

Support.com, Inc.
Form 10-Q
May 06, 2011

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

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended March 31, 2011

OR

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

For the transition period from _____ to _____

Commission File No. 000-30901

SUPPORT.COM, INC.
(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction
of Incorporation or Organization)

94-3282005
(I.R.S. Employer Identification No.)

1900 Seaport Boulevard, 3rd Floor
Redwood City, CA 94063

(Address of Principal Executive Offices)
(Zip Code)

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

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

On April 30, 2011, 48,483,736 shares of the Registrant's Common Stock, \$0.0001 par value, were outstanding.

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SUPPORT.COM, INC.

FORM 10-Q

QUARTERLY PERIOD ENDED MARCH 31, 2011

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SUPPORT.COM, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands)

| | March 31, 2011 (Unaudited) | December 31, 2010 (1) |
|---|----------------------------------|-----------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 18,932 | \$ 18,561 |
| Short-term investments | 51,175 | 53,007 |
| Accounts receivable, net | 5,859 | 5,133 |
| Prepaid expenses and other current assets | 1,232 | 1,617 |
| Total current assets | 77,198 | 78,318 |
| Long-term investments | 2,598 | 2,667 |
| Property and equipment, net | 601 | 623 |
| Goodwill | 10,181 | 10,181 |
| Purchased technology, net | 206 | 226 |
| Intangible assets, net | 993 | 1,076 |
| Other assets | 684 | 648 |
| Total assets | \$92,461 | \$ 93,739 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 372 | \$ 536 |
| Accrued compensation | 1,864 | 1,248 |
| Other accrued liabilities | 3,710 | 3,575 |
| Deferred revenue | 1,996 | 1,574 |
| Total current liabilities | 7,942 | 6,933 |
| Other long-term liabilities | 716 | 749 |
| Total Liabilities | 8,658 | 7,682 |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Common stock | 5 | 5 |
| Additional paid-in capital | 230,713 | 229,692 |
| Accumulated other comprehensive loss | (1,464) | (1,331) |
| Accumulated deficit | (145,451) | (142,309) |
| Total stockholders' equity | 83,803 | 86,057 |
| Total liabilities and stockholders' equity | \$92,461 | \$ 93,739 |

(1) Derived from the December 31, 2010 audited Consolidated Financial Statements included in the Annual Report on Form 10-K, as filed with the Securities and Exchange Commission on March 11, 2011.

See accompanying notes.

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SUPPORT.COM, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)
(Unaudited)

| | Three Months Ended March 31, | |
|--|---------------------------------|------------|
| | 2011 | 2010 |
| Revenue: | | |
| Services | \$9,150 | \$6,730 |
| Software and other | 3,880 | 3,129 |
| Total revenue | 13,030 | 9,859 |
| Cost of revenue: | | |
| Cost of services | 6,817 | 5,484 |
| Cost of software and other | 404 | 348 |
| Total cost of revenue | 7,221 | 5,832 |
| Gross profit | 5,809 | 4,027 |
| Operating expenses: | | |
| Research and development | 1,448 | 1,343 |
| Sales and marketing | 4,785 | 3,971 |
| General and administrative | 2,786 | 2,952 |
| Amortization of intangible assets | 83 | 88 |
| Total operating expenses | 9,102 | 8,354 |
| Loss from operations | (3,293) | (4,327) |
| Interest income and other, net | 150 | 186 |
| Loss from continuing operations, before income taxes | (3,143) | (4,141) |
| Income tax provision | 2 | 12 |
| Loss from continuing operations, after income taxes | (3,145) | (4,153) |
| Income (loss) from discontinued operations, after income taxes | 3 | (5) |
| Net loss | \$(3,142) | \$(4,158) |
| Basic and diluted earnings per share: | | |
| Loss from continuing operations | \$(0.07) | \$(0.09) |
| Income (loss) from discontinued operations | 0.00 | (0.00) |
| Basic and diluted net loss per share | \$(0.07) | \$(0.09) |
| Shares used in computing basic and diluted net loss per share | 48,181 | 46,470 |

See accompanying notes.

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SUPPORT.COM, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)
(Unaudited)

| | Three Months Ended March 31, | |
|---|---------------------------------|------------|
| | 2011 | 2010 |
| Operating Activities: | | |
| Net loss | \$(3,142) | \$(4,158) |
| Adjustments to reconcile net loss to net cash provided by (used in) operating activities: | | |
| Depreciation | 100 | 91 |
| Amortization of premiums and discounts on investments | 438 | 185 |
| Amortization of purchased technology | 20 | 21 |
| Amortization of intangible assets | 83 | 88 |
| Realized loss on auction-rate securities put option re-valuation | — | 472 |
| Realized gain on auction-rate securities | — | (472) |
| Stock-based compensation | 805 | 855 |
| Changes in assets and liabilities: | | |
| Accounts receivable, net | (726) | (125) |
| Prepaid expenses and other current assets | 381 | (186) |
| Other long-term assets | (56) | (8) |
| Accounts payable | (167) | 10 |
| Accrued compensation | 610 | 749 |
| Other accrued liabilities | 128 | 856 |
| Other long-term liabilities | (62) | (15) |
| Deferred revenue | 422 | 435 |
| Net cash used in operating activities | (1,166) | (1,202) |
| Investing Activities: | | |
| Purchases of property and equipment | (78) | (72) |
| Purchases of investments | (17,452) | (11,512) |
| Sales of investments | 3,998 | 2,400 |
| Maturities of investments | 14,844 | 10,340 |
| Net cash provided by investing activities | 1,312 | 1,156 |
| Financing Activities: | | |
| Proceeds from issuances of common stock | 216 | 34 |
| Net cash provided by financing activities | 216 | 34 |
| Net increase (decrease) in cash and cash equivalents | 362 | (12) |
| Effect of exchange rate changes on cash and cash equivalents | 9 | 0 |
| Cash and cash equivalents at beginning of period | 18,561 | 23,547 |
| Cash and cash equivalents at end of period | \$18,932 | \$23,535 |
| Supplemental schedule of cash flow information: | | |
| Income taxes paid (refunded) | \$(8) | \$55 |

See accompanying notes.

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SUPPORT.COM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Significant Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Support.com, Inc. (the “Company”, “Support.com”, “we” or “us”) and its wholly owned subsidiaries. All intercompany balances and transactions have been eliminated. The balance sheet as of March 31, 2011 and the statements of operations for the three months ended March 31, 2011 and 2010 and cash flows for the three months ended March 31, 2011 and 2010 are unaudited. In the opinion of management, these unaudited interim condensed consolidated financial statements reflect all adjustments (consisting of normal recurring adjustments) that are necessary for a fair presentation of the results for, and as of, the periods shown. The results of operations for such periods are not necessarily indicative of the results expected for the full fiscal year or for any future period. The condensed consolidated balance sheet information as of December 31, 2010 is derived from audited financial statements as of that date. These unaudited interim condensed consolidated financial statements should be read with the consolidated financial statements and related notes included in the Company’s Annual Report on Form 10-K, filed with the Securities and Exchange Commission on March 11, 2011.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. The accounting estimates that require management’s most significant, difficult and subjective judgments include accounting for revenue recognition, fair value measurements, fair value estimates – auction-rate securities (“ARS”) put option, business combinations – purchase accounting, accounting for goodwill and other intangible assets, stock-based compensation and accounting for income taxes. Actual results could differ materially from these estimates.

Revenue Recognition

For all transactions, we recognize revenue only when all of the following criteria are met:

- Persuasive evidence of an arrangement exists;
- Delivery has occurred;
- Collection is considered probable; and
- The fees are fixed or determinable.

We consider all arrangements with payment terms longer than 90 days not to be fixed or determinable. If the fee is considered not to be fixed or determinable, revenue is recognized as payment becomes due from the customer.

Services Revenue

Services revenue is comprised primarily of fees for technology support services, including the set-up, protection, optimization and repair of new and existing computers as well as other technology devices. We provide these services

remotely, using work-from-home Personal Technology Experts who utilize our proprietary technology to deliver the services.

We provide services to consumers and small business, either through our channel partners (which include brick and mortar and online retailers, anti-virus providers, PC/consumer electronics (“PC/CE”) manufacturers, internet service providers (“ISP’s”), and others) or directly via our website (www.support.com). We transact with customers via reseller programs, referral programs and direct transactions. In reseller programs, the channel partner generally executes the financial transactions with the consumer and pays a fee to us which we recognize as revenue when the service is provided. In referral programs, we transact with the consumer directly and pay a referral fee to the referring party. Referral fees are expensed in the period in which the customer was acquired. In such instances, since we are the transacting party and bear substantially all risks associated with the transaction, we record the gross amount of revenue. In direct-to-consumer transactions, we sell directly to the consumer at the retail price.

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Our services are of three types for revenue recognition purposes:

Incident-Based Services—Customers purchase a discrete, one-time service. Revenue recognition occurs at the time of service delivery. Fees paid for services sold but not yet delivered are recorded as deferred revenue and recognized at the time of service delivery.

Subscriptions—Customers purchase subscriptions or “service plans” under which certain services are provided over a fixed subscription period. Revenues for subscriptions are recognized ratably over the respective subscription periods.

Service Cards / Gift Cards—Customers purchase a service card and/or a gift card, which entitles the cardholder to redeem a certain service at a time of their choosing. For these sales, revenue is deferred until the card has been redeemed and the service has been provided.

For certain direct and channel partnerships, we are paid for services that are sold but not yet delivered. We initially record such balances as deferred revenue, and recognize revenue when the service has been provided or, on the non-subscription portion of these balances, when the likelihood of the service being redeemed by the customer is remote (“services breakage”). Based upon our historical redemption patterns for these relationships, we believe that the likelihood of a service being delivered more than 90 days after sale is remote. Beginning in the second quarter of 2010, we therefore recognized non-subscription deferred revenue balances older than 90 days as services revenue. For the three months ended March 31, 2011, services breakage revenue was immaterial, and accounted for less than one percent of revenue.

Channel partners are generally invoiced monthly. Fees from consumers via referral programs and direct transactions are generally paid with a credit card at the time of sale. Revenue is recognized net of any applicable sales tax.

We generally provide a refund period on services, during which refunds may be granted to consumers under certain circumstances, including inability to resolve certain support issues. For our channel sales, the refund period varies by partner, but is generally between 5 and 10 days. For referral programs and direct transactions, the refund period is generally 5 days. For all channels, we recognize revenue net of refunds and cancellations during the period. Refunds and cancellations have not been material.

Software and Other Revenue

Software and other revenue is comprised primarily of fees for software products provided through direct consumer downloads and, to a lesser extent, through the sale of this software via channel partners. Our software is sold to consumers as a perpetual license. We act as the primary obligor and generally control fulfillment, pricing, product requirements, and collection risk and therefore we recognize revenues using the gross method in the period in which the software products were sold. We provide a limited amount of free technical support to customers. We therefore do not defer the recognition of any revenue associated with sales of these products, since the cost of providing this free technical support is insignificant. The technical support is generally provided within one year after the associated revenue is recognized and free product enhancements are minimal and infrequent. Other revenue consists primarily of revenue generated through partners advertising to our customer base in various forms, including toolbar advertising, email marketing, and free trial offers. We recognize other revenue as it is earned.

Cash, Cash Equivalents and Investments

All liquid instruments with an original maturity at the date of purchase of ninety days or less are classified as cash equivalents. Cash equivalents and short-term investments consist primarily of money market funds, commercial paper and corporate and municipal bonds. Our interest income on cash, cash equivalents and investments is recorded

monthly and reported as interest income and other in our condensed consolidated statements of operations.

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Long-term investments consist of auction-rate securities (“ARS”). Our cash equivalents, short-term and long-term investments are classified as available-for-sale, and are reported at fair value with unrealized gains/losses (when deemed to be temporary) included in accumulated other comprehensive income within stockholders’ equity in the condensed consolidated balance sheets. We recorded net unrealized losses on our available-for-sale securities of \$200,000 and \$127,000 at March 31, 2011 and December 31, 2010, respectively.

Prior to June 30, 2010 we held certain ARS with UBS. On June 30, 2010 we exercised our Rights Agreement (“the “ARS put option”) with UBS and settled the ARS for cash on June 30 and July 1, 2010. The ARS held with UBS were classified as trading securities and reported at fair value with realized gains/losses included in interest income (expense) and other, net in the condensed consolidated statements of operations. Furthermore, we carried the ARS put option at fair value and re-measured the fair value each reporting period with gains/losses included in interest income (expense) and other. The impact of the re-measurement of the ARS put option substantially offset changes in the fair value of the ARS held by UBS. For the three months ended March 31, 2011, we recorded zero realized gains/losses as a result of ARS held by UBS that were settled in 2010. For the three months ended March 31, 2010, we recorded a realized loss of \$472,000 on re-valuation of the ARS put option, offset with a realized gain of \$472,000 on the ARS held with UBS, for a net realized loss of zero.

We monitor our investments for impairment on a quarterly basis and determine whether a decline in fair value is other-than-temporary by considering factors such as current economic and market conditions, the credit rating of the security’s issuer, the length of time an investment’s fair value has been below our carrying value, our intent to sell the security and our belief that we will not be required to sell the security before the recovery of our amortized cost. If an investment’s decline in fair value is deemed to be other-than-temporary, we reduce its carrying value to its estimated fair value, as determined based on quoted market prices or liquidation values. Declines in value judged to be other-than-temporary, if any, are recorded in operations as incurred. At March 31, 2011, we evaluated our unrealized gains/losses on available-for-sale securities, the majority of which are from the long-term ARS, and determined them to be temporary. The long-term investments have been in continuous unrealized loss positions for more than 12 months. We currently do not intend to sell these securities with unrealized losses and we concluded that we will not be required to sell these securities before the recovery of our amortized cost basis.

The following is a summary of cash, cash equivalents and investments at March 31, 2011 and December 31, 2010 (in thousands):

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|-------------------------|-------------------|------------------------------|-------------------------------|------------|
| As of March 31, 2011 | | | | |
| Cash | \$3,323 | \$— | \$— | \$3,323 |
| Money market funds | 13,610 | — | — | 13,610 |
| Corporate bonds | 25,266 | 14 | (21) | 25,259 |
| Corporate notes | 16,910 | 15 | (2) | 16,923 |
| Commercial paper | 3,997 | 1 | — | 3,998 |
| Treasuries | 7,000 | 1 | (7) | 6,994 |
| Auction-rate securities | 2,800 | — | (202) | 2,598 |
| | \$72,906 | \$31 | \$(232) | \$72,705 |

Classified as:

| | | | | |
|---------------------------|----------|-----|--------|----------|
| Cash and cash equivalents | \$18,932 | \$— | \$— | \$18,932 |
| Short-term investments | 51,174 | 31 | (30) | 51,175 |
| Long-term investments | 2,800 | — | (202) | 2,598 |

| | | | | |
|----------|------|--------|---|----------|
| \$72,906 | \$31 | \$(232 |) | \$72,705 |
|----------|------|--------|---|----------|

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| As of December 31, 2010 | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---------------------------|-------------------|------------------------------|-------------------------------|------------|
| Cash | \$2,340 | \$— | \$— | \$2,340 |
| Money market fund | 14,221 | — | — | 14,221 |
| Commercial paper | 6,992 | — | (2) | 6,990 |
| Corporate bonds | 22,013 | 19 | (20) | 22,012 |
| Corporate notes | 20,997 | 25 | (14) | 21,008 |
| Treasuries | 4,999 | — | (2) | 4,997 |
| Auction-rate securities | 2,800 | — | (133) | 2,667 |
| | \$74,362 | \$44 | \$(171) | \$74,235 |
| Classified as: | | | | |
| Cash and cash equivalents | \$18,561 | \$— | \$— | \$18,561 |
| Short-term investments | 53,001 | 44 | (38) | 53,007 |
| Long-term investments | 2,800 | — | (133) | 2,667 |
| | \$74,362 | \$44 | \$(171) | \$74,235 |

The following table summarizes the estimated fair value of our available-for-sale securities classified by the stated maturity date of the security (in thousands):

| | March 31 2011 | December 31 2010 |
|-----------------------|------------------|---------------------|
| Due within one year | \$43,260 | \$ 50,350 |
| Due within two years | 9,914 | 4,657 |
| Due after three years | 2,598 | 2,667 |
| | \$55,772 | \$ 57,674 |

At March 31, 2011 and December 31, 2010 we had investments in AAA-rated ARS with various state student loan authorities with estimated fair values aggregating \$2.6 million and \$2.7 million, respectively. The student loans made by these authorities are substantially guaranteed by the federal government through the Federal Family Education Loan Program (FFELP). ARS are long-term floating rate bonds tied to short-term interest rates. After the initial issuance of the securities, the interest rate on the securities is reset periodically, at intervals established at the time of issuance (e.g., every seven days, twenty-eight days, thirty-five days, or every six months), based on market demand, if the auctions are successful. ARS are bought and sold in the marketplace through a competitive bidding process often referred to as a "Dutch auction." If there is insufficient interest in the securities at the time of an auction, the auction may not be completed and the ARS then pays a default interest rate. Following such a failed auction, we cannot access our funds that are invested in the corresponding ARS until a future auction of these investments is successful, new buyers express interest in purchasing these securities in between reset dates, issuers establish a different form of financing to replace these securities or final payments become due according to contractual maturities. Commencing in February 2008, conditions in the global credit markets resulted in failed auctions for all of the ARS we held. In the near term, our ability to liquidate our investments in ARS or fully recover the carrying values may be limited or not exist.

Fair value for all ARS, including both the UBS securities classified as trading securities and the other ARS classified as available-for-sale, was based on a discounted cash flow valuation that takes into account a number of factors including the weighted average remaining term (WART) of the underlying securities, the expected return, and the discount rate. The actual WART from servicing reports was used where available. For securities where the actual WART was not available an estimate based on other securities held was used. The expected return was calculated based on the last twelve months average for the 91 day U.S., treasury bill plus a spread. The discount rate was

calculated using the 3-month LIBOR rate plus adjustments for the security type. Changes in any of the above estimates, especially the weighted average remaining term or the discount rate, could result in a material change to the fair value. At March 31, 2011, all ARS were classified as Level 3 assets. Presently we have determined the decline in value for the available-for-sale ARS to be temporary because i) we have no current intent to sell these securities, and we believe that we will not be required to sell these securities before the recovery of its amortized cost due to our current cash, cash equivalents, and other investment balances; ii) through March 31, 2011 all of the securities have maintained AAA credit ratings; and iii) loans made by the issuers are backed by the federal government.

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However, if circumstances change, we may be required to record an other-than-temporary impairment charge on the available-for-sale ARS. We may similarly be required to record other-than-temporary impairment charges if the ratings on any of these securities are reduced or if any of the issuers default on their obligations. In addition to impairment charges, any of these events could cause us to lose part or all of our investment in these securities. Any of these events could materially affect our results of operations and our financial condition. We currently believe these securities are not significantly impaired for the reasons described above; however, it could take until the final maturity of the underlying notes (up to 30 years) to realize our investments' recorded value.

Fair Value Measurements

Fair value is defined under ASC 820, Fair Value Measurements and Disclosures, as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value ASC 820 must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value, which are the following:

Level 1 - Quoted prices in active markets for identical assets or liabilities.

Level 2 - Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

In accordance with ASC 820, the following table represents our fair value hierarchy for our financial assets (cash equivalents and investments) measured at fair value on a recurring basis as of March 31, 2011 and December 31, 2010 (in thousands):

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| As of March 31, 2011 | Level 1 | Level 2 | Level 3 | Total |
|-------------------------|-----------|----------|---------|----------|
| Money market funds | \$13,610 | \$— | \$— | \$13,610 |
| Corporate bonds | — | 25,259 | — | 25,259 |
| Corporate notes | — | 16,923 | — | 16,923 |
| Commercial paper | — | 3,998 | — | 3,998 |
| Treasuries | — | 6,994 | — | 6,994 |
| Auction-rate securities | — | — | 2,598 | 2,598 |
| Total | \$13,6106 | \$53,174 | \$2,598 | \$69,382 |

| As of December 31, 2010 | Level 1 | Level 2 | Level 3 | Total |
|-------------------------|----------|----------|---------|----------|
| Money market funds | \$14,221 | \$— | \$— | \$14,221 |
| Commercial paper | — | 6,990 | — | 6,990 |
| Corporate bonds | — | 22,012 | — | 22,012 |
| Corporate notes | — | 21,008 | — | 21,008 |
| Treasuries | — | 4,997 | — | 4,997 |
| Auction-rate securities | — | — | 2,667 | 2,667 |
| Total | \$14,221 | \$55,007 | \$2,667 | \$71,895 |

Level 2 securities are priced using quoted market prices for similar instruments, nonbinding market prices that are corroborated by observable market data, or discounted cash flow techniques. There have been no transfers between Level 1 and Level 2 measurements during the three months ended March 31, 2011.

Level 3 assets consist of ARS with various state student loan authorities and the ARS put option. Beginning in February 2008, all auctions for the ARS have failed. Based on the continued failure of these auctions and the underlying maturities of the securities, we continue to classify our ARS holdings as long-term assets. The fair value of the auction-rate securities as of March 31, 2011 and December 31, 2010 was estimated by management.

The following table provides a summary of changes in fair value of our Level 3 financial assets as of March 31, 2011 and 2010 (in thousands):

| | Three Months Ended March 31, 2011 Auction-Rate Securities | |
|---|--|----------|
| Beginning balance at December 31, 2010 | \$ | 2,667 |
| Transfer into Level 3 | | — |
| Total gains/(losses): | | |
| Included in interest income(expense) and other, net | | — |
| Included in other comprehensive income | | (69) |
| Ending balance at March 31, 2011 | \$ | 2,598 |
| | Three Months Ended March 31, 2010 Auction-Rate Securities | |
| Beginning balance at December 31, 2009 | \$22,655 | \$ 1,289 |

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| | | |
|---|----------|--------|
| Transfer into Level 3 | — | — |
| Sales | (300) | — |
| Total gains/(losses): | | |
| Included in interest income(expense) and other, net | 472 | (472) |
| Included in other comprehensive income | (22) | — |
| Ending balance at March 31, 2010 | \$22,805 | \$ 817 |

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Concentrations of Credit Risk

Financial instruments that potentially subject us to concentrations of credit risk consist principally of cash equivalents, investments and trade accounts receivable. Our investment portfolio consists of investment grade securities. Except for obligations of the United States government and securities issued by agencies of the United States government, we diversify our investments by limiting our holdings with any individual issuer. We are exposed to credit risks in the event of default by the issuers to the extent of the amount recorded on the balance sheet. At March 31, 2011, we held approximately \$2.6 million of AAA-rated student loan auction-rate debt securities. See the Cash, Cash Equivalents and Investments section of this Note 1 to the condensed consolidated financial statements for more information.

The credit risk in our trade accounts receivable is mitigated by our credit evaluation process and reasonably short payment terms. At March 31, 2011, Customer A, Customer B, Customer C and Customer D accounted for 32%, 28%, 11% and 12%, of our total accounts receivable, net and no other customers represented greater than 10% of our total accounts receivable, net. At December 31, 2010, Customer A, Customer B and Customer C accounted for 57%, 21% and 12%, of our total accounts receivable, net, and no other customers represented greater than 10% or over of our total accounts receivable, net.

For the three months ended March 31, 2011, Customer A and Customer B accounted for 31% and 20% of our total revenue. No other customers accounted for 10% or more of total revenue. For the three months ended March 31, 2010, Customer A accounted for 52% of our total revenue. No other customers accounted for 10% or more of total revenue.

Trade Accounts Receivable and Allowance for Doubtful Accounts

Trade accounts receivable are recorded at the invoiced amount. We perform evaluations of our customers' financial condition and generally do not require collateral. We make judgments as to our ability to collect outstanding receivables and provide allowances for a portion of receivables when collection becomes doubtful. Provisions are made based upon a specific review of all significant outstanding invoices. For those invoices not specifically provided for, provisions are recorded at differing rates, based upon the age of the receivable. In determining these percentages, we analyze our historical collection experience and current payment trends. The determination of past-due accounts is based on contractual terms. At March 31, 2011 and December 31, 2010, we had an allowance for doubtful accounts of \$18,000 and \$43,000, respectively.

Property and Equipment

Property and equipment is stated at cost, less accumulated depreciation which is determined using the straight-line method over the estimated useful lives of 2 years for computer equipment and software, 3 years for furniture and fixtures, and the shorter of the estimated useful lives or the lease term for leasehold improvements. Repairs and maintenance costs are expensed as incurred.

Business Combinations – Purchase Accounting

Under the purchase method of accounting, we allocate the purchase price of acquired companies to the tangible and intangible assets acquired and liabilities assumed based on their estimated fair values. We record the excess of purchase price over the aggregate fair values as goodwill. We engage third-party appraisal firms to assist us in determining the fair values of assets acquired and liabilities assumed. These valuations require us to make significant estimates and assumptions, especially with respect to intangible assets. Such estimates include assumptions regarding future revenue streams, market performance, customer base, and various vendor relationships. We estimate the economic lives of certain acquired assets and these lives are used to calculate depreciation and amortization

expenses. We estimate the future cash flows to be derived from such assets, and these estimates are used to determine the fair value of the assets. If any of these estimates change, depreciation or amortization expenses could be accelerated and the value of our intangible assets could be impaired.

Purchased Technology and Internal Use Software

We capitalize costs related to software that we license and incorporate into our product and service offerings or develop for internal use. In July 2009, we licensed source code for technology associated with remote computer access in the amount of \$350,000. We recorded amortization expense related to this technology of \$20,000 for the three months ended March 31, 2011. In addition, as of March 31, 2011, we are carrying \$70,000 of capitalized costs incurred in connection with the development of software for internal use. This software is not yet implemented. We will amortize this cost over the useful life of this software once it is placed into service.

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Accounting for Goodwill and Other Intangible Assets

We assess the impairment of goodwill annually or more often if events or changes in circumstances indicate that the carrying value may not be recoverable. We perform our annual impairment test on September 30 each year. An impairment loss would be recognized if the fair value of the reporting unit is less than the carrying value of the reporting unit's net assets on the date of the evaluation. The estimate of cash flow is based upon, among other things, certain assumptions about expected future operating performance and an appropriate discount rate determined by our management. Our estimates of discounted cash flows may differ from actual cash flows due to, among other things, economic conditions, changes to the business model or changes in operating performance. If our estimates were to change, our assessment of goodwill impairment could change and could result in write-downs of goodwill, which would be reflected by charges to our operating results for any period presented.

We assess the impairment of identifiable intangible assets whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss would be recognized when the sum of the future net cash flows expected to result from the use of the asset and its eventual disposition is less than its carrying amount. If our estimates regarding future cash flows derived from such assets were to change, we may record an impairment to the value of these assets. Such impairment loss would be measured as the difference between the carrying amount of the asset and its fair value.

Stock-Based Compensation

We recognize compensation expense for all stock-based payment awards, including grants of stock and options to purchase stock, made to employees and directors based on estimated fair values.

For the three months ended March 31, 2011, options to acquire 1,021,000 shares of our common stock were granted. For the three months ended March 31, 2010, options to acquire 571,000 shares of our common stock were granted. The fair value of the stock options granted to employees was estimated using the following assumptions:

| | Three Months Ended March 31, | | | |
|---|---------------------------------|---|--------|---|
| | 2011 | | 2010 | |
| Stock Option Plan: | | | | |
| Risk-free interest rate | 1.73 | % | 2.12 | % |
| Expected term (in years) | 3.58 | | 3.59 | |
| Volatility | 61.66 | % | 68.41 | % |
| Expected dividend | 0 | % | 0 | % |
| Weighted average fair value (per share) | \$2.81 | | \$1.34 | |

We recorded the following stock-based compensation expense for the three months ended March 31, 2011 and 2010:

| | Three Months Ended March 31, | |
|---|---------------------------------|-------|
| | 2011 | 2010 |
| Stock option compensation expense recognized in: | | |
| Cost of services | \$55 | \$40 |
| Research and development | 161 | 148 |
| Sales and marketing | 152 | 151 |
| General and administrative | 437 | 516 |
| Stock-based compensation expense included in total costs and expenses | \$805 | \$855 |

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The following table represents stock option activity for the three months ended March 31, 2011:

| | Number of Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term | Aggregate Intrinsic Value (in '000's) |
|--|---------------------|---------------------------------------|---|---|
| Outstanding options at December 31, 2010 | 9,586,364 | \$ 2.83 | 4.48 | \$ 35,074 |
| Granted | 1,020,650 | \$ 6.13 | | |
| Exercised | (90,998) | \$ 2.37 | | |
| Forfeited | (60,685) | \$ 3.05 | | |
| Outstanding options at the end of the period | 10,455,331 | \$ 3.15 | 4.50 | \$ 22,446 |
| Options vested and expected to vest | 10,431,375 | \$ 3.15 | 4.49 | \$ 22,410 |
| Outstanding exercisable at the end of the period | 4,327,544 | \$ 3.05 | 3.61 | \$ 9,371 |

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value that would have been received by the option holders had they all exercised their options on March 31, 2011. This amount changes based on the fair market value of our stock. During the three months ended March 31, 2011 and 2010, the aggregate intrinsic value of options exercised under our stock option plans was \$543,000 and \$42,000 respectively. Total fair value of options vested during the three months ended March 31, 2011 and 2010 was \$805,000 and \$855,000, respectively.

At March 31, 2011, there was \$8.4 million of unrecognized compensation cost related to existing options outstanding which is expected to be recognized over a weighted average period of 2.4 years.

Net Loss Per Share

Basic net loss per share is computed using our net loss and the weighted average number of common shares outstanding during the reporting period. Diluted net loss per share is computed using our net loss and the weighted average number of common shares outstanding, including the effect from the potential issuance of common stock such as stock issuable pursuant to the exercise of stock options using the treasury stock method when dilutive. For the three months ended March 31, 2011 and 2010, 2.7 million and 134,000 outstanding options were excluded from the computation of diluted net loss per share since their effect would have been anti-dilutive.

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

| | Three months ended March 31, | |
|---|---------------------------------|------------|
| | 2011 | 2010 |
| Net loss | \$(3,142) | \$(4,158) |
| Shares used in computing basic and diluted net loss per share | 48,181 | 46,470 |

Basic and diluted net loss per share

\$(0.07) \$(0.09)

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Warranties and Indemnifications

We generally provide a refund period on sales, during which refunds may be granted to consumers under certain circumstances, including our inability to resolve certain support issues. For our channel sales, the refund period varies by channel partner, but is generally between 5-10 days. For referral programs and direct transactions, the refund period is generally 5 days. For all sales channels, we recognize revenue net of refunds and cancellations during the period. Refunds and cancellations have not been material to date.

We generally agree to indemnify our customers against legal claims that our software products infringe certain third-party intellectual property rights. As of March 31, 2011, we have not been required to make any payment resulting from infringement claims asserted against our customers and have not recorded any related reserves.

Recent Accounting Pronouncements

Multiple-Deliverable Revenue Arrangements

In October 2009 the Financial Accounting Standards Board (FASB) amended the accounting standards applicable to revenue recognition for multiple-deliverable revenue arrangements that are outside the scope of industry-specific software revenue recognition guidance. This new guidance amends the criteria for allocating consideration in multiple-deliverable revenue arrangements by establishing a selling price hierarchy. The selling price used for each deliverable will be based on vendor-specific objective evidence (VSOE) if available, third-party evidence (TPE) if VSOE is not available, or estimated selling price (ESP) if neither VSOE nor TPE is available. The guidance also eliminates the use of the residual method of allocation and requires that arrangement consideration be allocated at the inception of the arrangement to all deliverables using the relative selling price method.

We adopted this guidance on a prospective basis on January 1, 2011, and therefore applied it to relevant revenue arrangements originating or materially modified on or after that date. The adoption of this guidance did not have a significant impact on our results of operations or financial position.

Note 2. Comprehensive Loss

Comprehensive net income/loss includes the impact of foreign currency translation adjustments and changes in the fair value of available-for-sale securities. The following are the components of comprehensive loss (in thousands):

| | Three months ended March 31, | |
|---|---------------------------------|------------|
| | 2011 | 2010 |
| Net loss | \$(3,142) | \$(4,158) |
| Net unrealized gain (loss) on available-for-sale securities | (74) | 21 |
| Foreign currency translation gain (loss) | (59) | 28 |
| Comprehensive loss | \$(3,275) | \$(4,109) |

The amounts noted in the table above are shown before taking into account the related income tax impact. The income tax effect allocated to each component of other comprehensive income for each of the periods presented is not significant.

Note 3. Income Taxes

As a result of the sale of our Enterprise Business to Consona in the second quarter of 2009, we are reporting all historical financial activity for that segment – including revenues, direct expenses, gain on sale, and the tax impact of the gain on the sale– as discontinued operations. The income tax provision reported in this footnote relates to the tax position of our continuing operations.

We recorded an income tax provision of \$2,000 and \$12,000 for the three months ended March 31, 2011 and 2010, respectively. The provision for income taxes is comprised of estimates of current taxes due in domestic and foreign jurisdictions. Due to the expiration of our tax holiday in India, our tax provision for the current period includes India taxes, which are partially offset by an India tax benefit. In addition, our current period provision includes a state tax provision. Due to the Company's loss position in each period presented, we did not record a federal tax provision.

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As of March 31, 2011, our deferred tax assets are fully offset by a valuation allowance except in those jurisdictions where it is determined that a valuation allowance is not required. ASC 740 provides for the recognition of deferred tax assets if realization of such assets is more likely than not. Based upon the weight of available evidence, which includes historical operating performance, reported cumulative net losses since inception and difficulty in accurately forecasting our future results, we provided a full valuation allowance against our net U.S. deferred tax assets and a full valuation allowance on certain foreign deferred tax assets. We reassess the need for our valuation allowance on a quarterly basis. If it is later determined that a portion of the valuation allowance should be reversed, it may be a benefit to the income tax provision.

Note 4. Contingencies

Tax contingencies

We are required to make periodic filings in the jurisdictions where we are deemed to have a presence for tax purposes. We have undergone audits in the past and have paid assessments arising from these audits. Our India entity was issued notices of income tax assessment pertaining to the 2004-2005, 2005-2006 and 2006-2007 fiscal years. The notices claimed that the transfer price used in our inter-company agreements with our India entity was too low, and that the rate should be increased. We believe our current transfer pricing position is more likely than not to be sustained. We believe that this will be resolved through the normal judicial appeal process used in India, and have submitted our case to the court.

We may be subject to other income tax assessments in the future. We evaluate estimated expenses that could arise from those assessments in accordance with ASC 740. We consider such factors as the degree of probability of an unfavorable outcome and the ability to make a reasonable estimate on the amount of expenses. We record the estimated liability amount for those assessments that we consider to be more likely than not in our balance sheet.

Legal contingencies

In November 2001, a class action lawsuit was filed against us, two of our former officers and certain underwriters in the United States District Court for the Southern District of New York. Similar complaints have been filed against 55 underwriters and more than 300 other companies and other individual officers and directors of those companies; the consolidated case is *In re Initial Public Offering Securities Litigation*, No. 21 MC 92 (SAS) (S.D.N.Y.). The lawsuit, which sought unspecified damages, fees and costs, alleged that our registration statement and prospectus dated July 18, 2000 for the issuance and initial public offering of 4,250,000 shares of our common stock contained material misrepresentations and/or omissions related to alleged inflated commissions received by the underwriters of the offering. On April 1, 2009, all parties entered into a Stipulation and Agreement of Settlement that would resolve all claims and dismiss the case against us and our former officers, without any payment by us or our former officers. On October 5, 2009, the court issued an order approving the settlement. Certain other parties have appealed the settlement and the appeal is pending.

We are also subject to other routine legal proceedings, as well as demands, claims and threatened litigation, that arise in the normal course of our business, potentially including assertions that we may be infringing patents or other intellectual property rights of others. We currently do not believe that the ultimate amount of liability, if any, for any pending claims of any type (alone or combined) will materially affect our financial position, results of operations or cash flows. The ultimate outcome of any litigation is uncertain, however, and unfavorable outcomes could have a material negative impact on our financial condition and operating results. Regardless of outcome, litigation can have an adverse impact on us because of defense costs, negative publicity, diversion of management resources and other factors.

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Guarantees

We have identified guarantees in accordance with ASC 450. The guidance stipulates that an entity must recognize an initial liability for the fair value, or market value, of the obligation it assumes under the guarantee at the time it issues such a guarantee, and must disclose that information in its interim and annual financial statements. We have entered into various service level agreements with our channel partners, in which we may guarantee the maintenance of certain service level thresholds. Under some circumstances, if we do not meet these thresholds, we may be liable for certain financial costs. We evaluate costs for such guarantees under the statement for accounting for contingencies, as interpreted by the guidance for guarantor's accounting and disclosure requirements for guarantees. We consider such factors as the degree of probability that we would be required to satisfy the liability associated with the guarantee and the ability to make a reasonable estimate of the resulting cost. To date, we have not incurred material costs as a result of any such obligations and have not accrued any liabilities related to such obligations in our financial statements.

Note 5. Restructuring Obligations and Other Charges

In the first quarter of 2009, we implemented a reduction in our workforce and closed certain facilities worldwide in order to reduce our ongoing cost structure. As a result, we recorded a restructuring charge of \$896,000 in the first quarter of 2009. The restructuring charge was primarily comprised of employee termination costs, professional services costs and facilities impairment costs. As of March 31, 2011, the remaining balance of the restructuring obligation was \$60,000, related to one facility in the United Kingdom, which we expect to pay through 2011.

In the third quarter of 2009, we ceased using a portion of our headquarters office in order to align our facilities usage with our current size. As a result, we impaired approximately 46% of our Redwood City facility. We recorded a restructuring charge of approximately \$1.3 million, which related to the facility impairment. As of March 31, 2010, the remaining balance on this restructuring obligation was \$463,000, which we expect to pay through 2012.

In the first quarter of 2011, we implemented a reduction in our work-from-home workforce impacting a group with a specialized skill-set. We reduced our workforce by 21 employees, or less than 1% of our agent headcount. All of the affected employees were terminated as of March 17, 2011. As a result, we recorded a restructuring charge of \$37,000 for cost of services in the first quarter of 2011. As of March 31, 2011, the remaining balance of the restructuring obligation was \$11,000, which we expect to pay through April 2011.

The following table summarizes activity associated with the restructuring and related expenses incurred as of March 31, 2011 (in thousands):

| | Severance(1) | Facilities(2) | Impairment | Total |
|---|--------------|---------------|------------|--------|
| Restructuring obligations, December 31, 2010 | \$ — | \$ 661 | \$ — | \$ 661 |
| Restructuring costs incurred in the first quarter of 2011 | 37 | — | — | 37 |
| Cash payments | (26) | (138) | — | (164) |
| Restructuring obligations, March 31, 2011 | \$ 11 | \$ 523 | \$ — | \$ 534 |

(1) Severance costs include those expenses related to severance pay and related employee benefit obligations.

(2) Facilities costs include obligations under non-cancelable leases for facilities that we will no longer occupy, as well as penalties associated with early terminations of leases and disposal of fixed assets. No sublease income has been included because subleasing is not permitted under the terms of our lease.

Note 6. Warrants

On October 25, 2010, Support.com, Inc. entered into a Support Services Agreement (the “Customer Agreement”) with Comcast Cable Communications Management, LLC (“Comcast”), under which Support.com will provide technology support services to customers of Comcast in exchange for fees. In connection with the Customer Agreement, Support.com and Comcast entered into a Warrant Agreement, under which Support.com agreed to issue to Comcast warrants to purchase up to 975,000 shares of Support.com common stock in the future in the event that Comcast meets specified sales milestones under the Customer Agreement. Each warrant, if issued, will have an exercise price per share of \$4.9498 and a term of three years from issuance. As of March 31, 2011, none of the performance milestones had been met, and therefore no warrants had been issued. Consequently, the Company has not recorded any warrant-related charges against our revenue for the period ending March 31, 2011. The warrants will be valued as they are earned, and the resulting value will be recorded as a charge against revenue in the period in which the performance milestone is met and the warrant is earned.

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

The following discussion of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and the related notes included elsewhere in this Form 10-Q and the section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2010. The following discussion includes forward-looking statements. Please see "Risk Factors" in Item 1A of this Report for important information to consider when evaluating these statements.

Overview

Support.com is a leading independent provider of online care for the digital home and small business.

Our technology services and software products help install, set up, connect, secure, repair and optimize personal computers (PCs), tablets, printers, routers, home gateways, smart phones, gaming devices, digital cameras, music players and other devices that are essential to our customers' digital lives. We offer one-time and subscription services, and licenses of our software products.

Our Personal Technology Experts® deliver our services to customers online and by telephone, leveraging our patented market-leading proprietary technology platform. They generally work from their homes rather than in brick and mortar facilities. Our software products include award-winning tools designed to address some of the most common computer problem areas, including Windows registry errors, hard disk management and computer memory optimization.

We market our services through channel partners and directly to consumers. Our channel partners include leading retail, internet service provider, software and PC/consumer electronics (CE) brands. We market our software products directly and through channel partners using "free trial" versions to encourage customers to experience the products before buying. Our sales and marketing efforts principally target North American consumers and small businesses.

Our total revenue for the first quarter of 2011 grew 32% year-over-year and 6% from the prior quarter. Revenue from services grew 36% year-over-year and decreased 2% from the prior quarter. Our programs' performance will vary depending on client-specific circumstances and the acceleration of new program launches. Revenue from software grew 24% year-over-year and 35% from the prior quarter. Software revenue growth was driven by the release of the 2011 version of ARO, our computer repair and optimization product, improvements in the toolbar we distribute with our software products, and expansion of one of our distribution channels. Gross margin for the first quarter of 2011 was 45%, an increase of five points from the prior quarter, driven by an increased percentage of software in the revenue mix. First quarter operating expenses grew 9% year-on-year, and 2% over the prior quarter's expenses.

In line with prior years, we expect Q1 services revenue to be below Q4 levels due to negative seasonality in our established retail services programs. We expect software revenue to grow in the second quarter. We believe gross margin will be at or below Q1 levels, and expect operating expenses to increase from Q1 driven by higher sales and marketing spend associated with the hiring of additional work-from-home sales agents to support growing call volumes within new programs.

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We intend the following discussion of our financial condition and results of operations to provide information that will assist in understanding our financial statements, the changes in certain key items in those financial statements from year to year, and the primary factors that accounted for those changes, as well as how certain accounting principles, policies and estimates affect our financial statements.

Critical Accounting Policies and Estimates

In preparing our financial statements, we make estimates, assumptions and judgments that can have a significant impact on our net revenue, operating income or loss and net income or loss, as well as on the value of certain assets and liabilities on our balance sheet. We believe that the estimates, assumptions and judgments involved in the accounting policies described in Management's Discussion and Analysis of Financial Condition and Results of Operations in Item 7 of our Annual Report on Form 10-K for the fiscal year ended December 31, 2010 have the greatest potential impact on our financial statements, so we consider them to be our critical accounting policies and estimates. There have been no significant changes in these critical accounting policies and estimates during the three months ending March 31, 2011.

RESULTS OF OPERATIONS

The following table sets forth the results of operations for the three months ended March 31, 2011 and 2010 expressed as a percentage of total revenue.

| | Three Months Ended March 31, | |
|--|---------------------------------|------|
| | 2011 | 2010 |
| Revenue: | | |
| Services | 70 | 68 |
| Software and other | 30 | 32 |
| Total revenue | 100 | 100 |
| Costs of revenue: | | |
| Cost of services | 52 | 56 |
| Cost of software and other | 3 | 3 |
| Total cost of revenue | 55 | 59 |
| Gross profit | 45 | 41 |
| Operating expenses: | | |
| Research and development | 11 | 14 |
| Sales and marketing | 37 | 40 |
| General and administrative | 21 | 30 |
| Amortization of intangible assets | 1 | 1 |
| Total operating expenses | 70 | 85 |
| Loss from operations | (25) | (44) |
| Interest income and other, net | 1 | 2 |
| Loss from continuing operations, before income taxes | (24) | (42) |
| Income taxes (benefit) | (0) | (0) |
| Loss from continuing operations, after income taxes | (24) | (42) |

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| | | | | |
|---|-----|----|-----|----|
| Gain from discontinued operations, after income taxes | 0 | | 0 | |
| Net loss | (24 |)% | (42 |)% |

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Three Months Ended March 31, 2011 and 2010

REVENUE

| In thousands, except percentages | Three Months Ended March 31, | | \$ Change | % | |
|----------------------------------|------------------------------------|----------|--------------|--------|--------|
| | 2011 | 2010 | | Change | Change |
| Services | \$ 9,150 | \$ 6,730 | \$ 2,420 | 36 | % |
| Software and other | 3,880 | 3,129 | 751 | 24 | % |
| Total revenue | \$ 13,030 | \$ 9,859 | \$ 3,171 | 32 | % |

Services revenue is comprised primarily of fees for technology support services, including the set-up, protection, optimization and repair of new and existing computers as well as other technology devices. We provide these services remotely, using work-from-home Personal Technology Experts who utilize our proprietary technology to deliver the services. Services revenue was \$9.2 million for the three months ended March 31, 2011 compared to \$6.7 million for the same quarter of 2010. The increase was due primarily to expansion of our existing channel partner services programs.

Software and other revenue was comprised primarily of fees for software products provided through direct consumer downloads and, to a lesser extent, through the sale of this software via channel partners. Software and other revenue was \$3.9 million for the three months ended March 31, 2011 compared to \$3.1 million for the same quarter of 2010. The increase was due to product enhancements and growth of one of our existing distribution channels, expansion in certain channel distribution partnerships, and an expansion of our direct software sales.

COSTS OF REVENUE

| In thousands, except percentages | Three Months Ended March 31, | | \$ Change | % | |
|----------------------------------|------------------------------------|----------|--------------|--------|--------|
| | 2011 | 2010 | | Change | Change |
| Cost of services | \$ 6,817 | \$ 5,484 | \$ 1,333 | 24 | % |
| Cost of software and other | 404 | 348 | 56 | 16 | % |
| Total cost of revenue | \$ 7,221 | \$ 5,832 | \$ 1,389 | 24 | % |

Cost of services. Cost of services consists primarily of salary and related expenses for our Personal Technology Experts, technology and telecommunication expenses related to the delivery of services and other employee-related expenses for our service delivery organization. Cost of services was \$6.8 million for the three months ended March 31, 2011 compared to \$5.5 million for the same quarter of 2010. The increase for 2011 as compared to 2010 reflects the increase in salary and related overhead expense as a result of growing our workforce of Personal Technology Experts to meet the increased demand for our services.

Cost of software and other. Cost of software and other fees consists primarily of third-party royalty fees for our software products. Certain of these products were developed using third-party research and development resources, and this third party receives royalty payments on sales of products it developed. Cost of software and other was \$404,000 for the three months ended March 31, 2011 compared to \$348,000 in the same quarter of 2010. The increase for 2011 over 2010 was primarily due to higher third-party royalty arrangements associated with higher

revenue.

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OPERATING EXPENSES

| In thousands, except percentages | Three Months Ended March 31, | | \$ Change | % Change | |
|----------------------------------|------------------------------------|----------|--------------|-------------|----|
| | 2011 | 2010 | | | |
| Research and development | \$ 1,448 | \$ 1,343 | \$ 105 | 8 | % |
| Sales and marketing | \$ 4,785 | \$ 3,971 | \$ 814 | 20 | % |
| General and administrative | \$ 2,786 | \$ 2,952 | \$ (166) | (6) |)% |

Research and development. Research and development expense consists primarily of compensation costs, third-party consulting expenses and related overhead costs for research and development personnel. Research and development costs are generally expensed as incurred. Research and development expense was \$1.4 million for the three months ended March 31, 2011 compared to \$1.3 million for the same quarter of 2010. The increase for 2011 as compared to 2010 resulted primarily from higher salary and related overhead expenses.

Sales and marketing. Sales and marketing expense consists primarily of compensation costs, including salaries and sales commissions, for sales, business development, account management and marketing personnel and expenses for lead generation activities and promotional activities, including public relations, advertising and marketing events. Sales and marketing expense was \$4.8 million for the three months ended March 31, 2011 compared to \$4.0 million for the same quarter of 2010. The increase for 2011 as compared to 2010 resulted primarily from an increase in advertising expense related to our software products, and to a lesser extent from increased sales and marketing personnel and related costs.

General and administrative. General and administrative expense consists primarily of compensation costs and related overhead costs for administrative personnel and professional fees for legal, accounting and other services. General and administrative expense was \$2.8 million for the three months ended March 31, 2011 compared to \$3.0 million for the same quarter of 2010. The decrease for 2011 as compared to 2010 resulted primarily from lower legal costs and certain personnel related professional services fees.

Amortization of Intangible Assets

| In thousands, except percentages | Three Months Ended March 31, | | \$ Change | % Change | |
|-----------------------------------|------------------------------------|-------|--------------|-------------|----|
| | 2011 | 2010 | | | |
| Amortization of intangible assets | \$ 83 | \$ 88 | \$ (5) | (6) |)% |

Amortization of intangible assets was \$83,000 for the three months ended March 31, 2011 compared to \$88,000 for the same quarter in 2010. The decrease from 2010 to 2011 is associated with one of the intangible assets acquired as part of the Xeriton transaction in December 2009, which was fully amortized in the fourth quarter of 2010.

INTEREST INCOME AND OTHER, NET

| | Three Months Ended March 31, | \$ | % |
|--|------------------------------------|----|---|
|--|------------------------------------|----|---|

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| In thousands, except percentages | 2011 | 2010 | Change | Change |
|----------------------------------|--------|--------|----------|--------|
| Interest and other, net | \$ 150 | \$ 186 | \$ (36) | (19)% |

The decrease in interest income and other for the three months ended March 31, 2011 was primarily due to lower interest income on our investments as a result of lower yields and lower balances in our portfolio.

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PROVISION FOR INCOME TAXES

| In thousands, except percentages | Three Months Ended March 31, | | \$ Change | % Change |
|----------------------------------|------------------------------------|-------|--------------|-------------|
| | 2011 | 2010 | | |
| Provision for income taxes | \$ 2 | \$ 12 | \$ (10) | (83)% |

The provision for income taxes is comprised of estimates of current taxes due in domestic and foreign jurisdictions. Our tax holiday in India expired during the first quarter of 2011, and therefore the current period provision includes India taxes partially offset by an India tax benefit, as well as a provision for domestic state tax. Given the Company's loss position for all periods presented, we did not record a federal tax provision.

LIQUIDITY AND CAPITAL RESOURCES

Total cash, cash equivalents and investments at March 31, 2011 was \$72.7 million. This was a \$1.5 million reduction from the balance of \$74.2 million at December 31, 2010.

Operating Activities

Net cash used in operating activities was \$1.2 million and \$1.2 million for the three months ended March 31, 2011 and 2010, respectively. Amounts included in net loss, which do not require the use of cash, primarily include the depreciation, amortization of premiums and discounts on investments, stock-based compensation expense, amortization of intangible assets, realized gain on our auction-rate securities and realized loss on our auction-rate securities put option. The sum of these items was \$1.4 million and \$1.2 million in the first quarter of 2011 and 2010, respectively. Net cash used in operating activities in the first quarter of 2011 was primarily the result of the net loss of \$3.1 million and an increase in accrued compensation of \$610,000, partially offset by non-cash items of \$1.4 million. Net cash used in operating activities in the first quarter of 2010 was primarily the result of the net loss of \$4.2 million, an increase in accrued compensation and an increase in other accrued liabilities, the largest of which was an accrual related to advertising for the software products we acquired in the Xeriton transaction in December 2009.

Investing Activities

Net cash provided by investing activities was \$1.3 million and \$1.2 million for the three months ended March 31, 2011 and 2010, respectively. Net cash provided by investing activities for the three months ended March 31, 2011 was primarily due to sales and maturities of \$18.8 million in investments offset by the purchases of \$17.5 million in investments and expenditures of \$78,000 for property and equipment. Net cash provided by investing activities for the three months ended March 31, 2010 was primarily due to sales and maturities of \$12.7 million in investments offset by the purchases of \$11.5 million in investments and expenditures of \$72,000 for property and equipment.

Financing Activities

Net cash generated by financing activities was \$216,000 for the three months ended March 31, 2011 and \$34,000 for the three months ended March 31, 2010. Net cash provided by financing activities for the three months ended March 31, 2011 and 2010 was primarily attributable to the exercise of employee stock options.

Working Capital and Capital Expenditure Requirements

At March 31, 2011, we had stockholders' equity of \$83.8 million and working capital of \$69.3 million. Our capital expenditures in the first quarter of 2011 were \$78,000. We believe that our existing cash balances will be sufficient to meet our working capital requirements, as well as our planned capital expenditures for at least the next 12 months.

If we require additional capital resources to grow our business internally or to acquire complementary technologies and businesses at any time in the future, we may seek to sell additional equity or debt securities. The sale of additional equity could result in dilution to our existing stockholders.

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We plan to continue to make investments in our business during 2011. We believe these investments are essential to creating sustainable growth in our business in the future. Because these investments will likely precede any associated revenues, we expect our working capital to decrease in the near term. Additionally, we may choose to acquire other businesses or complimentary technologies to enhance our product capabilities and such acquisitions would likely require the use of cash.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate and Market Risk

There has been significant deterioration and instability in the financial markets since 2008. This extraordinary disruption and readjustment in the financial markets exposes us to additional investment risk. The value and liquidity of the securities in which we invest could deteriorate rapidly and the issuers of such securities could be subject to credit rating downgrades. In light of the current market conditions and these additional risks, we actively monitor market conditions and developments specific to the securities and security classes in which we invest. While we believe we take prudent measures to mitigate investment related risks, such risks cannot be fully eliminated, as there are circumstances outside of our control.

The primary objective of our investment activities is to preserve principal while at the same time maximizing the income we receive from our investments without significantly increasing risk. To achieve this objective, we invest our excess cash in a variety of securities, including U.S government agency securities, ARS, corporate notes and bonds, commercial paper and money market funds meeting certain criteria. These securities are classified as available-for-sale. Consequently, our available-for-sale securities are recorded on the balance sheet at fair value with unrealized gains or losses reported as a separate component of accumulated other comprehensive income (loss). Our holdings of the securities of any one issuer, except government agencies, do not exceed 10% of our portfolio. We do not utilize derivative financial instruments to manage our interest rate risks.

As of March 31, 2011, we held \$53.8 million in investments (excluding cash and cash equivalents), which consisted primarily of government debt securities, ARS, corporate notes and bonds, and commercial paper. The weighted average interest rate of our portfolio was approximately 0.69% at March 31, 2011. A decline in interest rates over time would reduce our interest income from our investments. A decrease in interest rates of 100 basis points would cause a corresponding decrease in our annual interest income of approximately \$538,000.

At March 31, 2011 and December 31, 2010 we had investments in AAA-rated ARS with various state student loan authorities with estimated fair values of \$2.6 million and \$2.7 million, respectively. The student loans made by these authorities are substantially guaranteed by the federal government through the Federal Family Education Loan Program (FFELP). ARS are long-term floating rate bonds tied to short-term interest rates. After the initial issuance of the securities, the interest rate on the securities is reset periodically, at intervals established at the time of issuance (e.g., every seven days, twenty-eight days, thirty-five days, or every six months), based on market demand, if the auctions are successful. ARS are bought and sold in the marketplace through a competitive bidding process often referred to as a "Dutch auction." If there is insufficient interest in the securities at the time of an auction, the auction may not be completed and the ARS then pays a default interest rate. Following such a failed auction, we cannot access our funds that are invested in the corresponding ARS until a future auction of these investments is successful, new buyers express interest in purchasing these securities in between reset dates, issuers establish a different form of financing to replace these securities or final payments become due according to contractual maturities. Commencing in February 2008, conditions in the global credit markets resulted in failed auctions for all of the ARS we held. In the near term, our ability to liquidate our investments in ARS or fully recover the carrying values may be limited or not exist.

The fair value of our remaining \$2.6 million of ARS, classified as available-for-sale, was based on a discounted cash flow valuation that takes into account a number of factors including the weighted average remaining term (WART) of the underlying securities, the expected return, and the discount rate. The actual WART from servicing reports was used where available. For securities where the actual WART was not available an estimate based on other securities held was used. The expected return was calculated based on the last twelve months average for the 91 day U.S. treasury bill plus a spread. This rate is the typical default rate for ARS held by us. The discount rate was calculated using the 3-month LIBOR rate plus adjustments for the security type. Changes in any of the above estimates, especially the WART or the discount rate, could result in a material change to the fair value. At March 31, 2011, all ARS were classified as Level 3 assets. Presently we have determined the decline in value for the available-for-sale ARS to be temporary because i) we have no current intent to sell the security, and we believe that we will not be required to sell the security before the recovery of its amortized cost due to our large cash reserves; ii) through March 31, 2011 all of the securities have maintained AAA credit ratings; and iii) loans made by the issuers are backed by the federal government. We have also determined that we do not intend to sell an impaired available-for-sale security and will not be required to sell such a security before the recovery of our amortized cost basis due to its large cash reserves.

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However, if circumstances change, we may be required to record an other-than-temporary impairment charge on the available-for-sale ARS. We may similarly be required to record other-than-temporary impairment charges if the ratings on any of these securities are reduced or if any of the issuers default on their obligations. In addition to impairment charges, any of these events could cause us to lose part or all of our investment in these securities. As of March 31, 2011, we had investments in ARS with estimated fair values of \$2.6 million. Any of these events could materially affect our results of operations and our financial condition. We currently believe these securities are not significantly impaired for the reasons described above; however, it could take until the final maturity of the underlying notes (up to 30 years) to realize our investments' recorded value.

Impact of Foreign Currency Rate Changes

The functional currencies of our international operating subsidiaries are the local currencies. We translate the assets and liabilities of our foreign subsidiaries at the exchange rates in effect on the balance sheet date. We translate their income and expenses at the average rates of exchange in effect during the period. We include translation gains and losses in the stockholders' equity section of our balance sheet. We include net gains and losses resulting from foreign exchange transactions in interest income and other in our statements of operations. Since we translate foreign currencies (primarily Canadian dollars, British Pound Sterling, and Indian rupees) into U.S. dollars for financial reporting purposes, currency fluctuations may have a material impact on our financial results. We have both revenue and expenses that are denominated in foreign currencies. Foreign currency losses are generally larger than foreign currency gains. A weaker U.S. dollar environment would generally have an immaterial negative impact on our statement of operations, while a stronger U.S. dollar environment would have an immaterial positive impact on our statement of operations. The historical impact of currency fluctuations has generally been immaterial. As of March 31, 2011 we did not engage in foreign currency hedging activities.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain "disclosure controls and procedures," as such term is defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act"), that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Our disclosure controls and procedures have been designed to meet, and management believes they meet, reasonable assurance standards. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Our Chief Executive Officer and our Chief Financial Officer, after evaluating the effectiveness of our "disclosure controls and procedures" as of the end of the period covered by this quarterly report, have concluded that our disclosure controls and procedures are effective based on their evaluation of these controls and procedures required by paragraph (b) of Exchange Act Rules 13a-15 or 15d-15.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended March 31, 2011 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

See Note 4 Contingencies to the condensed consolidated financial statements in Part I, Item 1 of this Quarterly Report on Form 10-Q for a description of legal proceedings.

ITEM 1A. RISK FACTORS

This report contains forward-looking statements regarding our business and expected future performance as well as assumptions underlying or relating to such statements of expectation, all of which are “forward looking statements” within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. We are subject to many risks and uncertainties that may materially affect our business and future performance and cause those forward-looking statements to be inaccurate. Words such as “expects,” “anticipates,” “intends,” “plans,” “believes,” “forecasts,” “estimates,” “seeks,” “may result in,” “focused on,” “continue to,” and similar expressions often identify forward-looking statements. In this report, forward-looking statements include, without limitation, the following:

Our expectations and beliefs regarding future financial results, conduct and growth of our business;

Our expectations regarding channel partners and the anticipated timing and magnitude of revenue from these partners;

Our expectations regarding sales of our software products, our ability to source, develop and distribute additional software products and our efforts to market services to buyers of our software products;

Our expectations regarding our ability to deliver premium technology services efficiently and through arrangements that are profitable;

Our ability to offer subscriptions to our services in a profitable manner;

Our ability to hire, train, manage and retain Personal Technology Experts in a home-based model and to expand the breadth and flexibility of our staffing model;

Our ability to match staffing levels with service volume in a cost-effective manner;

Our beliefs and expectations regarding the introduction of new services and products, including additional software products, service offerings for devices beyond the computer and small business services;

Our beliefs and expectations regarding new business opportunities and renewals of existing relationships;

Our expectations regarding revenues, cash flows and expenses, including cost of goods sold, sales and marketing, research and development efforts, and administrative expenses;

Our assessment of seasonality, mix of revenue, and other trends for our business;

Our expectations regarding the costs and other effects of acquisition and disposition transactions;

Our expectations regarding unit volumes, pricing and other factors in the market for computers and other devices, and the effects of such factors on our business;

The assumptions underlying our Critical Accounting Policies and Estimates, including our assumptions regarding revenue recognition; assumptions used to estimate the fair value of share-based compensation; assumptions regarding the impairment of goodwill and intangible assets; and expected accounting for income taxes; and

The expected effects of the adoption of new accounting standards.

An investment in our stock involves risk, and we caution investors that forward-looking statements are only predictions based on our current expectations about future events and are not guarantees of future performance. We encourage you to read carefully all information provided in this report and in our other filings with the SEC before deciding to invest in our stock or to maintain or change your investment. Forward-looking statements are based on information as of the filing date of this report, and we undertake no obligation to publicly revise or update any forward-looking statement for any reason.

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Because forward-looking statements involve risks and uncertainties, there are important factors that may cause actual results to differ materially from our stated expectations. These factors are described below. This list does not include all risks that could affect our business, and if these or any other risks or uncertainties materialize, or if our underlying assumptions prove to be inaccurate, actual results could differ materially from past results and from our expected future results.

Our business has not been profitable and may not achieve profitability in future periods.

We have not been profitable since 2005. We intend to make significant investments in support of our business, and may continue to sustain losses in the future notwithstanding our efforts to achieve profitability. If we fail to achieve revenue growth as a result of our additional investments or if such revenue growth does not result in our achieving profitability, the market price of our common stock will likely decline. We expect to continue to consume cash until we achieve profitability. A sustained period of losses would result in an increased usage of cash to fund our operating activities and a corresponding reduction in our cash balance.

Our business has a limited operating history and is based on a relatively new business model.

Our technology-enabled services business launched in 2007 to provide services and software that help consumers and small businesses with their technology needs. Prior to 2007, we operated an enterprise software business focused on technical support, which we sold in the second quarter of 2009. We are executing a plan to grow our business by providing premium technology services and software to customers both through channel partners and directly. We may not be able to offer these services and software products successfully. Our Personal Technology Experts are generally home-based, which requires a high degree of coordination and quality control of employees working from diverse and remote locations. We are currently experiencing financial losses in our business and we may continue to use cash and incur costs to support our growth initiatives. Our investments, which typically are made in advance of revenue, may not yield increased revenue to offset these expenses. As a result of these factors, the future revenue and income potential of our business is uncertain. Any evaluation of our business and our prospects must be considered in light of these factors and the risks and uncertainties often encountered by companies in our early stage of development. Some of these risks and uncertainties relate to our ability to do the following:

Maintain our current relationships, and develop new relationships, with channel partners on acceptable terms or at all;

Reach consumers and small businesses directly in a cost-effective fashion;

Hire, train, manage and retain our home-based Personal Technology Experts and sales agents and expand the breadth and flexibility of our staffing model;

Meet anticipated growth targets;

Manage our business to provide services on an efficient basis in order to achieve profitability;

Offer subscriptions to our services in a profitable manner;

Successfully introduce new, and adapt our existing, services and products for consumers and small businesses;

Respond effectively to competition;

Execute successfully on any acquisitions we make;

Adapt to industry consolidation;

Respond to government regulations relating to our business;

Attract and retain qualified management and employees; and

Manage our expanding operations and implement and improve our operational, financial and management controls.

If we are unable to address these risks, our business, results of operations and prospects could suffer.

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Our quarterly results have in the past, and may in the future, fluctuate significantly.

Our quarterly revenue and operating results have in the past and may in the future fluctuate from quarter to quarter. As a result, we believe that quarter-to-quarter and year-to-year comparisons of our revenue and operating results may not be accurate indicators of future performance.

Several factors that have contributed or may in the future contribute to fluctuations in our operating results include:

Demand for our services and products;

Our ability to increase the efficiency and capacity of our service delivery and sales organizations;

The performance of our channel partners;

Our ability to effectively match staffing levels with service volumes on a cost-effective basis, particularly with newer partners using models, such as subscriptions, without adequate or comparable historical data for forecasting purposes;

Our reliance on a relatively small number of channel partners for a substantial portion of our revenue;

Our ability to attract and retain customers and channel partners;

Our ability to reach customers directly in a cost effective manner;

The rate of expansion of our offerings and our investments therein;

The price and mix of products and services we or our competitors offer;

Usage rates on the subscriptions we offer;

Changes in the PC/CE markets relating to unit volume, pricing and other factors and the effects of such changes on our business;

Continued instability in the global macroeconomic climate and its effect on our and our channel partners' operations;

Our ability to adapt to our customers' needs in a market space defined by frequent technological change;

Seasonal trends resulting from consumer spending patterns;

The amount and timing of operating costs and capital expenditures in our business;

Diversion of management's attention from other business concerns and disruption of our ongoing business activities as a result of acquisitions or divestitures by us;

Potential losses on investments, or other losses from financial instruments we may hold that are exposed to market risk; and

The exercise of judgment by our management in making accounting decisions in accordance with our accounting policies.

Our inability to meet future financial performance targets that we announce or that are published by research analysts could cause the market price of our common stock to decline.

From time-to-time, we provide guidance related to our future financial performance. In addition, financial analysts may publish their own expectations of our future financial performance. Because our quarterly revenue and our operating results fluctuate and are difficult to predict, future financial performance is difficult to predict. In the past, including without limitation in the second quarter of 2010, we have failed to meet our guidance and our stock price has declined. Generally, the market prices of technology companies have been extremely volatile. Stock prices of many technology companies have often fluctuated in a manner unrelated or disproportionate to the operating performance of such companies. In the past, following periods of market volatility, stockholders have often initiated securities class action litigation relating to the stock trading and price volatility of the technology company in question. Any securities litigation we may become involved in could result in our incurring substantial defense costs and diverting resources and the attention of management from our business.

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Because a small number of customers and channel partners have historically accounted for and may in future periods account for the substantial majority of our revenue, delays of specific programs or losses of certain customers could decrease our revenue substantially.

In 2009, one customer, Office Depot, accounted for the substantial majority of our total revenue after giving effect to the sale of our Enterprise business. Over the course of 2009 and 2010, the percentage of revenue attributable to Office Depot has decreased each quarter. We expect the percent of revenue attributable to Office Depot to decline further in 2011 as we continue to expand our service channel partnerships and grow our software business. Our renewed agreement with Office Depot has resulted in lower wholesale prices. It also has a limited term through March 2012, and provides for a renewal period if agreed to by the parties. This agreement might not be renewed on acceptable terms or at all. Even if the agreement continues to be renewed, however, it does not require Office Depot to conduct any minimum amount of business with us, and therefore Office Depot could decide at any time to reduce or eliminate its use of our services. Our revenue from Office Depot is expected to decline in 2011 as a result of the lower wholesale prices in the renewed agreement, unless the program expands. Our services revenue could decline significantly because of the loss or decline in activity of Office Depot or the delay or loss of a significant program by other channel partners. In 2011, we expect certain other channel partners' revenue streams to become increasingly significant to us and the failure of those partners to achieve their targets could adversely affect our business. Additionally, we may not obtain new channel partners or customers. The failure to obtain significant new channel partners or the loss or decline of any significant channel partner would have a material adverse effect on our operating results. Further risks associated with the loss or decline in a significant channel partner are detailed in "Our failure to establish and expand successful partnerships to sell our services and products would harm our operating results" below.

Our failure to establish and expand successful partnerships to sell our services and products would harm our operating results.

Our current business model requires us to establish and maintain relationships with third parties who market and sell our services and products. Failure to establish or maintain third-party relationships in our business, particularly with firms that sell our services and products, could materially and adversely affect the success of our business. We sell to numerous consumers through each of these channel partners, and therefore a delay in the launch or rollout of our services with even one of these channel partners could cause us to miss revenue or other financial targets. The process of establishing a relationship with a channel partner can be complex and time consuming, and we must pass multiple levels of review in order to be selected. If we are unable to establish a sufficient number of new channel partners on a timely basis our sales will suffer. There is also the risk that, once established, our programs with these channel partners may take longer than we expect to produce revenue or may not produce revenue at all, and the revenue produced may not be profitable if the costs of performing under the program are greater than anticipated or the program terminates early before up-front investments can be recouped. One or more of our key channel partners may also discontinue selling our services, offer them only on a limited basis or devote insufficient time and attention to promoting them to their customers. Some of our partners may prefer not to work with us if we also partner with their competitors. If any of these key channel partners merge with a competitor, all of these risks could be exacerbated. Each of these risks could reduce our sales and significantly harm our operating results.

If we fail to attract, train and manage our service delivery and sales agents in a manner that provides an adequate level of support for our customers, our reputation and financial performance could be harmed.

Our business depends in part on our ability to attract, manage and retain our Personal Technology Experts and other support personnel in order to satisfy fluctuating day-by-day demand for our services than can be materially affected by growth, seasonality, the impact of channel partner promotions and other factors. If we are unable to attract, train and manage in a cost-effective manner adequate numbers of competent Personal Technology Experts and other support

personnel to be available as service volumes vary, particularly as we seek to expand the breadth and flexibility of our staffing model, our service levels could decline, which could harm our reputation, result in financial losses under contract, cause us to lose customers and channel partners, and otherwise adversely affect our financial performance. Although our service delivery and communications infrastructure enables us to monitor and manage Personal Technology Experts remotely, because they are typically home-based and geographically dispersed we could experience difficulties meeting services levels and effectively managing the costs, performance and compliance of these Personal Technology Experts and other support personnel. Any problems we encounter in effectively attracting, managing and retaining our Personal Technology Experts and other support personnel could seriously jeopardize our service delivery operations and our financial results.

We are increasing the number of work-from-home sales agents we employ. Failure to attract, train and manage these employees in a cost effective manner could harm our reputation, result in financial losses under contract, cause us to lose customers and channel partners, and otherwise adversely affect our financial performance.

From time to time, we enter into relationships with third parties to provide on-site and other services for certain channel partners and customers. We may be less able to manage the quality of services provided by third-party service providers as directly as we would our own employees. In addition, providing these services may be more costly. We also face the risk that disruptions or delays in these third parties' communications and information technology infrastructure could cause lengthy interruptions in the availability of our services. Any of these risks could harm our operating results.

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Disruptions in our information technology and service delivery infrastructure and operations, including interruptions or delays in service from our third-party web hosting provider, could impair the delivery of our services and harm our business.

We depend on the continuing operation of our information technology and communication systems and those of our external service providers. Any damage to or failure of those systems could result in interruptions in our service, which could reduce our revenues and damage our reputation. The technology we use to serve customers is hosted at a third-party facility located in the United States, and we use a separate, independent third-party facility in the United States for emergency back-up and failover services in support of the hosted site. These two facilities are operated by unrelated publicly held companies specializing in operating such facilities, and we do not control the operation of these facilities. These facilities may experience unplanned outages and other technical difficulties in the future, and are vulnerable to damage or interruption from fires, floods, earthquakes, telecommunications and connectivity failures, power failures, and similar events. These facilities are also subject to risks from vandalism, break-ins, intrusion, and other malicious attacks. Despite substantial precautions taken, such as disaster recovery planning and back-up procedures, a natural disaster, act of terrorism or other unanticipated problem could cause a loss of information and data and lengthy interruptions in the availability of our services and hosted solutions offerings, as our backup systems may not be able to meet our needs for an extended period of time. We rely on hosted systems maintained by third-party providers to deliver technology services to consumers, including taking customer orders, handling telecommunications for customer calls, and tracking sales and service delivery. Any interruption or failure of our internal or external systems could prevent us or our service providers from accepting orders and delivering services, or cause company and consumer data to be unintentionally disclosed. Our continuing efforts to upgrade and enhance the security and reliability of our information technology and communications infrastructure could be very costly, and we may have to expend significant resources to remedy problems such as a security breach or service interruption. Interruptions in our services resulting from labor disputes, telephone or internet failures, power or service outages, natural disasters or other events, or a security breach could reduce our revenue, increase our costs, cause customers and channel partners to fail to renew or to terminate their use of our offerings, and harm our reputation and our ability to attract new customers.

Our software revenues are dependent on online traffic patterns and the availability and cost of online advertising in certain key placements.

Most of our software revenue stream is highly dependent on obtaining advertising placements in a cost-effective manner in certain key online media placements. Periodically a disruptive trend will impact the online media space, decreasing traffic and/or significantly increasing the cost of online advertising and therefore compromising our ability to purchase a desired volume and placement of advertisements at profitable rates. If such a trend were to occur, we might be unable to attract desired amounts of traffic, our costs for advertising may increase beyond our forecasts and/or our software revenues could decrease. As a result, our operating results would be negatively impacted.

We must compete successfully in the markets in which we operate or our business will suffer.

We compete in markets that are highly competitive, subject to rapid change and significantly affected by new service introductions and other market activities of industry participants. We compete with a number of companies in the market for online technology services and software products. In addition, our channel partners may develop similar offerings internally.

The markets for our services and software products are still rapidly evolving, and we may not be able to compete successfully against current and potential competitors. Our ability to expand our business will depend on our ability to maintain our technological advantage, introduce timely enhanced products to meet growing support needs, deliver on-going value to our customers and scale our business. Competition in our markets could reduce our market share or

require us to reduce the price of products and services, which could harm our business, financial condition and operating results.

The competitors in our markets for services and software can have some or all of the following comparative advantages: longer operating histories; greater economies of scale; greater financial resources; greater engineering and technical resources; greater sales and marketing resources; stronger strategic alliances and distribution channels; lower labor costs; products with different functions and feature sets; and greater brand recognition than we have. We expect new competitors to continue to enter our services market given its relatively early stage, and we expect our software market to remain competitive.

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Our future service and product offerings may not achieve market acceptance.

If we fail to develop new and enhanced versions of our services and products in a timely manner or to provide services and products that achieve rapid and broad market acceptance, we may not maintain or expand our market share. We may fail to identify new service and product opportunities for our current market or new markets that we enter in the future. In addition, our existing services and products may become obsolete if we fail to introduce new services and products that meet new customer demands or support new standards. While we are developing new services and products, there can be no assurance that they will be timely released or ever be completed, and if they are, that they will gain market acceptance or generate material revenue for us. We have limited control over factors that affect market acceptance of our services and products, including the willingness of channel partners to offer our services and products and customer preferences for competitors' services, products and delivery models. We rely in part on a third party to develop certain of our software products. If our relationship with that third party were to deteriorate, or if the third party were unable to develop innovative and saleable products, we could be forced to identify a new developer and our future revenue could suffer.

We may make acquisitions that may not prove successful.

We have made acquisitions in the past and may make additional acquisitions in the future. We may not be able to identify suitable acquisition candidates at prices we consider appropriate. If we do identify an appropriate acquisition candidate, we may not be able to successfully negotiate the terms of the acquisition. Our management may not be able to effectively implement our acquisition program and internal growth strategy simultaneously. The integration of acquisitions involves a number of risks and presents financial, managerial and operational challenges. We may have difficulty, and may incur unanticipated expenses related to, integrating management and personnel from these acquired entities with our management and personnel. Our failure to identify, consummate or integrate suitable acquisitions could adversely affect our business and results of operations. We cannot readily predict the timing, size or success of our future acquisitions. Even successful acquisitions could have the effect of reducing our cash balances. Acquisitions could involve a number of other potential risks to our business, including the following, any of which could harm our business results:

Unanticipated costs and liabilities and unforeseen accounting charges or fluctuations;

Delays and difficulties in delivery of services and products;

Failure to effectively integrate or separate management information systems, personnel, research and development, marketing, sales and support operations;

Loss of key employees;

Economic dilution to gross and operating profit;

Diversion of management's attention from other business concerns and disruption of our ongoing business;

Difficulty in maintaining controls and procedures;

Uncertainty on the part of our existing customers about our ability to operate after a transaction;

Loss of customers;

Loss of partnerships;

Declines in revenue and increases in losses;

Failure to realize the potential financial or strategic benefits of the acquisition or divestiture; and

Failure to successfully further develop the combined or remaining technology, resulting in the impairment of amounts recorded as goodwill or other intangible assets.

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Our systems collect, access, use, and store personal customer information and enable customer transactions, which poses security risks, requires us to invest significant resources to prevent or correct problems caused by security breaches, and may harm our business.

A fundamental requirement for online communications, transactions and support is the secure collection, storage and transmission of confidential information. Our systems collect and store confidential and/or personal information of our individual customers as well as our channel partners and their customers' users, including credit card information, and our employees and contractors may access and use that information in the course of providing services. In addition, we collect and retain personal information of our employees in the ordinary course of our business. We and our third-party contractors use commercially available technologies to secure this information. Despite these measures, third parties may attempt to breach the security of our data or that of our customers. In addition, errors in the storage or transmission of data could breach the security of that information. We may be liable to our customers for any breach in security and any breach could subject us to governmental or administrative proceedings or monetary penalties, damage our relationships with channel partners and harm our business and reputation. Also, computers are vulnerable to computer viruses, physical or electronic break-ins and similar disruptions, which could lead to interruptions, delays or loss of data. We may be required to expend significant capital and other resources to comply with mandatory privacy and security standards required by law, industry standard, or contract, and to further protect against security breaches or to correct problems caused by any security breach.

We are exposed to risks associated with credit card and payment fraud and with credit card processing.

Certain of our customers use credit cards to pay for our services and products. We may suffer losses as a result of orders placed with fraudulent credit cards or other payment data. Our failure to detect or control payment fraud could have an adverse effect on our results of operations. We are also subject to payment card association operating standards and requirements, as in effect from time to time. Compliance with those standards requires us to invest in network and systems infrastructure and processes. Failure to comply with these rules or requirements may subject us to fines, potential contractual liabilities, and other costs, resulting in harm to our business and results of operations.

Privacy concerns and laws or other domestic or foreign regulations may require us to incur significant costs and may reduce the effectiveness of our solutions, and our failure to comply with those laws or regulations may harm our business and cause us to lose customers.

Our software contains features that allow our Personal Technology Experts to access, control, monitor and collect information from computers running our software. Federal, state and foreign government bodies and agencies, however, have adopted or are considering adopting laws and regulations restricting or otherwise regulating the collection, use and disclosure of personal information obtained from consumers and individuals. Those regulations could require costly compliance measures, could reduce the efficiency of our operations, or could require us to modify or cease to provide our systems or services. Liability for violation of, costs of compliance with, and other burdens imposed by such laws and regulations may limit the use and adoption of our services and reduce overall demand for them. Even the perception of privacy concerns, whether or not valid, may harm our reputation and inhibit adoption of our solutions by current and future customers. In addition, we may face claims about invasion of privacy or inappropriate disclosure, use, storage, or loss of information obtained from our customers. Any imposition of liability could harm our reputation, cause us to lose customers and cause our operating results to suffer.

We rely on third-party technologies in providing certain of our services and software. Our inability to use, retain or integrate third-party technologies and relationships could delay service or software development and could harm our business.

We license technologies from third parties which are integrated into our services and software. We rely on a third party to develop certain of our software products. Our use of technologies licensed on a non-exclusive basis from third parties, including the developer of certain of our software products, poses certain risks. Some of the third-party technologies we license may be provided under “open source” licenses, which may have terms that require us to make generally available our modifications or derivative works based on such open source code. Our inability to obtain or integrate third-party technologies with our own technology could delay service development until equivalent compatible technology can be identified, licensed and integrated. These third-party technologies may not continue to be available to us on commercially reasonable terms or at all. If our relationship with third parties were to deteriorate, or if such third parties were unable to develop innovative and saleable products, we could be forced to identify a new developer and our future revenue could suffer. We may fail to successfully integrate any licensed technology into our services or software, or maintain it through our own development work, which would harm our business and operating results. Third-party licenses also expose us to increased risks that include:

Risks of product malfunction after new technology is integrated;

Risks that we may be unable to obtain or continue to obtain support, maintenance and updates from the technology supplier;

The diversion of resources from the development of our own proprietary technology;
and

Our inability to generate revenue from new technology sufficient to offset associated acquisition and maintenance costs.

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We rely upon intellectual property laws to protect our proprietary rights, and if these rights are not sufficiently protected or we are not able to obtain sufficient protection for our technology, it could harm our ability to compete and to generate revenue.

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

Laws and contractual restrictions may not adequately prevent infringement of our proprietary rights and misappropriation of our technologies or deter others from developing similar technologies; and

Policing infringement of our patents, trademarks and copyrights, misappropriation of our trade secrets, and unauthorized use of our products is difficult, expensive and time-consuming, and we may be unable to determine the existence or extent of this infringement or unauthorized use.

Intellectual property litigation is expensive and time-consuming and could divert management's attention from our business. The outcome of any litigation is uncertain and could significantly impact our financial results. Also, the laws of other countries in which we market our products may offer little or no protection of our proprietary technologies. Reverse engineering, unauthorized copying or other misappropriation of our proprietary technologies could enable third parties to benefit from our technologies without paying us for them, which would harm our competitive position and market share.

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

We may not be issued patents we may seek to protect our technology;

Competitors may independently develop similar technologies or design around any of our patents;

Patents issued to us may not be broad enough to protect our proprietary rights; and

Our issued patents could be successfully challenged.

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

Our business relies upon the use and licensing of technology. Other parties may assert intellectual property infringement claims against us or our customers, and our products may infringe the intellectual property rights of third parties. For example, our products may infringe patents issued to third parties. In addition, as is increasingly common in the technology sector, we may be confronted with the aggressive enforcement of patents by companies whose primary business activity is to acquire patents for the purpose of offensively asserting them against other companies. From time to time, we have received allegations of intellectual property infringement, and we may receive more claims in the future. We may also be required to pursue litigation to protect our intellectual property rights. Intellectual property litigation is expensive and time-consuming and could divert management's attention from our business. The outcome of any litigation is uncertain and could significantly impact our financial results. If there is a

successful claim of infringement, we may be required to develop non-infringing technology or enter into royalty or license agreements, which may not be available on acceptable terms, if at all. Our failure to develop non-infringing technologies or license proprietary rights on a timely basis would harm our business.

Changes in the market for computers and other consumer electronics could adversely affect our business.

Reductions in unit volumes of sales for computers and other devices we support, or in the prices of such equipment, could adversely affect our business. We offer both services that are attached to the sales of new computers and other devices, and services designed to fix existing computers and other devices. Declines in the unit volumes sold of these devices or declines in the pricing of such devices could adversely affect demand for our services and/or our revenue mix, either of which would harm our operating results. Further, we do not support all types of computers and devices, meaning that we must select and focus on certain operating systems and technology standards for computers, smart phones, and other devices. We may not be successful in supporting popular equipment and platforms; consumers and small businesses may trend toward use of equipment we do not support, and the process of migration away from platforms we support may decrease the market for our services and products. Any of these risks could harm our operating results.

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We have recorded long-lived assets, and our results of operations would be adversely affected if their value becomes impaired.

Goodwill and identifiable intangible assets were recorded in part due to our acquisition of substantially all of the assets and liabilities of YourTechOnline.com in May 2008 and our acquisition of substantially all of the assets of Xeriton in December 2009. We also have certain intangible assets with indefinite lives. We assess the impairment of goodwill and indefinite lived intangible assets annually or more often if events or changes in circumstances indicate that the carrying value may not be recoverable. We assess the impairment of acquired product rights and other finite lived intangible assets whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. Our results of operations would be adversely affected if impairment of our goodwill or intangible assets occurred.

ITEM 6. EXHIBITS

Exhibits.

31.1 Chief Executive Officer Section 302 Certification

31.2 Chief Financial Officer Section 302 Certification

32.1 Statement of the Chief Executive Officer under 18 U.S.C. § 1350(1)

32.2 Statement of the Chief Financial Officer under 18 U.S.C. § 1350(1)

- (1) The certifications filed as Exhibits 32.1 and 32.2 are not deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934 and are not to be incorporated by reference into any filing of the Company under the Securities Exchange Act of 1933 or the Securities Exchange Act of 1934, whether made before or after the date hereof irrespective of any general incorporation by reference language contained in any such filing, except to the extent that the registrant specifically incorporates it by reference.

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SIGNATURE

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

May 6, 2011

SUPPORT.COM, INC.

By:

/s/ Shelly Schaffer
Shelly Schaffer
Chief Financial Officer and
Executive Vice President of
Finance and
Administration

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EXHIBIT INDEX TO SUPPORT.COM, INC.

QUARTERLY REPORT ON FORM 10-Q

FOR THE QUARTER ENDED MARCH 31, 2011

| | |
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| <u>31.1</u> | Chief Executive Officer Section 302 Certification |
| <u>31.2</u> | Chief Financial Officer Section 302 Certification |
| <u>32.1</u> | Statement of the Chief Executive Officer under 18 U.S.C. § 1350(1) |
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