows from financing activities:		
Proceeds from long-term debt		60,000
Debt issuance cost	(229)	(2,878)
Principal payments on borrowings		(1,764)
Principal payments on capital lease	(92)	(18)
Note repayments from stockholders		310
Proceeds upon exercise of stock options	585	1,549
Proceeds from ESPP shares issued	619	337
Net cash provided by financing activities	883	57,536
Effect of exchange rate changes on cash and cash equivalents	58	18
Net increase in cash and cash equivalents	10,919	7,882
Cash and cash equivalents at beginning of period	12,991	7,842

Cash and cash equivalents at end of period	$	23,910	$	15,724

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

INTELLISYNC CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 The Company and a Summary of its Significant Accounting Policies

The Company

Intellisync Corporation, Intellisync or the   Company,   develops, markets and supports desktop, enterprise and mobile carrier-class push-email, synchronization and systems management software that enables consumers, business professionals and information technology professionals to extend the capabilities of enterprise groupware and vertical applications, handheld organizers/computers, Web-enabled mobile phones, pagers and other wireless or wireline personal communications platforms. The Company s Identity Systems (formerly Search Software America) subsidiaries develop, market and support global solutions that enhance an organization s ability to search, find, match (synchronize), screen and group identity data within their computer systems and network databases.

Liquidity and Capital Resources

The Company has incurred losses and negative cash flows since inception. The Company incurred a net loss of approximately $8,841,000 and negative cash flows from operations of approximately $1,849,000 for the nine months ended April 30, 2005. The Company s cash balances may decline further, although the Company believes that its existing cash resources, combined with revenue from continuing operations, will be adequate to fund its operations, including potential acquisitions, for at least the next 12 months. Failure to generate sufficient revenue or control spending could adversely affect the Company s ability to achieve its business objectives.

Basis of Presentation and Consolidation

The accompanying condensed consolidated financial statements of Intellisync as of April 30, 2005 and for the three and nine months ended April 30, 2005 are unaudited and reflect all normal recurring adjustments which are, in the opinion of management, necessary for their fair statement. These condensed consolidated financial statements should be read in conjunction with the Company s consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the fiscal year ended July 31, 2004. The condensed consolidated balance sheet as of July 31, 2004 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. The results of operations for the interim period ended April 30, 2005 are not necessarily indicative of results to be expected for the full year.

The accompanying condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant inter-company balances and transactions have been eliminated in consolidation.

Use of Estimates and Assumptions

The preparation of the condensed consolidated financial statements in conformity with generally accepted accounting principles requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. On an on-going basis, the Company evaluates its estimates, including those related to provision for doubtful accounts, channel inventory and product returns, valuation of intangibles, investments and other long-lived assets, restructuring accruals, license and service revenue recognition, taxes and contingencies. The Company bases its estimates on various factors and information which may include, but are not limited to, history and prior experience, experience of other enterprises in the same industry, new related events, current economic conditions and information from third party professionals that are believed to be reasonable under the circumstances, the results of which form the basis for

taking judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Revenue Recognition

Revenue is derived from software licenses and related services, which include implementation and integration of software solutions, post contract support, training, hosting and consulting.

Transactions involving the sale of software products are accounted for under the American Institute of Certified Public Accountants (AICPA) Statement of Position (SOP) No. 97-2, *Software Revenue Recognition*, as amended by SOP No. 98-9, *Modification of 97-2, Software Revenue Recognition with Respect to Certain Transactions*. For contracts with multiple elements, and for which vendor-specific objective evidence of fair value for the undelivered elements exists, revenue is recognized for the delivered elements based upon the residual contract value as prescribed by SOP No. 98-9. The Company has accumulated relevant information from contracts to use in determining the availability of vendor-specific objective evidence and believes that such information complies with the criteria established in SOP No. 97-2 as follows:

Customers are required to pay separately for maintenance. Optional stated future renewal rates are included as a term of the contracts. The Company uses the renewal rate as vendor-specific objective evidence of fair value for maintenance.

The Company charges standard hourly rates for consulting services, when such services are sold separately, based upon the nature of the services and experience of the professionals performing the services.

For training, the Company charges standard rates for each course based upon the duration of the course, and such courses are separately priced in contracts. The Company has a history of selling such courses separately.

Revenue from license fees is recognized when persuasive evidence of an arrangement exists, delivery of the product has occurred, no significant Company obligations with regard to implementation or integration exist, the fee is fixed or determinable and collectibility is probable. Arrangements for which the fees are not deemed probable for collection are recognized upon cash collection. Payments from customers received in advance of revenue recognition are recorded as deferred revenue.

Service revenue primarily comprises revenue from consulting fees, maintenance contracts, training and hosting fees. Service revenue from consulting, hosting and training is recognized as the service is performed. Maintenance contracts include the right to unspecified upgrades and ongoing support. Maintenance revenue is deferred and recognized ratably as services are provided over the maintenance period.

License and service revenue on contracts involving significant implementation, customization or services, that are essential to the functionality of the software is recognized over the period of each engagement, primarily using the percentage-of-completion method. Labor hours incurred is generally used as the measure of progress towards completion as prescribed by SOP No. 81-1, *Accounting for Performance of Construction-Type and Certain Product-Type Contracts*. Revenue for these arrangements is classified as license revenue and service revenue based upon estimates of fair value for each element, and the revenue is recognized based on the percentage-of-completion ratio for the arrangement. A provision for estimated losses on engagements is made in the period in which the loss becomes probable and can be reasonably estimated. The Company considers a project completed when all contractual obligations have been met (generally the go live date).

The Company currently licenses its products directly to individuals, small businesses and corporations, to original equipment manufacturers, or OEMs, and to distributors and value-added resellers in North America, Europe, the Asia-Pacific region, South America and Africa. Revenue from products distributed indirectly through major distributors and resellers is recognized on a sell through basis. Agreements with the Company s major distributors and resellers contain specific product return privileges for stock rotation and obsolete products that are generally limited to contractual amounts. Reserves for estimated future returns are provided for upon revenue recognition.

Product returns are recorded as a reduction of revenue. Accordingly, the Company has established a product returns reserve composed of 100% of product inventories held at the Company s distribution partners, as well as an estimated amount for returns from customers of the distributors and other resellers as a result of stock rotation and obsolete products. Such reserves are based on:

historical product returns and inventory levels on a product by product basis;

current inventory levels and sell through data on a product by product basis as reported by the Company s major distributors worldwide;

demand forecast by product in each of the principal geographic markets, which is impacted by the Company s product release schedule, seasonal trends and analyses developed by the Company s internal sales and marketing group; and

general economic conditions.

The Company licenses rights to use its technology portfolio, whereby licensees, particularly OEMs, typically pay a non-refundable license fee in one or more installments and on-going royalties based on their sales of products incorporating the Company s technology. Revenue from OEMs under minimum guaranteed royalty arrangements, which are not subject to future obligations, is recognized when such royalties are earned and become payable. Royalty revenue is recognized as earned when reasonable estimates of such amounts can be made. Royalty revenue that is subject to future obligations is recognized when such obligations are fulfilled. Royalty revenue that exceeds minimum guarantees is recognized in the period earned.

Stock-Based Compensation

The Company accounts for non-cash stock-based employee compensation using the intrinsic method in accordance with Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees and Related Interpretations*, and complies with the disclosure provisions of Statement of Financial Accounting Standards (SFAS) No. 123, *Accounting for Stock-Based Compensation* and SFAS No. 148, *Accounting for Stock-Based Compensation, Transition and Disclosures*. Stock and other equity instruments issued to non-employees is accounted for in accordance with SFAS No. 123 and Emerging Issues Task Force Issue (EITF) No. 96-18, *Accounting for Equity Instruments Issued to Other than Employees for Acquiring, or in Conjunction with Selling Goods or Services* and valued using the Black-Scholes model. Expense associated with stock-based compensation is being amortized on an accelerated basis over the vesting period of the individual award consistent with the method described in Financial Accounting Standards Board (FASB) Interpretation (FIN) No. 28.

If compensation cost for the Company s stock plans had been determined consistent with SFAS No. 123 *Accounting for Stock-Based Compensation*, the Company s net loss and loss per common share would have been adjusted to the pro-forma amounts indicated below (in thousands, except per common share data):

	Three Months Ended April 30,		**Nine Months Ended April 30,**	
	2005	**2004**	**2005**	**2004**
Net loss as reported	$ (4,361)	$ (2,184)	$ (8,841)	$ (7,697)

Add: Stock-based employee compensation expense (recovery) included in reported net loss		70		(535)		(9)		729
Deduct: Total stock-based employee compensation expense determined under fair value method for all awards		1,782		1,127		4,280		2,926
Pro forma net loss	$	(6,073)	$	(3,846)	$	(13,130)	$	(9,894)
Basic and diluted net loss per common share as reported	$	(0.07)	$	(0.03)	$	(0.14)	$	(0.14)
Basic and diluted pro forma net loss per common share	$	(0.09)	$	(0.06)	$	(0.20)	$	(0.18)

Because the Black-Scholes option valuation model was developed for traded options and requires the input of subjective assumptions and the number of future shares to be issued or cancelled is not known, the resulting pro forma compensation cost may not be representative of that to be expected in future years.

Derivative Instruments

The Company applies SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended, which establishes accounting and reporting standards for derivative instruments and for hedging activities. SFAS No. 133 requires that an entity recognize derivatives as either assets or liabilities on the balance sheet and measure those instruments at fair value. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation. The Company designates its derivatives based upon criteria established by SFAS No. 133. For a derivative designated as a fair value hedge, the gain or loss is recognized in earnings in the period of change together with the offsetting loss or gain on the hedged item attributed to the risk being hedged. For a derivative designated as a cash flow hedge, the effective portion of the derivative s gain or loss is initially reported as a component of accumulated other comprehensive income and subsequently reclassified into earnings when the hedged exposure affects earnings. The ineffective portion of the gain or loss is reported in earnings immediately. Refer to Note 7 for details on the Company s only derivative instrument.

Note 2 Recently Issued Accounting Pronouncements

Other-Than-Temporary Impairment

In March 2004, the EITF reached consensus on Issue 03-01, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*. EITF No. 03-01 includes new guidance for evaluating and recording impairment losses on debt and equity investments, as well as new disclosure requirements for investments that are deemed to be temporarily impaired. The disclosure requirements are effective for fiscal years ending after June 15, 2004. The Company has adopted the disclosure requirements in fiscal 2004 accordingly and incorporated such disclosures in note 3 to consolidated financial statements included in its Annual Report on Form 10-K for the fiscal year ended July 31, 2004. The accounting guidance of EITF No. 03-01 is applicable for reporting periods after June 15, 2004. However, the effective date of such guidance has been delayed until the FASB issues a Staff Interpretation on this matter. The delay does not have a specified date. Until an effective date is determined, existing guidance continues to apply in determining if an impairment is other than temporary. The Company will evaluate the impact of EITF No. 03-01 once final guidance is issued.

Contingently Convertible Debt on Diluted Earnings per Share

In October 2004, the EITF reached a consensus on EITF No. 04-8 *The Effect of Contingently Convertible Debt on Diluted Earnings per Share,* that the dilutive effect of contingent convertible debt instruments (CoCo s) must be included in diluted earnings per share regardless of whether the triggering contingency has been satisfied, if dilutive. Adoption of EITF No. 04-08 would be on a retroactive basis and would require restatement of prior period diluted earnings per share, subject to certain transition provisions. It is effective for all periods ending after December 15, 2004. Due to the losses the Company incurred for the three and nine months ended April 30, 2005, diluted net loss per share does not differ from basic net loss per share, since potential shares of common stock issuable upon the conversion of the convertible debt are anti-dilutive for all periods presented. EITF No. 04-8 could have a future impact on the Company s results of operations in the event that the potential shares of common stock issuable upon conversion of the convertible debt were included in the diluted earnings per share calculation.

Inventory Costs

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs - an amendment of ARB No. 43, Chapter 4,* that requires that items such as idle facility expense, excessive spoilage, double freight and handling costs be recognized as current period charges. In addition, it requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. SFAS No. 151 will be effective in

fiscal years beginning after June 2005. The Company expects SFAS No. 151 to have no material effect on its consolidated financial statements.

Discontinued Operations

In November 2004, the EITF reached a consensus on No. 03-13, *Applying the Conditions in Paragraph 42 of FASB Statement No. 144 in Determining Whether to Report Discontinued* Operations. EITF No. 03-13 relates to components of an enterprise that are either disposed of or classified as held for sale in fiscal periods beginning after December 15, 2004. EITF No. 03-13 allows significant events or circumstances that occur after the balance sheet date but before the issuance of financial statements to be taken into consideration in the evaluation of whether a component should be presented as discontinued or continuing operations, and modifies assessment period guidance to allow for an assessment period greater than one year. The consensus in EITF No. 03-13 was effective for the Company beginning February 1, 2005. The impact to the Company of adopting EITF Issue No. 03-13 will depend on the nature and extent of any long-lived assets disposed of or held for sale after the effective date, but the Company does not currently expect EITF No. 03-13 to have a material impact on its consolidated results of operations, cash flows or financial position.

Exchanges of Nonmonetary Assets

In December 2004, the FASB issued SFAS No. 153, *Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29, Accounting for Nonmonetary Transactions.* SFAS No. 153 states that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, SFAS No. 153 eliminates the narrow exception for nonmonetary exchanges of similar productive assets and replaces it with a broader exception for exchanges of nonmonetary assets that do not have commercial substance. SFAS No. 153 is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date of issuance. The provisions of SFAS No. 153 shall be applied prospectively. The Company does not believe the adoption of SFAS No. 153 will have a significant impact on its consolidated results of operations or financial position.

Share-Based Payment

In December 2004, the FASB issued SFAS No. 123R, *Share-Based Payment, an amendment of FASB Statements No. 123 and 95.* The principal effect of SFAS No. 123R will be to require the inclusion in the Company s earnings of a compensation expense for stock option grants and employee stock plan purchases that previously was only reported as a disclosure in a note to the Company s consolidated financial statements. The Company is required to adopt the provisions of SFAS No. 123R as of August 1, 2005 but may elect to early adopt the provision effective the first day of any quarter prior to that date. The Company is presently studying SFAS No. 123R and has not yet determined which method it will select for its adoption of SFAS No. 123R, which the Company expects to have a potential material impact on its annual earnings.

On March 29, 2005, the SEC staff issued Staff Accounting Bulletin (SAB) No. 107, *Share-Based Payment* to express the views of the staff regarding the interaction between SFAS No. 123R and certain SEC rules and regulations and to provide the staff s views regarding the valuation of share-based payment arrangements for public companies. The Company is currently in the process of implementing SFAS No. 123R, effective as of August 1, 2005, and will take into consideration the additional guidance provided by SAB No. 107 in connection with the implementation of SFAS No. 123R.

Tax Deduction Provided For In the American Jobs Creation Act of 2004

In December 2004, the FASB issued FASB Staff Position No. 109-1, *Application of SFAS No. 109 to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004.* This staff position provides guidance for the accounting of a deduction provided to U. S. manufacturing companies and is effective immediately. The Company believes the adoption of this position will not currently have a material effect

on its financial position or results of operations due to the Company s net operating losses. However, there is no assurance that there will not be a material impact in the future.

Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004

In December 2004, the FASB issued FASB Staff Position No. 109-2, *Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004* . The American Jobs Creation Act introduces a special one-time dividends received deduction on the repatriation of certain foreign earnings to a U.S. taxpayer (repatriation provision), provided certain criteria are met. This position provides accounting and disclosure guidance for the repatriation provision. The Company does not believe the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004 nor the FASB Staff Position will have a material impact on its financial condition or results of operations.

Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143

In March 2005, the FASB issued FIN No. 47, *Accounting for Conditional Asset Retirement Obligations, an interpretation of FASB Statement No. 143*, *Accounting for Asset Retirement Obligations.* FIN No. 47 clarifies when an entity would be required to recognize a liability for the fair value of an asset retirement obligation that is conditional on a future event if the liability s fair value can be reasonably estimated. Uncertainty surrounding the timing and method of settlement that may be conditional on events occurring in the future would be factored into the measurement of the liability rather than the recognition of the liability. FIN No. 47 is effective for fiscal years ending after December 15, 2005. The Company is currently assessing the impact that the interpretation may have on its consolidated financial position and results of operations.

Note 3 Balance Sheets Components

Inventories consist of the following (in thousands):

		April 30, 2005		July 31, 2004
Raw materials	$	28	$	54
Finished goods and work-in-process		5		15
Inventories	$	33	$	69

Note 4 Acquisitions

The Company acquired Tourmaline Networks, Inc. in March 2005. In addition, the following acquisitions were closed in fiscal 2004: SoftVision SRL s workforce through a transfer agreement; SPL Worldgroup Software, Inc., SPL Worldgroup Ltd. and Search Software America Pty. Ltd., or collectively SSA and now called Identity Systems; Synchrologic, Inc.; and Spontaneous Technology, Inc. The Tourmaline, Identity Systems, Synchrologic and Spontaneous Technology transactions were accounted for as a business combination under SFAS No. 141, *Business*

Combinations. The SoftVision workforce transfer was accounted for as an asset purchase.

Tourmaline Networks, Inc.

On March 1, 2005, the Company completed its acquisition of all of the issued and outstanding stock of Tourmaline Networks, Inc., a privately held developer and marketer of mobile email based on QUALCOMM s BREW® solution headquartered in San Diego, California. Under the terms of an Agreement and Plan of Merger, dated as of February 9, 2005, the outstanding shares of Tourmaline common stock were converted into the right to receive (i) an aggregate of approximately $4,118,000 in aggregate initial cash consideration and (ii) an aggregate of up to $2,881,918 in cash earnout consideration (based on future revenue generated by the Company from the former Tourmaline client base), subject to the deposit of a certain portion of the initial cash consideration and earnout

consideration in escrow to be available to compensate Intellisync pursuant to the indemnification obligations of the holders of Tourmaline common stock. The earnout consideration is due and payable shortly following the first anniversary of the acquisition.

The condensed consolidated financial statements include the results of operations of Tourmaline since the date of acquisition. Under the purchase method of accounting, the total purchase price was allocated to Tourmaline s net tangible and intangible assets based upon their estimated fair value as of the acquisition date. The purchase price of $4,218,000 (including estimated acquisition costs of $100,000) was assigned to the fair value of the assets acquired, including the following (in thousands):

Tangible assets acquired	$	342
Deferred tax assets		795
Liabilities assumed		(275)
Deferred tax liability assumed		(795)
Developed and core technology		712
Customer base		1,285
Goodwill		2,154
	$	4,218

In accordance with SFAS No. 109, *Accounting for Income Taxes*, deferred tax liabilities of approximately $795,000 have been recorded for the tax effect of the amortizable intangible assets. Deferred tax assets of $795,000 have also been recorded by the Company to account for the tax effect of the Company s net operating loss and credit carryforwards.

Tangible assets acquired, which includes $23,000 of cash, and liabilities assumed were valued at their respective carrying amounts as the Company believes that these amounts approximated their current fair values at the acquisition date. The valuation of identifiable intangible assets acquired was based on management s estimates, currently available information and reasonable and supportable assumptions. This allocation was generally based on the fair value of these assets determined using the income approach.

An estimate of $2,154,000 has been allocated to goodwill. Goodwill represents the excess of the purchase price over the fair value of the net tangible and intangible assets acquired. In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, goodwill will not be amortized but will be tested for impairment at least annually.

The purchase price allocation for Tourmaline is subject to further revision as more detailed analysis is completed and additional information on the fair values of Tourmaline s assets and liabilities becomes available. Any change in the fair value of the net assets of Tourmaline will change the amount of the purchase price allocable to goodwill. Final purchase accounting may therefore differ materially from the information presented above.

Of the total purchase price, $1,997,000 was allocated to amortizable intangibles included in the above list. The amortizable intangible assets are being amortized using an accelerated method according to the expected cash flows to be received from the underlying assets over their respective estimated useful life of three to six years. Refer to Note 5.

SoftVision SRL

On June 14, 2004, the Company completed the transfer of 91 employees from SoftVision SRL, an offshore software development company with headquarters in Cluj-Napoca, Romania, pursuant to an Employee Transfer Agreement dated as of February 5, 2004. Under the terms of the agreement, the Company paid cash of approximately $693,000 and assumed certain employee-related liabilities of approximately $31,000. The SoftVision workforce acquisition was accounted for as an asset purchase. The condensed consolidated financial statements include the effect of additional employees the Company acquired from SoftVision since the date of acquisition.

The full amount of the preliminary purchase price of $724,000 was assigned to the fair value of the acquired workforce. The amortizable acquired workforce is being amortized using the straight-line method over its estimated useful life of two years. Refer to Note 5.

Identity Systems (formerly Search Software America)

On March 16, 2004, the Company completed its acquisition of all of the issued and outstanding stock of SPL Worldgroup Software, Inc., SPL Worldgroup Ltd. and Search Software America Pty. Ltd., or collectively SSA , privately held divisions of SPL WorldGroup and headquartered in Sydney, Australia, pursuant to a Stock Purchase Agreement dated as of February 24, 2004. SSA, now called Identity Systems, with operations in the United States, United Kingdom, and Australia, is a developer of solutions that enhance the ability to find, match and group (synchronize) identity data within computer systems and network databases. Under the terms of the stock purchase agreement, the Company paid cash of $22,129,000.

The condensed consolidated financial statements include the results of operations of Identity Systems since the date of acquisition. Under the purchase method of accounting, the total purchase price was allocated to Identity System s net tangible and intangible assets based upon their estimated fair value as of the acquisition date. The purchase price of $22,179,000 (including acquisition costs of $50,000) was assigned to the fair value of the assets acquired, including the following (in thousands):

Tangible assets acquired	$	3,728
Liabilities assumed		(3,987)
Deferred tax liability assumed		(646)
In-process research and development		775
Developed and core technology		5,513
Customer base		8,777
Goodwill		8,019
	$	22,179

In accordance with SFAS No. 109, *Accounting for Income Taxes*, deferred tax liabilities of approximately $646,000 have been recorded for the tax effect of the amortizable intangible assets, which are not deductible for tax purposes.

The valuation of identifiable intangible assets acquired was based on management s estimates, currently available information and reasonable and supportable assumptions. This allocation was generally based on the fair value of these assets determined using the income approach.

Tangible assets acquired, which includes $2,146,000 of cash, and liabilities assumed were valued at their respective carrying amounts as the Company believes that these amounts approximated their current fair values at the acquisition date. The valuation of identifiable intangible assets acquired was based on management s estimates, currently available information and reasonable and supportable assumptions. This allocation was generally based on the fair value of these assets determined using the income approach.

$8,019,000 was allocated to goodwill. Goodwill represents the excess of the purchase price over the fair value of the net tangible and intangible assets acquired. In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, goodwill will not be amortized but will be tested for impairment at least annually.

Of the total purchase price, $14,290,000 was allocated to amortizable intangibles included in the above list. The amortizable intangible assets are being amortized using an accelerated method according to the expected cash flows to be received from the underlying assets over their respective estimated useful life of seven to ten years. Refer to Note 5.

As of the acquisition date, technological feasibility of the in-process technology had not been established and the technology had no alternative future use. Accordingly, the Company expensed the in-process research and development at the date of the acquisition.

The amount of the purchase price allocated to in-process research and technology was based on established valuation techniques used in the high-technology software industry. The fair value assigned to the acquired in-process research and development was determined using the income approach, which discounts expected future cash flows to present value. The key assumptions used in the valuation include, among others, expected completion date of the in-process projects identified as of the acquisition date, estimated costs to complete the projects, revenue contributions and expense projections assuming the resulting product has entered the market, and discount rate based on the risks associated with the development life cycle of the in-process technology acquired. The discount rate used in the present value calculations are normally obtained from a weighted-average cost of capital analysis, adjusted upward to account for the inherent uncertainties surrounding the successful development of the in-process research and development, the expected profitability levels of such technology, and the uncertainty of technological advances that could potentially impact the estimates. The Company assumes the pricing model for the resulting product of the acquired in process research and technology to be standard within its industry. The Company, however, did not take into consideration any consequential amount of expense reductions from integrating the acquired in-process technology with other existing in-process or completed technology. Therefore, the valuation assumptions do not include significant anticipated cost savings.

The key assumptions underlying the valuation of acquired in-process research and development from Identity Systems are as follows (in thousands):

Project names: SSA-NAME3 Version 3.0 and IDS Version 3.0

Percent completed as of acquisition date: 10%

Estimated costs to complete technology at acquisition date: $600,000

Risk-adjusted discount rate: 25%

First period expected revenue: June 2005

The development of the above technology remains highly dependent on the remaining efforts to achieve technical viability, rapidly changing customer markets, uncertain standards for a new product, and significant competitive threats from several companies. The nature of the efforts to develop this technology into a commercially viable product consists primarily of planning, designing, experimenting, and testing activities necessary to determine that the technology can meet market expectations, including functionality and technical requirements. Failure to bring the product to market in a timely manner could result in a loss of market share or a lost opportunity to capitalize on emerging markets, and could have a material adverse impact on the Company s business and operating results.

Subsequent to the acquisition of Identity Systems, there have been no significant developments related to the current status of the acquired in-process research and development project that would result in material changes to the assumptions.

Synchrologic, Inc.

On December 29, 2003, the Company completed its acquisition of all of the issued and outstanding stock of Synchrologic, Inc. headquartered in Atlanta, Georgia pursuant to an Agreement and Plan of Merger, dated as of September 14, 2003. Synchrologic s product line provides mobile access to enterprise applications, email and personal information management, or PIM, data, file content, intranet sites, and Web content, while giving IT groups the tools to manage mobile devices remotely.

In the merger, all outstanding shares of Synchrologic common stock and preferred stock were converted into the right to receive a total of 15,130,171 shares of the Company s common stock. In addition, all outstanding options to purchase Synchrologic common stock were converted into options to purchase a total of 1,018,952 shares of the Company s common stock. The total number of shares issued was determined by dividing $60,000,000 by the

average closing price of $5.22 of the shares of the Company s common stock for the thirty consecutive trading days ending on the last complete trading day immediately preceding the closing date of the merger (which amount was subject to adjustment based on the transaction expenses incurred by Synchrologic in connection with the merger), provided that the number of shares did not exceed 19,800,000 or be fewer than 16,200,000 (in each case subject to adjustment based on the transaction expenses incurred by Synchrologic in connection with the merger). The shares were valued at approximately $62,125,000 using the five-trading-day average price surrounding the date the acquisition was announced of $4.11 per share, and the options were valued at approximately $4,123,000 using the Black-Scholes option pricing model. The following assumptions were used to perform the calculations of the fair market value of stock options issued: fair value of Company s common stock of $4.05, expected life of 3.9 years, risk-free interest rate of 3.4%, expected volatility of 132% and no expected dividend yield.

The condensed consolidated financial statements include the results of operations of Synchrologic since the date of acquisition. Under the purchase method of accounting, the total purchase price was allocated to Synchrologic s net tangible and intangible assets based upon the fair value as of the acquisition date. The purchase price of $67,037,000 (comprising the value of the shares and options described above and the estimated acquisition costs of $900,000 and net of a $111,000 adjustment for writing-off a certain liability due to Synchrologic) was assigned to the fair value of the assets acquired, including the following (in thousands):

Tangible assets acquired	$	4,105
Deferred tax assets		6,094
Liabilities assumed		(5,552)
Deferred tax liability assumed		(6,094)
In-process research and development		2,423
Developed and core technology		10,493
Patents		1,321
Customer base		3,487
Goodwill		50,760
	$	67,037

In accordance with SFAS No. 109, *Accounting for Income Taxes*, deferred tax liabilities of approximately $6,094,000 have been recorded for the tax effect of the amortizable intangible assets. Deferred tax assets of $6,094,000 have also been recorded by the Company to account for the tax effect of Synchrologic s net operating loss and credit carryforwards.

The valuation of identifiable intangible assets acquired was based on management s estimates, currently available information and reasonable and supportable assumptions. This allocation was generally based on the fair value of these assets determined using the income approach.

Approximately $50,760,000, as adjusted, was allocated to goodwill. Goodwill represents the excess of the purchase price over the fair value of the net tangible and intangible assets acquired. In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets,* goodwill associated with Synchrologic acquisition will not be amortized but will be tested for impairment at least annually.

Of the total purchase price, $15,301,000 was allocated to amortizable intangibles included in the above list. The amortizable intangible assets are being amortized using the straight-line method over the estimated useful life of the respective assets of four years. Refer to Note 5.

As of the acquisition date, technological feasibility of the in-process technology had not been established and the technology had no alternative future use. Accordingly, the Company expensed the in-process research and development at the date of the acquisition.

The amount of the purchase price allocated to in-process research and technology was based on established valuation techniques used in the high-technology software industry. The fair value assigned to the acquired

in-process research and development was determined using the income approach, which discounts expected future cash flows to present value. The key assumptions used in the valuation include, among others, expected completion date of the in-process projects identified as of the acquisition date, estimated costs to complete the projects, revenue contributions and expense projections assuming the resulting product has entered the market, and discount rate based on the risks associated with the development life cycle of the in-process technology acquired. The discount rate used in the present value calculations are normally obtained from a weighted-average cost of capital analysis, adjusted upward to account for the inherent uncertainties surrounding the successful development of the in-process research and development, the expected profitability levels of such technology, and the uncertainty of technological advances that could potentially impact the estimates. The Company assumed the pricing model for the resulting product of the acquired in process research and technology to be standard within its industry. The Company, however, did not take into consideration any consequential amount of expense reductions from integrating the acquired in-process technology with other existing in-process or completed technology. Therefore, the valuation assumptions do not include significant anticipated cost savings.

The key assumptions underlying the valuation of acquired in-process research and development from Synchrologic were as follows (in thousands):

Project names: Version upgrade of Data Sync, File Sync, E-mail Accelerator and Systems Management products

Percent completed as of acquisition date: 60%-70%

Estimated costs to complete technology at acquisition date: $3,000,000

Risk-adjusted discount rate: 22%

First period expected revenue: calendar year 2004

The development of the above technology was highly dependent on the remaining efforts to achieve technical viability, rapidly changing customer markets, uncertain standards for a new product, and significant competitive threats from several companies. The nature of the efforts to develop this technology into a commercially viable product consisted primarily of planning, designing, experimenting, and testing activities necessary to determine that the technology could meet market expectations, including functionality and technical requirements. Failure to bring the product to market in a timely manner could have resulted in a loss of market share or a lost opportunity to capitalize on emerging markets, and could have a material adverse impact on the Company s business and operating results.

Subsequent to the acquisition of Synchrologic, there have been no significant developments related to the current status of the acquired in-process research and development project that would result in material changes to the assumptions.

The liabilities assumed by the Company included Synchrologic s outstanding balance of approximately $1,764,000 under a credit facility agreement with a bank. The Company fully paid the outstanding balance during fiscal 2004. The bank credit facility agreement was automatically terminated upon the Company s acquisition of Synchrologic.

Spontaneous Technology, Inc.

On September 17, 2003, the Company consummated the acquisition of Spontaneous Technology, Inc. of Salt Lake City, Utah, a provider of enterprise secure Virtual Private Network, or sVPN™, software designed to extend existing corporate applications to most wireless devices. Under the terms of the agreement, the Company issued a total of 869,259 shares of Intellisync s common stock valued at approximately $2,999,000 using the five-trading-day average price surrounding the date the acquisition was announced of $3.45 per share, less registration costs. The number of shares were calculated using the average price of the Company s common stock for ten consecutive trading days ended three business days prior the date of acquisition. Later during fiscal 2004, Intellisync paid cash of approximately $752,000 for the satisfaction of another pre-acquisition clause related to an acquired customer contract. There were also 224,417 additional shares released from escrow during fiscal 2005 that were issued upon satisfaction of a pre-acquisition clause. Additionally, Intellisync was required to pay Spontaneous Technology

additional consideration of up to $7,000,000 in shares of Intellisync s common stock. The additional consideration was contingent upon the amount of Intellisync s revenue associated with sales of its products including certain technology of Spontaneous Technology during the period ended September 30, 2004. The earnout period ended with Intellisync s aggregate revenue on products associated with Spontaneous Technology amounting to less than the given earnout threshold. Consequently, no additional consideration was paid to Spontaneous Technology.

The condensed consolidated financial statements include the results of operations of Spontaneous Technology since the date of acquisition. Under the purchase method of accounting, the total purchase price was allocated to Spontaneous Technology s net tangible and intangible assets based upon their fair value as of the acquisition date. The purchase price of $4,071,000 (including acquisition costs of $320,000 and the payment made for the resolution of the contingency of $752,000) was assigned to the fair value of the assets acquired, including the following (in thousands):

Tangible assets acquired	$	18
Liabilities assumed		(1,726)
In-process research and development		469
Developed and core technology		889
Patents		168
Customer base		499
Goodwill		3,754
	$	4,071

Tangible assets acquired and liabilities assumed were valued at their respective carrying amounts as the Company believes that these amounts approximated their current fair values at the acquisition date. The valuation of identifiable intangible assets acquired was based on management s estimates, currently available information and reasonable and supportable assumptions. This allocation was generally based on the fair value of these assets determined using the income approach.

Approximately $3,754,000, as adjusted, was allocated to goodwill. Goodwill represents the excess of the purchase price over the fair value of the net tangible and intangible assets acquired. In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets,* goodwill will not be amortized but will be tested for impairment at least annually.

Of the total purchase price, $1,556,000 was allocated to amortizable intangibles included in the above list. The amortizable intangible assets are being amortized using the straight-line method over the estimated useful life of the respective assets of four years. Refer to Note 5.

As of the acquisition date, technological feasibility of the in-process technology had not been established and the technology had no alternative future use. Accordingly, the Company expensed the in-process research and development at the date of the acquisition.

The amount of the purchase price allocated to in-process research and technology was based on established valuation techniques used in the high-technology software industry. The fair value assigned to the acquired in-process research and development was determined using the income approach, which discounts expected future cash flows to present value. The key assumptions used in the valuation include, among others, expected completion date of the in-process projects identified as of the acquisition date, estimated costs to complete the projects, revenue contributions and expense projections assuming the resulting product has entered the market, and discount rate based on the risks associated with the development life cycle of the in-process technology acquired. The discount rate used in the present value calculations are normally obtained from a weighted-average cost of capital analysis, adjusted upward to account for the inherent uncertainties surrounding the successful development of the in-process research and development, the expected profitability levels of such technology, and the uncertainty of

technological advances that could potentially impact the estimates. The Company assumed the pricing model for the resulting product of the acquired in process research and technology to be standard within its industry. The Company, however, did not take into consideration any consequential amount of expense reductions from integrating the acquired in-process

technology with other existing in-process or completed technology. Therefore, the valuation assumptions do not include significant anticipated cost savings.

The key assumptions underlying the valuation of acquired in-process research and development from Spontaneous Technology were as follows (in thousands):

Project names: Version upgrade of Spontaneous Technology s secure Virtual Private Network (sVPN)

Percent completed as of acquisition date: 60%

Estimated costs to complete technology at acquisition date: $125,000

Risk-adjusted discount rate: 22%

First period expected revenue: calendar year 2004

The development of the above technology was highly dependent on the remaining efforts to achieve technical viability, rapidly changing customer markets, uncertain standards for a new product, and significant competitive threats from several companies. The nature of the efforts to develop this technology into a commercially viable product consisted primarily of planning, designing, experimenting, and testing activities necessary to determine that the technology could meet market expectations, including functionality and technical requirements. Failure to bring the product to market in a timely manner could have resulted in a loss of market share or a lost opportunity to capitalize on emerging markets, and could have had a material adverse impact on the Company s business and operating results.

Subsequent to the acquisition of Spontaneous Technology, there have been no significant developments related to the current status of the acquired in-process research and development project that would result in material changes to the assumptions.

Unaudited Pro Forma Consolidated Combined Results

The following unaudited pro-forma consolidated financial information reflects the results of operations for the three and nine months ended April 30, 2005 and 2004, as if Tourmaline, Identity Systems, Synchrologic and Spontaneous Technology acquisitions had occurred on the beginning of each period presented and after giving effect to purchase accounting adjustments. The effect of SoftVision s transfer of workforce has been excluded from the pro forma financial information as amounts are considered immaterial to the Company.

These pro forma results have been prepared for comparative purposes only and do not purport to be indicative of what operating results would have been had the acquisitions in aggregate actually taken place on the beginning of each period presented. In addition, these results are not intended to be a projection of future results and do not reflect any synergies that might be achieved from the combined operation (in thousands, except per share data):

	Three Months Ended April 30,		Nine Months Ended April 30,	
	2005	**2004**	**2005**	**2004**
Pro forma revenue	$ 15,386	$ 12,339	$ 44,544	$ 40,940
Pro forma net loss	$ (4,407)	$ (1,949)	$ (5,377)	$ (11,811)
Pro forma basic and diluted net loss per common share	$ (0.07)	$ (0.03)	$ (0.08)	$ (0.18)

The effect of the in-process research and development charges has been excluded in the above unaudited pro forma consolidated financial information as they represent non-recurring charges directly related to the acquisitions.

Note 5 Goodwill, Developed and Core Technology and Other Intangible Assets

The following table sets forth the changes in goodwill during the first two quarters of fiscal 2005 (in thousands):

	Goodwill
Balance at July 31, 2004	$ 65,288
Acquired from Tourmaline	1,911
Foreign exchange effects on non-US dollar-denominated goodwill	94
Balance at April 30, 2005	$ 67,293

Other intangible assets, net, consist of the following (in thousands, except weighted average useful life):

	Weighted Average Useful Life	April 30, 2005 Gross	April 30, 2005 Accumulated Amortization	April 30, 2005 Net	July 31, 2004 Gross	July 31, 2004 Accumulated Amortization	July 31, 2004 Net
Developed and core technology	4.3 years	$ 22,536	$ (8,964)	$ 13,572	$ 21,237	$ (5,370)	$ 15,867
Patents	4.0 years	1,680	(610)	1,070	1,680	(298)	1,382
Trademarks	2.5 years	250	(160)	90	250	(75)	175
Customer base	5.1 years	14,676	(3,822)	10,854	13,129	(1,472)	11,657
Covenant not-to-compete	2.0 years	105	(93)	12	105	(54)	51
Existing contracts	16.5 months	313	(306)	7	313	(296)	17
Acquired workforce	16 months	724	(453)	271	724	(45)	679
		$ 40,284	$ (14,408)	$ 25,876	$ 37,438	$ (7,610)	$ 29,828

Other intangible assets as of April 30, 2005 include a total of approximately $1,997,000 amortizable identifiable intangibles obtained from the Company s acquisition of Tourmaline during the third quarter of fiscal 2005. The foreign exchange effects on non-US dollar-denominated intangibles and associated accumulated depreciation were $849,000 and $107,000, respectively, for the first three quarters of fiscal 2005.

The amortization of developed technology amounted to $1,187,000 and $3,515,000 for the three and nine months ended April 30, 2005, respectively, and $990,000 and $1,543,000 for the corresponding periods in fiscal 2004. The amortization of other intangible assets amounted to $1,074,000 and $3,176,000 for the three and nine months ended April 30, 2005, respectively, and $679,000 and $1,003,000 for the corresponding periods in fiscal 2004.

Based on acquisitions completed as of April 30, 2005, the estimated future amortization expense of other intangible assets is as follows (in thousands):

	Developed and Core Technology	Other Intangibles
Three months ending July 31, 2005	$ 1,183	$ 1,056
Fiscal year ending July 31,		

2006		4,624		3,614
2007		4,381		3,076
2008		2,046		1,793
2009		685		955
2010		456		679
Thereafter		197		1,131
	$	13,572	$	12,304

Note 6 Restructuring Accrual

The Company implemented a number of cost-reduction plans aimed at reducing costs that were not integral to its overall strategy, better aligning its expense levels with current revenue levels and ensuring conservative spending during periods of economic uncertainty. These initiatives included a reduction in workforce and facilities consolidation.

The following table sets forth the activities in the restructuring accrual account during the first three quarters of fiscal 2005 (in thousands):

		Consolidation of Excess Facilities
Balance at July 31, 2004	$	1,080
Cash payments		(330)
Balance at October 31, 2004	$	750
Cash payments		(218)
Balance at January 31, 2005	$	532
Cash payments		(225)
Balance at April 30, 2005	$	307

The remaining unpaid amount as of April 30, 2005 of $307,000 related to the net lease expense due to the consolidation of excess facilities, will be paid over the respective lease terms through June 2006 using cash from operations.

The current and long-term portions of the restructuring accrual of $267,000 and $40,000 are classified as Accrued Liabilities and Other Liabilities, respectively, in the condensed consolidated balance sheet as of April 30, 2005.

The Company continually evaluates the balance of the restructuring reserve it records in prior periods based on the remaining estimated amounts to be paid. Differences, if any, between the estimated amounts accrued and the actual amounts paid will be reflected in operating expenses in future periods.

Note 7 Long-Term Debt

The following table sets forth the Company s long-term obligations, excluding capital lease obligations (in thousands):

	April 30, 2005		July 31, 2004	
3% convertible senior notes, interest due semi-annually, principal due in March 2009	$	57,884	$	58,443
Interest rate swap fair value hedge adjustment on $60 million of 3% convertible senior notes		2,116		1,557
		60,000		60,000
Less: current portion				
Long-term portion	$	60,000	$	60,000

3% Convertible Senior Notes

During the third quarter of fiscal 2004, the Company completed the offering of $60,000,000 of convertible senior notes to qualified institutional buyers in reliance on Rule 144A under the Securities Act. The notes are senior

unsecured obligations of Intellisync and rank junior to any future secured debt, on a parity with all of the Company s other existing and future senior unsecured debt and prior to any existing or future subordinated debt. As of April 30, 2005, the Company had no other senior or subordinated debt, except for ordinary course trade payables. The Company may not redeem any of the notes prior to their maturity. Holders, however, may require the Company to repurchase the notes upon some types of change in control transactions. The notes will mature on March 1, 2009 unless earlier converted or redeemed. Neither the Company nor any of its subsidiaries are subject to any financial covenants under the indenture. In addition, neither the Company nor any of its subsidiaries are restricted under the indenture from paying dividends, incurring debt, or issuing or repurchasing its securities.

The notes are convertible into shares of common stock of the Company at any time prior to the close of business on the final maturity date of the notes, subject to prior redemption of the notes. The initial conversion rate is 250.0000 shares per each $1,000 principal amount of notes which represents an initial conversion price of $4.00 per share. The conversion rate is subject to adjustment for certain events, including the payment of dividends, and other events specified in the indenture.

The notes bear interest at a rate of 3% per annum. Interest on the notes will be paid on March 1 and on September 1 of each year.

Interest Rate Swap

During fiscal 2004, the Company entered into two interest rate swap agreements with a financial institution on a total notional amount of $60,000,000, whereby the Company receives fixed-rate interest of 3% in exchange for variable interest payments. The interest rate swaps expire upon the maturity of the Company s $60,000,000, 3% convertible senior notes in March 2009, and effectively convert fixed-rate notes into variable-rate borrowings. The interest rate is reset semi-annually and is equal to the 6-month LIBOR rate less a rate spread. The total variable interest rate, approximately 2.9% at April 30, 2005, resulted in interest expense savings relative to fixed rates of approximately $486,000 for the first three quarters of fiscal 2005. Under the provisions of SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended, this arrangement has been designated and qualifies as an effective fair value hedge of interest rate risk related to the $60,000,000 convertible senior notes. As the terms of the swaps match those of the underlying hedged debt, the changes in the fair value of these swaps are offset by corresponding changes in the carrying value of the hedged debt, and therefore do not impact the Company s net earnings. As of April 30, 2005, the fair value of the interest rate swaps was approximately $2,116,000 and recorded in Other Liabilities with an equal adjustment recorded to the carrying value of the $60,000,000 convertible senior notes.

Refer to Note 8 for the description of the collateral required on the interest rate swap.

Note 8 Commitments and Contingencies

Leases

During the first quarter of fiscal 2005, the Company entered into a capital lease agreement for computer peripherals, which expires in September 2007. In addition, during fiscal 2004, the Company entered into a capital lease agreement for a phone system, which expires in February 2008. Assets and future obligations related to the capital leases are included in the accompanying condensed consolidated balance sheet as of April 30, 2005 in property and equipment and in the respective liability accounts, respectively. Current and long-term portions of the

capital leases amounted to $149,000 and $250,000, respectively, at April 30, 2005. Depreciation of assets held under the capital leases is included in depreciation and amortization expense.

The Company leases its facilities under operating leases that expire at various dates through December 2008. The total amount of rental payments due over the lease term is being charged to rent on the straight-line method over the term of the lease. The difference between rent expense recorded and the amount paid is credited or charged to deferred rent which is included in current liabilities in the accompanying balance sheets. Deferred rent was approximately $301,000 at April 30, 2005. Total rent expense was approximately $645,000 and $1,851,000 for the

three and nine months ended April 30, 2005, respectively, and approximately $499,000 and $1,152,000 for the corresponding periods in fiscal 2004.

Future minimum lease payments for all non-cancelable capital and operating lease agreements at April 30, 2005, were as follows (in thousands):

	Total	Three months ending July 31, 2005	Fiscal year ending July 31, 2006	2007	2008	2009
Capital lease obligation(1)	$ 438	$ 44	$ 177	$ 177	$ 40	$
Operating leases:						
Operating leases	5,225	924	2,786	766	544	205
Proceeds from subleases	(162)	(116)	(46)			
Net operating leases	5,063	808	2,740	766	544	205
Future minimum lease payments	$ 5,501	$ 852	$ 2,917	$ 943	$ 584	$ 205

(1) Includes interest payments due.

Guarantees

The Company has three letters of credit that collateralize certain operating lease obligations and total approximately $369,000 and $397,000 at April 30, 2005 and July 31, 2004, respectively. The Company collateralizes these letters of credit with cash deposits made with three of its financial institutions and has classified the short-term and the long-term portions of approximately $187,000 and $182,000 at April 30, 2005, and $101,000 and $296,000 at July 31, 2004 as Other Current Assets and Restricted Cash, respectively, in the condensed consolidated balance sheets. The long-term portion expires through June 2006. The holders of the letters of credit are able to draw on each respective letter of credit in the event that the Company is found to be in default of its obligations under each of its operating leases.

Under the terms of the interest rate swap agreement into which the Company entered during fiscal 2004, the Company must provide collateral to match any unfavorable mark-to-market exposure (fair value) on the swap. The amount of collateral required totals a minimum of $1,800,000 plus an amount equal to the unfavorable mark-to-market exposure on the swap. Generally, the required collateral will rise as interest rates rise. As of April 30, 2005, and July 31, 2004, the Company has posted approximately $3,797,000 and $3,736,000, respectively, of collateral under this swap agreement which is included in Restricted Cash in its condensed consolidated balance sheet.

In the event of early termination of the Company s service agreement with e deltacom, a division of ITC^DeltaCom, Inc. and a managed service provider, the Company may be required to pay e deltacom a penalty fee of up to approximately $45,000.

Litigation

In August 2004, a patent-infringement claim was filed against the Company by NCR Corporation in the U.S. District Court for the Southern District of Ohio. In the complaint, NCR alleged certain of the Company s products infringe three of its patents which allegedly cover technology for synchronizing databases between personal digital assistants and host computers. Based on a lengthy review, the Company believes that NCR s claims against it are without merit and the Company does not infringe on any of the asserted NCR patents. Separately, on September 9, 2004, the Company filed a complaint in the U.S. District Court for the Northern District of California against NCR requesting, among other things, that a declaratory judgment be entered finding that the Company does not infringe an NCR patent (6,473,765) that was asserted against one of the Company s licensees, Garmin Ltd. The Company has certain indemnification obligations to Garmin for claims related to intellectual property infringement. In response, NCR amended its suit against Garmin to withdraw its allegation of infringement of the 765 patent and stated that the Company has no liability to NCR for infringement of the 765 patent. NCR then moved to dismiss the California case on the basis that, because the Company could not be sued for infringement, the Court lacked jurisdiction to

adjudicate the Company s declaratory judgment action. Subsequently, the motion was granted and the California case was dismissed.

The Company is also involved in various litigation and claims arising in the normal course of business. In management s opinion, these matters are not expected to have a material impact on the Company s consolidated results of operations or financial condition.

Note 9 Net Loss Per Common Share

Basic net loss per common share is computed by dividing net loss available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted net loss per common share is computed by dividing net loss by the weighted average number of dilutive potential common shares that were outstanding during the period. Diluted weighted average shares reflect the dilutive effect, if any, of potential common shares based on the treasury stock method.

Basic and diluted net loss per common share were calculated as follows (in thousands, except per common share amounts):

	Three Months Ended April 30,		Nine Months Ended April 30,	
	2005	2004	2005	2004
Numerator:				
Net loss	$ (4,361)	$ (2,184)	$ (8,841)	$ (7,697)
Denominator:				
Weighted average shares outstanding used to compute basic and diluted net loss per common share	66,523	63,859	65,451	55,575
Basic and diluted net loss per common share	$ (0.07)	$ (0.03)	$ (0.14)	$ (0.14)

All common shares that were held in escrow or that were subject to repurchase by the Company, totaling approximately zero and 1,389,000 as of April 30, 2005 and 2004, respectively, were excluded from basic and diluted net loss per common share calculations.

Potential common shares attributable to stock options, convertible senior notes, shares held in escrow and shares subject to repurchase by the Company of 27,701,165 and 25,784,894 were outstanding at April 30, 2005 and 2004, respectively. However, as a result of a net loss incurred by the Company in the three and nine months ended April 30, 2005 and 2004, none of the in-the-money potential common shares were included in the weighted average outstanding shares (using the treasury stock method) used to calculate net loss per common share because the effect would have been antidilutive.

Note 10 Comprehensive Loss

Accumulated other comprehensive loss consists of net unrealized gain/loss on available for sale investments and foreign currency translation adjustments. Total comprehensive loss for the three and nine months ended April 30, 2005 and 2004, respectively, is presented in the following table (in thousands):

	Three Months Ended April 30,		Nine Months Ended April 30,	
	2005	2004	2005	2004
Net loss	$ (4,361)	$ (2,184)	$ (8,841)	$ (7,697)
Other comprehensive income (loss):				
Change in net unrealized income (loss) on investments	18	(47)	(7)	(81)
Realized loss on investments	(10)		(10)	
Change in currency translation adjustments	7	(32)	1,063	23
Total other comprehensive income (loss)	15	(79)	1,046	(58)
Total comprehensive loss	$ (4,346)	$ (2,263)	$ (7,795)	$ (7,755)

Note 11 Business Segments

Operating segments are identified as components of an enterprise about which separate, discrete financial information is available that is evaluated by the chief operating decision maker or decision-making group to make decisions about how to allocate resources and assess performance. The Company s chief operating decision maker is the chief executive officer. To date, the Company has reviewed its operations principally in a single segment.

The Company operates in a single industry segment encompassing the development, marketing and support of software and services that provide synchronization, wireless email, mobile application development, application/device management, real-time remote information access, secure VPN and identity searching/matching/screening capabilities. The Company s customer base consists primarily of corporate organizations, business development organizations, industry associations, mobile carriers, resellers, international system integrators, large OEMs in the personal computer, or PC, market and selected distributors, which primarily market to the retail channel, in North America, Europe, the Asia-Pacific region, South America, and Africa.

Revenue is attributed to regions based on the location of customers. Revenue information by geographic region is as follows (in thousands):

	Three Months Ended April 30,		Nine Months Ended April 30,	
	2005	2004	2005	2004
United States	$ 10,287	$ 7,658	$ 29,704	$ 19,291
Japan	677	1,174	2,053	4,547
Other International	4,273	2,175	12,038	5,188
Total revenue	$ 15,237	$ 11,007	$ 43,795	$ 29,026

Revenue information by product group is as follows (in thousands):

	Three Months Ended April 30,		Nine Months Ended April 30,	
	2005	2004	2005	2004
Enterprise and retail products	$ 7,803	$ 6,576	$ 25,880	$ 14,172
Technology licensing components	7,434	4,431	17,915	14,854
Total revenue	$ 15,237	$ 11,007	$ 43,795	$ 29,026

The Company s enterprise and retail products include Intellisync® Handheld Edition, Intellisync Handheld Edition for Enterprise, Intellisync Phone Edition, Intellisync Mobile Suite® and Identity Search Server, as well as related support and maintenance. Technology licensing components include various licensed technology platforms, including Intellisync Mobile Suite, Identity Search Server, Intellisync goAnywhere, Intellisync Software Development Platform, Intellisync Server-to-Server, professional services, hosting services, non-recurring engineering services and related maintenance contract programs. Technology licensing components also include our Tourmaline products such as Soda-Pop Mail®, Email Executive , AOL® Mail and Eudora2go

One customer accounted for 11% of the Company s total revenue for the three months ended April 30, 2005. No customers accounted for more than 10% of the Company s total revenue for the nine months ended April 30, 2005 and for the three and nine months ended April 30, 2004.

Goodwill information by geographic region is as follows (in thousands):

	April 30, 2005	July 31, 2004
United States	$ 60,691	$ 58,780
United Kingdom	4,922	4,828
Other International	1,680	1,680
Total goodwill	$ 67,293	$ 65,288

Other long-lived asset information by geographic region is as follows (in thousands):

	April 30, 2005	July 31, 2004
United States	$ 27,362	$ 29,829
United Kingdom	1,776	2,030
Australia	5,624	6,209
Other International	503	416
Total long-lived assets	$ 35,265	$ 38,484

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

The following information should be read in conjunction with the condensed consolidated financial statements and the notes thereto contained elsewhere in this Form 10-Q and in conjunction with the consolidated financial statements and management s discussion and analysis of financial condition and results of operations in our Form 10-K for the fiscal year ended July 31, 2004. This quarterly report on Form 10-Q, and in particular management s discussion and analysis of financial condition and results of operations, contains forward-looking statements regarding future events or our future performance that involve certain risks and uncertainties including those discussed in Factors That May Affect Future Operating Results below. In this Form 10-Q, the words anticipates, believes, expects, intends, future and similar expres identify forward-looking statements. All statements that address operating performance, our stock price, expectations regarding the impact of litigation, events or developments that we expect or anticipate will occur in the future, including statements relating to planned product releases and composition of revenue, both in terms of segment and geographical source and our expectations as to the future revenue from our enterprise and retail products, are forward-looking statements. Such forward-looking statements are based on management s current views and assumptions regarding future events and operating performance, and speak only as of the date hereof. We undertake no obligation to publicly update or revise any forward-looking statements whether as a result of new information, future events or otherwise. Actual events or our actual future results may differ materially from any forward-looking statements due to the risks and uncertainties outlined below.

Management s discussion and analysis includes:

A business overview.

Estimates, assumptions and critical accounting policies.

A comparison of our results of operations in the three and nine months ended April 30, 2005 with the results in the corresponding periods in fiscal 2004.

Recently issued accounting pronouncements.

A discussion of our operating liquidity and capital resources.

A discussion of factors that may affect our future operating results.

Business Overview

We develop, market and support desktop, enterprise and mobile carrier-class push-email, synchronization and systems management software that enables consumers, business professionals and information technology professionals to extend the capabilities of enterprise groupware and vertical applications, handheld organizers/computers, Web-enabled mobile phones, pagers and other wireless or wireline personal communications platforms. Our Identity Systems (formerly Search Software America, or SSA) subsidiaries develop, market and support global solutions that enhance an organization s ability to search, find, match (synchronize), screen and group identity data within their computer systems and network databases.

We have organized our operations into a single operating segment encompassing the development, marketing and support of software and services that provide synchronization, wireless email, mobile application development, application/device management, real-time remote information access, secure VPN and identity searching/matching/screening capabilities.

We license our software products directly to corporations, mobile carriers, original equipment manufacturers, or OEMs, and business development organizations worldwide. In addition, we sell our retail products through several

distribution channels both in the United States and internationally, including major distributors, resellers, computer dealers, retailers and mail-order companies. Internationally, we are represented by distributors, resellers and retailers in North America, Europe, the Asia-Pacific region, South America and Africa.

Recent Event

On March 1, 2005, we completed our acquisition of all of the issued and outstanding stock of Tourmaline Networks, Inc., a privately held developer and marketer of mobile email based on QUALCOMM s BREW® solution headquartered in San Diego, California. Refer to the discussion under the caption *Liquidity and Capital Resources* set forth below for more information.

Estimates, Assumptions and Critical Accounting Policies

Our financial statements and accompanying notes are prepared in accordance with generally accepted accounting principles in the United States of America. Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, sales and expenses. These estimates and assumptions are affected by management s application of accounting policies. Our critical accounting policies include license and service revenue recognition, channel inventory and product returns, valuation of goodwill, other intangibles, investments and other long-lived assets, restructuring accruals, loss contingencies and provision for doubtful accounts which are discussed in more detail under the caption *Estimates, Assumptions and Critical Accounting Policies* in our Annual Report on Form 10-K for the fiscal year ended July 31, 2004.

Results of Operations

The following table sets forth items included in the condensed consolidated statements of operations as a percentage of revenue for the periods indicated.

	Three Months Ended April 30,		Nine Months Ended April 30,	
	2005	2004	2005	2004
Revenue				
License	63.3%	68.2%	65.4%	70.1%
Services	36.7	31.8	34.6	29.9
Total revenue	100.0%	100.0%	100.0%	100.0%
Cost and operating expenses:				
Cost of revenue	16.6	20.3	16.9	19.5
Amortization of developed and core technology	7.8	9.0	8.0	5.3
Research and development	25.0	31.8	24.7	27.9
Sales and marketing	53.9	41.9	45.8	39.5
General and administrative	14.6	14.4	14.6	20.3
Amortization of intangibles	7.0	6.2	7.2	3.5
In-process research and development		7.0		12.6
Other charges		2.3		3.2
Total cost and operating expenses	124.9	132.9	117.2	131.8
Operating loss	(24.9)	(32.9)	(17.2)	(31.8)
Other income (expense):				
Interest income	2.0	1.6	1.8	1.4
Interest expense	(2.6)	(0.9)	(2.1)	(0.3)
Other, net	(1.0)	(0.9)	(1.4)	(0.3)
Litigation settlement gain, net		14.3		5.4
Total other income (expense)	(1.6)	14.1	(1.7)	6.2
Loss before income taxes	(26.5)	(18.8)	(18.9)	(25.6)
Provision for income taxes	(2.1)	(1.1)	(1.3)	(0.9)
Net loss	(28.6)%	(19.9)%	(20.2)%	(26.5)%

Revenue

	Three Months Ended April 30,			Nine Months Ended April 30,		
	2005	Percent Change	2004	2005	Percent Change	2004
	(In thousands, except percentage)					
Total revenue	$ 15,237	38.4%	$ 11,007	$ 43,795	50.9%	$ 29,026

We derive revenue from two primary sources: software licenses and fees for services. The increase in revenue for the three and nine months ended April 30, 2005 was primarily due from revenue contributions of Synchrologic, Inc. and Identity Systems (formerly Search Software America, or SSA) product sales, both of which we acquired during fiscal 2004. The increase was also brought about by the continued

fundamental shift in our customer base and revenue streams as we launched new wireless products and ramped up our wireless email solution with the global wireless market.

While the market for smartphones and other wireless mobile devices has grown recently, the market for wired or traditional personal digital assistants, or PDAs, has continued to face challenges. The overall decline in traditional PDA sales has had a direct impact on sales of our Intellisync products through the consumer and online channels,

where sales of our synchronization software typically occur at the same time a PDA is purchased, or shortly thereafter. Due to this decline, our retail revenue, which consists of sales to distributors and direct sales to end-users, decreased during the first three quarters of fiscal 2005.

License Revenue

	Three Months Ended April 30,			Nine Months Ended April 30,		
	2005	Percent Change	2004	2005	Percent Change	2004
	(In thousands, except percentage)					
License revenue	$ 9,643	28.4%	$ 7,512	$ 28,662	40.9%	$ 20,336
As percentage of total revenue	63.3%		68.2%	65.4%		70.1%

License revenue is earned from the sale and use of software products (including our technology licensing components) and royalty agreements with original equipment manufacturers, or OEMs. The increase in license revenue in absolute dollars for the three months ended April 30, 2005 as compared with that for the corresponding period of fiscal 2004 reflected an increase of $1,395,000 in revenue from technology licensing components and $736,000 in revenue from enterprise products. The increase in license revenue in absolute dollars for the nine months ended April 30, 2005 as compared with that for the corresponding period of fiscal 2004 reflected an increase of $6,536,000 in revenue from enterprise products and an increase of $1,790,000 in revenue from technology licensing components. A significant portion of the increase in our enterprise revenue was contributed by Synchrologic, Inc. (acquired in December 2003), particularly Intellisync Mobile Suite, and Identity Systems (acquired in March 2004) product sales. The decrease in license revenue as a percentage of total revenue was primarily due to the increase in service revenue in the three and nine months ended April 30, 2005 as described below.

Service Revenue

	Three Months Ended April 30,			Nine Months Ended April 30,		
	2005	Percent Change	2004	2005	Percent Change	2004
	(In thousands, except percentage)					
Service revenue	$ 5,594	60.1%	$ 3,495	$ 15,133	74.1%	$ 8,690
As percentage of total revenue	36.7%		31.8%	34.6%		29.9%

Service revenue is derived from fees for services, including fixed-price and time-and-materials professional services arrangements and amortization of maintenance contract programs. The increase in service revenue for the three months ended April 30, 2005 as compared with that for the corresponding period of fiscal 2004 resulted from a total increase of $2,756,000 brought about by an increase in amortization of our maintenance contract programs relating to the increase in license revenue, as well as revenue from our hosting services. This increase was offset by a $657,000 decrease in professional service revenue associated with our technology licensing partners. The increase in service revenue for the nine months ended April 30, 2005 as compared with that for the corresponding period of fiscal 2004 reflected an increase of $8,055,000 in revenue from our maintenance contract programs and hosting services, slightly offset by $1,612,000 decrease in professional service revenue.

In any period, service revenue from time and materials contracts is dependent, among other things, on license transactions closed during the current and preceding quarters and customer decisions regarding implementations of licensed software.

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Enterprise and Retail Products

	Three Months Ended April 30,			Nine Months Ended April 30,		
	2005	Percent Change	2004	2005	Percent Change	2004
	(In thousands, except percentage)					
Enterprise and retail products	$ 7,803	18.7%	$ 6,576	$ 25,880	82.6%	$ 14,172
As percentage of total revenue	51.2%		59.7%	59.1%		48.8%

Our enterprise and retail products revenue includes sales to retail distribution channels, as well as direct sales of our personal and server products licensed to corporations for internal use. Enterprise and retail products include Intellisync Handheld Edition, Intellisync Handheld Edition for Enterprise, Intellisync Phone Edition, Intellisync Mobile Suite and Identity Search Server (formerly Identity Systems), as well as related support and maintenance. Enterprise sales frequently involve large up-front license fees, which can result in lengthy sales cycles and uncertainties as to the timing of sales driven by customers budgetary processes. As a result, we generally have less visibility into future enterprise sales than is typically the case in our royalty-based technology licensing business. In addition, while enterprise sales generally result in ongoing maintenance revenue and may lead to follow-on purchases or upgrades, we are typically dependent on sales to new customers for a significant portion of our enterprise revenue in a given quarter.

The increase in enterprise and retail products revenue for the three months ended April 30, 2005 as compared with that for the corresponding period of fiscal 2004 resulted from contributions of $1,503,000 from Identity Systems and Synchrologic products and an increase of $987,000 in revenue from amortization of support and maintenance based on a higher license revenue base. This increase was slightly offset by a $1,263,000 decrease in revenue from Intellisync Handheld Edition for Enterprise and in retail sales of our Intellisync software. The increase in enterprise and retail products revenue for the nine months ended April 30, 2005 as compared with that for the corresponding period of fiscal 2004 resulted from contributions of $9,576,000 from Identity Systems and Synchrologic products and an increase of $4,948,000 in revenue from amortization of support and maintenance, slightly offset by a $2,816,000 decrease in revenue from retail sales of our Intellisync software. Less emphasis on marketing of Intellisync Handheld Edition for Enterprise, and more on the transition of our enterprise server offering to Intellisync Mobile Suite, during the most recent quarters contributed to the decrease in revenue from Intellisync Handheld Edition for Enterprise. We expect revenue in absolute dollars from enterprise and retail products to remain at the current level or decrease in the following quarter, which we believe will occur as a result of seasonal factors in the enterprise and retail business inherent with the summer, as well as of continued decrease in revenue related to our legacy products.

Technology Licensing Components

	Three Months Ended April 30,			Nine Months Ended April 30,		
	2005	Percent Change	2004	2005	Percent Change	2004
	(In thousands, except percentage)					
Technology licensing components	$ 7,434	67.8%	$ 4,431	$ 17,915	20.6%	$ 14,854
As percentage of total revenue	48.8%		40.3%	40.9%		51.2%

Technology licensing components include various licensed technology platforms, including Intellisync Mobile Suite, Intellisync goAnywhere, Intellisync Software Development Platform, Intellisync Server-to-Server, professional services, non-recurring engineering services and related maintenance contract programs. The increase in technology licensing revenue for the three months ended April 30, 2005 as compared with that

for the corresponding period of fiscal 2004 resulted from contributions of $3,164,000 from Intellisync Software Development Platform and hosting service revenue, offset slightly by a $161,000 decrease in revenue from professional services. Revenue from hosting services grew in the quarter through a combination of growth from existing carrier customers and the signing of several new carrier contracts during the quarter. The increase in technology licensing revenue for the nine months ended April 30, 2005 as compared with that for the corresponding period of fiscal 2004 resulted from contributions of $4,896,000 from Intellisync Software Development Platform and

hosting service revenue, offset slightly by $1,835,000 decrease in revenue from professional services. We expect that a further increase in revenue from our carrier business during the next quarter will result in an overall increase in our technology licensing revenue as compared with the recent previous quarters.

International Revenue

	Three Months Ended April 30,			Nine Months Ended April 30,		
	2005	Percent Change	2004	2005	Percent Change	2004
	(In thousands, except percentage)					
International revenue	$ 4,950	47.8%	$ 3,349	$ 14,091	44.7%	$ 9,735
As percentage of total revenue	32.5%		30.4%	32.2%		33.5%

The year-over-year increase in our international revenue represented 38% and 29% of our total revenue increase for the three and nine months ended April 30, 2005. Our international revenue growth, in absolute dollars, was a result of a number of factors including an increase in the number of our international technology licensing partners, particularly in Europe; the full-quarter and the full nine-month revenue effect of Identity Systems during fiscal 2005; an increase in the number of sales people worldwide; and the effect of foreign exchange translation. The slight decrease in international revenue as a percentage of total revenue for the nine months ended April 30, 2005, on the other hand, is primarily due to increased revenue from our newer offerings in the United States. We expect that our acquisitions of Synchrologic and Identity Systems will further strengthen our presence in Europe, as well as in Asia-Pacific. We believe, however, that international revenue will fluctuate on a quarter to quarter basis as we periodically enter into new agreements for professional services and new international partner contracts for technology licensing. International revenue may be subject to certain risks not normally encountered in operations in the United States, including exposure to tariffs, various trade regulations, fluctuations in currency exchange rates, as well as international software piracy as described more fully in *Factors That May Affect Future Operating Results* set forth below. We believe that continued growth will require further expansion in international markets. We have utilized and will likely continue to utilize substantial resources both to expand and establish international operations in the future.

Top Customers

One customer accounted for 11% of our total revenue for the three months ended April 30, 2005. No customers accounted for more than 10% of our total revenue for the nine months ended April 30, 2005 and for the three and nine months ended April 30, 2004.

Cost of Revenue

	Three Months Ended April 30,			Nine Months Ended April 30,		
	2005	Percent Change	2004	2005	Percent Change	2004
	(In thousands, except percentage)					
Cost of revenue	$ 2,537	13.4%	$ 2,237	$ 7,397	30.5%	$ 5,667
As percentage of total revenue	16.6%		20.3%	16.9%		19.5%

Cost of revenue consists of license costs and service costs. License costs comprise product-packaging expenses such as product media and duplication, manuals, packing supplies, and shipping costs. Service costs comprise personnel-related expenses such as salaries and other related costs associated with work performed under professional service contracts, non-recurring engineering agreements, post-sales customer support costs and hosting costs for hosting services associated with technology licensing partners and end users. Hosting costs include expenses related to bandwidth for hosting, tape backup, security and storage, third-party fees and internal personnel costs associated with logistics and operational support of the hosting services. Service costs can be expected to vary significantly from period to period depending on the mix of services we provide.

In general, license revenue costs represent a smaller percentage of license revenue when compared with service revenue costs as a percentage of service revenue; this is due to the high cost structure of service revenue. Additionally, license costs tend to be variable based on license revenue volumes, whereas service costs tend to be fixed within certain service revenue volume ranges. We would expect that an increase in service revenue as a percentage of our total revenue would generate lower overall gross margins as a percentage of total revenue. Also, given the high level of fixed costs associated with the professional services group and our hosting operations, our inability to generate revenue sufficient to absorb these fixed costs could lead to low or negative service gross margins.

The increase in cost of revenue in absolute dollars reflected the effect of planned increases in mobile hosting and post-sales support infrastructure. The increase in overall revenue contributed to improvement in our gross margins for the three and nine months ended April 30, 2005. In future periods, cost of revenue may further fluctuate from quarter to quarter due to potential changes in the infrastructure and other requirements of our hosting operations to meet carriers demand. These changes, which may be costly, are difficult to forecast. In addition, our cost of revenue is primarily driven by our expectation for different margin characteristics within and between license and service revenue as well as the expected mix between products and channels.

Amortization of Developed and Core Technology

	Three Months Ended April 30,			Nine Months Ended April 30,		
	2005	Percent Change	2004	2005	Percent Change	2004
	(In thousands, except percentage)					
Amortization of developed and core technology						