

ACTUATE CORP  
Form 10-K  
March 12, 2009  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

**FORM 10-K**

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

**For the fiscal year ended December 31, 2008**

**OR**

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

**For the transition period from                      to**

**Commission file number: 0-24607**

**ACTUATE CORPORATION**

**(Exact name of registrant as specified in its charter)**

**Delaware** **94-3193197**  
**(State or other jurisdiction of incorporation or organization)** **(I.R.S. Employer Identification No.)**  
**2207 Bridgepointe Parkway, Suite 500**

**San Mateo, California 94404**

**(650) 645-3000**

**(Registrant's telephone number, including area code)**

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Securities registered pursuant to Section 12(b) of the Act: None

**Title Of Each Class**  
**Common Stock, \$0.001 par value**

**Name Of Each Exchange On Which Registered**  
**Nasdaq Global Market**

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.

Yes  No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

As of June 30, 2008, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was \$180,057,490 based on the closing sale price as reported on The Nasdaq Global Market.

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

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| Class                                  | Outstanding at February 27, 2009 |
|--|----------------------------------|
| <b>Common Stock, \$0.001 par value</b> | 44,695,350                       |

**DOCUMENTS INCORPORATED BY REFERENCE**

The information called for by Part III is incorporated by reference to specified portions of the registrant's definitive Proxy Statement for its 2009 Annual Meeting of Stockholders, which is expected to be filed with the Securities and Exchange Commission not later than 120 days after the registrant's fiscal year ended December 31, 2008.

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**Annual Report on Form 10-K  
for the fiscal year ended December 31, 2008**

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**SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS**

*Some of the statements in this Annual Report on Form 10-K under Business, Risk Factors, Management's Discussion and Analysis of Financial Condition and Results of Operations, and elsewhere constitute forward-looking statements within the meaning of Section 21E of the Securities and Exchange Act of 1934, as amended. Forward-looking statements include statements regarding Actuate's expectations, beliefs or strategies regarding the future. These statements involve known and unknown risks, uncertainties, and other factors that may cause our actual results, levels of activity, performance, or achievement to be materially different from any future results, levels of activity, performance, or achievements expressed or implied by such forward-looking statements. Such factors include, among other things, those listed under Risk Factors and elsewhere in this Annual Report on Form 10-K. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance, or achievements. Moreover, neither we nor any other person assumes responsibility for the accuracy and completeness of such statements. We are under no duty to update any of the forward-looking statements contained in this Report on Form 10-K after the date hereof or to conform such statements to actual results. Readers are cautioned not to place undue reliance on forward-looking statements and should carefully review the risk factors described in other documents Actuate files from time to time with the Securities and Exchange Commission, including current reports on Form 8-K and quarterly reports on Form 10-Q filed by Actuate during 2008.*

**PART I**

**ITEM 1. BUSINESS**

**Overview**

Actuate Corporation ( We, Actuate or the Company ) was incorporated in November 1993 in the State of California and reincorporated in the State of Delaware in July 1998. Actuate provides software and services to develop and deploy Rich Internet Applications ( RIAs ) Without Limits. These RIAs deliver rich interactive content that improve customer loyalty and corporate performance. Applications built on Actuate's open source-based platform provide all stakeholders inside and outside the firewall, including employees, customers, partners and citizens, with information that they can easily access and understand to maximize revenue, cut costs, improve customer satisfaction, streamline operations, create competitive advantage and make better decisions. Our goal is to ensure that all users can use decision-making information in their day-to-day activities, opening up completely new avenues for improving corporate performance. Actuate's telephone number is 650-645-3000. Actuate maintains a Web site at [www.actuate.com](http://www.actuate.com). The information posted on our Web site is not incorporated into this Annual Report.

**Industry Background**

The emergence and acceptance of, as well as the dependence on, the Internet have fundamentally changed the way that consumers and businesses communicate, obtain information, purchase goods and transact business. Through the frequent and widespread usage of the Internet and more recently the emergence of RIAs, users have developed a new set of expectations for accessing relevant, timely and dynamic information.

While these new user expectations have been developing, organizations have been striving to improve corporate performance. A common strategy for improving performance has been to better leverage the information captured by applications that have been implemented to manage business process such as sales, marketing, service, finance, manufacturing, distribution and human resources. Organizations have been seeking

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to use the captured data to make informed decisions regarding both day-to-day operations and high-level strategies. These efforts have been largely unsuccessful due to the disruptive nature of traditional Business Intelligence tools used to access and analyze this data. Because these tools demand that users invest time and

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effort in learning new interfaces and acquiring new skills, user adoption has been low, and as a consequence, use of decision-making information throughout the organization has been limited.

In order to achieve 100% user adoption of decision-making information, and reap the resulting benefits in corporate performance, organizations are turning to developing and deploying RIAs. These applications eliminate the traditional obstacles to user adoption by providing decision-making information through intuitive, Web portal-like interfaces within a context of business processes that satisfy new user expectations for information accessibility and relevance. RIAs can also extend the usage of information outside the firewall to customers and partners.

## **The Actuate Solution**

Actuate offers a portfolio of products to develop and deploy RIAs that deliver rich interactive content. The Actuate product line assures that 100% of users inside and outside the firewall can gain value from all enterprise information assets. A variety of intuitive, personalized and easy to use RIAs present data integrated from all relevant sources. Flexible deployment options can support all projects, no matter how small or large.

**Business Intelligence and Reporting:** Actuate provides a complete suite of Business Intelligence and Reporting products that provide interactive web reports, brochure-quality reporting, business analytics, and spreadsheet reporting. These capabilities are delivered within an easy-to-use integrated RIA experience to maximize user adoption.

Our Actuate Business Intelligence and Reporting product line provides a platform upon which Global 9000 organizations (companies with annual revenues greater than \$1 billion) and packaged application software vendors develop and deploy mission-critical RIAs that deliver rich interactive content. Such applications retrieve business information from corporate databases and deliver it as interactive Web pages, Excel spreadsheets, and analytic cubes to customers, partners and employees around the globe. Our products and services are used by our customers to develop and deploy RIAs across a range of business functions including financial management, sales management, account management, and customer self-service. Actuate is a comprehensive platform that can be seamlessly integrated into any enterprise IT infrastructure and consists of a highly scalable and reliable server and a robust development environment for building RIAs that deliver rich interactive content of any scale. Actuate's powerful development and deployment architecture allows developers to create content from virtually any data source and present it in virtually any format required by users.

**Performance Management:** The Actuate Performancesoft Suite of products engages the entire organization in improving performance from Metrics Management which provides management visibility into key measures of performance, to Activity Management which helps manage the execution of day-to-day activities that drive performance, and Root Cause Analysis which enables user to make informed decisions to take action to address the problem at its root cause.

Actuate Performancesoft Views has been designed specifically to address real-life Performance Management situations. With a simple-to-use web interface, users across the enterprise can access relevant Performance Management information to help them make the right decisions. Actuate Performancesoft Track provides executive level insight into the activities that drive organizational performance and delivers true Activity Management by providing color-coded, performance-based status into all initiatives, linked to overall strategy and communicated organization-wide. Actuate Performancesoft BI greatly simplifies the dissemination and analysis of Performance Management information by offering users interactive, intuitive reports that drill directly from any measure in their Views scorecard to the operational detail that explains that measure's status. In 2008, Actuate extended the Performancesoft Views application as a Software-as-a-Service (SaaS) offering called OnPerformance. To date, revenues from this offering have not been significant.





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The combination of Actuate's Performance Management applications and its RIA-ready information platform provides capabilities for distributing accountability throughout the enterprise. Our customers are now able to quickly build and deploy rich, intuitive and easy to use Performance Management applications. These applications offer managers at all levels the ability to drill-through from executive level information to real-time operational details, resulting in heightened management effectiveness and breakthrough corporate performance throughout the enterprise.

**Actuate BIRT and e.Spreadsheet:** Actuate BIRT is based on the Eclipse Open Source Business Intelligence Reporting and Tools ( BIRT ) project, founded and co-led by Actuate. Actuate BIRT provides indemnification, supports the Actuate 10 Collaborative Reporting Architecture and can leverage all the Actuate deployment options embedded in applications or deployed in workgroups or enterprise-wide. Actuate e.Spreadsheet products are Excel-based and deliver Excel-like reporting, formatting and calculation functionality within Java applications. Actuate e.Spreadsheet products can also leverage all the Actuate deployment options embedded in applications or deployed in workgroups or enterprise-wide.

## **Strategy**

Our goal is to be the leader in delivering Rich Internet Applications Without Limits by increasing the richness, interactivity and effectiveness of enterprise information, for everyone, everywhere. Actuate delivers the next generation RIA-ready information platform for both customer and employee-facing applications. The Actuate platform boasts unmatched scalability, high-performance, reliability and security. Its proven RIA capabilities and highly collaborative development architecture are backed by the world's largest open source business application developer community, grounded in BIRT, the Eclipse Foundation's only top level Business Intelligence and reporting project. Key elements of our strategy include:

***Expand Market Leadership Position through Strategic Relationships.*** We believe that we have established a leading position in the market for RIA that delivers rich interactive content. To accelerate the adoption of the Actuate portfolio of products, we have established strategic relationships with leading software application vendors, systems integrators, consulting firms, specialized Performance Management consultants and development partners. We intend to further develop our existing strategic relationships and enter into new partnerships to expand our market presence and leadership.

***Extend Technology Leadership.*** Since inception, we have focused our research and development efforts on developing core technologies that address the requirements of developing and deploying RIAs that deliver rich interactive content in the areas of Business Intelligence and Performance Management. Our products integrate a number of advanced technologies, including a patented method of providing page level security in a report, LDAP integration, advanced viewing technology incorporating Java, PDF, DHTML, Unicode, XML, AJAX, Flash and Web services, a patented method of storing report objects, a multi-tier architecture, Web access and delivery technology, EII data access technology, patent-pending spreadsheet technology and intuitive Performance Management interfaces such as Briefing Books. In addition, we have in the past rapidly incorporated new technology into our product offerings. We believe that we provide a leading RIA-ready information platform technology and we intend to extend this leadership position by continuing to devote significant resources to research and development efforts, and by acquiring and integrating complementary technologies when and if appropriate.

***Broaden Distribution Channels.*** To date, our products have been sold worldwide by our direct sales force and through our software application vendors, original equipment manufacturers (OEMs), resellers, and systems integrators. In addition, we intend to continue to leverage and grow our existing network of OEMs, systems integrators, and resellers and expand our indirect distribution channel worldwide.

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***Focus on Key Application Areas.*** Our technology is uniquely suited to meet customer requirements for RIAs that deliver rich interactive content for specific business functions such as financial management, customer

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self-service, sales management, account management, workforce management and operational Performance Management. We intend to continue to focus on these areas within our sales and marketing functions as well as provide more complete customer solutions through targeted partnering and technology development.

***Leverage Professional Services Capabilities.*** We have established successful relationships with our customers by serving as an advisor in developing and deploying RIA. We are extending our direct Professional Services capabilities to provide an expanded set of services to address areas such as application development strategy, project management, security integration and application design. In addition, we offer similar high-quality Professional Services capabilities through third-party alliances and are currently focused on the development of relationships with global and national systems integrators. By offering our clients a full range of Professional Services on a global basis, we believe that we can broaden market awareness about the advantages of our platform and create opportunities to sell new or additional products to clients.

***International Presence.*** Outside North America, we have established subsidiaries in a number of countries and have reseller relationships throughout Europe, Middle East and Asia/Pacific region. We have localized versions of our products in French, German, Spanish, and Japanese and we also support Chinese, Korean, and right-to-left reporting. We intend to grow our international operations by expanding our indirect distribution channels worldwide and by continuing the localization of our products in selected markets. International sales accounted for 28%, 27%, and 25% of our total revenues in 2008, 2007, and 2006, respectively.

***Leverage Open Source.*** We plan to build a community of developers adopting the open source Eclipse BIRT project. We offer a number of complementary commercial products and services that build on the open source BIRT project offering and we intend to offer additional complementary commercial products and services in the future.

## **Products and Technology**

Actuate 10 is a unified software platform for developing and deploying RIAs that deliver rich interactive content. These applications can provide decision-making information with the simplicity, consistency, and relevance necessary for adoption by 100% of users, both inside and outside the firewall.

The Actuate Performancesoft Suite is a set of RIAs that helps high-performing organizations drive strategy at all levels, improve decision making, and ensure better operational performance and execution.

The Actuate product line assures that 100% of users, customers, partners and employees can get the information they need to drive prompt, effective action. Whether our customers wish to make better decisions, implement stronger customer relationships or manage to performance goals, Actuate provides a variety of intuitive, personalized and easy-to-use formats that present data integrated from all relevant sources. Our flexible deployment options and world class scalability support various types of projects, no matter how small or large.

Actuate 10 extends Eclipse BIRT (Business Intelligence and Reporting Tools) to deliver rich, highly interactive enterprise and customer-facing information applications. Organizations that want to present structured data as RIAs using BIRT as a foundation can now use the Actuate 10 value added product line to:

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Build any information rich interactive content using BIRT: including Flash-based content, dashboards and dynamic statements for any interface.

Deploy BIRT to satisfy any scope: leveraging Actuate's industry leading performance, scale, reliability and security capabilities.

Develop BIRT content efficiently: using a developer-centric design environment and open APIs to satisfy any content requirement.

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The release of Actuate 10 builds on the Company's strategy to ensure the low cost, efficient commercial deployment of RIAs by:

Lowering costs associated with application development, maintenance and deployment by tapping in to the skill sets and shared resources of a large and growing community of Eclipse developers.

Increasing developer productivity, by promoting interoperability and standards-based development to allow BIRT to fit seamlessly and effortlessly within any environment.

Meeting continuously evolving user requirements by encouraging participation across the user base from developers to everyday consumers to refine their own information presentation through a variety of interactive and engaging interfaces.

In the case of direct sales to end user customers, our products have been typically priced on a per CPU basis, a per named user basis or a mix of CPU and named user based pricing. Our development products are typically priced on a per named user basis. Indirect sales are usually either fixed price, unlimited usage arrangements, or arrangements where royalties are paid based on sell through to end-users.

| <b>Actuate Products</b>                       | <b>Product Description</b>  |
|---|---|
| Actuate iServer Enterprise                    | Scalable information server for generating, managing, and securely delivering reporting and analytic content that is adopted by 100% of an organization's users.  |
| Actuate iServer Express                       | High-end report server in a single-server, single-project configuration that provides BIRT and e.Spreadsheet reports generation and delivery to multiple users securely and on a schedule and paves the path for an easy and secure upgrade to the iServer Enterprise.        |
| Actuate BIRT Report Option                    | Enables professional application developers and report developers to build dynamic, interactive enterprise reports ready for deployment to end users and create composite report design templates for Actuate BusinessReports.  |
| Actuate BIRT Report Interactive Viewer Option | AJAX-powered interactivity that enables every type of user to think beyond the current structure of the report and personalize it into his or her own perspective. Users have the flexibility to modify report views, reducing the number of reports that need to be created. |
| Actuate Query Option                          | Web-based query tool for end-users of all levels of computing sophistication.   |
| Actuate Analytics Option                      | Server option that provides Web-based Online Analytical Processing (OLAP) capabilities to power users, business analysts, and management.   |
| Actuate Data Integration Option               | Server option licenses Information Objects deployed on the server to combine data from two or more disparate data sources.  |
| Actuate e.Report Option                       | Server option for generating enterprise reports for employees, customers, and business partners in browser-based Web formats.   |
| Actuate e.Spreadsheet Option                  | Server option for generating, managing, and distributing critical business information over the Internet in easy-to-use and intuitive desktop spreadsheets.   |
| Actuate SmartSheet Security Option            | SmartSheets cache both data and design in the iServer. When requested, SmartSheets constructs a personalized workbook for each user by dynamically assembling the workbook as requested, which allows SmartSheets to combine both cached and real-time data, at that moment.  |

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| <b>Actuate Products</b>                        | <b>Product Description</b>  |
|--|---|
| Actuate e.Analysis Option                      | Server option that delivers to users browser-based, interactive analysis of report data without requiring any configuration or warehousing of application data.   |
| Actuate Page Level Security Option             | This server option allows users to view reports using page-level security.  |
| Actuate Analytics Cube Designer                | Enables IT to control access to the data and define the structure of each cube delivered by the Actuate iServer. Additionally, enables IT to blend Analytics seamlessly into existing Enterprise Reporting applications and provide a branded, personalized end-user experience that requires almost no training.   |
| Actuate e.Report Designer Professional         | Provides a comprehensive, object-oriented environment for professional developers to create tightly integrated, highly flexible enterprise reports for any Web-enabled application.   |
| Actuate e.Report Designer                      | Wizard-driven development tool that enables Web developers to rapidly publish database information to the Web in the form of embedded, actionable reports.  |
| Actuate e.Spreadsheet Designer                 | Development environment for creating flexible and customizable Excel-based spreadsheet reports.   |
| Actuate Information Object Designer            | Development environment that enables professional developers to create controlled views of enterprise data for end-user querying. Additionally, enables the creation of Information Objects that pull and integrate real-time data from any number of heterogeneous data sources.   |
| Actuate BIRT Report Designer                   | A plug-in for the Open Source Eclipse IDE that offers an HTML page-oriented design metaphor (similar HTML editors) to build reports that are intuitive to create and integrate easily into web applications.  |
| Actuate BIRT Report Designer Professional      | A Rich Client Platform (RCP) version of Actuate BIRT Report Designer that offers a simplified interface without a need for the additional perspectives available in the standard Eclipse platform.  |
| Actuate BIRT Report Studio for iServer Express | A web-based ad-hoc report authoring tool for workgroup deployments. BIRT Report Studio for iServer Express is ideal for mid-sized Business Intelligence projects who seek the benefits of collaborative reporting in a single server environment.   |
| Actuate BIRT Report Studio for iServer         | An enterprise ad-hoc web reporting environment. BIRT Report Studio for iServer harnesses the power of the Actuate iServer for access to Information Object metadata, report storage and scheduling, and scalability. BIRT Report Studio for iServer is an integral member of the collaborative reporting architecture, allowing power users to participate in report definition and evolution alongside IT, using the Actuate BIRT Designers, and end-users with Interactive Viewing. |
| Actuate e.Spreadsheet Engine                   | Provides an API-driven component that Java developers use to embed Excel reporting functionality into projects deployed from J2EE application and Web servers.  |
| Actuate BIRT Report Engine                     | 100% pure Java tool for extracting, formatting, and delivering data from a variety of data sources including Java objects inside applications, databases, Enterprise JavaBeans, and text files.   |
| Formula One Active X component                 | Provides an API-driven, Excel-compatible spreadsheet component for building Windows applications in visual development environments such as Visual Basic and Visual C++.  |

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The Actuate Performancesoft Suite helps high-performing organizations drive strategy at all levels, improve decision making, and ensure better operational performance and execution. In 2008, Actuate extended the Performancesoft Views application as a Software-as-a-Service (SaaS) offering called OnPerformance.

The following table sets forth the products that comprise the Actuate Performancesoft Suite.

| <b>Actuate Products</b>       | <b>Product Description</b>  |
|-------------------------------|---|
| Actuate Performancesoft Views | A Performance Management application made up of three modules: Briefing Books, Performance Views and Performance Strategy Maps.   |
| Actuate Performancesoft Track | A Performance Management application that provides executive level insight into the activities that drive organizational performance.   |
| Actuate Performancesoft BI    | Gives Actuate Performancesoft users the ability to drill directly from any measure in their Views scorecard to the operational detail that explains that measure's status.  |
| Actuate OnPerformance         | Actuate OnPerformance is cost effective Software-as-a-Service (SaaS) solution that securely provides relevant Key Performance Indicators (KPIs) to managers who can positively impact performance. The easy-to-use, web-based solution provides a flexible system to address specific methodologies such as Balanced Scorecard, Malcolm Baldrige, as well as operational Performance Management initiatives. At the same time, OnPerformance helps to control the costs typically associated with traditional Corporate Performance Management deployments. |

**Eclipse Business Intelligence and Reporting Tools Project**

In August 2004, Actuate joined the Eclipse Foundation, a community committed to the implementation of a universal platform for tools integration, as strategic developer and board member. Actuate proposed a BIRT project to the Eclipse open-source community for review at the same time. The Eclipse Foundation approved the project in September 2004. Actuate is leading the development of BIRT, which culminated in the industry's first open Business Intelligence and Reporting platform in June 2005. The second version of BIRT was released in June 2006 followed by the third version in June 2007 and the fourth version of BIRT in June of 2008. The next major version of BIRT from the Eclipse Foundation is planned for June of 2009.

**Customers**

Our customers operate in a wide variety of industries, including financial services, government, health care, manufacturing, pharmaceuticals, telecommunications, high technology, utilities, automotive, education, entertainment, travel, retail and others. For additional financial information regarding our business segments see Management's Discussion and Analysis of Financial Condition and Results of Operations, and the Consolidated Financial Statements and Notes thereto that are included elsewhere in this Form 10-K.

**Sales**

We sell our software and services worldwide through two primary channels: (i) directly to corporate and government customers through our direct sales force and (ii) through indirect channel partners such as original equipment manufacturers (OEMs), systems integrators, and resellers.

*Direct Sales Organization.* Our direct sales force focuses most of its sales efforts on Global 9000 companies and public sector organizations. The direct sales process involves the generation of sales leads through Web-based marketing, direct mail, seminars and telemarketing. As part of the direct sales effort, our field sales force typically conducts demonstrations and presentations of our products to developers and managers



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at customer sites. Our telesales force conducts demonstrations via the Web and sells our products to new and existing customers over the phone. Actuate also has a group focused on qualifying prospective customers over the phone. We maintain sales offices in a number of locations throughout North America, Europe and Asia/Pacific.

*OEM Sales Organization.* A separate sales force addresses the OEM market. Our OEMs integrate our products for distribution with their applications either directly or in hosted environments. The OEM's end-user customer is licensed to use our products solely in conjunction with the OEM's application.

*Systems Integrators.* We have a business development group that focuses on establishing and maintaining relationships with systems integrators. Systems integrators typically re-market our products to their customer base as part of a software application being built for a customer. Systems integrators are offered discounts on our products and sell a full use license of the product. Our systems integrators do not provide post-sales support.

*Resellers.* Resellers are typically given the non-exclusive right to market our software in a specific territory and are offered discounts on our products. Resellers typically provide customers with some post-sales support and services.

## **Marketing**

Our marketing organization is focused on generating leads, building market awareness and promoting acceptance of our Company and our products, as well as on developing strategic marketing, technology and other relationships. We have a comprehensive marketing strategy with several key components: image, awareness and credibility building, direct marketing to both prospective and existing customers, a strong Web presence, comprehensive sales support materials as well as broad-scale marketing programs in conjunction with key partners. Our corporate marketing strategy includes online advertising, search engine optimization, public relations activities, trade shows and user group meetings. We also engage in programs to work closely with industry analysts and other influential third parties. Our direct marketing activities include extensive Web-based marketing campaigns, participation in selected trade shows and conferences and targeted ongoing direct mail and email efforts to existing and prospective customers. We also offer seminars, both in-person and over the Web, to educate prospective customers about our RIAs built with our industry leading RIA-ready information platform. Finally, we have invested in building a partner and channel marketing function to conduct cooperative marketing programs with our partners.

## **Professional Services**

Our Professional Services organization provides high value consulting services to customers developing and deploying RIAs with our products. These services include application development strategy, project management, security integration and application design. We also actively recruit and train third party consulting firms to provide consulting services for our products. Due to the critical nature of RIAs built with our industry leading RIA-ready information platform, we believe that our Professional Services group and relationships with our consulting partners play a key role in facilitating initial license sales and enabling customers to successfully develop and deploy Actuate-based applications. In addition, we offer, directly and through our network of certified training partners, classes and training programs for our products.

## **Customer Service**

We believe that providing superior customer service is critical to successfully selling and marketing our products. Our maintenance and support contracts are typically for 12 months, and may be renewed annually. Maintenance fees are typically set at either a percentage of the total license fees paid by a customer or a percentage of the list price of the underlying products. Maintenance and support contracts entitle the customer to receive software patches, updates and enhancements, when and if available. Customers purchasing maintenance

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are able to access Actuate's local support centers located in the United States, Canada, Singapore, Switzerland and the United Kingdom via email and telephone during normal business hours. We supplement our telephone support with Web-based support services, including access to cases, resolutions, online Web forums and a software patch download area. We also offer an extended maintenance plan that gives our customers access to 24x7 support and additional support services. To improve access to our explanatory materials, we provide online documentation with all of our products.

## **Research and Development**

Our research and development organization is divided into groups, typically consisting of product managers, development engineers, quality assurance engineers, technical writers and developer communications personnel. Our development process begins with requirement specification, followed by functional and technical design, and concludes with implementation. Requirements are based on the needs of customers and prospects, as well as competitive, technological and industry factors.

We have development centers located in San Mateo, California, Overland Park, Kansas, Shanghai, China and Toronto, Canada. Research and development expenses were \$22.0 million, \$21.8 million, and \$21.1 million in fiscal years 2008, 2007, and 2006, respectively. We intend to continue to invest in research and development and related activities to maintain and enhance our product lines. We believe that our future success will depend on our ability to create products that directly address our customers' needs, are of high quality, and leverage the latest technological innovations. These products must also support current and future releases of popular operating systems platforms, development languages, databases, Internet standards, and enterprise software applications. We intend to maintain and improve our current product line and to timely develop or acquire new products. Our ability to achieve future revenue growth will depend in large part on the market acceptance of our current and future products.

## **Competition**

Our market is intensely competitive and characterized by rapidly changing technology, evolving standards and new product releases by our competitors that are marketed to compete directly with our products. Our competition comes in four principal forms:

Competition from current or future Business Intelligence software vendors such as Business Objects (acquired by SAP), Cognos (acquired by IBM), Information Builders and MicroStrategy, which offer Business Intelligence, Reporting and Performance Management products;

Competition from other large software vendors such as IBM, Microsoft, Oracle and SAP, to the extent that these vendors now or in the future, include reporting functionality with their applications or databases;

Competition from the IT departments of current or potential customers that may develop scalable Business Intelligence, Performance Management and RIA products internally, which may be cheaper and more customized than the Company's products.

Competition from BIRT. The Company expects that BIRT, which is free, may in the short term cannibalize some smaller sales of its Business Intelligence and RIA products.

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Most of our current and potential competitors have significantly greater financial, technical, marketing and other resources than we do. These competitors may be able to respond more quickly to new or emerging technologies and changes in customer requirements or devote greater resources to the development, promotion and sales of their products than we may. Also, most current and potential competitors have greater name recognition and the ability to leverage a significant installed customer base. These companies have released and can continue to release competing RIAs or significantly increase the functionality of their existing reporting software products. We expect additional competition as other established and emerging companies enter the RIA market and new products and technologies are introduced.

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### **Intellectual Property Rights**

We rely primarily on a combination of copyright and trademark laws, trade secrets, confidentiality procedures and contractual provisions to protect our proprietary technology. For example, we license our software pursuant to shrink/click-wrap or signed license agreements that impose certain restrictions on licensees' ability to utilize the software. In addition, we take precautions to avoid disclosure of our intellectual property. These precautions include requiring those persons with access to our proprietary information to execute confidentiality agreements with us and by restricting access to our source code. We seek to protect our software, documentation, and other written materials under trade secret patent, copyright and trademark laws, which afford only limited protection. We also have a small number of issued and pending U.S. patents expiring at varying times ranging from 2015 to 2020. The expiration of any such patents would not have a material effect on our business.

### **Employees**

As of December 31, 2008, we had 533 full-time employees, including 160 in sales and marketing, 155 in research and development, 111 in services and support, and 107 in general and administrative functions. None of our employees are represented by a collective bargaining agreement, nor have we experienced a work stoppage. We believe our employee relations are good. We also believe that our future success will depend in large part upon our continuing ability to attract and retain highly skilled managerial, sales, marketing, customer support and research and development personnel and, in particular, executive officers.

### **Website Access to Actuate's Reports**

Our Annual Reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to section 13(a) or 15(d) of the Securities and Exchange Act of 1934, as amended, are available free of charge through our Web site at [www.actuate.com](http://www.actuate.com) as soon as reasonably practicable after they are electronically filed with, or furnished to, the Securities and Exchange Commission. Information contained in our Web site is not part of this report.

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**ITEM 1A. RISK FACTORS**

*Investors should carefully consider the following risk factors and warnings before making an investment decision. The risks described below are not the only ones facing Actuate. Additional risks that we do not yet know of or that we currently think are immaterial may also impair our business operations. If any of the following risks actually occur, our business, operating results or financial condition could be materially harmed. In such case, the trading price of our common stock could decline and you may lose all or part of your investment. Investors should also refer to the other information set forth in this Report on Form 10-K, including the financial statements and the notes thereto.*

**THE COMPANY'S OPERATING RESULTS MAY BE VOLATILE AND DIFFICULT TO PREDICT. IF IT FAILS TO MEET ITS ESTIMATES OF FUTURE OPERATING RESULTS OR IT FAILS TO MEET THE EXPECTATIONS OF PUBLIC MARKET ANALYSTS AND INVESTORS, THE MARKET PRICE OF ITS STOCK MAY DECREASE SIGNIFICANTLY.**

The susceptibility of the Company's operating results to significant fluctuations makes any prediction, including the Company's estimates of future operating results, difficult. In addition, the Company believes that period-to-period comparisons of its operating results are not necessarily meaningful and investors should not rely on them as indications of the Company's future performance. The Company's operating results have in the past varied, and may in the future vary significantly due to factors such as the following:

Demand for its products;

The size and timing of significant orders for its products;

A slowdown or a decrease in spending on information technology by its current and/or prospective customers;

Competition from products that are directly competitive with its products;

Lost revenue from introduction or market acceptance of open source products that are directly competitive with its products;

The management, performance and expansion of its international operations;

Foreign currency exchange rate fluctuations;

Customers' desire to consolidate their purchases of RIA, Performance Management and Business Intelligence software to one or a very small number of vendors from which a customer has already purchased software;

General domestic and international economic and political conditions, including war, terrorism, and the threat of war or terrorism;

Sales cycles and sales performance of its indirect channel partners;

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Changes in the way it and its competitors price their respective products and services, including maintenance and transfer fees;

Continued successful relationships and the establishment of new relationships with OEMs;

Changes in its level of operating expenses and its ability to control costs;

The outcome or publicity surrounding any pending or threatened lawsuits;

Ability to make new products and product enhancements commercially available in a timely manner;

Ability to effectively launch new or enhanced products, including the timely education of the Company's sales, marketing and consulting personnel with respect to such new or enhanced products.;

Customers delaying purchasing decisions in anticipation of new products or product enhancements;

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Budgeting cycles of its customers;

Failure to successfully manage its acquisitions;

Defects in its products and other product quality problems;

Failure to successfully meet hiring needs including for qualified professional services employees and unexpected personnel changes;

Changes in the market segments and types of customers at which it focuses its sales and marketing efforts;

Changes in perpetual licensing models to term- or subscription-based models with respect to which license revenue is not fully recognizable at the time of initial sale;

Changes in service models with respect to which consulting services are performed on a fixed-fee, rather than variable fee, basis; and

Potential impairments of Auction Rate Securities ( ARS ), goodwill, intangibles and other investments.

Because the Company's software products are typically shipped shortly after orders are received, total revenues in any quarter are substantially dependent on orders booked and shipped throughout that quarter. Furthermore, several factors may require the Company, in accordance with accounting principles generally accepted in the United States, to defer recognition of license fee revenue for a significant period of time after entering into a license agreement, including:

Whether the license agreement includes both software products that are then currently available and software products or other enhancements that are still under development;

Whether the license agreement relates entirely or partly to software products that are currently not available;

Whether the license agreement requires the performance of services that may preclude revenue recognition until successful completion of such services;

Whether the license agreement includes acceptance criteria that may preclude revenue recognition prior to customer acceptance;

Whether the license agreement includes undelivered elements (including limited terms or durations) that may preclude revenue recognition prior to customer acceptance; and

Whether the license agreement includes extended payment terms that may delay revenue recognition until the payment becomes due.



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In addition, the Company may in the future experience fluctuations in its gross and operating margins due to changes in the mix of its domestic and international revenues, changes in the mix of its direct sales and indirect sales and changes in the mix of license revenues and service revenues, as well as changes in the mix among the indirect channels through which its products are offered.

A significant portion of the Company's total revenues in any given quarter is derived from existing customers. The Company's ability to achieve future revenue growth, if any, will be substantially dependent upon its ability to increase revenues from license fees and services from existing customers, to expand its customer base and to increase the average size of its orders. To the extent that such increases do not occur in a timely manner, the Company's business, operating results and financial condition would be harmed.

The Company's expense levels and any plans for expansion are based in significant part on its expectations of future revenues and are relatively fixed in the short-term. If revenues fall below expectations and the Company is unable to respond quickly by reducing its spending, the Company's business, operating results, and financial condition could be harmed.

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The Company often implements changes to its license pricing structure for all of its products including increased prices and modified licensing parameters. If these changes are not accepted by the Company's current customers or future customers, its business, operating results, and financial condition could be harmed.

Based upon all of the factors described above, the Company has a limited ability to forecast the amount and mix of future revenues and expenses and it is likely that at some time, the Company's operating results will fall below its estimates or the expectations of public market analysts and investors. In the event that operating results are below its estimates or other expectations, the price of the Company's common stock is likely to decline.

### **THE COMPANY HAS MADE, AND MAY IN THE FUTURE MAKE, ACQUISITIONS, WHICH INVOLVE NUMEROUS RISKS.**

The Company's business is highly competitive, and as such, its growth is dependent upon market growth and its ability to enhance its existing products, introduce new products on a timely basis and expand its distribution channels and professional services organization. One of the ways the Company has addressed and will continue to address these issues is through acquisitions of other companies.

Generally, acquisitions involve numerous risks, including the following:

The benefits of the acquisition not materializing as planned or not materializing within the time periods or to the extent anticipated;

The Company's ability to manage acquired entities' people and processes that are headquartered in separate geographical locations from the Company's headquarters;

The possibility that the Company will pay more than the value it derives from the acquisition;

Difficulties in integration of the operations, technologies, and products of the acquired companies;

The assumption of certain known and unknown liabilities of the acquired companies;

Difficulties in retaining key relationships with customers, partners and suppliers of the acquired company;

The risk of diverting management's attention from normal daily operations of the business;

The Company's ability to issue new releases of the acquired company's products on existing or other platforms;

Negative impact to the Company's financial condition and results of operations and the potential write down of impaired goodwill and intangible assets resulting from combining the acquired company's financial condition and results of operations with its financial

statements;

Risks of entering markets in which the Company has no or limited direct prior experience; and

The potential loss of key employees of the acquired company.

Mergers and acquisitions of high-technology companies are inherently risky, and the Company cannot be certain that any acquisition will be successful and will not materially harm the Company's business, operating results or financial condition.

**INTELLECTUAL PROPERTY CLAIMS AGAINST THE COMPANY CAN BE COSTLY AND COULD RESULT IN THE LOSS OF SIGNIFICANT RIGHTS.**

Third parties may claim that the Company's current or future products infringe their intellectual property rights. The Company has been subject to infringement claims in the past and it expects that companies in the Business Intelligence, RIA or Performance Management software market will increasingly be subject to infringement claims as the number of products and/or competitors in its industry segment grows and the

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functionality of products in different industry segments overlaps. Any such claims, with or without merit, could be time-consuming to defend, result in significant litigation and other expenses, divert management's attention and resources, cause product shipment delays or require the Company to enter into royalty or licensing agreements. Such royalty or licensing agreements, if required, may not be available on terms acceptable to the Company or at all. A successful claim of product infringement against the Company and its failure or inability to license the infringed or similar technology could materially harm the Company's business, operating results and financial condition.

**THE COMPANY MAY NOT BE ABLE TO PROTECT ITS SOURCE CODE FROM COPYING.**

Source code, the detailed program commands for our operating systems and other software programs, is critical to our business. Although we take significant measures to protect the secrecy of large portions of our source code, unauthorized disclosure or reverse engineering of a significant portion of our source code could make it easier for third parties to compete with our products by copying functionality, which could adversely affect our revenue and operating margins.

**IF THE COMPANY FAILS TO GROW REVENUE FROM INTERNATIONAL OPERATIONS AND EXPAND ITS INTERNATIONAL OPERATIONS ITS BUSINESS WOULD BE SERIOUSLY HARMED.**

The Company's total revenues derived from sales outside North America were 28%, 27% and 25% for the fiscal years 2008, 2007 and 2006, respectively. Its ability to achieve revenue growth in the future will depend in large part on its success in increasing revenues from international sales. The Company intends to continue to invest significant resources to expand its sales and support operations outside North America and to potentially enter additional international markets. In order to expand international sales, the Company must establish additional foreign operations, expand its international channel management and support organizations, hire additional personnel, recruit additional international resellers and increase the productivity of existing international resellers. The Company intends to continue to shift its focus from direct sales to indirect sales in certain of its international markets in 2009. If it is not successful in expanding international operations in a timely and cost-effective manner, the Company's business, operating results and financial condition could be materially harmed.

**IF THE COMPANY DOES NOT SUCCESSFULLY EXPAND ITS DISTRIBUTION CHANNELS AND DEVELOP AND MAINTAIN RELATIONSHIPS WITH OEMs, ITS BUSINESS WOULD BE SERIOUSLY HARMED.**

To date, the Company has sold its products principally through its direct sales force, as well as through indirect sales channels, such as its OEMs, resellers and systems integrators. The Company's revenues from license fees resulting from sales through indirect channel partners were approximately 32%, 28%, and 37% of total revenues from license fees for fiscal years 2008, 2007 and 2006, respectively. The Company's ability to achieve significant revenue growth in the future will depend in large part on the success of its sales force in further establishing and maintaining relationships with indirect channel partners. In particular, a significant element of the Company's strategy is to embed its technology in products offered by OEMs for resale or as a hosted application to such OEMs' customers and end-users. The Company also intends to establish and expand its relationships with resellers and systems integrators so that such resellers and systems integrators will increasingly recommend its products to their clients. The Company's future success will depend on the ability of its indirect channel partners to sell and support its products. If the sales and implementation cycles of its indirect channel partners are lengthy or variable or its OEMs experience difficulties embedding its technology into their products or it fails to train the sales and customer support personnel of such indirect channel partners in a timely or effective fashion, the Company's business, operating results and financial condition would be materially harmed.

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Although the Company is currently investing, and plans to continue to invest, significant resources to expand and develop relationships with OEMs and resellers, it has at times experienced and continues to experience difficulty in establishing and maintaining these relationships. If the Company is unable to successfully expand this distribution channel and secure license agreements with additional OEMs and resellers on commercially reasonable terms, including significant up-front payments of minimum license fees, and extend existing license agreements with existing OEMs on commercially reasonable terms, the Company's operating results would be adversely affected. Any inability by the Company to maintain existing or establish new relationships with indirect channel partners, including systems integrators and resellers, or, if such efforts are successful, a failure of the Company's revenues to increase correspondingly with expenses incurred in pursuing such relationships, would materially harm the Company's business, operating results and financial condition.

### **THE COMPANY MAY NOT BE ABLE TO COMPETE SUCCESSFULLY AGAINST ITS CURRENT AND FUTURE COMPETITORS.**

The Company's market is intensely competitive and characterized by rapidly changing technology, evolving standards and product releases by the Company's competitors that are marketed to compete directly with the Company's products. The Company's competition comes in five principal forms:

Competition from current or future Business Intelligence software vendors such as Information Builders and MicroStrategy, each of which offers reporting products;

Competition from other large software vendors such as IBM, Microsoft, Oracle and SAP, to the extent they sell as separate products or include RIA and Performance Management functionality with their applications or databases;

Competition from other software vendors and software development tool vendors including providers of open-source software products that may develop scalable Business Intelligence, Performance Management and RIA products;

Competition from the IT departments of current or potential customers that may develop scalable Business Intelligence, Performance Management and RIA products internally, which may be cheaper and more customized than the Company's products; and

Competition from BIRT. The Company expects that BIRT, which is free, may in the short term cannibalize some smaller sales of its Business Intelligence and RIA products.

Most of the Company's current and potential competitors have significantly greater financial, technical, marketing and other resources than it does. These competitors may be able to respond more quickly to new or emerging technologies and changes in customer requirements or devote greater resources to the development, promotion and sales of their products than the Company. Also, most current and potential competitors have greater name recognition and the ability to leverage a significant installed customer base. These companies have released and can continue to release competing Business Intelligence, Performance Management and RIA software products or significantly increase the functionality of their existing software products, either of which could result in a loss of market share for the Company. The Company expects additional competition as other established and emerging companies enter the Business Intelligence, Performance Management and RIA software market and new products and technologies are introduced. Increased competition could result in price reductions, fewer customer orders, reduced gross margins, longer sales cycles and loss of market share, any of which would harm the Company's business, operating results and financial condition.

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Current and potential competitors may make strategic acquisitions or establish cooperative relationships among themselves or with third parties, thereby increasing their ability to address the needs of the Company's customers. Also, the Company's current or future channel partners may have established in the past, or may in the future, establish cooperative relationships with the Company's current or potential competitors, thereby limiting the Company's ability to sell its products through particular distribution channels. It is possible that new competitors or alliances among current and new competitors may emerge and rapidly gain significant market share. Such competition could reduce the Company's revenues from license fees and services from new or

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existing customers on terms favorable to us. If the Company is unable to compete successfully against current and future competitors, the Company's business, operating results and financial condition would be materially harmed.

### **IF THE MARKET FOR BUSINESS INTELLIGENCE, RIA AND PERFORMANCE MANAGEMENT SOFTWARE DOES NOT GROW AS THE COMPANY EXPECTS, ITS BUSINESS WOULD BE SERIOUSLY HARMED.**

The Company cannot be certain that the market for Business Intelligence and RIA and Performance Management software products will continue to grow or that, even if the market does grow, businesses will purchase the Company's products. If the market for Business Intelligence and RIA and Performance Management software products declines, fails to grow or grows more slowly than the Company expects, its business, operating results and financial condition would be harmed. To date, all of the Company's revenues have been derived from licenses for its Business Intelligence and RIA and software and Performance Management related products and services, and it expects this to continue for the foreseeable future. The Company has spent, and intends to continue to spend, considerable resources educating potential customers and indirect channel partners about Business Intelligence and RIA and Performance Management software and its products. However, if such expenditures do not enable its products to achieve any significant degree of market acceptance, the Company's business, operating results and financial condition would be materially harmed.

### **BECAUSE THE SALES CYCLES OF THE COMPANY'S PRODUCTS ARE LENGTHY AND VARIABLE, ITS QUARTERLY RESULTS MAY FLUCTUATE.**

The purchase of the Company's products by its end-user customers for deployment within the customer's organization typically involves a significant commitment of capital and other resources, and is therefore subject to delays that are beyond the Company's control. These delays can arise from a customer's internal procedures to approve large capital expenditures, budgetary constraints, the testing and acceptance of new technologies that affect key operations and general economic and political events. The sales cycle for initial orders and larger follow-on orders for the Company's products can be lengthy and variable. Additionally, sales cycles for sales of the Company's products to OEMs tend to be longer, ranging from 6 to 24 months or more, and may involve convincing the OEMs' entire organization that the Company's products are the appropriate software for their applications. This time period does not include the sales and implementation cycles of such OEMs' own products, which can be longer than the Company's sales and implementation cycles. Certain of the Company's customers have in the past, or may in the future, experience difficulty completing the initial implementation of Actuate's products. Any difficulties or delays in the initial implementation by the Company's end-user customers or indirect channel partners could cause such customers or partners to reject the Company's software or lead to the delay or non-receipt of future orders for the large-scale deployment of its products, in which case the Company's business, operating results and financial condition would be materially harmed.

### **ADVANCES IN HARDWARE AND SOFTWARE TECHNOLOGY MAY CAUSE OUR SOFTWARE REVENUE TO DECLINE.**

In the past, the Company has licensed software for a certain number of processors or CPUs to many of its customers. Advances in hardware technology, including, but not limited to, greater CPU clock speeds, multiple-core processors and virtualization, have afforded software performance gains to some customers, causing them to defer additional software purchases from the Company. The occurrence of any of these events, and other future advances, could seriously harm the Company's business, operating results and financial condition. Use of the Company's software on more advanced hardware than the hardware on which the software was originally installed, without payment of a transfer fee, is prohibited by the terms of applicable license agreements or Company policies. The Company intends to require compliance with such terms. As a result of its enforcement efforts, customers may defer or cease purchasing additional software or maintenance and support. The occurrence of any of these events could materially harm the Company's business, operating results and financial condition.





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**IF THE COMPANY IS UNABLE TO FAVORABLY ASSESS THE EFFECTIVENESS OF ITS INTERNAL CONTROL OVER FINANCIAL REPORTING IN FUTURE PERIODS OR IF THE COMPANY'S INDEPENDENT AUDITORS ARE UNABLE TO PROVIDE AN UNQUALIFIED ATTESTATION REPORT ON SUCH ASSESSMENT, THE COMPANY'S STOCK PRICE COULD BE ADVERSELY AFFECTED.**

Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, as amended (Section 404), the Company's management is required to report on, and its independent auditors are required to attest to, the effectiveness of the Company's internal controls over financial reporting on an ongoing basis. The Company's assessment, testing and evaluation of the design and operating effectiveness of its internal control over financial reporting are ongoing. Management assessed the effectiveness of its internal control over financial reporting as of December 31, 2007, and this assessment identified a material weakness in the Company's internal control over financial reporting related to its income tax provision. Specifically, the Company did not maintain effective controls over the review of the income tax provision calculation by someone other than the preparer. During the fiscal year 2008, the Company modified its internal control over financial reporting with respect to accounting for income taxes. The Company used a third-party tax service provider to complete the preparation, reconciliation and analysis of its income tax provision and income tax related accounts and modified its review procedures over schedules, supporting the Company's income tax provision. As a result of these actions, management has concluded that the Company has remediated the material weakness as of the end of the period covered by this report. The Company cannot predict the outcome of its testing in future periods. If in future periods the Company concludes that its internal control over financial reporting is not effective, it may be required to change its internal control over financial reporting to remediate deficiencies, and investors may lose confidence in the reliability of its financial statements, causing the Company's stock price to decline significantly.

**SECTION 404 AND REGULATORY CHANGES HAVE CAUSED THE COMPANY TO INCUR INCREASED COSTS AND OPERATING EXPENSES, INCLUDING ADDITIONAL COST AND EXPENSES ASSOCIATED WITH HIRING QUALIFIED PERSONNEL TO COMPLY WITH SUCH REGULATORY REQUIREMENT.**

The Sarbanes-Oxley Act of 2002 and regulatory changes by the SEC and Nasdaq have caused the Company to incur significant increased costs. In particular, the rules governing the standards that must be met for management to assess its internal controls over financial reporting under Section 404 are complex, and require significant documentation, testing and possible remediation. This ongoing process of reviewing, documenting and testing the Company's internal controls over financial reporting has resulted in, and will likely continue to result in ongoing cost to the Company. Furthermore, achieving and maintaining compliance with Sarbanes-Oxley and other new rules and regulations has and will continue to require the Company to hire additional personnel and to use additional outside legal, accounting and advisory services.

In addition, any acquisitions made by the Company will also put a significant strain on its management, information systems and resources. Any expansion of the Company's international operations will lead to increased financial and administrative demands associated with managing its international operations and managing an increasing number of relationships with foreign partners and customers and expanded treasury functions to manage foreign currency risks, all of which will require the Company to incur additional cost to implement necessary changes to maintain effective internal controls over financial reporting.

**IF THE COMPANY DOES NOT RESPOND TO RAPID TECHNOLOGICAL CHANGES, ITS PRODUCTS COULD BECOME OBSOLETE.**

The market for the Company's products is characterized by rapid technological changes, frequent new product introductions and enhancements, changing customer demands, and evolving industry standards. Any of these factors can render existing products obsolete and unmarketable. The Company believes that its future success will depend in large part on its ability to support current and future releases of popular operating systems



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and computer programming languages, databases and software applications, to timely develop new products that achieve market acceptance and to meet an expanding range of customer requirements. If the announcement or introduction of new products by the Company or its competitors or any change in industry standards causes customers to defer or cancel purchases of existing products, the Company's business, operating results and financial condition would be harmed.

As a result of the complexities inherent in Business Intelligence, RIA and Performance Management software, major new products and product enhancements can require long development and testing periods. In addition, customers may delay their purchasing decisions in anticipation of the general availability of new or enhanced versions of the Company's products. As a result, significant delays in the general availability of such new releases or significant problems in the installation or implementation of such new releases could harm the Company's business, operating results and financial condition. If the Company fails to successfully develop, on a timely and cost effective basis, product enhancements or new products that respond to technological change, evolving industry standards or customer requirements or such new products and product enhancements fail to achieve market acceptance, the Company's business, operating results and financial condition would be harmed.

**IF THE COMPANY DOES NOT RELEASE NEW PRODUCTS AND ENHANCEMENTS TO EXISTING PRODUCTS IN A TIMELY MANNER OR IF SUCH NEW PRODUCTS AND ENHANCEMENTS, INCLUDING THE COMPANY'S OPEN SOURCE PROJECT, FAIL TO ACHIEVE MARKET ACCEPTANCE, THE COMPANY'S BUSINESS COULD BE SERIOUSLY HARMED.**

The Company believes that its future success will depend in large part on the success of new products and enhancements to its products that it makes generally available. Prior to the release of any new products or enhancements, the products must undergo a long development and testing period. To date, the development and testing of new products and enhancements have taken longer than expected. In the event the development and testing of new products and enhancements continue to take longer than expected, the release of new products and enhancements will be delayed. If the Company fails to release new products and enhancements in a timely manner, its business, operating results and financial condition would be harmed. In addition, if such new products and enhancements do not achieve market acceptance, the Company's business, operating results and financial condition would be harmed.

The Company has developed a BIRT open source product through its involvement in the Eclipse Foundation. The Company hopes that BIRT and a commercialized version of BIRT will be widely adopted by Java developers and will result in such developers recommending to their employees and customers that they license the Company's commercially available products. If BIRT does not achieve market acceptance and result in promoting sales of commercially available products, the Company's business, operating results and financial condition may be harmed.

**THE SUCCESS OF THE COMPANY'S OPEN-SOURCE BIRT INITIATIVE IS DEPENDENT ON BUILDING A DEVELOPER COMMUNITY AROUND BIRT.**

The success of the Company's BIRT initiative is dependent on the open source contributions of third-party programmers and corporations, and if they cease to make these contributions to the Eclipse open source project, the BIRT project, or the general open source movement, the Company's BIRT product strategy could be adversely affected. If key members, or a significant percentage, of this group of developers or corporations decides to cease development of Eclipse, BIRT or other open source applications, the Company would have to either rely on another party (or parties) to develop these technologies, develop them itself or adapt its open source product strategy accordingly. This could increase the Company's development expenses, delay its product releases and upgrades or adversely impact customer acceptance of open source offerings.

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**THE COMPANY'S INTERNATIONAL OPERATIONS ARE SUBJECT TO SIGNIFICANT RISKS.**

A substantial portion of the Company's revenues is derived from international sales. International operations and sales are subject to a number of risks, any of which could harm the Company's business, operating results and financial conditions. These risks include the following:

Economic and political instability, including war and terrorism or the threat of war and terrorism;

Difficulty of managing an organization spread across many countries;

Multiple and conflicting tax laws and regulations;

Costs of localizing products for foreign countries;

Difficulty in hiring employees and difficulties and high costs associated with terminating employees and restructuring operations in foreign countries;

Trade laws and business practices favoring local competition;

Dependence on local vendors;

Increasing dependence on resellers in certain geographies;

Compliance with multiple, conflicting and changing government laws and regulations;

Weaker intellectual property protection in foreign countries and potential loss of proprietary information due to piracy or misappropriation;

Longer sales cycles;

Import and export restrictions and tariffs;

Difficulties in staffing and managing foreign operations;

The significant presence of some of our competitors in certain international markets;

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Greater difficulty or delay in accounts receivable collection; and

Foreign currency exchange rate fluctuations.

The Company believes that, over time, an increasing portion of its revenues and costs will be denominated in foreign currencies. To the extent such denomination in foreign currencies does occur, gains and losses on the conversion to U.S. dollars of accounts receivable, accounts payable and other monetary assets and liabilities arising from international operations may contribute to fluctuations in the Company's results of operations. Although the Company may in the future decide to undertake foreign exchange hedging transactions to cover a portion of its foreign currency transaction exposure, it currently does not attempt to cover any foreign currency exposure. If it is not effective in any future foreign exchange hedging transactions in which it engages, the Company's business, operating results and financial condition could be materially harmed.

### **THE COMPANY'S EXECUTIVE OFFICERS AND CERTAIN KEY PERSONNEL ARE CRITICAL TO ITS BUSINESS AND IT MAY NOT BE ABLE TO RECRUIT AND RETAIN THE PERSONNEL IT NEEDS.**

The Company's future success depends upon the continued service of its executive officers and other key engineering, sales, marketing and customer support personnel. None of its officers or key employees is bound by an employment agreement for any specific term. If the Company loses the service of one or more of its key employees, or if one or more of its executive officers or key employees decide to join a competitor or otherwise compete directly or indirectly with it, it could have a significant adverse effect on the Company's business.

In addition, because experienced personnel in the Company's industry are in high demand and competition for their talents is intense, the Company has relied on its ability to grant stock options as one mechanism for

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recruiting and retaining this highly skilled talent. Accounting standards require the expensing of stock options, which impairs the Company's ability to provide these incentives without incurring significant compensation costs. There can be no assurance that the Company will continue to successfully attract and retain key personnel in the future.

**CHANGES IN OR INTERPRETATIONS OF, ACCOUNTING STANDARDS COULD RESULT IN UNFAVORABLE ACCOUNTING CHARGES.**

The Company prepares its Consolidated Financial Statements in conformity with accounting principles generally accepted in the United States of America. These principles are subject to interpretation by the SEC and various bodies formed to interpret and create appropriate accounting standards. The Company's accounting policies that recently have been or may be affected by changes in the accounting rules are as follows:

Software revenue recognition;

Accounting for income taxes;

Accounting for business combinations and related goodwill;

Accounting for stock issued to employees; and

Assessing fair value of financial and non-financial assets.

A change in accounting standards applicable to us can have a significant effect on the Company's reported results and may even retroactively affect previously reported transactions.

**THE COMPANY MAY BE UNABLE TO SUSTAIN OR INCREASE ITS PROFITABILITY.**

While the Company was profitable in its last five fiscal years, it incurred net losses during fiscal year 2003 and 2002. Its ability to sustain or increase profitability on a quarterly or annual basis will be affected by changes in its business. It expects its operating expenses to increase as its business grows, and it anticipates that it will make investments in its business. Therefore, the Company's results of operations will be harmed if its revenues do not increase at a rate equal to or greater than increases in its expenses or are insufficient for it to sustain profitability.

**IF THE COMPANY OVERESTIMATES REVENUES, IT MAY BE UNABLE TO REDUCE ITS EXPENSES TO AVOID OR MINIMIZE A NEGATIVE IMPACT ON ITS RESULTS OF OPERATIONS.**

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The Company's revenues are difficult to forecast and are likely to fluctuate significantly from period to period. The Company bases its operating expense budgets on expected revenue trends. The Company's estimates of sales trends may not correlate with actual revenues in a particular quarter or over a longer period of time. Variations in the rate and timing of conversion of the Company's sales prospects into actual licensing revenues could cause it to plan or budget inaccurately and those variations could adversely affect the Company's financial results. In particular, delays, reductions in amount or cancellation of customers' purchases would adversely affect the overall level and timing of the Company's revenues and its business, results of operations and financial condition could be harmed. In addition, many of its expenses, such as office and equipment leases and certain personnel costs, are relatively fixed. It may be unable to adjust spending quickly enough to offset any unexpected revenue shortfall. Accordingly, any shortfall in revenue may cause a material variation in operating results in any period.

### **IF THE COMPANY'S PRODUCTS CONTAIN MATERIAL DEFECTS, ITS REVENUES MAY DECLINE.**

Software products as complex as those offered by the Company often contain errors or defects, particularly when first introduced, when new versions or enhancements are released and when configured to individual

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customer computing systems. The Company currently has known errors and defects in its products. Despite testing conducted by the Company, if additional defects and errors are found in current versions, new versions or enhancements of its products after commencement of commercial shipment, or if such errors or defects cannot be cured or repaired timely, it could result in the loss of revenues or a delay in market acceptance or an increase in the rate of return of the Company's products. The occurrence of any of these events could materially harm the Company's business, operating results and financial condition.

### **THE COMPANY MAY BE SUBJECT TO PRODUCT LIABILITY CLAIMS.**

Although license agreements with its customers typically contain provisions designed to limit the Company's exposure to potential product liability claims, it is possible that such limitation of liability provisions may not be effective as a result of existing or future laws or unfavorable judicial decisions. The sale and support of the Company's products may entail the risk of such claims, which are likely to be substantial in light of the use of its products in business-critical applications. A product liability claim brought against the Company could materially harm its business, operating results and financial condition.

### **THE PROTECTION OF OUR PROPRIETARY RIGHTS MAY BE INADEQUATE.**

The Company has a small number of issued and pending U.S. patents expiring at varying times ranging from 2015 to 2020. The Company relies primarily on a combination of copyright and trademark laws, trade secrets, confidentiality procedures and contractual provisions to protect its proprietary technology. For example, the Company licenses its software pursuant to click-wrap or signed license agreements that impose certain restrictions on licensees' ability to utilize the software. In addition, the Company seeks to avoid disclosure of its intellectual property, including by requiring those persons with access to its proprietary information to execute confidentiality agreements with the Company and by restricting access to its source code. The Company takes precautions to protect our software, certain documentation, and other written materials under trade secret and copyright laws, which afford only limited protection.

Despite the Company's efforts to protect its proprietary rights, unauthorized parties may attempt to copy aspects of its products or to obtain and use information that the Company regards as proprietary. Policing unauthorized use of the Company's products is difficult, and while it is unable to determine the extent to which piracy of its software products exists, software piracy can be expected to be a persistent problem. In addition, the laws of many countries do not protect the Company's proprietary rights to as great an extent as do the laws of the United States. If the Company's means of protecting its proprietary rights is not adequate or its competitors independently develop similar technology, the Company's business could be materially harmed.

### **THE COMPANY'S COMMON STOCK PRICE MAY BE VOLATILE, WHICH COULD RESULT IN SUBSTANTIAL LOSSES FOR STOCKHOLDERS.**

The market price of shares of the Company's common stock has been and is likely to continue to be highly volatile and may be significantly affected by factors such as the following:

Actual or anticipated fluctuations in its operating results;



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Changes in the economic and political conditions in the United States and abroad;

Terrorist attacks, war or the threat of terrorist attacks and war;

The announcement of mergers or acquisitions by the Company or its competitors;

Developments in ongoing or threatened litigation;

Announcements of technological innovations;

Failure to comply with the requirements of Section 404 of the Sarbanes-Oxley Act;

New products, including open source products, or new contracts announced by it or its competitors;

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Developments with respect to copyrights or proprietary rights;

Price and volume fluctuations in the stock market;

Changes in corporate purchasing of Business Intelligence, RIA and Performance Management software;

Adoption of new accounting standards affecting the software industry; and

Changes in financial estimates by securities analysts.

In addition, following periods of volatility in the market price of a particular company's securities, securities class action litigation has often been brought against such companies. If the Company is involved in such litigation, it could result in substantial costs and a diversion of management's attention and resources and could materially harm the Company's business, operating results and financial condition.

**CHANGES IN TAX RATES OR NEGATIVE TAX RULINGS COULD ADVERSELY IMPACT THE COMPANY'S FINANCIAL RESULTS.**

The Company is taxable principally in the United States and certain jurisdictions in Europe and Asia/Pacific. All of these jurisdictions have in the past and may in the future make changes to their corporate income tax rates and other income tax laws, which could increase the Company's future income tax provision. While the Company believes that all material income tax liabilities are reflected properly in its Consolidated Balance Sheet, it has no assurance that it will prevail in all cases in the event the taxing authorities disagree with its interpretations of the tax law. Future levels of research and development spending, and employment of a required minimum of employees in Switzerland, will impact the Company's entitlement to related tax credits, which generally lower its effective income tax rate. Future effective income tax rates could be adversely affected if earnings are lower than anticipated in jurisdictions where the Company has statutory tax rates lower than in the United States.

**CERTAIN OF THE COMPANY'S CHARTER PROVISIONS AND DELAWARE LAW MAY PREVENT OR DETER A CHANGE IN CONTROL OF ACTUATE.**

The Company's Certificate of Incorporation, as amended and restated (the "Certificate of Incorporation"), and Bylaws, as amended and restated ("Bylaws"), contain certain provisions that may have the effect of discouraging, delaying or preventing a change in control of the Company or unsolicited acquisition proposals that a stockholder might consider favorable, including provisions authorizing the issuance of blank check preferred stock, eliminating the ability of stockholder to act by written consent and requiring stockholders to provide advance notice for proposals and nomination of directors at stockholder meetings. In addition, certain provisions of Delaware law and the Company's stock option plans may also have the effect of discouraging, delaying or preventing a change in control or unsolicited acquisition proposals. The anti-takeover effect of these provisions may also have an adverse effect on the public trading price of the Company's common stock.

**DEPENDENCE ON THE FINANCIAL SERVICES INDUSTRY COULD SIGNIFICANTLY AFFECT THE COMPANY'S REVENUES.**

A significant portion of the Company's revenues are derived from customers in the financial services industry and the Company expects it will continue to derive a significant portion of its revenues from these customers for the foreseeable future. Accordingly, unfavorable economic conditions adversely impacting the financial services industry has had a material adverse effect on the Company's business, financial condition and results of operations. For example, the financial services industry has experienced and may continue to experience cyclical fluctuations in profitability, which may affect timing of, or actual purchases of, the Company's products which would have a material adverse effect on the Company's business, financial condition and results of operations.

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**IF THE RECENT CREDIT MARKET CONDITIONS CONTINUE OR DETORiate FURTHER, IT COULD HAVE A MATERIAL ADVERSE IMPACT ON OUR INVESTMENT PORTFOLIO.**

Recent U.S. sub-prime mortgage defaults have had a significant impact across various sectors of the financial markets, causing global credit and liquidity issues. The short-term funding markets experienced credit issues throughout fiscal year 2008. This led to liquidity disruption in asset-backed commercial paper and failed auctions in the auction rate market. If the global credit market continues to deteriorate, our investment portfolio may be impacted and we could determine that some of our investments are other than temporarily impaired. This could have a material adverse impact on our results of operations and financial condition.

Our investment portfolio includes Auction Rate Securities ( ARS ) which are investments with contractual maturities. They are usually found in the form of municipal bonds, a pool of student loans or collateralized debt obligations whose interest rates are subject to reset through an auction process. At the end of each reset period, investors can sell or continue to hold the securities at par. The ARS held by us are primarily backed by highly rated municipal issuers. As of December 31, 2008, we had \$16.4 million invested in ARS which included a realized loss of approximately \$84,000 related to the difference between the gains recognized on the Put Option and the realized loss on the \$16.5 million (par value) portion of our ARS portfolio.

All ARS are classified as long-term investments at December 31, 2008 regardless of the underlying reset date. The ARS are investments with long-term contractual maturities. These ARS investments are intended to provide liquidity via an auction process that resets the applicable interest rate at predetermined calendar intervals, allowing investors to either roll over their holdings or gain immediate liquidity by selling such interests at par. The recent uncertainties in the credit markets have affected all of the Company s holdings in ARS investments and auctions for the Company s investments in these securities have failed to settle on their respective settlement dates.

In November 2008, we elected to participate in a rights offering by UBS AG ( UBS ), our investment broker, which provides us with rights (the Put Option ) to sell UBS \$16.5 million of our ARS portfolio at par value, at any time during a two-year sale period beginning June 30, 2010. By electing to participate in the rights offering, we granted UBS the right, exercisable at any time prior to June 30, 2010 or during the two-year sale period, to purchase or cause the sale of our ARS (the Call Right ). UBS has stated that it will only exercise the Call Right for the purpose of restructurings, dispositions or other solutions that will provide their clients with par value for their ARS.

The ARS investments are not currently liquid and the Company will not be able to access these funds until a future auction of these investments is successful, we exercise the Put Option , or a buyer is found outside of the auction process. All of the ARS investments were investment grade quality and were in compliance with the Company s investment policy at the time of acquisition. The Company currently has the ability and intends to hold these ARS investments until a recovery of the auction process, until we exercise the Put Option, or until maturity.

If we need to access the funds associated with ARS but are unable to do so, our operations and financial position could be materially harmed.

**WE HAVE SUBSTANTIAL INDEBTNESS AND DEBT SERVICE REQUIREMENTS.**

On November 2, 2008, Actuate entered into a four year revolving line of Credit Agreement with Wells Fargo Foothill, LLC ( Wells Fargo ) as the arranger, administrative agent and lender (the Credit Agreement ). The Credit Agreement was effective as of November 3, 2008. The Company used \$30.0 million of the proceeds from the Credit Agreement in the tender offer it completed in December 2008 and for working

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capital, issuance of commercial and standby letters of credit, capital expenditures and other general corporate purposes. At December 31, 2008, our outstanding debt under the Credit Agreement was approximately \$30 million.

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The Credit Agreement allows for cash borrowings and letters of credit under a secured revolving credit facility of up to a maximum of \$50.0 million, but in any event not to exceed 80% of the Company's Trailing Recurring Revenue (as defined in the Credit Agreement). Interest will accrue based on a floating rate based on, at the Company's election, (i) LIBOR or (ii) the greater of (a) the Federal Funds Rate plus an applicable margin or (b) Wells Fargo's prime rate, in each case, plus an applicable margin based on the outstanding balance of the amount drawn down under the Credit Agreement. If the Company's borrowings and letter of credit usage plus any bank product reserves established by Wells Fargo exceeds 80% of its Trailing Recurring Revenue (as defined in the Credit Agreement), or if the sum of available funds under the Credit Agreement plus Qualified Cash (as defined in the Credit Agreement) is less than \$10,000,000, the Company will be required to meet certain EBITDA targets and be subject to a limit on annual capital expenditures, subject to a cure mechanism described in the Credit Agreement. The Company is required to make interest payments and pay an unused commitment fee on a monthly basis. The Credit Agreement includes limitations on the Company's ability to incur debt, grant liens, make acquisitions, make certain restricted payments such as dividend payments, and dispose of assets. The events of default under the Credit Agreement include payment defaults, cross defaults with certain other indebtedness, breaches of covenants and bankruptcy events. In the case of a continuing event of default, the lenders under the Credit Agreement may, among other remedies, eliminate their commitments to make credit available, declare due all unpaid principal amounts outstanding, and require cash collateral for any letter of credit obligations and foreclose on all collateral.

Because of our indebtedness, a significant portion of our cash flow from operations is and will be required for debt service. Our levels of debt could have negative consequences for us. You should note that:

a substantial portion of our cash flow is, and will be, dedicated to debt service and is not, and will not be, available for other purposes;

our ability to obtain additional financing for working capital, capital expenditures, acquisitions and general corporate or other purposes may be impaired in the future;

certain of our borrowings are, and will be, at variable rates of interest, which may expose us to the risk of increases in interest rates; and

our level of indebtedness could make us more vulnerable to economic downturns, limit our ability to withstand competitive pressures and reduce our flexibility in responding to changing business and economic conditions.

We believe that cash flows from operations will be sufficient to meet our current debt service requirements for interest and any required prepayments under the Credit Agreement. However, if such cash flow is not sufficient, we may be required to issue additional debt or equity securities, refinance our obligations, or take other actions in order to make such scheduled payments. We cannot be sure that we would be able to effect any such transactions on favorable terms, if at all. Failure to do so may cause an event of default under the Credit Agreement, which will have a material adverse effect on our business, operating results and financial conditions.

### **OUR DEBT COVENANTS RESTRICT OUR FINANCIAL AND OPERATIONAL FLEXIBILITY.**

As discussed above, the Credit Agreement contains a number of financial covenants, which, among other things, require us to maintain specified financial ratios and impose certain limitations on us with respect to lines of business, mergers, investments and acquisitions, additional indebtedness, distributions, guarantees, liens and encumbrances. Our ability to meet the financial ratios can be affected by operating performance or other events beyond our control, and we cannot assure you that we will meet those ratios and failure to do so may cause an event of default under the Credit Agreement. Our indebtedness under the Credit Agreement is secured by a lien on substantially all of our assets and of our subsidiaries, by a pledge of our operating and license subsidiaries' stock and by a guarantee of our subsidiaries. If the amounts outstanding under the Credit Agreement were accelerated due to an event of default, the lenders could proceed against such available collateral by forcing

the sales of these assets.

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**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2. PROPERTIES**

Actuate's properties consist of leased facilities for sales and marketing, research and development, services and support and administrative personnel. Actuate's headquarters facilities consist of approximately 83,000 square feet of office space in the Bridgepointe Campus in San Mateo, California. The lease on these headquarter facilities will expire in July 2012. Actuate also leases an additional 50,400 square feet in one facility in South San Francisco, California. The lease on this additional facility will expire in April 2011 and this facility is entirely being subleased. Actuate also leases office facilities in various locations in the United States and abroad. All facilities are leased under operating leases.

As a result of the Company's California facilities being located near major earthquake fault lines, in the event of an earthquake its business, financial condition and operating results could be seriously harmed. In addition, California has in the past experienced energy power shortages. If future power shortages result in numerous or prolonged brownouts or blackouts, the Company's business, financial condition and operating results could be seriously harmed.

**ITEM 3. LEGAL PROCEEDINGS**

We are engaged in certain legal actions arising in the ordinary course of business. Although there can be no assurance as to the outcome of such litigation, we believe we have adequate legal defenses and we believe that the ultimate outcome of any of these actions will not have a material effect on our financial position or results of operations.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None.



**Table of Contents****PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

Our common stock is traded on The Nasdaq Global Market under the symbol ACTU and has been traded on Nasdaq since Actuate's initial public offering in 1998. The following table sets forth the high and low closing sales prices of our common stock during the last two fiscal years:

|                               | <b>High</b> | <b>Low</b> |
|-------------------------------|-------------|------------|
| First Quarter of Fiscal 2007  | \$ 5.80     | \$ 4.89    |
| Second Quarter of Fiscal 2007 | \$ 6.79     | \$ 5.28    |
| Third Quarter of Fiscal 2007  | \$ 7.09     | \$ 5.92    |
| Fourth Quarter of Fiscal 2007 | \$ 8.79     | \$ 6.51    |
| First Quarter of Fiscal 2008  | \$ 7.81     | \$ 3.93    |
| Second Quarter of Fiscal 2008 | \$ 5.00     | \$ 3.88    |
| Third Quarter of Fiscal 2008  | \$ 4.56     | \$ 3.39    |
| Fourth Quarter of Fiscal 2008 | \$ 3.50     | \$ 2.20    |

According to the records of our transfer agent, as of February 17, 2009, Actuate had 103 stockholders of record (which number does not include the number of stockholders whose shares are held by a brokerage house or clearing agency, but does include, as one record holder each such brokerage house or clearing agency). We believe we had approximately 8,700 beneficial owners of our common stock. On February 27, 2009, the closing price of our common stock was \$3.58 per share.

We have never paid a cash dividend on our common stock and do not intend to pay cash dividends on our common stock in the foreseeable future.

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**Performance Graph**

The following performance graph shall not be deemed to be soliciting material or to be filed with the SEC or subject to Regulation 14A or 14C or the liabilities of section 18 of the Securities Exchange Act of 1934, as amended ( Exchange Act ), and shall not be deemed to be incorporated by reference into any of our filings under the Securities Act of 1933, as amended, or the Exchange Act.

The following graphs compare:

- I. The cumulative total stockholder return on the common stock of the Company from December 31, 2003 (the last trading day before the beginning of the Company's fifth preceding fiscal year) to December 31, 2008 (the last trading day of the fiscal year ended December 31, 2008) with the cumulative total return of (i) the Total Return Index for The Nasdaq Stock Market (U.S. Companies) (the Nasdaq Index ) and (ii) the RDG Software Composite Index (the RDG Software Index ). This graph assumes the investment of \$100 on December 31, 2003 in the common stock of the Company, the Nasdaq Index and the RDG Software Index.

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- II. The cumulative total stockholder return on the common stock of the Company from December 31, 2007 to December 31, 2008 with the cumulative total return of (i) the Total Return Index for the Nasdaq Index and (ii) the RDG Software Index. This graph assumes the investment of \$100 on January 1, 2008 in the common stock of the Company, the Nasdaq Index and the RDG Software Index.

The comparisons in the graphs above are based on historical data and are not indicative of, nor intended to forecast, future performance of our common stock.

**Purchases of Equity Securities**

| <b>Period</b>                        | <b>Total<br/>Number<br/>of Shares<br/>Purchased</b> | <b>Average Price<br/>Paid per<br/>Share</b> | <b>Total<br/>Number of<br/>Shares<br/>Purchased as<br/>Part of Publicly<br/>Announced<br/>Program</b> | <b>Maximum Number<br/>of Shares<br/>That May<br/>Yet Be Purchased<br/>Under the<br/>Program</b> |
|--------------------------------------|---|---|---|---|
| October 1, 2008 - October 30, 2008   |   |   |   |   |
| November 1, 2008 - November 30, 2008 |   |   |   |   |
| December 1, 2008 - December 31, 2008 | 17,142,857  | \$ 3.50                                     | 17,142,857  |   |
| <b>Total</b>                         | <b>17,142,857</b>                                   |   | <b>17,142,857</b>   |   |

On November 3, 2008, the Company announced its intention to commence a modified Dutch auction tender offer to purchase up to \$60.0 million worth of its common stock, at a price per share not less than \$3.15 and not greater than \$3.50. On December 29, 2008, the Company announced the final results of its tender offer and purchased and paid for 17,142,857 shares at \$3.50 per share for a total cost of \$60.0 million.

**Table of Contents****ITEM 6. SELECTED FINANCIAL DATA**

The following selected consolidated financial data should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations, and with the Consolidated Financial Statements and Notes thereto that are included elsewhere in this Form 10-K. The Consolidated Statements of Income data for the years ended December 31, 2008, 2007 and 2006 and the Consolidated Balance Sheets data at December 31, 2008 and 2007 are derived from the audited Consolidated Financial Statements included elsewhere in this Form 10-K. The Consolidated Statements of Income data for the years ended December 31, 2005 and 2004 and the Consolidated Balance Sheets data as of December 31, 2006, 2005 and 2004 are derived from audited Consolidated Financial Statements that are not included in this Form 10-K. Historical results are not necessarily indicative of results to be anticipated in the future.

|   | Year ended December 31,                          |                  |                  |                  |                 |
|---|--|------------------|------------------|------------------|-----------------|
|   | 2008   | 2007             | 2006             | 2005             | 2004            |
|   | (in thousands, excepts share and per share data) |                  |                  |                  |                 |
| <b>Consolidated Statement of Income Data:</b>               |  |                  |                  |                  |                 |
| Revenues:   |  |                  |                  |                  |                 |
| License fees  | \$ 39,989  | \$ 53,216        | \$ 46,919        | \$ 36,939        | \$ 42,703       |
| Maintenance   | 76,695   | 71,336           | 63,145           | 52,671           | 45,419          |
| Professional services and training                          | 14,306   | 16,074           | 18,505           | 16,791           | 16,535          |
| <b>Total revenues</b>                                       | <b>130,990</b>                                   | <b>140,626</b>   | <b>128,569</b>   | <b>106,401</b>   | <b>104,657</b>  |
| Costs and expenses:   |  |                  |                  |                  |                 |
| Cost of license fees  | 1,396  | 1,997            | 2,095            | 2,294            | 3,417           |
| Cost of services  | 23,330   | 24,927           | 27,914           | 23,723           | 24,763          |
| Sales and marketing   | 51,830   | 55,312           | 49,009           | 37,070           | 41,296          |
| Research and development                                    | 22,035   | 21,826           | 21,055           | 16,533           | 19,847          |
| General and administrative                                  | 18,470   | 17,784           | 16,026           | 13,115           | 10,856          |
| Amortization of other intangibles                           | 948  | 948              | 948              | 487              | 1,110           |
| Purchased in-process research and development               |  |                  | 900              |                  |                 |
| Restructuring charges                                       | 1,506  | 1,686            | 16               | 665              | 2,006           |
| <b>Total costs and expenses</b>                             | <b>119,515</b>                                   | <b>124,480</b>   | <b>117,963</b>   | <b>93,887</b>    | <b>103,295</b>  |
| <b>Income from operations</b>                               | <b>11,475</b>                                    | <b>16,146</b>    | <b>10,606</b>    | <b>12,514</b>    | <b>1,362</b>    |
| Interest and other income, net                              | 785  | 3,155            | 2,217            | 1,436            | 822             |
| <b>Income before income taxes</b>                           | <b>12,260</b>                                    | <b>19,301</b>    | <b>12,823</b>    | <b>13,950</b>    | <b>2,184</b>    |
| Provision (benefit) for income taxes                        | (1,318)  | (863)            | (974)            | 2,359            | 886             |
| <b>Net income</b>   | <b>\$ 13,578</b>                                 | <b>\$ 20,164</b> | <b>\$ 13,797</b> | <b>\$ 11,591</b> | <b>\$ 1,298</b> |
| Basic net income per share (1)                              | \$ 0.23  | \$ 0.33          | \$ 0.23          | \$ 0.19          | \$ 0.02         |
| Shares used in basic net income per share calculation (1)   | 60,025   | 60,838           | 60,375           | 61,057           | 61,577          |
| Diluted net income per share (1)                            | \$ 0.21  | \$ 0.29          | \$ 0.21          | \$ 0.18          | \$ 0.02         |
| Shares used in diluted net income per share calculation (1) | 65,049   | 68,722           | 66,814           | 63,269           | 65,202          |



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|   | 2008      | 2007      | December 31,<br>2006<br>(in thousands) | 2005      | 2004      |
|---|-----------|-----------|--|-----------|-----------|
| <b>Consolidated Balance Sheet Data:</b>     |           |           |  |           |           |
| Cash, cash equivalents and investments      | \$ 58,441 | \$ 68,415 | \$ 60,079                              | \$ 54,397 | \$ 47,273 |
| Working capital                             | 20,701    | 54,045    | 37,298                                 | 38,889    | 30,362    |
| Total assets                                | 150,512   | 169,908   | 147,589                                | 111,581   | 105,455   |
| Long-term liabilities, less current portion | 38,278    | 10,712    | 10,532                                 | 10,996    | 14,325    |
| Stockholders' equity                        | 56,248    | 100,973   | 77,810                                 | 55,368    | 46,945    |

- (1) See Note 1 of Notes to the Consolidated Financial Statements for an explanation of the method used to determine the number of shares used in computing net income per share.

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### **ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

#### **Overview**

This Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ) should be read in conjunction with the other sections of this Annual Report on Form 10-K, including Business, Selected Financial Data, and Financial Statements and Supplementary Data, as well as the Notes to the Consolidated Financial Statements. This MD&A contains a number of forward-looking statements, all of which are based on our current expectations, beliefs and strategies and could be affected by the uncertainties and risk factors described throughout this filing and particularly in the Risk Factors section.

Our actual results may differ materially from those indicated in such forward-looking statements. See Risk Factors and Special Note Regarding Forward-Looking Statements in this Report on Form 10-K and the risks discussed in other reports we have furnished or filed from time to time with the SEC.

#### **Our Business**

##### **General**

Actuate Corporation ( We, Actuate or the Company ) was incorporated in November 1993 in the State of California and reincorporated in the State of Delaware in July 1998. Actuate provides software and services to develop and deploy Rich Internet Applications ( RIA ) that deliver rich interactive content that improve customer loyalty and corporate performance. Applications built on Actuate's open source-based platform provide all stakeholders inside and outside the firewall, including employees, customers, partners and citizens with information that they can easily access and understand to maximize revenue, cut costs, improve customer satisfaction, streamline operations, create competitive advantage and make better decisions. Our goal is to ensure that all users can use decision-making information in their day-to-day activities, opening up completely new avenues for improving corporate performance.

The software industry is currently experiencing significant challenges, primarily due to a deteriorating macroeconomic environment, which is primarily characterized by diminished product demand. As a result of this downturn, some of our customers may face financial challenges in fiscal 2009. It is unclear when the macroeconomic environment may improve. We are seeing increasing pressures on our customers' Information Technology budgets, and therefore our customers are looking for more flexibility in the type of software and the timing of such purchases. The current economic downturn in our customers' industries has contributed to the reduction in our license revenues and could continue to adversely impact our future business, operating results and financial condition.

Facing uncertainty and cost pressures in their own businesses, some of our customers are waiting to purchase our products and are increasingly seeking purchasing terms and conditions that are less favorable to us. This trend has partially contributed to lower license revenues for fiscal 2008 and this trend may continue in fiscal 2009.

Our customers may also experience adverse changes in their business and, as a result, may delay or default on their payment obligations, file for bankruptcy or modify or cancel plans to license our products. If our customers are not successful in generating sufficient revenue or are

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precluded from securing financing, they may not be able to pay, or may delay payment of, accounts receivable that are owed to us, although these obligations are generally not cancelable. Additionally, our customers may seek to renegotiate existing contractual commitments. Though we have not yet experienced any unusual levels of defaults, any material payment default by our customers or significant reductions in existing contractual commitments could have a material adverse effect on our financial condition and operating results.



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### **Business Model**

We began shipping our first product in January 1996. We sell software products through two primary means: (i) directly to end-user customers through our direct sales force and (ii) through indirect channel partners such as OEMs, resellers and system integrators. OEMs generally integrate our products with their applications and either provide hosting services or resell them with their products. Our other indirect channel partners resell our products to end-user customers. Our revenues are derived from license fees for software products and fees for services relating to such products, including software maintenance and support, consulting and training.

### **Fiscal Year 2008**

Our total revenues for fiscal year 2008 were \$130.9 million, which were approximately 7% lower than our prior fiscal year revenues of \$140.6 million. License revenues decreased by 25% from \$53.2 million in fiscal year 2007 to \$39.9 million in fiscal year 2008. The decrease was primarily due to unfavorable economic conditions that began in late fiscal 2007 and continue to adversely impact the financial services industry, a key component of Actuate's customer portfolio. This decrease in license revenue was partially offset by a 4% increase in services revenues. This increase was primarily driven by maintenance and support revenues that continue to grow as our installed base increases. For fiscal year 2008, we reported net income of \$13.6 million or \$0.21 per diluted share compared to net income of \$20.2 million or \$0.29 per diluted share in fiscal year 2007. This decrease in net income was driven primarily by the lower license revenues over the same period last year. Our operating margin decreased from \$16.1 million or 11% of total revenues in fiscal year 2007 to \$11.5 million, or 9% of total revenues in fiscal year 2008. Our operating margins were negatively impacted by approximately \$360,000 as a result of fluctuations in foreign currency exchange rates which positively impacted our revenues by approximately \$110,000 and negatively impacted our expenses by approximately \$470,000 for fiscal year 2008.

In order to size the operations to meet the expected business and economic environment for our products, we implemented a restructuring plan during the second half of the year to eliminate 46 positions held by Actuate employees primarily in North America. This restructuring impacted all functional areas. The reduction in force was completed in fiscal year 2008. The restructuring plan also resulted in the recognition of costs related to the consolidation of facilities, the cancellation of certain lease contracts and the write-off of fixed assets located at facilities that have been vacated.

In early November of 2008, we entered into a revolving Credit Agreement with Wells Fargo Foothill, LLC ( "WFF" ), part of Wells Fargo & Company. The Credit Agreement provided for a revolving line of credit in the principal amount of up to \$50 million and was arranged in anticipation of a stock buyback through a modified Dutch auction tender offer in December 2008. The tender offer was successfully completed in late December 2008 and resulted in repurchase of approximately 17.1 million shares at a price of \$3.50 per share. The offering resulted in a total cost of \$60 million and was equally funded with both cash reserves and borrowings from the Credit Agreement with WFF. Prior to the commencement of the tender offer in the fourth quarter of fiscal year 2008, we had repurchased an additional 2.6 million shares through our accelerated stock buy back program that was authorized by our Board in early February 2008.

Recent U.S. sub-prime mortgage defaults have had a significant impact across various sectors of the financial markets, causing global credit and liquidity issues. The short-term funding markets experienced credit issues during fiscal 2008. This led to liquidity disruption in asset-backed commercial paper and failed auctions in the auction rate market. If the global credit market continues to deteriorate, our investment portfolio may be impacted and we could determine that some of our investments are other than temporarily impaired. This could materially adversely impact our results of operations and financial condition.

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We own investments in marketable securities that have been designated as available for sale or trading securities in accordance with SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. Available for sale securities are carried at fair value with the unrealized gains and losses reported in

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Accumulated Other Comprehensive Income (Loss), a component of Stockholders' Equity. Trading securities are carried at fair value with unrealized gains and losses reported in results of operations.

At December 31, 2008, we held \$16.5 million (par value) of investments comprised of ARS, which are variable-rate debt securities and have a long-term maturity with the interest rate being reset through Dutch auctions that are typically held every 28 days. Prior to February 2008, the securities had historically traded at par and are callable at par at the option of the issuer. Interest is typically paid at the end of each auction period or semiannually. At December 31, 2008, all of the ARS we held were AAA/Aaa rated, with most collateralized by student loans guaranteed by the U.S. government under the Federal Family Education Loan Program.

In November 2008, we elected to participate in a rights offering by UBS, our investment broker, which provides us with rights (the Put Option) to sell UBS \$16.5 million of our ARS portfolio at par value, at any time during a two-year sale period beginning June 30, 2010. By electing to participate in the rights offering, we granted UBS the right, exercisable at any time prior to June 30, 2010 or during the two-year sale period, to purchase or cause the sale of our ARS (the Call Right). UBS has stated that it will only exercise the Call Right for the purpose of restructurings, dispositions or other solutions that will provide their clients with par value for their ARS. UBS has agreed to pay their clients the par value of their ARS within one day of settlement of any Call Right transaction. Notwithstanding the Call Right, we are permitted to sell ARS to parties other than UBS, in which case the Put Option attached to the ARS that are sold would be extinguished. We classified the Put Option as a non-current security. As such, we recorded a net realized loss of approximately \$84,000 related to the difference between the gain recognized on the Put Option and the realized loss on the \$16.5 million (par value) portion of our ARS portfolio.

We have no reason to believe that any of the underlying issuers of our ARS are presently at risk of default. Through December 31, 2008, we have continued to receive interest payments on the ARS in accordance with their terms. We believe we will ultimately be able to liquidate our ARS related investments without significant loss primarily due to the collateral securing ARS and the legal settlements we have entered into with UBS. However, it could take until final maturity of the ARS (up to 39 years) to realize our investments' par value. Due to the changes and uncertainty in the ARS market, we believe the recovery period for these investments is likely to be longer than 12 months and as a result, we have classified these investments as long-term as of December 31, 2008.

Since February 2008, most ARS auctions have failed for these securities and there is no assurance that future auctions will succeed and, as a result, our ability to liquidate our investment and fully recover the par value in the near term may be limited non-existent. In the event the Company needs to access these funds, it will not be able to do so without a loss of principal, unless a future auction on these investments is successful. The Company has reduced the carrying value of these ARS investments as of December 31, 2008 through a charge to other income/(expense). This reduction was largely offset by a gain recognized on the Put Option described above. The net reduction amounted to approximately \$84,000. The Company will evaluate these investments on a quarterly basis. For additional discussion please refer to the Note 4 of our Consolidated Financial Statements.

During the first half of fiscal year 2008, we recorded facility related restructuring charges totaling \$271,000. These charges primarily related to lease exit costs associated with our South San Francisco facility; the closure of one of the three floors in our Toronto, Canada facility and the consolidation of our Vienna, Virginia facilities into one location. We also incurred approximately \$132,000 in legal fees related to a previous restructuring which involved the terminations of former employees in one of our European subsidiaries.

During the second half of fiscal year 2008, we recorded approximately \$1.1 million in costs consisting of severance, benefits and related legal fees when we initiated a restructuring of our North America sales force to size the operation to meet the expected business and economic environment. This restructuring resulted in workforce reductions of 46 total personnel and was concentrated mainly in North America across all levels of the sales organization.



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All restructuring charges were accounted for in accordance with Financial Accounting Standards ( SFAS ) No. 146, *Accounting for Costs Associated with Exit or Disposal Activities* ( SFAS 146 ).

Our total headcount at the end of fiscal year 2008 was 533 compared to 581 employees at the end of last year.

### **Fiscal Year 2009**

A significant portion of our revenues have historically been derived from customers in the financial services industry. The Company expects that it will continue to derive a significant portion of its revenues from these financial services customers for the foreseeable future. Unfavorable economic conditions starting in late fiscal 2007 have adversely impacted the financial services industry throughout fiscal 2008. If this trend continues into 2009, it will likely have a material adverse effect on the Company's business, financial condition and results of operations. We currently anticipate that our total revenues in fiscal year 2009 will be lower than those levels experienced in fiscal year 2008, and fiscal year 2009 license revenues may decrease by as much as 20% from fiscal year 2008 levels.

During fiscal year 2009, we expect three additional trends to continue that would have a significant impact on the results of our operations. We currently believe that corporate IT budgets will grow only modestly if at all in the fiscal year 2009, particularly among financial services companies in the United States. Second, corporations are reluctant to buy software from new vendors and we continue to witness corporations consolidating their Business Intelligence, RIA and Performance Management software purchases into fewer suppliers. Finally, we expect to experience vigorous competition in the RIA market. Several of our competitors have released products that are marketed to be directly competitive with our RIA offerings. The existence of these competitive products may require additional sales and marketing efforts to differentiate our products, which could result in extended sales cycles. We believe that competition in the RIA market will be vigorous in the near future.

For fiscal year 2009, we will continue to pursue the strategic initiatives to improve revenue growth that we began introducing in fiscal year 2004 as well as an initiative related to Performance Management, which we introduced in fiscal 2007. These initiatives are as follows:

**Selling to IT Management** We are re-focusing our sales efforts on selling our products to IT managers who we believe generally recognize the technical advantages of our products. We hope this initiative will result in increased license revenue in the short term.

**Solution Selling to Line-of-Business Management** We are creating Performance Management applications and software solutions to market to line-of-business managers. These offerings are in the areas of performance management and customer self service reporting. We hope these initiatives will result in increased license revenue over the medium-to-long term.

**Investing in BIRT** We are continuing to make a significant investment in creating a new open source business intelligence and reporting tool, known as BIRT. We hope that BIRT will eventually become widely adopted by Java developers and will create demand for our other commercially available products. The BIRT project is a long-term initiative.

**Selling to Global 9000 Corporations in the Financial Services Sector** We are continuing to focus on selling our products to Global 9000 financial services companies in an effort to increase our substantive market share in this sector. We anticipate a negative impact of the ongoing credit crunch on the Financial Services sector in 2009. However, we believe that once the short term issues in Financial

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Services are resolved, the industry will once again lead in the adoption of RIA both inside and outside the firewall.

**Delivering a Highly Differentiated Performance Management Offering** We intend to combine Actuate PerformanceSoft Performance Management applications and Actuate's RIA-ready information platform to provide capabilities for distributing accountability throughout the enterprise.

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We have a limited ability to forecast future revenues and expenses, thus the prediction of future operating results is difficult. In addition, historical growth rates in our revenues and earnings should not be considered indicative of future revenue or earnings growth rates or operating results. There can be no assurance that any of our business strategies will be successful or that we will be able to achieve and maintain profitability on a quarterly or annual basis. It is possible that in some future quarter our operating results will be below the expectations of public market analysts and investors, and in such event the price of our common stock could decline.

### **Critical Accounting Policies, Judgments and Estimates**

**General.** The discussion and analysis of our financial condition and results of operations are based upon our Consolidated Financial Statements, which have been prepared in accordance with generally accepted accounting principles in the United States of America. The preparation of these financial statements requires us to make estimates, assumptions and judgments that can have a significant impact on the reported amounts of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our financial statements. We base our estimates, assumptions and judgments on historical experience and various other factors that we believe to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. On a regular basis we evaluate our estimates, assumptions and judgments and make changes accordingly. We also discuss our critical accounting estimates with the Audit Committee of our Board of Directors. We believe that the estimates, assumptions and judgments involved in revenue recognition, allowances for doubtful accounts, returns and discounts, valuation and impairment of investments, stock-based compensation, accounting for income taxes, contingencies, restructuring and integration costs, impairment of goodwill, intangible assets and long-lived assets have the greatest potential impact on our Consolidated Financial Statements, so we consider these to be our critical accounting policies.

We discuss below the critical accounting estimates associated with these policies. Historically, our estimates, assumptions and judgments relative to our critical accounting policies have not differed materially from actual results. For further information on our significant accounting policies, see the discussion in Note 1 to our Consolidated Financial Statements included in this Annual Report on Form 10-K.

**Revenue Recognition.** Actuate generates revenues from sales of software licenses and related services. The Company receives software license revenues from licensing its products directly to end-users and indirectly through resellers, system integrators and original equipment manufacturers (OEMs). The Company receives service revenues from maintenance contracts, consulting services and training that Actuate performs for customers.

Actuate recognizes revenues in accordance with AICPA Statement of Position ( SOP ) 97-2 ( SOP 97-2 ), *Software Revenue Recognition*, as amended and modified by SOP 98-9, *Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions*. For sales to end-user customers, Actuate recognizes license revenues when a license agreement has been signed by both parties or a definitive agreement has been received from the customer, the product has been shipped, there are no unusual uncertainties surrounding the product acceptance, the fees are fixed or determinable, collectibility is probable and vendor-specific objective evidence of fair value exists to allocate the fee to the undelivered elements of the arrangement. Vendor-specific objective evidence of sales to end users is based on the price charged when an element is sold separately. Actuate has not established vendor-specific objective evidence of fair value for its licenses. Therefore, the Company recognizes revenues from arrangements with multiple elements involving software licenses under the residual method. If the license agreement contains payment terms that would indicate that the fee is not fixed or determinable, revenues are recognized as the payments become due and payable, assuming that all other revenue recognition criteria are met.

Actuate enters into reseller and distributor arrangements that typically give such distributors and resellers the right to distribute its products to end-users headquartered in specified territories. Actuate recognizes license





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revenues from arrangements with U.S. resellers and distributors when there is persuasive evidence of an arrangement with the reseller or distributor, the product has been shipped, the fees are fixed or determinable, and collectibility is probable and vendor-specific objective evidence of fair value exists to allocate the fee to the undelivered elements of the arrangement. Actuate recognizes license revenues from arrangements with international resellers and distributors upon receipt of evidence of sell-through and when all other revenue recognition criteria have been met. If it is not practical to obtain evidence of sell-through, the Company defers revenues until the end-user has been identified and cash has been received. In some instances there is a timing difference between when a reseller completes its sale to the end-user and the period in which Actuate receives the documentation required for revenue recognition. Because Actuate delays revenue recognition until the reporting period in which the required documentation is obtained, it may recognize revenue in a period subsequent to the period in which the reseller completes the sale to its end-user.

Actuate also enters into OEM arrangements that provide for license fees based on the bundling or embedding of its products with the OEM's products. These arrangements generally provide for fixed, irrevocable royalty payments. Actuate recognizes license fee revenues from U.S. and international OEM arrangements when a license agreement has been executed by both parties, the product has been shipped, there are no unusual uncertainties surrounding the product acceptance, the fees are fixed or determinable, collectibility is probable and vendor-specific objective evidence of fair value exists to allocate the fee to the undelivered elements of the arrangement.

Credit-worthiness and collectibility for end-users are assessed based on payment history and current credit profile. When a customer is not deemed credit-worthy, revenues are deferred and recognized upon cash receipt.

Actuate recognizes maintenance revenues, which consist of fees for ongoing support and unspecified product updates, ratably over the term of the contract, typically one year. Consulting revenues are primarily related to standard implementation and configuration. Training revenues are generated from classes offered at the Company's headquarters and customer locations. Revenues from consulting and training services are typically recognized as the services are performed. When a contract includes both, license and service elements, the license fee is typically recognized on delivery of the software, assuming all other revenue recognition criteria are met, provided services do not include significant customization or modification of the product and are not otherwise essential to the functionality of the software.

***Allowance for Doubtful Accounts.*** Our accounts receivable is subject to collection risks. Our gross accounts receivable is reserved against this risk through an allowance for doubtful accounts. This allowance is for estimated losses resulting from the inability of our customers to make required payments. It is a significant estimate and is regularly evaluated by us for adequacy by taking into consideration a combination of factors. We look at factors such as past experience, credit quality of the customer, age of the receivable balance, and current economic conditions. These factors are reviewed to determine whether a specific reserve for bad debt should be recorded to reduce the related receivable to the amount believed to be collectible. We also cease recognizing future revenues on any outstanding domestic maintenance renewal invoices which are older than 90 days past due.

We also record unspecified reserves for bad debt for all other customers based on a variety of factors, including length of time the receivables are past due and historical experience. A reserve percentage is applied to various aged categories of receivables based on historical experience to determine how much of an unspecified reserve is needed. The use of different estimates or assumptions could produce different allowance balances. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances might be required.

***Fair Value of Financial Instruments and Concentration of Credit Risk.*** Carrying amounts of our financial instruments including accounts receivable, accounts payable, accrued liabilities and long term debt approximate fair value. The fair values of our cash equivalents, available-for-sale investments in marketable securities and derivative instruments are detailed further in Note 4 of the Consolidated Financial Statements.



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**Stock-based Compensation.** Effective January 1, 2006, we adopted Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment* (SFAS 123(R)), using the modified prospective method, in which compensation cost was recognized based on the requirements of SFAS 123R for (a) all share-based payments granted or modified after the effective date and (b) for all awards granted to employees prior to the effective date of FAS 123R that remain unvested on the effective date. FAS 123R requires the use of judgment and estimates in performing multiple calculations. We have estimated the expected volatility as an input into the Black-Scholes-Merton valuation formula when assessing the fair value of options granted. Our estimate of volatility is based upon the historical volatility experienced in our stock price. To the extent volatility of our stock price increases in the future, our estimates of the fair value of options granted in the future could increase, thereby increasing stock-based compensation expense in future periods. In addition, we apply an expected forfeiture rate when amortizing stock-based compensation expense. Our estimate of the forfeiture rate is based primarily upon historical experience. To the extent we revise this estimate in the future, our stock-based compensation expense could be materially impacted in the quarter of revision, as well as in following quarters. Our estimate of the expected term of options granted is derived from historical share option exercise experience. In the future, we may change our estimate of the expected term. This change could impact the fair value of our options granted in the future.

**Income Taxes.** Income taxes are accounted for under the asset and liability method required by Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes* (SFAS No. 109). Under this method deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that includes the enactment date.

SFAS No. 109 requires that the deferred tax assets be reduced by a valuation allowance, if based on the weight of available evidence, it is more likely than not that some portion or all of the recorded deferred tax assets will not be realized in future periods. In evaluating our ability to recover our deferred tax assets, in full or in part, we consider all available positive and negative evidence, including our past operating results, the existence of cumulative losses in the most recent years and our forecast of future taxable income on a jurisdiction by jurisdiction basis. In determining future taxable income, we are responsible for assumptions utilized including the amount of state, federal and international pre-tax operating income, the reversal of temporary differences and the implementation of feasible and prudent tax planning strategies. These assumptions require significant judgment about the forecasts of future taxable income and are consistent with the plans and estimates we are using to manage the underlying businesses.

For fiscal year 2008, we continue to believe there is sufficient positive evidence to support the utilization of our deferred tax assets. This positive evidence includes the continued experience of generating net income and positive projections of future U.S. and foreign net income. We believe this constitutes significant positive evidence which indicates that there is no need for a valuation allowance related to certain deferred tax assets. We do have certain deferred tax assets that require a valuation allowance. A portion of our deferred tax assets are related to foreign net operating losses where there is sufficient negative evidence to require a valuation allowance. The remaining deferred tax assets that have a valuation allowance are related to research and development tax credits which have been previously benefited on a book basis. A valuation allowance on these deferred tax assets is required until the credits are actually utilized. At future dates, if sufficient positive evidence exists with regards to the foreign deferred tax assets and it is more likely than not that the benefit will be realized with respect to the remaining deferred tax assets, we will release a portion of the remaining valuation allowance. This adjustment to the valuation allowance depending on the respective deferred tax assets would decrease tax expense, reduce goodwill or intangibles and/or increase shareholder's equity in the period such a determination was made. Likewise, if there is a reduction in the projection of future U.S. and foreign net income and significant negative evidence exists, we would be required to increase the valuation allowance with respect to

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specific deferred tax assets. An increase in the valuation allowance depending on the respective deferred tax assets would increase tax expense, increase goodwill or intangibles or decrease shareholder's equity in the period such a determination was made.

The Company adopted the provisions of FASB Interpretation No. 48 *Accounting for Uncertainty in Income Taxes* (FIN 48) on January 1, 2007. FIN 48 prescribes a new recognition threshold and measurement attribute for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return. Under FIN 48, only income tax positions that meet the more likely than not recognition threshold may be recognized in the financial statements. An income tax position that meets the more likely than not recognition threshold shall initially and subsequently be measured as the largest amount of tax benefit that is greater than 50 percent likely of being realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information.

Significant judgment is required in applying the principles of FIN 48 and SFAS No. 109. The calculation of our provision for income taxes involves dealing with uncertainties in the application of complex tax laws and regulations. In determining the adequacy of our provision for income taxes, we regularly assess the potential settlement outcomes resulting from income tax examinations. However, the final outcome of tax examinations, including the total amount payable or the timing of any such payments upon resolution of these issues, cannot be predicted with certainty. In addition, we cannot be certain that such amount will not be materially different than that which is reflected in our historical income tax provisions and accruals. Should the IRS or other tax authorities assess additional taxes as a result of a current or a future examination, we may be required to record charges to operations in future periods that could have a material impact on the results of operations, financial position or cash flows in the applicable period or periods.

On October 3, 2008, Congress enacted H.R. 1424, the Emergency Economic Stabilization Act of 2008 (the Act). The Act renewed the federal R&D credit (which previously expired on December 31, 2007) through 2009. The R & D credits calculated in the income tax provision are estimates based on the expected final calculations which will be completed at the time the federal and California income tax returns are finalized.

**Contingencies.** We are or have been engaged in legal actions arising in the ordinary course of business. We are required to assess the likelihood of any adverse judgments or outcomes to these matters as well as potential ranges of probable losses. A determination of the amount of reserves required, if any, for these contingencies is made after careful analysis of each individual matter. The required reserves may change in the future due to new developments in each matter or changes in approach, such as a change in litigation or settlement strategy for a particular matter.

**Accrual for Restructuring Charges.** During the fiscal years ended December 31, 2008, and 2007 we incurred certain restructuring charges that were a combination of reductions in workforce, exits of idle facilities and disposals of fixed assets. These restructuring charges were based on actual and estimated costs incurred including estimates of sublease income on portions of our idle facilities that we periodically update based on market conditions and in accordance with our restructuring plans. These estimates were impacted by the rules governing the termination of employees, especially those in foreign countries.

**In-process research and development.** We have recorded in-process research and development as a component of our acquisitions. At the time of these acquisitions, SFAS 141 *Business Combinations* was the relevant guidance. Subsequently, SFAS 141R was issued which alters the treatment of in-process research and development in accounting for business combinations. However, SFAS 141R treatment is only applicable prospectively to business combinations for which the acquisition date is on or after the first annual reporting period beginning on or after December 15, 2008.



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In adherence to SFAS 141, we reviewed our acquisitions and determined if there were any intangible assets relating to purchased in-process research and development. Projects that had not achieved technological feasibility and had no alternative future use were valued at fair market value using a discounted cash flow analysis and were expensed in the Consolidated Statement of Income on the date of acquisition. We used a discount rate that reflected the development stage of the technology and the risks associated with attaining full technological and commercial feasibility. When we valued in-process research and development, we had to make a number of estimates, including the timing and amounts of future cash flows to be generated as a result of the projects, how close the projects were to technological feasibility and how much risk and cost were involved in finalizing the projects. It was reasonably likely that our estimates for these amounts would differ from actual results, in which case our in-process research and development charge may have been over- or under-valued, which would also have resulted in an under- or over-valuation of our goodwill.

***Valuation of Goodwill and Other Purchased Intangible Assets.*** We evaluate our intangible assets for indications of impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Intangible assets consist of purchased technology, customer lists, non-compete agreements, experienced workforce, and trademarks. Factors that could trigger an impairment review include significant under-performance relative to expected historical or projected future operating results, significant changes in the manner of our use of the acquired assets, or the strategy for our overall business or significant negative industry or economic trends. If this evaluation indicates that the value of the intangible asset may be impaired, we make an assessment of the recoverability of the net carrying value of the asset over its remaining useful life. If the assessment indicates that the intangible asset is not recoverable, we will reduce the net carrying value of the related intangible asset to fair value and may adjust the remaining amortization period. Any such impairment charge could be significant and could have a material adverse effect on our reported financial results. As of December 31, 2008 the net carrying amount of our intangible assets was \$1.8 million.

We evaluate goodwill at least annually for indications of impairment based on our fair value as determined by our market capitalization in accordance with Statement of Financial Standards No. 142 ( SFAS 142 ), Goodwill and Other Intangible Assets . If this evaluation indicates that the value of the goodwill may be impaired, we make an assessment of the impairment of the goodwill using the two-step method prescribed by SFAS 142. Any such impairment charge could be significant and could have a material adverse effect on our reported financial results. We completed our annual impairment test in the fourth quarter of fiscal year 2008 and determined that there was no impairment.

***Valuation of Minority Interest in Actuate Japan.*** The minority shareholders of Actuate Japan have the non-expiring option to put their equity interest ( Minority Interest ) in Actuate Japan to the Company and the Company has the option to call the Minority Interest. The Minority Interest as of December 31, 2008 was approximately 12% of the total equity interest. If the Minority Interest Shareholder chose to put these remaining shares to the Company, Actuate would be required to pay approximately \$584,000 to purchase these shares. The Company will record a liability, if any, at the time that the put or call is probable of being exercised. Should an indicator arise that the Minority Interest has declined in value below the exercise price of the put and call option, the Company would conclude that exercise is probable at that point in time and recognize a liability for the intrinsic value of the option. The Company performs a periodic review of the value of the Minority Interest. This review may include making assumptions regarding projected future cash flows and discount rates. Variances in these assumptions could have a significant impact on the Company's conclusion as to whether it is necessary to record a liability. As of December 31, 2008, the Company concluded that it was not necessary to record a liability. The Company consolidated 100% of the operating results of Actuate Japan and all investments in the subsidiary are eliminated in consolidation. As of the date of this filing, the remaining minority shareholder has not notified the Company of any intent to exercise its put option.

***Recoverability of Long-Lived Assets.*** The Company evaluates the recoverability of its long-lived assets periodically by analyzing its operating results and considering significant events or changes in the business environment. At some point in the future, we may determine that our long-lived assets are impaired. The timing

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of such impairment may result in charges to our Consolidated Statement of Income to reduce the value of the asset carried on our Consolidated Balance Sheet to its estimated fair value. We determine whether we need to record an impairment charge based on various assumptions and estimates. Assumptions and estimates about future values can be complex and are often subjective. Although we believe the assumptions and estimates we have made in the past have been reasonable, different assumptions and estimates could materially affect our reported financial results.

**Results of Operations**

The following table sets forth certain Consolidated Statement of Income data as a percentage of total revenues for the periods indicated:

|   | Year Ended<br>December 31, |            |            |
|---|----------------------------|------------|------------|
|   | 2008                       | 2007       | 2006       |
| <b>Revenues:</b>                              |                            |            |            |
| License fees                                  | 31%                        | 38%        | 36%        |
| Maintenance                                   | 58                         | 51         | 49         |
| Professional services and training            | 11                         | 11         | 15         |
| <b>Total revenues</b>                         | <b>100</b>                 | <b>100</b> | <b>100</b> |
| <b>Costs and expenses:</b>                    |                            |            |            |
| Cost of license fees                          | 1                          | 1          | 2          |
| Cost of services                              | 18                         | 18         | 22         |
| Sales and marketing                           | 39                         | 39         | 38         |
| Research and development                      | 17                         | 16         | 16         |
| General and administrative                    | 14                         | 13         | 12         |
| Amortization of other intangibles             | 1                          | 1          | 1          |
| Purchased in-process research and development |                            |            | 1          |
| Restructuring charges                         | 1                          | 1          |            |
| <b>Total costs and expenses</b>               | <b>91</b>                  | <b>89</b>  | <b>92</b>  |
| Income from operations                        | 9                          | 11         | 8          |
| Interest and other income, net                |                            | 2          | 2          |
| Income before income taxes                    | 9                          | 13         | 10         |
| Benefit from income taxes                     | (1)                        | (1)        | (1)        |
| <b>Net income</b>                             | <b>10%</b>                 | <b>14%</b> | <b>11%</b> |

**Revenues**

| 2008                   | Year Ended December 31,<br>2007 | 2006 | \$ Change<br>2007 to 2008 | % Change | \$ Change<br>2006 to 2007 | % Change |
|------------------------|---------------------------------|------|---------------------------|----------|---------------------------|----------|
| (dollars in thousands) |                                 |      |                           |          |                           |          |

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|           |           |           |           |      |          |    |
|-----------|-----------|-----------|-----------|------|----------|----|
| \$130,990 | \$140,626 | \$128,569 | \$(9,636) | (7)% | \$12,057 | 9% |
|-----------|-----------|-----------|-----------|------|----------|----|

Our revenues are derived from license fees and services, which include software maintenance and support, consulting, and training. The decrease in total revenue for fiscal year 2008 compared to fiscal year 2007 was primarily due to lower demand for our products as a result of unfavorable economic conditions that began in late fiscal year 2007 and continue to adversely impact the financial services industry, a key component of our customer portfolio. As a result, license sales experienced a decline of approximately 25% over the prior year.



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We experienced declines in license sales across most of our sales regions including 22% or approximately \$7.9 million in North America and 31% or approximately \$5.2 million outside North America. Professional services revenues decreased 11% and was primarily the result of the continued increase in the adoption of BIRT-based projects by our customers which do not result in professional service revenues to the same extent as the Company's traditional designer products. Our BIRT-related business increased by approximately 90% over the same period last year. The success of the Company's BIRT initiative therefore results in a downward trend in the Company's revenue from professional services, as seen during the last two fiscal years. Our BIRT related business is expected to grow at a rate of approximately 30% in fiscal year 2009.

These decreases in license and consulting revenues were partially offset by an 8% or \$5.4 million increase in maintenance and support revenues over the same period last year. Of this increase in maintenance and support revenues, the majority was attributable to normal growth in support for our installed base. Since our existing renewal rate remains high, we anticipate maintenance revenues to continue to grow in 2009 regardless of software license growth.

For fiscal year 2008 we managed to close approximately 270 transactions in excess of \$100,000 compared to 290 in fiscal year 2007. In addition, we recognized license revenue of \$1.0 million or more on 4 transactions during fiscal year 2008 compared to 8 transactions in fiscal year 2007. The number of orders greater than \$1.0 million has historically ranged from none to three per quarter. We do not expect to rely on any one customer for our future business.

The increase in total revenue for fiscal year 2007 compared to fiscal year 2006 was primarily due to an increase in demand and a wider acceptance of our products by Global 9000 customers (companies with annual revenues greater than \$1.0 billion). This wider acceptance resulted in an increase in the number of large dollar value license deals (deals in excess of \$1.0 million) over fiscal year 2006. We experienced a 13% increase in our maintenance and support revenues. Approximately 37% of this increase related to a transaction with a customer who was out of compliance with its maintenance agreement and accordingly paid back maintenance. We also experienced a 31% growth in international license sales. Finally, the expansion of our BIRT initiative and application of our Business Intelligence, Performance Management and Reporting products and services resulted in the expansion of our products across more diverse industry groups in fiscal year 2007 including retail, government, technology and health care.

No single customer accounted for more than 10% of our total revenues for any of the periods presented.

**License Fees**

| 2008     | Year Ended December 31,<br>2007 | 2006     | \$ Change<br>2007 to 2008 | % Change | \$ Change<br>2006 to 2007 | % Change |
|----------|---------------------------------|----------|---------------------------|----------|---------------------------|----------|
|          |                                 |          | (dollars in thousands)    |          |                           |          |
| \$39,989 | \$53,216                        | \$46,919 | \$(13,227)                | (25)%    | \$6,297                   | 13%      |

The 25% decrease in license revenues for fiscal year 2008 over the same period in the prior year was primarily due to weak macro economic conditions that began in late fiscal year 2007 and continue to adversely impact the financial services industry, a key component of Actuate's customer portfolio. We experienced the sharpest decrease in license revenues over the previous fiscal year in Europe where software sales declined by 36% or approximately \$5.4 million when compared to the same period last year. We also experienced a decrease in North America license sales of 22% or approximately \$7.9 million from fiscal year 2007 to 2008.

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The increase in license revenues for fiscal year 2007 as compared to fiscal year 2006 was primarily due to improved sales across both international and domestic regions. International license revenues increased by 31% or approximately \$4.0 million and this growth was primarily seen in our European region. North American license revenues increased by 7% or approximately \$2.3 million over fiscal year 2006. In addition, we

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experienced an increase in the average size of license transactions and the number of license transactions in excess of \$1.0 million over the same period last fiscal year. We also experienced broader acceptance of the Company's BIRT initiative and application of our Business Intelligence, Performance Management and Reporting products by our existing and new Global 9000 customers.

**License Revenue**

| <i>(dollars in thousands)</i> | Year Ended December 31, |                  |                  | 2007 to 2008       |              | 2006 to 2007    |            |
|-------------------------------|-------------------------|------------------|------------------|--------------------|--------------|-----------------|------------|
|                               | 2008                    | 2007             | 2006             | \$ Change          | % Change     | \$ Change       | % Change   |
| North America                 | \$ 28,531               | \$ 36,503        | \$ 34,188        | \$ (7,972)         | (22)%        | \$ 2,315        | 7%         |
| Europe                        | 9,732                   | 15,122           | 10,519           | (5,390)            | (36)%        | 4,603           | 44%        |
| APAC                          | 1,726                   | 1,591            | 2,212            | 135                | 8%           | (621)           | (28)%      |
| <b>Total license revenue</b>  | <b>\$ 39,989</b>        | <b>\$ 53,216</b> | <b>\$ 46,919</b> | <b>\$ (13,227)</b> | <b>(25)%</b> | <b>\$ 6,297</b> | <b>13%</b> |
| Percentage of total revenue:  | 31%                     | 38%              | 36%              |                    |              |                 |            |

North America accounted for approximately 71% of the total license revenue while Europe and Asia Pacific regions combined accounted for 29% of the total license revenues for fiscal year 2008. For the same period last year, North America accounted for approximately 69% of the total license revenue while the Europe and Asia Pacific regions combined accounted for 31% of the total license revenues. Total license revenues were positively impacted by approximately \$110,000 due primarily to the strength of the Asian currencies against the U.S. dollar. As a percentage of total revenues, license fee revenues decreased from 38% in the fiscal year 2007 to 31% in fiscal year 2008.

The European region realized the most significant license revenue growth in fiscal year 2007 from fiscal year 2006. Approximately \$2.2 million of this growth was due to exchange rate fluctuations as a result of the strength of the Euro and the British Pound against the U.S. dollar. As a percentage of total revenues, license fee revenues increased from 36% in the fiscal year 2006 to 38% in fiscal year 2007.

**Services Revenue**

| <i>(dollars in thousands)</i>    | Year Ended December 31, |                  |                  | 2007 to 2008    |           | 2006 to 2007    |           |
|----------------------------------|-------------------------|------------------|------------------|-----------------|-----------|-----------------|-----------|
|                                  | 2008                    | 2007             | 2006             | \$ Change       | % Change  | \$ Change       | % Change  |
| Maintenance                      | \$ 76,695               | \$ 71,336        | \$ 63,145        | \$ 5,359        | 8%        | \$ 8,191        | 13%       |
| Professional services & training | 14,306                  | 16,074           | 18,505           | (1,768)         | (11)%     | (2,431)         | (13)%     |
| <b>Total services revenue</b>    | <b>\$ 91,001</b>        | <b>\$ 87,410</b> | <b>\$ 81,650</b> | <b>\$ 3,591</b> | <b>4%</b> | <b>\$ 5,760</b> | <b>7%</b> |
| Percentage of total revenue:     | 69%                     | 62%              | 64%              |                 |           |                 |           |

Services revenue is comprised of maintenance and support, professional services, and training. The 4% increase in services revenues was driven by the growth in our maintenance and support revenues, which continued to increase in fiscal year 2008. The fourth quarter of 2007 included an unusually large \$2.5 million maintenance catch-up transaction. Excluding this one time transaction for back maintenance, fiscal year 2008 maintenance revenue increased by 12% over fiscal year 2007. The increase in the installed base was evidenced by the fact that in fiscal year

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2008 we were supporting a large percentage of the \$53.2 million in licenses sold in fiscal year 2007, while our maintenance declination rate has remained consistent as we continue to experience high renewal rate from our existing customers.

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The decrease in professional services revenues was primarily the result of the increase in the adoption of BIRT-based projects by our customers which do not require professional service to the same extent as the Company's traditional designer products. Our BIRT-related business increased by approximately 90% over the same period last year. The success of the Company's BIRT initiative therefore results in a downward trend in the Company's revenue from professional services, as seen during the last two fiscal years. Due to this increased trend in BIRT-related business, we continued to experience reductions in our services headcount in fiscal year 2008 versus the same period last year.

By region, Europe accounted for the highest increase in services revenues for 2008. These increases were due primarily to the growth in our installed base of customers under maintenance plans in that region.

The growth in services revenues for fiscal year 2007 versus fiscal year 2006 was primarily attributed to the increase in our maintenance and support revenues driven by a continued growth in our installed base of customers under maintenance plans. The increase in the installed base was evidenced by the fact that in fiscal year 2007 we supported a large percentage of the \$46.9 million in licenses sold in fiscal year 2006, while our maintenance declination rate has remained consistent. In addition, we concluded a transaction in the fourth quarter of fiscal year 2007 with one of our customers who was out of compliance on their maintenance agreements. This arrangement brought the customer current on their maintenance and included approximately \$2.5 million of revenue related to maintenance periods preceding fiscal year 2007, but was recognized in fiscal year 2007. The amount related to the prior year was less than 2% of 2007 total revenue. The increase in maintenance revenue was offset by a 13% decrease in professional services revenues. This decrease was primarily the result of the increase in the adoption of BIRT-based projects by our customers which do not generate professional service revenues to the same extent as the Company's traditional designer products. The success of the Company's BIRT initiative therefore resulted in a reduction in the Company's revenue from professional services during the year.

The following table represents our services revenues by region (in thousands):

**Services Revenues**

| <i>(dollars in thousands)</i> | Year Ended December 31, |                  |                  | 2007 to 2008    |           | 2006 to 2007    |           |
|-------------------------------|-------------------------|------------------|------------------|-----------------|-----------|-----------------|-----------|
|                               | 2008                    | 2007             | 2006             | \$ Change       | % Change  | \$ Change       | % Change  |
| North America                 | \$ 65,578               | \$ 66,106        | \$ 62,767        | \$ (528)        | (1)%      | \$ 3,339        | 5%        |
| Europe                        | 22,747                  | 18,717           | 16,160           | 4,030           | 22%       | 2,557           | 16%       |
| APAC                          | 2,676                   | 2,587            | 2,723            | 89              | 3%        | (136)           | (5)%      |
| <b>Total services revenue</b> | <b>\$ 91,001</b>        | <b>\$ 87,410</b> | <b>\$ 81,650</b> | <b>\$ 3,591</b> | <b>4%</b> | <b>\$ 5,760</b> | <b>7%</b> |
| Percentage of total revenue:  | 69%                     | 62%              | 64%              |                 |           |                 |           |

**Costs and Expenses****Cost of License Fees**

| Year Ended December 31, | \$ Change | % Change | \$ Change | % Change |
|-------------------------|-----------|----------|-----------|----------|
|-------------------------|-----------|----------|-----------|----------|

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| 2008                         | 2007    | 2006    | 2007 to 2008 |       | 2006 to 2007 |      |
|------------------------------|---------|---------|--------------|-------|--------------|------|
| (dollars in thousands)       |         |         |              |       |              |      |
| \$1,396                      | \$1,997 | \$2,095 | \$(601)      | (30)% | \$(98)       | (5)% |
| (Percent of license revenue) |         |         |              |       |              |      |
| 3%                           | 4%      | 4%      |              |       |              |      |

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Cost of license fees consists primarily of salaries, production costs including printing and packaging, amortization of purchased technologies, third party royalty fees and localization costs. The decreases in cost of license fees in absolute dollars for fiscal year 2008, compared to the prior year, was due primarily to full amortization of purchased technologies totaling approximately \$340,000 in fiscal year 2008 relating to our acquisition of Nimble Technologies, which was acquired in fiscal year 2003.

The decrease in cost of license fees for fiscal year 2007 as compared to fiscal year 2006 was not significant.

We currently expect our cost of license fees, as a percentage of revenues from license fees, to remain between 2% and 4% of revenues from license fees for fiscal year 2009.

**Cost of Services**

| 2008                          | Year Ended December 31,<br>2007 | 2006     | \$ Change<br>2007 to 2008 | % Change | \$ Change<br>2006 to 2007 | % Change |
|-------------------------------|---------------------------------|----------|---------------------------|----------|---------------------------|----------|
| (dollars in thousands)        |                                 |          |                           |          |                           |          |
| \$23,330                      | \$24,927                        | \$27,914 | \$(1,597)                 | (6)%     | \$(2,987)                 | (11)%    |
| (Percent of services revenue) |                                 |          |                           |          |                           |          |
| 26%                           | 28%                             | 34%      |                           |          |                           |          |

Cost of services consists primarily of personnel and related costs, stock-based compensation, facilities costs incurred in providing software maintenance and support, training and consulting services, as well as third-party costs incurred in providing training and consulting services.

The decrease in cost of services in fiscal year 2008 as compared to fiscal year 2007 was primarily driven by a 23% decrease in our consulting headcount which consequently resulted in reductions in employee salaries, associated benefits and employee travel costs totaling approximately \$1.5 million. This decrease was primarily driven by the adoption of BIRT-based projects by our customers. BIRT-based projects do not generate professional service revenues to the same extent as the Company's traditional designer products. We also realized reductions in facilities related charges of approximately \$300,000 due partially to the closure of our service facility in Iselin, New Jersey in the second half of fiscal year 2007. These reductions were offset by an approximately \$200,000 increase in third party consulting fees as demand for Actuate's professional services engagements during the first half of fiscal year 2008 exceeded the supply of in-house consultants.

The decrease in cost of services in fiscal year 2007 as compared to fiscal year 2006 was primarily due to a reduction in headcount from 141 employees at the end of fiscal year 2006 to 118 employees at the end of fiscal year 2007. In addition, in fiscal year 2007 we also made a shift in company practice to reduce the use of outside third party consultants, thereby reducing costs. Third party consulting revenue decreased by 20% from approximately \$4.4 million in fiscal year 2006 to approximately \$3.5 million in fiscal year 2007. Also, there was lower demand for our professional services during 2007 as compared to last year primarily due to the increase in the adoption of BIRT-based projects by our customers which do not generate professional service revenues to the same extent as the Company's traditional designer products. Finally, there was a reduction in the allocation of sales support to the services function due to a decrease in professional consulting revenues.

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We currently expect our cost of services expenses as a percentage of total services revenues to be in the range of 24% to 30% of total services revenues for fiscal year 2009.



**Table of Contents****Sales and Marketing**

| 2008                       | Year Ended December 31,<br>2007 | 2006     | \$ Change<br>2007 to 2008 | % Change | \$ Change<br>2006 to 2007 | % Change |
|----------------------------|---------------------------------|----------|---------------------------|----------|---------------------------|----------|
| (dollars in thousands)     |                                 |          |                           |          |                           |          |
| \$51,830                   | \$55,312                        | \$49,009 | \$(3,482)                 | (6)%     | \$6,303                   | 13%      |
| (Percent of total revenue) |                                 |          |                           |          |                           |          |
| 39%                        | 39%                             | 38%      |                           |          |                           |          |

Sales and marketing expenses consist primarily of salaries, commissions and bonuses earned by sales and marketing personnel, stock-based compensation, promotional expenses, travel, entertainment and facility costs. For fiscal year 2008, the decrease in sales and marketing expenses compared to the corresponding period in the prior year was primarily due to decreases in salaries, sales commissions and employee travel of approximately \$5.0 million due to lower software sales and reductions in headcount. Total sales and marketing headcount decreased from 197 at December 31, 2007 to 160 at December 31, 2008. These decreases were partially offset by an increase of approximately \$1.1 million in marketing expenses driven by webinars, direct marketing, and tradeshow. In fiscal year 2008, we also recorded approximately \$420,000 in accrued legal fees related to a one-time employee termination charge as a result of the termination of a sales employee in our European division.

The increase in sales and marketing expenses in fiscal year 2007 over 2006 was primarily due to increases in salaries, sales commissions, related compensation and employee recruiting costs totaling approximately \$4.1 million. These increases were driven by 7% higher headcount in fiscal year 2007 and an increase in software license sales. In addition, as a result of lower consulting revenues, fewer sales support costs were allocated from sales and marketing to our professional services group in fiscal year 2007. These increases in cost were partially offset by an approximately \$400,000 decrease in travel and entertainment expense mainly due to improved cost controls.

At the end of fiscal year 2008, we had 160 employees in sales and marketing, compared with 197 and 180 employees at the end of fiscal years 2007 and 2006, respectively. We currently expect our sales and marketing expenses as a percentage of total revenues to be in the range of 38% to 40% of total revenues for fiscal year 2009.

**Research and Development**

| 2008                       | Year Ended December 31,<br>2007 | 2006     | \$ Change<br>2007 to 2008 | % Change | \$ Change<br>2006 to 2007 | % Change |
|----------------------------|---------------------------------|----------|---------------------------|----------|---------------------------|----------|
| (dollars in thousands)     |                                 |          |                           |          |                           |          |
| \$22,035                   | \$21,826                        | \$21,055 | \$209                     | 1%       | \$771                     | 4%       |
| (Percent of total revenue) |                                 |          |                           |          |                           |          |
| 17%                        | 16%                             | 16%      |                           |          |                           |          |

Research and development costs are expensed as incurred and consist primarily of personnel and related costs associated with the development of new products, the enhancement of existing products, quality assurance and testing. The increase in research and development expenses in fiscal year 2008, compared to the corresponding period in the prior year, was attributed to employee compensation and related costs driven mainly by annual salary adjustments and stock compensation expense. Our headcount remained comparable at 155 at the end of fiscal year 2008 compared to 159 at the end of fiscal year 2007. This increase in employee compensation expense was partially offset by decreases in facilities

related charges due partially to the consolidation of our Vienna, Virginia facilities into one location and lower fees paid to external contractors.

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The increase in research and development expenses for fiscal year 2007 compared to fiscal year 2006, was attributed to employee compensation driven by a 7% increase in our product development headcount, primarily in our Shanghai research and development facility. This increase was partially offset by lower professional consulting costs used for research and development purposes.

We believe that continued investments in technology and product development are essential for us to remain competitive in the markets we serve, and we expect our research and development expenses as a percentage of total revenues to be in the range of 16% to 19% of total revenues for fiscal year 2009.

**General and Administrative**

| 2008                       | Year Ended December 31,<br>2007 | 2006     | \$ Change<br>2007 to 2008 | % Change | \$ Change<br>2006 to 2007 | % Change |
|----------------------------|---------------------------------|----------|---------------------------|----------|---------------------------|----------|
| (dollars in thousands)     |                                 |          |                           |          |                           |          |
| \$18,470                   | \$17,784                        | \$16,026 | \$686                     | 4%       | \$1,758                   | 11%      |
| (Percent of total revenue) |                                 |          |                           |          |                           |          |
| 14%                        | 13%                             | 12%      |                           |          |                           |          |

General and administrative expenses consist primarily of personnel costs, stock-based compensation and related costs in finance, human resources, legal and tax functions, as well as audit and legal fees and bad debt expense. The increase in general and administrative expenses in fiscal year 2008 compared to fiscal year 2007 was mainly due to increased salaries and stock-based compensation expense of approximately \$1.1 million due primarily to annual salary adjustments and a 5% increase in headcount over the same period last year. We also experienced increases in legal and corporate advisory fees totaling approximately \$480,000 in fiscal year 2008 related to advice regarding strategic alternatives. These increases were partially offset by approximately \$500,000 in lower general accounting, tax and professional consulting services driven by lower SOX compliance costs. In addition, in fiscal year 2008, we experienced approximately \$300,000 lower costs for strategic consulting services in support of our BIRT initiative.

The increase in general and administrative expenses in fiscal year 2007 compared to fiscal year 2006 was primarily due to a) increased stock-based compensation expense of approximately \$1.1 million which was driven primarily by the issuance of new grants during fiscal year 2007 as well as increased stock prices during the year, b) \$400,000 increase in bad debt expense, which was primarily due to the fact that fiscal year 2006 bad debt expenses were unusually low as a result of significant improvements in our accounts receivable aging, and c) increase in strategic consulting services of approximately \$200,000 provided in support of our BIRT initiative. These increases were partially offset by approximately \$200,000 in lower accounting and legal fees.

We expect our general and administrative expenses to be in the range of 12% to 14% of total revenues for fiscal year 2009.

**Amortization of Other Intangibles**

| 2008 | Year Ended December 31,<br>2007 | 2006 | \$ Change<br>2007 to 2008 | % Change | \$ Change<br>2006 to 2007 | % Change |
|------|---------------------------------|------|---------------------------|----------|---------------------------|----------|
|------|---------------------------------|------|---------------------------|----------|---------------------------|----------|

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(dollars in thousands)

|       |       |       |
|-------|-------|-------|
| \$948 | \$948 | \$948 |
|-------|-------|-------|

(Percent of total revenue)

|    |    |    |
|----|----|----|
| 1% | 1% | 1% |
|----|----|----|

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In accordance with Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets ( SFAS 142 ), we perform a goodwill impairment test at least annually, which we complete on October 1 of each year. These annual impairment tests have not resulted in an impairment of recorded goodwill in fiscal 2008, 2007 or 2006.

For each year ended December 31, 2008, 2007 and 2006 we recorded \$948,000 for the amortization of other purchased intangibles. These costs represent the amortization of the intangibles associated with the acquisition of performancesoft on a straight-line basis.

We expect amortization expense of our existing other purchased intangible assets in fiscal year 2009 to decrease by approximately 28% as we fully depreciated the trademarks related to the performancesoft acquisition in fiscal year 2008.

**Restructuring charges**

| 2008                       | Year Ended December 31,<br>2007 | 2006 | \$ Change<br>2007 to 2008 | % Change | \$ Change<br>2006 to 2007 | % Change |
|----------------------------|---------------------------------|------|---------------------------|----------|---------------------------|----------|
| (dollars in thousands)     |                                 |      |                           |          |                           |          |
| \$1,506                    | \$1,686                         | \$16 | \$(180)                   | (11)%    | \$1,670                   | N/A      |
| (Percent of total revenue) |                                 |      |                           |          |                           |          |
| 1%                         | 1%                              |      |                           |          |                           |          |

During the first half of fiscal year 2007, we evaluated the consolidation of our facilities as a result of the performancesoft acquisition and determined that a \$297,000 facility-related restructuring charge was required. This charge was directly related to the consolidation of our three offices located in the United Kingdom into one office. These restructuring charges were accounted for in accordance with SFAS 146, which requires the recognition of costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan.

During the second half of fiscal year 2007, we recorded a restructuring charge related to the relocation of our headquarters facility from South San Francisco to San Mateo, California and the closure of our service facility in Iselin, New Jersey. These charges were primarily comprised of rent and operating expenses through the end of the lease term for the fully vacated portion of the South San Francisco facility, impairment of fixed assets and leasehold improvements considered abandoned, and relocation costs to the new facility. We also recorded restructuring charges for rent and operating expenses for the Iselin, New Jersey facility. As a result of these relocations, we recorded a total restructuring charge of approximately \$1.4 million in the second half of fiscal year 2007 in accordance with SFAS 146.

During the first half of fiscal year 2008, we recorded facility related restructuring charges totaling \$271,000. These charges primarily related to lease exit costs associated with our South San Francisco facility; the closure of one of the three floors in our Toronto, Canada facility and the consolidation of our Vienna, Virginia facilities into one location. We also incurred approximately \$132,000 in legal fees related to a previous restructuring which involved the terminations of former employees in one of our European subsidiaries.

In order to size the operations to meet the expected business and economic environment, we implemented a restructuring plan during the second half of the year to eliminate 46 positions held by Actuate employees primarily in North America. This restructuring impacted all functional

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areas. The reduction in force was completed in fiscal year 2008. The restructuring plan also resulted in the recognition of costs related to the consolidation of facilities, the cancellation of certain contracts and the write-off of fixed assets located at facilities that have been vacated.

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The following table summarizes the restructuring accrual activity for the fiscal years ended December 31, 2006, 2007 and 2008 (in thousands):

|  | Severance<br>& Benefits | Facility<br>Related | Total     |
|--|-------------------------|---------------------|-----------|
| Balance at December 31, 2005           | \$ 465                  | \$ 12,368           | \$ 12,833 |
| Restructuring charges                  | 45                      | (29)                | 16        |
| Cash payments                          | (89)                    | (3,450)             | (3,539)   |
| Changes in estimate                    | 29                      | 1                   | 30        |
| Rents collected on the sublease        |                         | 1,318               | 1,318     |
| Balance at December 31, 2006           | 450                     | 10,208              | 10,658    |
| Restructuring charges                  |                         | 1,686               | 1,686     |
| Cash payments                          |                         | (4,967)             | (4,967)   |
| Loss on disposal of assets             |                         | (244)               | (244)     |
| Changes in estimate                    | 14                      | (9)                 | 5         |
| Rents collected on the sublease        |                         | 1,669               | 1,669     |
| Balance at December 31, 2007           | 464                     | 8,343               | 8,807     |
| Restructuring charges                  | 1,101                   | 405                 | 1,506     |
| Cash payments                          | (1,027)                 | (4,666)             | (5,693)   |
| Changes in estimate                    | 23                      | (66)                | (43)      |
| Rents collected on the sublease        |                         | 1,721               | 1,721     |
|  | 561                     | 5,737               | 6,298     |
| Less: Current portion                  | (561)                   | (2,645)             | (3,206)   |
| Long-term balance at December 31, 2008 | \$                      | \$ 3,092            | \$ 3,092  |

**Interest and Other Income, Net**

| <i>(dollars in thousands)</i>                   | Year Ended December 31, |                 |                 | 2007 to 2008      |              | 2006 to 2007  |            |
|---|-------------------------|-----------------|-----------------|-------------------|--------------|---------------|------------|
|   | 2008                    | 2007            | 2006            | \$ Change         | % Change     | \$ Change     | % Change   |
| Interest income, net                            | \$ 2,116                | \$ 3,248        | \$ 2,005        | \$ (1,132)        | (35)%        | \$ 1,243      | 62%        |
| Foreign exchange gain/(loss)                    | (1,662)                 | (289)           | 93              | (1,373)           | (475)%       | (382)         | (411)%     |
| Other income, net                               | 331                     | 196             | 119             | 135               | 69%          | 77            | 65%        |
| <b>Total interest and other<br/>income, net</b> | <b>\$ 785</b>           | <b>\$ 3,155</b> | <b>\$ 2,217</b> | <b>\$ (2,370)</b> | <b>(75)%</b> | <b>\$ 938</b> | <b>42%</b> |
| Percentage of total revenue:                    |                         | 2%              | 2%              |                   |              |               |            |

Interest and other income, net, is comprised primarily of interest income earned by us on our cash and short-term investments, foreign currency exchange gains and losses, as well as other various charges or income which are not derived from our normal operations. For the year ended December 31, 2008, the decrease in interest and other income was due primarily to a lower weighted average interest rate on our investments resulting in a decrease in interest income. In addition, we recorded interest expense totaling approximately \$68,000 on the utilized portion of our credit facility with WFF. We also recorded commitment fees and capitalized debt issuance costs of approximately \$48,000 that are being amortized in accordance with SFAS 91, *Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases* over the term of the credit facility. We incurred foreign exchange losses that were primarily the result of sharp devaluations of the British Pound, the Euro and the U.S. Dollar currencies held by our Swiss subsidiary against the Swiss Franc mainly during

the first half of fiscal year 2008.



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The increase for fiscal year 2007 compared to fiscal year 2006 was primarily due to a higher weighted average interest rate received on our investments which resulted in approximately \$1.4 million in higher interest income, offset by accrued interest on the performance soft earnout obligation and translation losses due to a weaker U.S. Dollar compared to major foreign currencies in fiscal year 2007.

We expect interest and other income to decrease in fiscal year 2009 as we expect interest rates to remain low and we expect to incur a full year of interest charges under the credit facility signed with WFF in late fiscal year 2008.

**Benefit from Income Taxes**

| 2008      | Year Ended December 31,<br>2007 | 2006    | \$ Change<br>2007 to 2008 | % Change | \$ Change<br>2006 to 2007 | % Change |
|-----------|---------------------------------|---------|---------------------------|----------|---------------------------|----------|
|           |                                 |         | (dollars in thousands)    |          |                           |          |
| \$(1,318) | \$(863)                         | \$(974) | \$(455)                   | (53)%    | \$111                     | 11%      |

The benefit from income taxes represents primarily federal, state and foreign taxes as adjusted for the impact of operating losses utilized, income tax credits benefited and the reversal or establishment of reserves. The benefit for income taxes of \$1.3 million, \$863,000 and \$974,000 is based on pretax income of \$12.5 million, \$19.3 million, and \$12.8 million in fiscal years 2008, 2007 and 2006 respectively. The increase in the benefit for income taxes in fiscal year 2008 compared to fiscal year 2007 was primarily due to the tax benefit expected on the U.S. income tax returns for write off of the investment in and specific loans related to the tax liquidation of a foreign subsidiary. Additionally, there was a decrease in the provision for income taxes due to a \$1.3 million and \$6.8 million benefit from the decrease in the valuation allowance in 2008 and 2007, respectively. The decrease in the valuation allowance in fiscal year 2008 was the result of changes to our foreign deferred tax assets due to changes in foreign currency exchange rates, foreign tax rates and the expected utilization of specific deferred tax assets. Without the write off from the liquidation of the foreign subsidiary or the benefit from the decrease in the valuation allowance, there would have been an increase in the provision for income taxes in fiscal year 2008. The decrease in the valuation allowance in fiscal year 2007 was the result of management's determination that it was more likely than not that the deferred assets would be realized after weighing the applicable positive and negative evidence. Without the benefit from the valuation allowance, there would have been an increase in the provision for income taxes in fiscal year 2007 compared to 2006.

**Liquidity and Capital Resources**

This data should be read in conjunction with the Consolidated Statements of Cash Flows.

| (dollars in thousands)                 | Fiscal<br>2008 | % Change<br>2007 to 2008 | Fiscal<br>2007 | % Change<br>2006 to 2007 | Fiscal<br>2006 |
|--|----------------|--------------------------|----------------|--------------------------|----------------|
| Cash, cash equivalents and investments | \$ 58,441      | (15)%                    | \$ 68,415      | 14%                      | \$ 60,079      |
| Working capital                        | 20,701         | (62)%                    | 54,045         | 45%                      | 37,298         |
| Stockholders' equity                   | \$ 56,248      | (44)%                    | \$ 100,973     | 30%                      | \$ 77,810      |

Summary of our cash flows:

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|  | <b>Fiscal<br/>2008</b> | <b>Fiscal<br/>2007</b> | <b>Fiscal<br/>2006</b> |
|--|------------------------|------------------------|------------------------|
| Net cash provided by operating activities                              | \$ 29,535              | \$ 22,920              | \$ 22,134              |
| Net cash provided (used for) investing activities                      | 11,021                 | (26,558)               | (5,593)                |
| Net cash provided by (used for) financing activities                   | (35,739)               | (6,501)                | 1,558                  |
| Effect of foreign currency exchange rates on cash and cash equivalents | (1,513)                | 494                    | 524                    |
| Net increase (decrease) in cash and cash equivalents                   | \$ 3,304               | \$ (9,645)             | \$ 18,623              |

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The software industry is currently experiencing significant challenges, primarily due to a deteriorating macroeconomic environment, which is primarily characterized by diminished product demand. As a result of this downturn, some of our customers may face financial challenges in fiscal 2009. It is unclear when the macroeconomic environment may improve. We are seeing increasing pressures on our customers' Information Technology budgets, and therefore our customers are looking for more flexibility in the type of software and the timing of such purchases. The current economic downturn in our customers' industries has contributed to the reduction in our license revenues and could continue to adversely impact our future business, operating results and financial condition.

Facing uncertainty and cost pressures in their own businesses, some of our customers are waiting to purchase our products and are increasingly seeking purchasing terms and conditions that are less favorable to us. This trend has partially contributed to lower license revenues for fiscal 2008 and this trend may continue in fiscal 2009.

Our customers may also experience adverse changes in their business and, as a result, may delay or default on their payment obligations, file for bankruptcy or modify or cancel plans to license our products. If our customers are not successful in generating sufficient revenue or are precluded from securing financing, they may not be able to pay, or may delay payment of, accounts receivable that are owed to us, although these obligations are generally not cancelable. Additionally, our customers may seek to renegotiate existing contractual commitments. Though we have not yet experienced any unusual levels of defaults, any material payment default by our customers or significant reductions in existing contractual commitments could have a material adverse effect on our financial condition and operating results.

### ***Fiscal 2008***

Cash provided by operations is dependent primarily upon collection of monies from our license and maintenance agreements which consist of software fees and for ongoing support and unspecified product updates. Our maintenance revenues have remained robust over the past five years and have increased from 43% of total revenues or \$45.4 million in fiscal year 2004 to 59% of total revenues or \$76.7 million in fiscal year 2008. Historically, the maintenance renewal rates have remained strong. Based on these factors, we believe that future proceeds from the maintenance renewals will be the primary source of our operating cash flows.

In order to fund our on-going operations, we rely heavily on timely collections of our revenue stream. We therefore continue to place emphasis on our collection efforts as indicated by reductions in the days sales outstanding ( DSO ) in trade receivables which decreased from 91 days at the end of fiscal year 2007 to 78 days at the end of fiscal year 2008. We also continue to closely monitor the credit quality and payment history of our existing and new customers to better identify and minimize, in advance, the risk of our customers' potential inability to make required payments.

The primary uses of cash from operations consist of salaries, commissions and bonuses paid to our employees. These costs combined, accounted for approximately 55% of our total operating expenses for both fiscal years 2008 and 2007. We pay our employees on a semi-monthly basis and we generally pay our vendors within one month from receiving an invoice for services rendered. We are also contractually committed to pay rent and facility related charges in support of our worldwide operations. As of December 31, 2008, we remained contractually committed to \$15.5 million in net operating lease obligations related to our worldwide facilities and \$2.5 million in other operating and purchase obligations with our vendors. The majority of these obligations are due within the next five years.

Despite a challenging economic environment, we remain focused on increasing our cashflows from operations and improving our operating margins and profitability. The current economic uncertainties have reduced our visibility in forecasting our future license revenues, from which we largely depend on achieving these goals. As visibility associated with these future license revenues remain limited, we may, from time to

time, rely on cost cutting and swift resizing measures to achieve our objective of growth in operating cashflows, operating margins and profitability.

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Our capital expenditures for the past two years have primarily consisted of leasehold improvements related to our headquarter facility in San Mateo, California and software costs associated with our internal customer portal project. We currently do not foresee material cash outlays associated with capital projects in the coming fiscal year and expect to see lowered cash payments associated with these activities.

In early November of 2008, we entered into a revolving Credit Agreement with Wells Fargo Foothill and secured a revolving line of credit in the principal amount of up to \$50.0 million. During fourth quarter of fiscal year 2008, we used \$30.0 million of our cash along with \$30.0 million of funds available through this credit facility to complete a \$60.0 million common stock buy back. As of December 31, 2008, we owed \$30.0 million on the credit facility. Unpaid charges related to the issuance of the credit facility include legal and closing fees totaling approximately \$760,000 at December 31, 2008. Of these total fees, approximately \$630,000 will be payable in fiscal year 2009 and the remainder in fiscal year 2011. We are also obligated to make monthly interest payments and expect to pay approximately \$1.1 million in interest on the outstanding \$30.0 million loan balance annually. We expect that these payments will be made through fiscal year 2012 and total approximately \$4.5 million. These payments may fluctuate depending on the outstanding principal balance and changes in interest rates. We currently have full access to the remaining \$20.0 million of unused balance on the credit line and may use this amount to fund future operations or potential acquisitions. Because of our indebtedness, a significant portion of our cash flow from operations is and will be required for debt service. Our levels of debt could have negative consequences for us. It should be noted that:

a substantial portion of our cash flow is, and will be, dedicated to debt service and is not, and will not be, available for other purposes;

our ability to obtain additional financing for working capital, capital expenditures, acquisitions and general corporate or other purposes may be impaired in the future;

our borrowings are, and will be, at variable rates of interest, which may expose us to the risk of increases in interest rates; and

our level of indebtedness could make us more vulnerable to economic downturns, limit our ability to withstand competitive pressures and reduce our flexibility in responding to changing business and economic conditions.

We believe that cash flows from operations will be sufficient to meet our current debt service requirements for interest and any required prepayments under the Credit Agreement. However, if such cash flow is not sufficient, we may be required to issue additional debt or equity securities, refinance our obligations, or take other actions in order to make such scheduled payments. We cannot be sure that we would be able to effect any such transactions on favorable terms, if at all and failure to do so may cause an event of default under the Credit Agreement, which will have a material adverse effect on our business, operating results and financial conditions.

Similarly, the Credit Agreement includes limitations on the Company's ability to incur debt, grant liens, make acquisitions, make certain restricted payments such as dividend payments, and dispose of assets. The events of default under the Credit Agreement include payment defaults, cross defaults with certain other indebtedness, breaches of covenants and bankruptcy events. In the case of a continuing event of default, the lenders under the Credit Agreement may, among other remedies, eliminate their commitments to make credit available, declare due all unpaid principal amounts outstanding, and require cash collateral for any letter of credit obligations and foreclose on all collateral which will have a material adverse effect on our business, operating results and financial conditions.

In November 2008, we elected to participate in a rights offering by UBS, our investment broker, which provides us with the right (the Put Option) to sell UBS \$16.5 million of our ARS portfolio at par value, which we purchased through UBS, at any time during a two-year sale period beginning June 30, 2010. We classified this portion of our ARS portfolio as a non-current security. This treatment has resulted in a significant decrease to our cash, cash equivalents and short-term investments as well as our working capital. Despite these decreases,



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we believe that participation in this offering allows us further liquidity and access to available cash which enhances our operating position especially during the current period of economic uncertainty.

We hold our cash, cash equivalents and investments primarily in the United States, Switzerland, and Singapore. As of December 31, 2008, we held an aggregate of approximately \$44.0 million in cash, cash equivalents and investments in the United States and an aggregate of \$14.4 million in foreign accounts. Funds in foreign accounts are primarily generated from revenue outside North America and are used to fund oversea operations.

We expect cash provided by operating activities to fluctuate in future periods as a result of a number of factors, including timing of our billings and collections, our operating results, the timing and amount of tax and other liability payments and cash used in any future acquisitions.

### ***Fiscal 2007***

Cash provided by operating activities for fiscal year 2007, of \$22.9 million was primarily comprised of net income, net of non-cash related expenses. The primary working capital source of cash was an increase in deferred revenue due primarily to continued increase in maintenance and support obligations. We also experienced an increase in deferred rent due to six months of rent holiday extending through March of 2008 and approximately \$600,000 of lease incentives associated with our headquarter facility in San Mateo, California. Working capital uses of cash included payments made on restructured facilities. Our primary source of operating cash flows is the collection of accounts receivable from our customers, including maintenance which is typically billed annually in advance. Our trade receivables increased by approximately 24% due to increased revenue and increase in the days sales outstanding ( DSO ) in trade receivables from 82 days at the end of fiscal year 2006 to 91 days at the end of fiscal year 2007. We also experienced a decrease in accrued restructuring because of payments made during fiscal year 2007; please refer to Note 11 of the Notes to Consolidated Financial Statements for more information.

Cash used in investing activities was \$26.6 million for the year ended December 31, 2007 compared to \$5.6 million used in fiscal year 2006. The primary uses of cash during fiscal year 2007 were purchases of short-term investments offset in part by sales and maturities of short-term investments. We purchased property and equipment totaling \$2.9 million in fiscal year 2007 as compared to approximately \$1.3 million in fiscal year 2006. The purchases consisted primarily of leasehold improvements, computer equipment and software, and was primarily related to costs associated with the relocation to our new headquarters during the third quarter of fiscal year 2007. We also paid a final payment totaling approximately \$5.6 million for the performancesoft earnout obligation in the fourth quarter of fiscal year 2007.

Cash used in financing activities was \$6.5 million for the year ended December 31, 2007 compared to \$1.6 million provided by financing activities the same period in fiscal year 2006. This increase in cash used was primarily the result of payments totaling \$20.4 million in fiscal year 2007 to repurchase approximately 3.1 million shares of common stock in the open market, offset by higher proceeds from the issuance of common stock to our employees and associated tax benefits during fiscal year 2007.

### ***Fiscal 2006***

Cash provided by operating activities for fiscal year 2006, of \$22.1 million was primarily comprised of net income, net of non-cash related expenses. The primary working capital source of cash was an increase in deferred revenue due primarily to an increase in maintenance and support obligations. Accrued compensation increased due to increased sales resulting in higher year-end commission and bonus liabilities which

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were not paid out until January 2007. Working capital uses of cash included payments made on restructured facilities. Our operating cash flows are also impacted by the timing of payments to our vendors for accounts payable and other liabilities. We generally pay our vendors and service providers in accordance with the invoice terms and conditions. Our



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primary source of operating cash flows is the collection of accounts receivable from our customers, including maintenance which is typically billed annually in advance. Our trade receivables increased by approximately 17%. Days sales outstanding ( DSO ), calculated based on revenue for the most recent quarter and accounts receivable as of the balance sheet date, decreased to 82 days as of December 31, 2006 from 85 days as of December 31, 2005. The slight decrease in DSO despite a 17% increase in accounts receivable is attributable to higher revenue during the quarter. We also experienced a decrease in accrued restructuring because of payments made during fiscal year 2006; please refer to Note 11 of the Notes to Consolidated Financial Statements for more information.

Cash used in investing activities was \$5.6 million for the year ended December 31, 2006 compared to \$3.2 million used in fiscal year 2005. The primary driver for this change was the acquisition of performance software in fiscal year 2006, which resulted in a net cash payment of approximately \$15.7 million. Due to this acquisition, we liquidated our investments by a total of approximately \$13.2 million to accommodate the funding of this transaction. In addition, during February 2006, a minority shareholder of Actuate Japan notified us that it wished to exercise its rights to put its equity interest in Actuate Japan to us and as a result we paid approximately \$354,000 for this minority interest during the first quarter of 2006.

Cash provided by financing activities was approximately \$1.6 million for the year ended December 31, 2006 compared to \$5.1 million used in fiscal year 2005. The change in cash provided the result of higher proceeds from the issuance of common stock to our employees and associated tax benefits, offset by lower level of stock repurchases.

The table below sets forth information regarding repurchases of Actuate common stock by Actuate during the following fiscal years along with the associated costs (in thousands):

|                              | <b>Year ended December 31,</b>           |             |             |
|------------------------------|--|-------------|-------------|
|                              | <b>2008</b>                              | <b>2007</b> | <b>2006</b> |
|                              | <b>(In thousands, except share data)</b> |             |             |
| Number of shares repurchased | 19,781,417                               | 3,059,149   | 1,137,698   |
| Cost of shares repurchased   | \$ 72,675                                | \$ 20,423   | \$ 4,610    |

We believe that our current cash balances, funds available under our credit facility, and cash generated from operations will be sufficient to meet our working capital and capital expenditure requirements for at least the next twelve months. Thereafter, if cash generated from operations is insufficient to satisfy our liquidity requirements, we may find it necessary to sell additional equity, or obtain additional credit facilities. The sale of additional equity could result in additional dilution to our current stockholders. A portion of our cash may be used to acquire or invest in complementary businesses, including the acquisition of the minority interest in our 88% owned subsidiary in Japan, or complementary products or to obtain the right to use complementary technologies.

On October 24, 2007, our Board of Directors authorized an acceleration of our existing stock repurchase program. As of October 24, 2007, the Company was authorized to repurchase shares in an amount not to exceed \$6.3 million per quarter, and the cumulative amount not to exceed \$50.0 million over a two year period.

On February 4, 2008, our Board of Directors authorized a further acceleration of our existing stock repurchase program which allowed for the repurchase of approximately \$10.0 million of shares in the first quarter of fiscal year 2008. From the end of fiscal year 2007 through August 2008, the Company repurchased a total of 2.6 million shares for a total of approximately \$12.7 million in the open market under this stock repurchase plan.

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On November 3, 2008, we announced our intention to commence a modified Dutch auction tender offer to purchase up to \$60.0 million worth of our common stock, at a price per share not less than \$3.15 and not greater than \$3.50. On December 29, 2008, we completed the tender offer and purchase and paid \$3.50 per share for

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17,142,857 of these shares at a total cost of \$60.0 million. This repurchase was completed in fiscal year 2008 and funded by \$30.0 million in cash and an additional \$30.0 million drawn under the credit facility. We have subsequently suspended our stock repurchase program.

**Contractual Obligations and Commercial Commitments.**

In November 2008, the Company entered into a four year revolving line of credit agreement ( Credit Agreement ) with Wells Fargo Foothill, LLC ( Wells Fargo ). The Credit Agreement was effective as of November 3, 2008 and allows for cash borrowings and letters of credit under a secured revolving credit facility of up to a maximum of \$50.0 million, but not to exceed 80% of the Company s trailing four quarters of recurring maintenance revenue. Interest is based on a floating rate plus an applicable margin based on the outstanding balance of the amount drawn under the Credit Agreement. The floating rate is determined at the Company s election and may either be (i) London Interbank Offered Rate ( LIBOR ) or (ii) the greater of the Federal Funds Rate plus an applicable margin and the Prime Rate. If the Company s usage of the credit line exceeds 80% of its trailing four quarters of recurring maintenance revenue, or if the sum of available funds under the Credit Agreement plus available cash is less than \$10.0 million, the Company is required to meet certain minimum income targets and be subject to a limit on annual capital expenditures. The Company is required to make interest payments and pay an unused commitment fee on a monthly basis. The Credit Agreement also requires that the Company pay a closing fee based on a percentage of the overall available facility. These costs along with related legal costs are classified as current assets in the Company s Consolidated Balance Sheet at December 31, 2008 if payable within one year or non-current assets if payable beyond one year.

The Company reached the end of its lease term on its previous corporate headquarters located at 701 Gateway, in South San Francisco in February 2008. In anticipation of this event, on June 1, 2007, the Company entered into a five year sublease agreement with Oracle Corporation for approximately 83,000 square feet of office space in the Bridgepointe Campus in San Mateo, California. This lease is operating in nature, commenced on August 1, 2007 and ends on July 31, 2012. In addition, the lease provided for approximately nine months of free rent (rent holiday) and approximately \$600,000 in landlord incentives to be applied by Actuate towards construction of improvements. The incentives were applied to leasehold improvements completed during the fourth quarter of fiscal year 2007.

As of December 31, 2008, Actuate pledged \$655,000 of restricted cash, as collateral for a standby letter of credit that guarantees its contractual obligations relating to its sublease agreement for its new corporate headquarter facilities located at the Bridgepointe Campus in San Mateo, California. This restricted cash is classified as Other Assets in the accompanying Consolidated Balance Sheet.

The following table summarizes our contractual obligations as of December 31, 2008 (in thousands):

|                                   | Total            | Less than<br>1 year | 1 3<br>years     | 3 5<br>years    | Thereafter    |
|-----------------------------------|------------------|---------------------|------------------|-----------------|---------------|
| Obligations:                      |                  |                     |                  |                 |               |
| Operating leases (1)              | \$ 15,526        | \$ 5,256            | \$ 7,616         | \$ 2,180        | \$ 474        |
| Purchase obligations (2)          | 2,545            | 2,440               | 90               | 10              | 5             |
| Interest and loan obligations (3) | 4,879            | 1,376               | 2,377            | 1,126           |               |
| Obligations under FIN 48 (4)      | 1,660            |                     | 1,660            |                 |               |
| <b>Total</b>                      | <b>\$ 24,610</b> | <b>\$ 9,072</b>     | <b>\$ 11,743</b> | <b>\$ 3,316</b> | <b>\$ 479</b> |

(1)

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Our future contractual obligations include minimum lease payments under operating leases at December 31, 2008, net of contractual sublease proceeds. Of the remaining net future minimum lease payments, approximately \$4.5 million is included in restructuring liabilities on the Company's Consolidated Balance Sheet as of December 31, 2008.

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- (2) Purchase obligations represent an estimate of all open purchase orders and contractual obligations in the ordinary course of business for which we have not received the goods or services as of December 31, 2008. Although open purchase orders are considered enforceable and legally binding, the terms generally allow us the option to cancel, reschedule and adjust our requirements based on our business needs prior to the delivery of goods or performance of services.
- (3) Estimated interest and commitment fees related to the revolving line of Credit Agreement with Wells Fargo Foothill.
- (4) Represents the tax liability associated with the calculation of uncertain tax positions. See FIN 48 discussion in Note 11 of our Notes to Consolidated Financial Statements.

***Investment in Actuate Japan.*** The minority shareholders of Actuate Japan have the non-expiring option to put their equity interest ( Minority Interest ) in Actuate Japan to the Company and the Company has the option to call the Minority Interest. The Minority Interest as of December 31, 2008 was approximately 12% of the total equity interest. If the Minority Interest Shareholder chose to put these remaining shares to the Company, Actuate would be required to pay approximately \$584,000 to purchase these shares. The Company will record a liability, if any, at the time that the put or call is probable of being exercised. Should an indicator arise that the Minority Interest has declined in value below the exercise price of the put and call option, the Company would conclude that exercise is probable at that point in time and recognize a liability for the intrinsic value of the option. The Company performs a periodic review of the value of the Minority Interest. This review may include assumptions regarding projected future cash flows and discount rates. Variances in these assumptions could have a significant impact on the Company's conclusion as to whether it is necessary to record a liability. As of December 31, 2008, the Company concluded that it was not necessary to record a liability. The Company consolidated 100% of the operating results of Actuate Japan and all investments in the subsidiary are eliminated in consolidation. As of the date of this filing, the remaining minority shareholder has not notified the Company of any intent to exercise its put option.

***Indemnification.*** In the normal course of business, we provide customers with indemnification provisions of varying scope against claims of intellectual property infringement by third parties arising from the use of our products. Historically, costs related to these indemnification provisions have not been significant and we are unable to estimate the maximum potential impact of these indemnification provisions on our future results of operations.

**Recent Accounting Pronouncements**

*See Note 1 of our Notes to Consolidated Financial Statements for information regarding the effect of new accounting pronouncements on our Consolidated Financial Statements.*

**Table of Contents****ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

*Market Risk.* Market risk represents the risk of loss that may impact our financial position due to adverse changes in financial market prices and rates. Our market risk exposure is primarily a result of credit risk, fluctuations in interest rates and foreign exchange rates.

*Foreign Currency Exchange Risk.* During fiscal years 2008, 2007 and 2006 we derived 28%, 27% and 25%, respectively, of our total revenues from sales outside of North America. We face exposure to market risk on the related receivables with respect to fluctuations in the relative value of currencies. Our international revenues and expenses are denominated in foreign currencies, principally the Euro and the British Pound Sterling. The functional currency of each of our foreign subsidiaries is the local currency. We are also exposed to foreign exchange rate fluctuations as the financial results of foreign subsidiaries are translated into U.S. dollars in consolidation. As exchange rates vary, transaction gains and losses may vary from expectations and adversely impact overall expected profitability. Our losses due to foreign exchange rate fluctuations were approximately \$1.7 million in fiscal year 2008 compared to losses of approximately \$289,000 during fiscal year 2007 and gains of approximately \$93,000 in fiscal year 2006.

*Interest Rate Risk.* The primary objective of our investment activities is to preserve principal while at the same time maximizing yields without significantly increasing risk. To achieve this objective, we typically invest in high quality debt securities. Due to the nature of our investments, we believe that there is no material risk exposure. We are exposed to market risks related to fluctuations in interest rates on variable rate debt under our revolving credit facility. We have drawn \$30.0 million on the \$50.0 million Credit Facility as of December 31, 2008 and expect to pay approximately \$1.1 million in interest annually through fiscal year 2012. The interest may increase significantly if we decide to draw on the remaining \$20.0 million balance under this arrangement.

A sensitivity analysis was performed on the outstanding portion of our debt obligation as of December 31, 2008. The analysis is based on an estimate of the hypothetical changes in annual interest expense that would result from an immediate increase/decrease in interest rates.

The analysis is shown as of December 31, 2008:

| Change in interest expense (in thousands) |       |       |       |       |       |
|---|-------|-------|-------|-------|-------|
| -1.5%                                     | -1.0% | -0.5% | +0.5% | +1.0% | +1.5% |
| (450)                                     | (300) | (150) | 150   | 300   | 450   |

*Credit Risk.* Financial instruments that potentially subject us to concentrations of credit risk consist primarily of cash and cash equivalents, investments in marketable securities, and trade accounts receivable. We have policies that limit investments in investment grade securities and the amount of credit exposure to any one issuer. We perform ongoing credit evaluations of our customers and maintain an allowance for potential credit losses. We do not require collateral or other security to support customer receivables. Our credit risk is also mitigated because our customer base is diversified by geography and no single customer has accounted for more than 10% of our consolidated revenue on an annual basis. We generally do not use foreign exchange contracts to hedge the risk in receivables denominated in foreign currencies. We do not hold or issue derivative financial instruments for trading or speculative purposes.

Our investments portfolio includes ARS. Prior to February 2008, these securities historically traded at par and are callable at par at the option of the issuer. Interest is typically paid at the end of each auction period. At the end of fiscal 2008, all of the long-term ARS we held were AAA/Aaa rated with most collateralized by student loans guaranteed by the U.S. Government under the Federal Family Education Loan Program. Until fiscal 2008, the auction rate securities market was highly liquid. During Fiscal year 2008, a substantial number of auctions failed, meaning that

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there was not enough demand to sell the entire issue of the securities that holders desired to sell at auction. The immediate effect of a failed auction is that certain holders cannot sell the securities at auction and the interest or dividend rate on the security generally resets to a maximum auction rate. In the case of

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a failed auction, with respect to the ARS held by us, the ARS is deemed not currently liquid. In the case of funds invested by us in ARS which are the subject of a failed auction, we may not be able to access the funds prior to maturity without a loss of principal, unless a future auction on these investments is successful or the issuer calls the security pursuant to a mandatory tender or redemption.

In November 2008, we elected to participate in a rights offering by UBS, our investment broker, which provides us with rights (the Put Option) to sell UBS \$16.5 million of our ARS portfolio at par value, at any time during a two-year sale period beginning June 30, 2010. By electing to participate in the rights offering, we granted UBS the right, exercisable at any time prior to June 30, 2010 or during the two-year sale period, to purchase or cause the sale of our ARS (the Call Right). UBS has stated that it will only exercise the Call Right for the purpose of restructurings, dispositions or other solutions that will provide their clients with par value for their ARS. UBS has agreed to pay their clients the par value of their ARS within one day of settlement of any Call Right transaction. Notwithstanding the Call Right, we are permitted to sell ARS to parties other than UBS, in which case the Put Option attached to the ARS that are sold would be extinguished. We classified the Put Option as a non-current security. As such, we recorded a net realized loss of approximately \$84,000 related to the difference between the gain recognized on the Put Option and the realized loss on the \$16.5 million (par value) portion of our ARS portfolio.

Additional information regarding our investment portfolio is detailed in Note 4 to the Consolidated Financial Statements for the year ended December 31, 2008.

We do not believe that future market equity or interest rate risks related to our marketable investments or debt obligations will have a material impact on our results of operations.

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

The financial statements and supplementary data required by this Item 8 are listed in Item 14(a)(1) and begin at page F-1 of this report.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURES**

None.

**ITEM 9A. CONTROLS AND PROCEDURES**

**(a) Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures**

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of our disclosure controls and procedures, as of the end of the period covered under this report. Based on the evaluation of the effectiveness of our disclosure controls and procedures, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.



**(b) Management's Report on Internal Control Over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

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Our Annual Report on Form 10-K for the fiscal year ended December 31, 2007 disclosed a material weakness relating to accounting for income taxes. During the fiscal year of 2008, we modified our internal control over financial reporting with respect to accounting for income taxes. We use a third-party tax service provider to complete the preparation, reconciliation and analysis of our income tax provision and income tax related accounts and modified our review procedures over schedules, supporting our income tax provision. As a result of these actions, management has concluded that Actuate has remediated the material weakness as of the end of the period covered by this report.

In making its assessment of internal control over financial reporting, management used the criteria issued by the Committee of Sponsoring Organizations of the Treadway Commission, or COSO, In *Internal Control-Integrated Framework*. Based on our assessment we believe that our internal control over financial reporting is effective.

**(c) Changes in Internal Control Over Financial Reporting**

There were no changes in our internal control over financial reporting, other than the remediation of the material weakness discussed above, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting during the quarter ended December 31, 2008.

**ITEM 9B. OTHER INFORMATION**

None.

**Table of Contents****PART III****ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE****Actuate Executive Officers**

Actuate's executive officers as of February 10, 2009 are as follows:

| <b>Name</b>           | <b>Offices</b>  |
|-----------------------|---|
| Nicolas C. Nierenberg | Chairman of the Board and Chief Architect                         |
| Peter I. Cittadini    | Director, President and Chief Executive Officer                   |
| Daniel A. Gaudreau    | Senior Vice President, Operations and Chief Financial Officer     |
| Mark A. Coggins       | Senior Vice President, Engineering                                |
| N. Nobby Akiha        | Senior Vice President, Marketing                                  |
| Thomas E. McKeever    | Senior Vice President, General Counsel and, Corporate Development |
| Bernard Skomra        | Vice President and General Manager, Customer Service Group        |

*Nicolas C. Nierenberg*, 52, has been Chairman of the Board of Directors since he co-founded Actuate in November 1993 and became our Chief Architect in August 2000. Mr. Nierenberg was Chief Executive Officer of Actuate from November 1993 until August 2000 and President from November 1993 until October 1998. Prior to founding Actuate, from April 1993 to November 1993, Mr. Nierenberg worked as a consultant for Accel Partners, a venture capital firm, evaluating investment opportunities in the enterprise software market. Mr. Nierenberg co-founded Unify Corporation, which develops and markets relational database development tools. Mr. Nierenberg held a number of positions at Unify including, Chairman of the Board of Directors, Chief Executive Officer, President, Vice President, Engineering and Chief Technical Officer. Mr. Nierenberg is currently a director for privately held company AwarePoint, Inc., and is a member of the Board of Trustees for The Burnham Institute, a non-profit organization.

*Peter I. Cittadini*, 53, has been Chief Executive Officer of Actuate since August 2000 and has been the President of Actuate since October 1998. Mr. Cittadini was also Actuate's Chief Operating Officer from October 1998 until August 2000 and served as Actuate's Executive Vice President from January 1995 to October 1998. From 1992 to 1995, Mr. Cittadini held a number of positions at Interleaf, Inc., an enterprise software publishing company, including Senior Vice President of Worldwide Operations responsible for worldwide sales, marketing, customer support and services. From 1985 to 1991, Mr. Cittadini held a number of positions at Oracle Corporation, including Vice President, Northeast Division.

*Daniel A. Gaudreau*, 61, has been Senior Vice President, Operations and Chief Financial Officer since January 1999 and served as Vice President, Finance and Administration and Chief Financial Officer from February 1997 to January 1999. From January 1994 to February 1997, Mr. Gaudreau served as Vice President, Finance and Chief Financial Officer of Plantronics, Inc., a publicly traded telephone headset manufacturing company, where he was responsible for all financial and administrative operations. From January 1990 to January 1994, Mr. Gaudreau was Vice President, Finance and Chief Financial Officer at Ready Systems, an operating systems software company. Prior to that, Mr. Gaudreau spent two years at Apple Computer as the Controller of Fremont Manufacturing Operations, prior to which he spent 18 years at General Electric where he held various financial management positions.

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*Mark A. Coggins*, 51, has been Senior Vice President, Engineering since October 2003. From May 2001 to April 2003, Mr. Coggins was Vice President, Engineering at Verisign, a publicly traded security software company. From January 1999 to April 2001, Mr. Coggins was Vice President, Products at ShortCycles, a CRM software company. Prior to that, Mr. Coggins held positions in engineering and marketing management at Netscape Communications, Interactive Development Environments and Hewlett Packard.

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*N. Nobby Akiha*, 51, has been Senior Vice President, Marketing since June 2006 and served as Vice President of Marketing from August 2000. From August 1994 to July 2000, Mr. Akiha was Vice President, Marketing and Business Development at Inference Corporation. From October 1993 to July 1994, Mr. Akiha was a Senior Consultant at Regis McKenna, Inc. Prior to that, Mr. Akiha was Director of Marketing Communications at Interactive Development Environments and a Group Product Manager at Oracle Corporation.

*Thomas E. McKeever*, 41, has been Senior Vice President, General Counsel, Corporate Development and Secretary since January 2009 and served as General Counsel, Vice President Corporate Development and Secretary since May 2006. Mr. McKeever was formerly with Sun Microsystems, Inc., was an associate in several law firms in the San Francisco Bay Area and served as a law clerk to the Honorable Lawrence T. Lydick of the United States District Court for the Central District of California (Orange County).

*Bernard Skomra*, 47, has been Vice President and General Manager, Customer Service Group since December 2007. From April 2006 to November 2007, Mr. Skomra was the Senior Vice President of World Wide Field Operations at BigFix, Inc. Prior to BigFix, Inc., Mr. Skomra was the Chief Executive Officer, President and Founder of Apacheta Corporation from 2002 to 2006, and was the Vice President of North American Field Operations at Portal Software from April 1997 to February 2001. Prior to 1997, Mr. Skomra held sales and general management positions at Oracle, IBM and General Electric.

## **Adoption of Code of Ethics**

Actuate has adopted a Code of Ethics and Business Conduct (the Code) applicable to all of its Board members, employees and executive officers, including its Chief Executive Officer (Principal Executive Officer), Chief Financial Officer (Principal Financial and Accounting Officer) and Controller. We have made the Code available under the investors/corporate governance section of our website at [www.actuate.com](http://www.actuate.com).

We intend to satisfy the disclosure requirement under Item 10 of Form 8-K regarding (i) any amendments to the Code, or (ii) any waivers under the Code relating to our Chief Executive Officer or Chief Financial Officer, by posting such information under the investors/corporate governance section of our website at [www.actuate.com](http://www.actuate.com).

## **Stockholder Proposals**

As of December 31, 2008, there has been no material change to the policies and procedures by which the stockholders of the Company may recommend director candidates. As disclosed previously in Form 8-K filed on February 3, 2009, the Company amended and restated its Bylaws on January 30, 2009. A summary of the key changes made to the Bylaws follows:

*Advance Notice Provisions.* Procedures for stockholders to propose business or nominations for election of directors to be considered at annual or special meetings, which are referred to as advance notice provisions, have been added to the Bylaws to, among other things, change the procedure by which stockholders may nominate directors. The new advance notice provisions of the Bylaws, among other things:

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require stockholders to provide advance notice of stockholder proposals or nominations of directors at an annual meeting, and such advance notice must be delivered to the principal executive office of the Company not less than 90 days nor more than 120 days prior to the first anniversary of the preceding year's annual meeting, subject to certain conditions;

provide that the procedures and requirement set forth in the advance notice provisions are the exclusive means for a stockholder to propose business, including nomination of candidates to be elected as directors of the Company, at a stockholder meeting, other than matters properly brought under Rule 14a-8 of the Securities Exchange Act of 1934, as amended (the Exchange Act );

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require stockholders making proposals or nominations to disclose, among other things, all ownership interests, hedges, short positions, economic and profit incentives and rights to vote with respect to any security of the Company;

require stockholders nominating directors to disclose the same information about a proposed director nominee that would be required if such director nominee were submitting a proposal and any material relationships between the stockholder proponents and their affiliates, on the one hand, and the director nominees and their affiliates, on the other hand, and to respond to a questionnaire concerning the director nominee's background and qualifications;

require stockholders making proposals or nominations to provide a reasonably detailed description of all agreements, arrangements and understandings between proposing persons and other stockholders of the Company in connection with the proposed business or nomination; and

require that the additional disclosures discussed above be updated and supplemented, if necessary, so as to be accurate as of the record date for a meeting and as of shortly prior to the meeting;

These advance notice provisions were effective as of January 30, 2009 and stockholders must comply with such provisions for the 2009 annual meeting of stockholders of the Company to be held on May 21, 2009.

*Calling Special Meetings of Stockholders.* The procedure for calling a special meeting of stockholders have been revised to provide that only the Chairman, Chief Executive Officer or the Board Of Directors of the Company may call a special meeting of stockholders.

*Quorum at Stockholder Meetings.* The Bylaws change the threshold for achieving a quorum at a stockholders meeting such that holders of a majority in number of total outstanding shares of stock of the Company entitled to vote at such meeting, present in person or represented by proxy, constitute a quorum unless otherwise provided by law, our Certificate of Incorporation or our Bylaws.

*Voting Requirement at Stockholder Meetings.* The Bylaws change the voting requirement at stockholders meeting to provide that any matter other than election of directors shall be decided by the affirmative vote of a majority of the shares present in person or represented by proxy and entitled to vote thereon, except when a different vote is required by law, certificate of incorporation or bylaws.

*Officers.* The Bylaws revise provisions relating to the authority, responsibilities and status of officers of the Company.

*Indemnification.* The Amended and Restated Bylaws eliminate the indemnification provision covering directors.

## **ITEM 11. EXECUTIVE COMPENSATION**

The information required by this Item regarding executive compensation is incorporated herein by reference from the section entitled "Executive Compensation and Related Information" of the Proxy Statement.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

The information required by this Item regarding security ownership of certain beneficial owners and management is incorporated herein by reference from the section entitled "Security Ownership of Certain Beneficial Owners and Management" of the Proxy Statement.



**Table of Contents****Equity Compensation Plan Information**

Information about our equity compensation plans at December 31, 2008 that were either approved or not approved by stockholders was as follows:

| <b>Plan Category</b>                                       | <b>Number of securities to be issued upon exercise of outstanding options</b> | <b>Weighted average exercise price of outstanding options</b> | <b>Number of available securities remaining for future issuance</b> |
|--|---|---|---|
| Equity compensation plans approved by stockholders (1)     | 16,249,357  | \$ 3.89   | 16,322,313  |
| Equity compensation plans not approved by stockholders (2) | 627,256   | \$ 1.94   | 714,600   |
| <b>Total</b>   | <b>16,876,613</b>   | <b>\$ 3.82</b>  | <b>17,036,913</b>   |

- (1) Consists of five plans: our Amended and Restated 1998 Equity Incentive Plan, Tidestone 1998 Incentive Stock Option Plan, Tidestone Non-Qualified Stock Option Plan of 1999, 1998 Non-Employee Directors Option Plan, and the Amended and Restated 1998 Employee Stock Purchase Plan. As of January 1 of each year, the number of shares reserved for issuance under the Amended and Restated 1998 Equity Incentive Plan automatically increases by the lesser of (i) 5% of the total number of shares of common stock outstanding and (ii) 2,800,000 shares.
- (2) Consists of one plan: our 2001 Supplemental Stock Option Plan. See Note 9 of the Notes to Consolidated Financial Statements.

**ITEM 13. CERTAIN RELATIONSHIPS, RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE**

The information required by this Item regarding certain relationships and related transactions is incorporated herein by reference from the sections entitled "Certain Relationships, Related Transactions and Director Independence" of the Proxy Statement.

**ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES**

The information required by this Item regarding principal accounting fees and services is incorporated herein by reference from the section entitled "Principal Accounting Fees and Services" of the Proxy Statement.

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**PART IV**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

**(a)(1) Financial Statements**

See Index on Page F-1.

**(a)(2) Financial Statement Schedules**

Schedule II Valuation and Qualifying Accounts.

Other schedules have been omitted because the information required to be set forth therein is not applicable or is readily available in the financial statements or notes thereto.

**(a)(3) Exhibits**

| <b>Exhibit</b> |  |   |
|----------------|--|---|
| No.            |  | Description   |
| 2.1 (8)        |  | Share Purchase Agreement, dated as of January 5, 2006, by and among Actuate Corporation, performancesoft, Inc., the shareholders of performancesoft, Inc. and Michael Tipping, as shareholder s representative as amended by the Agreement and Notice dated October 11, 2006. |
| 3.1 (4)        |  | Form of Third Amended and Restated Certificate of Incorporation.  |
| 3.2 (10)       |  | Form of Amended and Restated Bylaws of the Registrant.  |
| 4.2 (2)        |  | Specimen Common Stock Certificate.  |
| 10.1 (11)      |  | Form of Indemnification Agreement.  |
| 10.2 (1)+      |  | 1994 Stock Option Plan, as amended.   |
| 10.3 (1)+      |  | Amended and Restated 1998 Equity Incentive Plan.  |
| 10.4 (1)+      |  | Amended and Restated 1998 Employee Stock Purchase Plan.   |
| 10.5 (1)+      |  | 1998 Non-Employee Directors Option Plan.  |
| 10.6 (5)+      |  | 2001 Supplemental Stock Option Plan.  |
| 10.7 (1)+      |  | Offer Letter between the Company and Daniel A. Gaudreau dated May 7, 1997.  |
| 10.8 (3)       |  | Office Building Lease between the Actuate and HMS Gateway Office, L.P. dated August 18, 1999.   |
| 10.9 (3)       |  | First Amendment to Office Building Lease between the Actuate and HMS Gateway Office, L.P. dated December 31, 1999.  |
| 10.10 (5)      |  | Office Building Lease between the Actuate and HMS Gateway Office, L.P. dated December 21, 2000.   |

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- 10.11 (7)+ Form of Severance Agreement (All Section 16 Officers)
- 10.12 (9) Credit Agreement between Actuate and Wells Fargo Foothill, LLC ( Wells Fargo ) dated November 5, 2008.
- 10.13 (12) Office Building Sublease between Actuate and Oracle Corporation dated June 5, 2007.
- 16.1 (6) Letter from Ernst & Young LLP to the Securities and Exchange Commission stating whether or not they agree with the statements made by the Registrant in Item 4 of this Current Report on Form 8-K.
- 21.1 Subsidiaries of Actuate Corporation.
- 23.1 Consent of Independent Registered Public Accounting Firms.
- 24.1 Power of Attorney. (See the signature page to this Form 10-K).
- 31.1 Rule 13a-14(a)/15d-14(a) Certification of the Chief Executive Officer
- 31.2 Rule 13a-14(a)/15d-14(a) Certification of the Chief Financial Officer
- 32.1 Section 1350 Certifications

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- (1) Incorporated by reference to our Registration Statement on Form S-1 (File No. 333-55741).
  - (2) Incorporated by reference to our Amended Registration Statement on Form S-1/A.
  - (3) Incorporated by reference to our Quarterly Report on Form 10-Q for the period ended September 30, 1999.
  - (4) Incorporated by reference to our Annual Report on Form 10-K for the period ended December 31, 2000.
  - (5) Incorporated by reference to our Annual Report on Form 10-K for the period ended December 31, 2001.
  - (6) Incorporated by reference to our Form 8-K filed on June 16, 2004.
  - (7) Incorporated by reference to our Form 8-K filed on October 25, 2007.
  - (8) Incorporated by reference to our Form 8-K filed on December 27, 2007.
  - (9) Incorporated by reference to our Annual Report on Form 10-K for the period ended December 31, 2007.
  - (10) Incorporated by reference to our Quarterly Report on Form 10-Q for the period ended September 30, 2008.
  - (11) Incorporated by reference to our Form 8-K filed on February 3, 2009.
  - (12) Incorporated by reference to our Form 8-K filed on June 5, 2007.
- + Indicates management or compensatory plan or arrangement.

**(b) Exhibits**

See (a)(3) above.

**(c) Financial Statement Schedule**

See (a)(2) above.

**Table of Contents****SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on our behalf by the undersigned thereunto duly authorized.

ACTUATE CORPORATION

(Registrant)

By: /s/ DANIEL A. GAUDREAU  
**Daniel A. Gaudreau**

**Senior Vice President, Operations and  
Chief Financial Officer**

Date: March 12, 2009

**POWER OF ATTORNEY**

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

| <b>Signature</b>  | <b>Title</b>   | <b>Date</b>    |
|---|--|----------------|
| /s/ NICOLAS C. NIERENBERG<br><b>Nicolas C. Nierenberg</b> | Chairman of the Board and Chief Architect  | March 12, 2009 |
| /s/ PETER I. CITTADINI<br><b>Peter I. Cittadini</b>       | Director, President and Chief Executive Officer<br>(Principal Executive Officer)                                 | March 12, 2009 |
| /s/ DANIEL A. GAUDREAU<br><b>Daniel A. Gaudreau</b>       | Senior Vice President, Operations and Chief<br>Financial Officer (Principal Financial and<br>Accounting Officer) | March 12, 2009 |
| /s/ GEORGE B. BEITZEL<br><b>George B. Beitzel</b>         | Director   | March 12, 2009 |
| /s/ KENNETH E. MARSHALL<br><b>Kenneth E. Marshall</b>     | Director   | March 12, 2009 |
| /s/ ARTHUR C. PATTERSON<br><b>Arthur C. Patterson</b>     | Director   | March 12, 2009 |

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**Arthur C. Patterson**

/s/ STEVEN D. WHITEMAN

Director

March 12, 2009

**Steven D. Whiteman**

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**ACTUATE CORPORATION**

**INDEX TO FINANCIAL STATEMENTS**

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| <u>Consolidated Balance Sheets</u>  | F-4         |
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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Stockholders

Actuate Corporation:

We have audited the accompanying consolidated balance sheets of Actuate Corporation and subsidiaries (the Company) as of December 31, 2008 and 2007, and the related consolidated statements of income, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2008. In connection with our audits of the consolidated financial statements, we have also audited the financial statement schedule as set forth in Item 15(a)(2). These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits. We also have audited the Company's internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying *Management's Report on Internal Control Over Financial Reporting*. Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Actuate Corporation and subsidiaries as of December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the years in



the three-year period ended December 31, 2008,

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in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein. Also in our opinion, Actuate Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

As discussed in Note 12 to the consolidated financial statements, effective January 1, 2007, the Company adopted the provisions of Financial Accounting Standards Board Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109.

/s/ KPMG LLP

Mountain View, California

March 12, 2009

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**Table of Contents****ACTUATE CORPORATION****CONSOLIDATED BALANCE SHEETS**

(in thousands, except share and per share data)

|   | December 31,      |                   |
|---|-------------------|-------------------|
|   | 2008              | 2007              |
| <b>ASSETS</b>   |                   |                   |
| Current assets:   |                   |                   |
| Cash and cash equivalents   | \$ 24,772         | \$ 21,468         |
| Short-term investments  | 17,278            | 46,947            |
| Accounts receivable, net of allowances of \$606 and \$1,141 at December 31, 2008 and 2007, respectively   | 28,017            | 38,575            |
| Other current assets  | 6,620             | 5,278             |
| <b>Total current assets</b>   | <b>76,687</b>     | <b>112,268</b>    |
| Property and equipment, net   | 4,729             | 5,269             |
| Goodwill  | 36,114            | 35,594            |
| Purchased intangibles   | 1,800             | 3,648             |
| Non-current deferred tax assets   | 12,602            | 11,996            |
| Investments   | 16,391            |                   |
| Other assets  | 2,189             | 1,133             |
|   | <b>\$ 150,512</b> | <b>\$ 169,908</b> |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>  |                   |                   |
| Current liabilities:  |                   |                   |
| Accounts payable  | \$ 2,067          | \$ 2,667          |
| Current portion of restructuring liabilities  | 3,206             | 3,201             |
| Accrued compensation  | 4,514             | 6,326             |
| Other accrued liabilities   | 5,299             | 5,677             |
| Deferred revenue  | 40,900            | 40,352            |
| <b>Total current liabilities</b>  | <b>55,986</b>     | <b>58,223</b>     |
| Long-term liabilities:  |                   |                   |
| Note payable  | 30,000            |                   |
| Other deferred liabilities  | 1,054             | 1,124             |
| Long-term deferred revenue  | 2,472             | 3,499             |
| Long-term income taxes payable  | 1,660             | 483               |
| Restructuring liabilities, net of current portion   | 3,092             | 5,606             |
| <b>Total long-term liabilities</b>  | <b>38,278</b>     | <b>10,712</b>     |
| Commitments and contingencies (Notes 8 and 14)  |                   |                   |
| Stockholders equity:  |                   |                   |
| Preferred stock, \$0.001 par value, issuable in series; 5,000,000 shares authorized; none issued or outstanding   |                   |                   |
| Common stock, \$0.001 par value, 100,000,000 shares authorized; issued 75,514,061 and 72,991,110 shares, respectively; outstanding 44,169,649 and 61,428,115 shares, respectively | 44                | 61                |
| Additional paid-in capital  | 161,203           | 144,471           |
| Treasury stock, at cost; 31,344,412 and 11,562,995 shares, respectively   | (117,256)         | (43,724)          |
| Accumulated other comprehensive income (loss)   | (887)             | 599               |

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|                             |            |            |
|-----------------------------|------------|------------|
| Retained earnings (deficit) | 13,144     | (434)      |
| Total stockholders' equity  | 56,248     | 100,973    |
|                             | \$ 150,512 | \$ 169,908 |

*See accompanying notes to Consolidated Financial Statements.*

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**Table of Contents****ACTUATE CORPORATION****CONSOLIDATED STATEMENTS OF INCOME****(in thousands, except per share data)**

|   | Year ended December 31, |                |                |
|---|-------------------------|----------------|----------------|
|   | 2008                    | 2007           | 2006           |
| <b>Revenues:</b>  |                         |                |                |
| License fees  | \$ 39,989               | \$ 53,216      | \$ 46,919      |
| Maintenance   | 76,695                  | 71,336         | 63,145         |
| Professional services and training                      | 14,306                  | 16,074         | 18,505         |
| <b>Total revenues</b>                                   | <b>130,990</b>          | <b>140,626</b> | <b>128,569</b> |
| <b>Costs and expenses:</b>                              |                         |                |                |
| Cost of license fees                                    | 1,396                   | 1,997          | 2,095          |
| Cost of services  | 23,330                  | 24,927         | 27,914         |
| Sales and marketing                                     | 51,830                  | 55,312         | 49,009         |
| Research and development                                | 22,035                  | 21,826         | 21,055         |
| General and administrative                              | 18,470                  | 17,784         | 16,026         |
| Amortization of purchased intangibles                   | 948                     | 948            | 948            |
| Purchased in-process research and development           |                         |                | 900            |
| Restructuring charges                                   | 1,506                   | 1,686          | 16             |
| <b>Total costs and expenses</b>                         | <b>119,515</b>          | <b>124,480</b> | <b>117,963</b> |
| Income from operations                                  | 11,475                  | 16,146         | 10,606         |
| Interest and other income, net                          | 785                     | 3,155          | 2,217          |
| Income before provision for income taxes                | 12,260                  | 19,301         | 12,823         |
| Benefit from income taxes                               | (1,318)                 | (863)          | (974)          |
| Net income  | \$ 13,578               | \$ 20,164      | \$ 13,797      |
| Basic net income per share                              | \$ 0.23                 | \$ 0.33        | \$ 0.23        |
| Shares used in basic net income per share calculation   | 60,025                  | 60,838         | 60,375         |
| Diluted net income per share                            | \$ 0.21                 | \$ 0.29        | \$ 0.21        |
| Shares used in diluted net income per share calculation | 65,049                  | 68,722         | 66,814         |

*See accompanying notes to Consolidated Financial Statements.*

**Table of Contents****ACTUATE CORPORATION****CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY AND  
COMPREHENSIVE INCOME**

(in thousands, except share data)

|   | Common Stock      |              |                                  | Treasury Stock      |                    | Accumulated<br>Other<br>Comprehensive<br>Income<br>(Loss) | Retained<br>Earnings<br>(Accumulated<br>Deficit) | Total<br>Stockholders<br>Equity |
|---|-------------------|--------------|----------------------------------|---------------------|--------------------|---|--|---------------------------------|
|   | Shares            | Amount       | Additional<br>Paid-in<br>Capital | Shares              | Amount             |   |  |                                 |
| <b>Balance at January 1, 2006</b>                           | <b>67,536,651</b> | <b>\$ 60</b> | <b>\$ 108,904</b>                | <b>(7,366,148)</b>  | <b>\$ (18,691)</b> | <b>\$ (555)</b>   | <b>\$ (34,350)</b>                               | <b>\$ 55,368</b>                |
| Comprehensive income  |                   |              |                                  |                     |                    |   |  |                                 |
| Net income  |                   |              |                                  |                     |                    |   | 13,797   | 13,797                          |
| Net unrealized gains on available-for- sale securities      |                   |              |                                  |                     |                    | 72  |  | 72                              |
| Currency translation  |                   |              |                                  |                     |                    | 523   |  | 523                             |
| Total comprehensive income                                  |                   |              |                                  |                     |                    |   |  | 14,392                          |
| Issuance of common stock upon exercise of stock options     | 1,640,855         | 2            | 3,430                            |                     |                    |   |  | 3,432                           |
| Issuance of common stock under Employee Stock Purchase Plan | 219,629           |              | 462                              |                     |                    |   |  | 462                             |
| Stock based compensation                                    |                   |              | 6,492                            |                     |                    |   |  | 6,492                           |
| Stock repurchase  |                   | (1)          |                                  | (1,137,698)         | (4,609)            |   |  | (4,610)                         |
| Tax benefits from employee stock options                    |                   |              | 2,274                            |                     |                    |   |  | 2,274                           |
| <b>Balance at December 31, 2006</b>                         | <b>69,397,135</b> | <b>\$ 61</b> | <b>\$ 121,562</b>                | <b>(8,503,846)</b>  | <b>\$ (23,300)</b> | <b>\$ 40</b>  | <b>\$ (20,553)</b>                               | <b>\$ 77,810</b>                |
| Comprehensive income  |                   |              |                                  |                     |                    |   |  |                                 |
| Net income  |                   |              |                                  |                     |                    |   | 20,164   | 20,164                          |
| Net unrealized gains on available-for- sale securities      |                   |              |                                  |                     |                    | 65  |  | 65                              |
| Currency translation  |                   |              |                                  |                     |                    | 494   |  | 494                             |
| Total comprehensive income                                  |                   |              |                                  |                     |                    |   |  | 20,723                          |
| Issuance of common stock upon exercise of stock options     | 3,282,257         | 4            | 8,285                            |                     |                    |   |  | 8,289                           |
| Issuance of common stock under Employee Stock Purchase Plan | 311,718           |              | 878                              |                     |                    |   |  | 878                             |
| Stock based compensation                                    |                   |              | 8,986                            |                     |                    |   |  | 8,986                           |
| Stock repurchase  |                   | (4)          |                                  | (3,059,149)         | (20,424)           |   |  | (20,428)                        |
| Impact from adoption of FIN 48                              |                   |              |                                  |                     |                    |   | (45)   | (45)                            |
| Tax benefits from employee stock options                    |                   |              | 4,760                            |                     |                    |   |  | 4,760                           |
| <b>Balance at December 31, 2007</b>                         | <b>72,991,110</b> | <b>\$ 61</b> | <b>\$ 144,471</b>                | <b>(11,562,995)</b> | <b>\$ (43,724)</b> | <b>\$ 599</b>   | <b>\$ (434)</b>                                  | <b>\$ 100,973</b>               |
| Comprehensive income  |                   |              |                                  |                     |                    |   |  |                                 |
| Net income  |                   |              |                                  |                     |                    |   | 13,578   | 13,578                          |
| Net unrealized gains on available-for- sale securities      |                   |              |                                  |                     |                    | 27  |  | 27                              |
| Currency translation  |                   |              |                                  |                     |                    | (1,513)   |  | (1,513)                         |

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|   |                   |              |                   |                     |                     |                 |                  |                  |  |          |
|---|-------------------|--------------|-------------------|---------------------|---------------------|-----------------|------------------|------------------|--|----------|
| Total comprehensive income                                  |                   |              |                   |                     |                     |                 |                  |                  |  | 12,092   |
| Issuance of common stock upon exercise of stock options     | 2,100,088         | 2            | 4,924             |                     |                     |                 |                  |                  |  | 4,926    |
| Issuance of common stock under Employee Stock Purchase Plan | 422,863           | 1            | 1,738             |                     |                     |                 |                  |                  |  | 1,739    |
| Stock based compensation                                    |                   |              | 9,122             |                     |                     |                 |                  |                  |  | 9,122    |
| Stock repurchase  |                   | (20)         |                   | (19,781,417)        | (73,532)            |                 |                  |                  |  | (73,552) |
| Tax benefits from employee stock options                    |                   |              | 948               |                     |                     |                 |                  |                  |  | 948      |
| <b>Balance at December 31, 2008</b>                         | <b>75,514,061</b> | <b>\$ 44</b> | <b>\$ 161,203</b> | <b>(31,344,412)</b> | <b>\$ (117,256)</b> | <b>\$ (887)</b> | <b>\$ 13,144</b> | <b>\$ 56,248</b> |  |          |

*See accompanying notes to Consolidated Financial Statements.*

**Table of Contents****ACTUATE CORPORATION****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)

|  | Year ended December 31, |           |           |
|--|-------------------------|-----------|-----------|
|  | 2008                    | 2007      | 2006      |
| <b>Operating activities</b>  |                         |           |           |
| Net income   | \$ 13,578               | \$ 20,164 | \$ 13,797 |
| Adjustments to reconcile net income to net cash from operating activities: |                         |           |           |
| Stock based compensation expense   | 9,122                   | 8,986     | 6,492     |
| Amortization of purchased intangibles                                      | 1,419                   | 1,947     | 1,986     |
| Amortization of debt issuance cost   | 48                      |           |           |
| Depreciation   | 2,228                   | 2,367     | 1,970     |
| Purchased in-process research and development                              |                         |           | 900       |
| Deferred tax asset utilization   | 135                     | (178)     | 783       |
| Other than temporary impairment of investments                             | 2,593                   |           |           |
| Gain on fair value of put option   | (2,509)                 |           |           |
| Accretion of discount on short-term investments                            | 252                     | (259)     | 47        |
| Net operating loss utilizations related to prior acquisitions              | (228)                   | 107       | 764       |
| Restructuring charges  | 1,506                   | 1,686     | 16        |
| Change in operating assets and liabilities, net of effects of acquisition: |                         |           |           |
| Accounts receivable  | 10,558                  | (7,342)   | (3,200)   |
| Other current assets   | 1,190                   | (795)     | 1,448     |
| Accounts payable   | (1,312)                 | 672       | (2,070)   |
| Accrued compensation   | (1,812)                 | 293       | 207       |
| Other accrued liabilities  | (1,023)                 | 1,194     | 895       |
| Deferred tax assets  | (3,469)                 | (5,903)   | (6,867)   |
| Income taxes receivable/payable  | 1,825                   | (265)     | 394       |
| Deferred tax liability   |                         | (420)     | 406       |
| Other deferred liabilities   | (70)                    | 1,101     | (174)     |
| Restructuring liabilities  | (4,017)                 | (3,433)   | (2,191)   |
| Deferred revenue   | (479)                   | 2,998     | 6,531     |
| Net cash generated by operating activities                                 | 29,535                  | 22,920    | 22,134    |
| <b>Investing activities</b>  |                         |           |           |
| Purchase of property and equipment   | (1,688)                 | (2,956)   | (1,279)   |
| Increase in restricted cash  | (260)                   | (395)     |           |
| Proceeds from maturities of short-term investments                         | 79,844                  | 118,022   | 76,833    |
| Purchase of short-term investments   | (66,875)                | (135,679) | (63,869)  |
| Acquisition of performancesoft, Inc., net of cash acquired                 |                         | (5,632)   | (15,668)  |
| Purchase of source code  |                         |           | (1,000)   |
| Purchase of minority shares of Actuate Japan                               |                         |           | (354)     |
| Proceeds from security deposit   |                         | 209       |           |
| Net change in other assets   |                         | (127)     | (256)     |
| Net cash generated by (used in) investing activities                       | 11,021                  | (26,558)  | (5,593)   |
| <b>Financing activities</b>  |                         |           |           |
| Proceeds from the credit facility, net of issuance cost                    | 29,598                  |           |           |
| Tax benefits from exercise of stock options                                | 948                     | 4,760     | 2,274     |



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|   |           |           |           |
|---|-----------|-----------|-----------|
| Proceeds from issuance of common stock                  | 6,661     | 9,162     | 3,894     |
| Stock repurchases                                       | (72,946)  | (20,423)  | (4,610)   |
| Net cash generated by (used in) financing activities    | (35,739)  | (6,501)   | 1,558     |
| Net increase (decrease) in cash and cash equivalents    | 4,817     | (10,139)  | 18,099    |
| Effect of exchange rate on cash and cash equivalents    | (1,513)   | 494       | 524       |
| Cash and cash equivalents at the beginning of the year  | 21,468    | 31,113    | 12,490    |
| Cash and cash equivalents at the end of the year        | \$ 24,772 | \$ 21,468 | \$ 31,113 |
| <b>Supplemental disclosure of cash flow information</b> |           |           |           |
| Cash paid for interest                                  | \$ 27     | \$ 154    | \$ 8      |
| Cash paid for income taxes                              | \$ 105    | \$ 2,333  | \$ 1,180  |

*See accompanying notes to Consolidated Financial Statements.*

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**ACTUATE CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. Summary of Significant Accounting Policies**

Actuate Corporation ( Actuate or the Company ) provides software and services to develop and deploy Rich Internet Applications ( RIAs ) that deliver rich interactive content that improve customer loyalty and corporate performance. Applications built on Actuate s open source-based platform provide stakeholders inside and outside the firewall, including employees, customers, partners and citizens with information that they can easily access and understand to increase revenue, cut costs, improve customer satisfaction, streamline operations, create competitive advantage and make better decisions.

Actuate was incorporated in November 1993 in the State of California and re-incorporated in the State of Delaware in July 1998. Actuate s principal executive offices are located at 2207 Bridgepointe Parkway, San Mateo California. Actuate s telephone number is 650-645-3000. Actuate maintains a Web site at [www.actuate.com](http://www.actuate.com).

***Basis of Presentation***

The Consolidated Financial Statements include the accounts of Actuate and its wholly-owned and majority-owned subsidiaries. Actuate has offices throughout North America, Europe and Asia including offices in United States, Canada, Switzerland, United Kingdom, Germany, Singapore, Japan and China. All intercompany balances and transactions have been eliminated.

As of December 31, 2008, Actuate owns approximately 88% of the outstanding voting stock of Actuate Japan Company Ltd. ( Actuate Japan ). The Company has consolidated the results of Actuate Japan from the date that it became the majority shareholder, which occurred in fiscal year 2000. Accumulated losses applicable to the minority shareholders exceed their equity capital in Actuate Japan and as a result, there is no minority interest presented on the accompanying Consolidated Balance Sheets. This excess loss applicable to the minority shareholders has been charged to Actuate, as the minority shareholders are not obligated to contribute their share of losses exceeding their equity capital.

***Use of Estimates***

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. On a regular basis, Actuate evaluates estimates, including those related to bad debts, goodwill, intangible assets, income taxes, restructuring charges, and the fair value of stock options and employee stock purchase plan shares. Actual results could differ materially from those estimates, particularly in light of the uncertain economic environment.

*Certain Risks and Uncertainties Pertaining to the Macroeconomy*

The software industry is currently experiencing significant challenges, primarily due to a deteriorating macroeconomic environment, which is primarily characterized by diminished product demand. As a result of this downturn, some of the Company's customers may face financial challenges in fiscal 2009. It is unclear when the macroeconomic environment may improve. The Company is seeing increasing pressures on its customers' information technology budgets, and therefore its customers are looking for more flexibility in the type of software and the timing of such purchases. The current economic downturn in the Company's customers' industries has affected its license revenues and could continue to adversely impact its future business.

The Company's customers may also experience adverse changes in their business and, as a result, may delay or default on their payment obligations, file for bankruptcy or modify or cancel plans to license its products. If

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**ACTUATE CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

the Company's customers are not successful in generating sufficient revenue or are precluded from securing financing, they may not be able to pay, or may delay payment of, accounts receivable that are owed to the Company, although these obligations are generally not cancelable. Though the Company has not yet experienced any unusual levels of defaults, any material payment default by its customers or significant reductions in existing contractual commitments could have an adverse effect on its operating results.

A significant portion of the Company's revenues are derived from customers in the financial services industry and the Company expects it will continue to derive a significant portion of its revenues from these customers for the foreseeable future. The unfavorable economic conditions described above have also adversely impacted the financial services industry. This has consequently had an adverse effect on the Company's business which could continue into the future.

***Revenues***

Actuate generates revenues from sales of software licenses and related services. The Company receives software license revenues from licensing its products directly to end-users and indirectly through resellers, system integrators and original equipment manufacturers (OEMs). The Company receives service revenues from maintenance contracts, consulting services and training that Actuate performs for customers.

Actuate recognizes revenues in accordance with AICPA Statement of Position (SOP) 97-2 (SOP 97-2), *Software Revenue Recognition*, as amended and modified by SOP 98-9, *Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions*. For sales to end-user customers, Actuate recognizes license revenues when a license agreement has been signed by both parties or a definitive agreement has been received from the customer, the product has been shipped, there are no unusual uncertainties surrounding the product acceptance, the fees are fixed or determinable, collectibility is probable and vendor-specific objective evidence of fair value exists to allocate the fee to the undelivered elements of the arrangement. Vendor-specific objective evidence of sales to end users is based on the price charged when an element is sold separately. Actuate has not established vendor-specific objective evidence of fair value for its licenses. Therefore, the Company recognizes revenues from arrangements with multiple elements involving software licenses under the residual method. If the license agreement contains payment terms that would indicate that the fee is not fixed or determinable, revenues are recognized as the payments become due and payable, assuming that all other revenue recognition criteria are met.

Actuate enters into reseller and distributor arrangements that typically give such distributors and resellers the right to distribute its products to end-users headquartered in specified territories. Actuate recognizes license revenues from arrangements with U.S. resellers and distributors when there is persuasive evidence of an arrangement with the reseller or distributor, the product has been shipped, the fees are fixed or determinable, and collectibility is probable and vendor-specific objective evidence of fair value exists to allocate the fee to the undelivered elements of the arrangement. Actuate recognizes license revenues from arrangements with international resellers and distributors upon receipt of evidence of sell-through and when all other revenue recognition criteria have been met. If it is not practical to obtain evidence of sell-through, the Company defers revenues until the end-user has been identified and cash has been received. In some instances there is a timing difference between when a reseller completes its sale to the end-user and the period in which Actuate receives the documentation required for revenue recognition. Because Actuate delays revenue recognition until the reporting period in which the required documentation is obtained, it may recognize revenue in a period subsequent to the period in which the reseller completes the sale to its end-user.

Actuate also enters into OEM arrangements that provide for license fees based on the bundling or embedding of its products with the OEM's products. These arrangements generally provide for fixed, irrevocable

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**ACTUATE CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

royalty payments. Actuate recognizes license fee revenues from U.S. and international OEM arrangements when a license agreement has been executed by both parties, the product has been shipped, there are no unusual uncertainties surrounding the product acceptance, the fees are fixed or determinable, collectibility is probable and vendor-specific objective evidence of fair value exists to allocate the fee to the undelivered elements of the arrangement.

Credit-worthiness and collectibility for end-users are assessed based on payment history and current credit profile. When a customer is not deemed credit-worthy, revenues are deferred and recognized upon cash receipt.

Actuate recognizes maintenance revenues, which consist of fees for ongoing support and unspecified product updates, ratably over the term of the contract, typically one year. Consulting revenues are primarily related to standard implementation and configuration. Training revenues are generated from classes offered at the Company's headquarters and customer locations. Revenues from consulting and training services are typically recognized as the services are performed. When a contract includes both license and service elements, the license fee is typically recognized on delivery of the software, assuming all other revenue recognition criteria are met, provided services do not include significant customization or modification of the product and are not otherwise essential to the functionality of the software.

***Cash, Cash Equivalents and Investments***

Cash and cash equivalents consist of cash deposited with banks and highly liquid, high-quality instruments with maturities at the date of purchase of 90 days or less. Such instruments typically include money market securities, commercial paper, and other high quality debt instruments. In accordance with FASB Statement Number 115, *Accounting for Certain Investments in Debt and Equity Securities*, and based on its intentions regarding these instruments, the Company classifies all of its short-term investments as available-for-sale, and account for these investments at fair value. Short-term investments consist primarily of high quality debt securities with original maturities over 90 days, and may include corporate notes, United States government agency notes, municipal notes, and auction rate securities. The cost of securities sold is based on the specific identification method.

In 2007, Actuate viewed its available-for-sale portfolio securities with maturity beyond 90 days to be available for use in current operations. Accordingly, Actuate classified all such marketable investments as short-term investments, even though the stated maturity dates may have been one year or more beyond the current balance sheet date, as they were highly liquid instruments. In addition, in 2007, all auction rate notes, including auction preferred and short-term municipals are classified as short-term investments regardless of the underlying reset date. In 2008, all ARS were reclassified to long-term investments due to the developments discussed below.

Since February 2008, all auctions have failed for the Company's ARS securities and there is no assurance that future auctions will succeed. In November 2008, the Company elected to participate in a rights offering by the Company's investment broker, which provides Actuate with rights (the Put Option) to sell UBS \$16.5 million of its ARS portfolio at par value, at any time during a two-year sale period beginning June 30, 2010. By electing to participate in the rights offering, the Company granted UBS the right, exercisable at any time prior to June 30, 2010 or during the two-year sale period, to purchase or cause the sale of our ARS (the Call Right). UBS has stated that it will only exercise the Call Right for the

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purpose of restructurings, dispositions or other solutions that will provide their clients with par value for their ARS. UBS has agreed to pay their clients the par value of their ARS within one day of settlement of any Call Right transaction. Notwithstanding the Call Right, the Company is permitted to sell ARS to parties other than UBS, in which case the Put Option attached to the ARS that are sold would be extinguished. The Company has classified the Put Option as a non-current investment. As such, the Company recorded a realized loss of approximately \$84,000 related to the difference

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**ACTUATE CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

between the gain of approximately \$2.5 million recognized on the Put Option and the realized loss of approximately \$2.6 million on the \$16.5 million (par value) portion of our ARS portfolio. The Company will evaluate these investments on a quarterly basis. For additional discussion please refer to the Note 4 of the Consolidated Financial Statements.

The Company has no reason to believe that any of the underlying issuers of its ARS are presently at risk of default. Through December 31, 2008, the Company has continued to receive interest payments on the ARS in accordance with their terms. The Company believes that it will ultimately be able to liquidate its ARS related investments without significant loss primarily due to the collateral securing ARS and the legal settlement it has entered into with UBS. However, if UBS were not to honor their settlement commitment, it could take until final maturity of the ARS (up to 39 years) to realize the investments' par value. Due to the changes and uncertainty in the ARS market, the Company believes the recovery period for these investments is likely to be longer than 12 months and as a result, the Company has classified these investments as long-term as of December 31, 2008. Also, as a result of the settlement offer, the Company has classified the ARS as trading securities at December 31, 2008. As such, all temporary changes in fair value of the ARS are recognized in results of operations on the Consolidated Statement of Income. Prior to the fourth quarter of fiscal year 2008, the ARS were classified as available-for-sale and all temporary changes in fair value were recognized in Accumulated Other Comprehensive Income (Loss) on the Company's Consolidated Balance Sheet.

The Company currently has the ability and intends to hold these ARS investments until recovery of the auction process, until it exercises the Put Option, or until maturity. However, if the Company needs to access the funds associated with ARS but are unable to do so, its operations and financial position could be materially harmed.

***Fair Values of Financial Instruments***

The carrying value of the Company's financial instruments, including cash and cash equivalents, investments, accounts receivable and accounts payable approximates fair value due to the short term nature of these instruments. The fair market value of Actuate's long-term debt approximate its carrying value based upon current market rates of interest. The Company maintains its cash, cash equivalents and investments with high quality financial institutions and limits its investment in individual securities based on the type and credit quality associated with such investments.

The Company performs ongoing credit evaluations of its customers and generally does not require collateral on accounts receivable. The Company maintains allowances for potential credit losses. No customer had a balance in excess of 10% of our net accounts receivable as of December 31, 2008 or 2007.

***Concentration of Credit Risk***



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Financial instruments that potentially subject the Company to credit risk principally consist of investments and accounts receivable. Actuate places its investments with high-credit-quality multiple issuers. The Company sells to a diverse customer base, predominantly to customers in the United States. No single customer has accounted for more than 10% of sales in any period presented. Actuate does not require collateral on sales with credit terms.

The Company's accounts receivable is subject to collection risks. The Company's gross accounts receivable is reduced for this risk by an allowance for doubtful accounts. This allowance is for estimated losses resulting from the inability of Actuate's customers to make required payments. It is an estimate and is regularly evaluated for adequacy by taking into consideration a combination of factors. The Company looks at factors such as past

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**ACTUATE CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

collection experience, credit quality of the customer, age of the receivable balance, and current economic conditions. These facts are reviewed to determine whether a specific reserve for bad debt should be recorded to reduce the related receivable to the amount believed to be collectible. The Company also ceases recognizing revenues on any outstanding domestic maintenance renewal invoices which are older than 90 days past due.

The Company also records unspecified reserves for bad debts for all other customers based on a variety of factors, including length of time the receivables are past due and historical collection experience. Reserve percentages are applied to various aged categories of receivables based on historical collection experience to determine how much of an unspecified reserve is needed. The use of different estimates or assumptions could produce different allowance balances. If the financial condition of Actuate's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances might be required.

***Software Development Costs***

Software development costs associated with new products and enhancements to existing software products are expensed as incurred until technological feasibility in the form of a working model has been established. To date, the time period between the establishment of technological feasibility and completion of software development has been short, and no significant development costs have been incurred during that period. Accordingly, Actuate has not capitalized any software development costs to date.

***Property and Equipment***

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is provided using the straight-line method over the estimated useful lives of the respective assets, which range from two to seven years. Leasehold improvements are amortized over the shorter of the lease term or estimated useful life, which range from four to ten years. The Company only capitalizes fixed assets with an initial value in excess of the \$2,000 threshold. Purchased items below that initial threshold value are immediately expensed.

***Goodwill and Other Purchased Intangible Assets***

The Company applies the provisions of Statement of Financial Accounting Standards ( SFAS ) No. 141 ( SFAS 141 ), *Business Combinations* , and No. 142, *Goodwill and Other Intangible Assets* ( SFAS 142 ). Under SFAS 142, goodwill and is tested for impairment annually, or more frequently, if impairment indicators arise. Other intangible assets consist of customer lists, purchased technologies, and trademarks acquired from various acquisitions. Intangible assets acquired in business acquisitions are recorded at their fair values using the income approach or cost approach. These other intangible assets are being amortized over their expected useful lives not exceeding five years using the straight-line method. See Note 6 for further discussion.

*Impairment of Long-Lived Assets*

The Company evaluates its long-lived assets for impairment annually or whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of any asset to future net undiscounted cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the excess of the carrying amount of the assets over the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less the costs to sell.

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**ACTUATE CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

***Advertising Costs***

Advertising costs are expensed as incurred. Advertising costs are included in sales and marketing expense and amounted to \$609,000, \$857,000 and \$679,000 in fiscal years 2008, 2007 and 2006, respectively.

***Income Taxes***

The Company provides for the effect of income taxes in its Consolidated Financial Statements in accordance with Statement of Financial Accounting Standards, or SFAS, No. 109, Accounting for Income Taxes and FASB Interpretation 48 ( FIN 48 ), Accounting for Income Tax Uncertainties. Under SFAS No. 109, income tax expense (benefit) is recognized for the amount of taxes payable or refundable for the current year, and for deferred tax assets and liabilities for the tax consequences of events that have been recognized in an entity's financial statements or tax returns. On January 1, 2007, the Company adopted the provisions of FIN 48. Under FIN 48, only income tax positions that meet the more likely than not recognition threshold may be recognized in the financial statements. If an income tax position meets the more likely than not recognition threshold, then the Company must measure the amount of the tax benefit to be recognized by determining the largest amount of tax benefit that has a greater than a 50% likelihood of being realized upon effective settlement with a taxing authority that has full knowledge of all of the relevant facts. It is inherently difficult and subjective to estimate such amounts, as this requires us to determine the probability of various possible settlement outcomes. To determine if a tax position is effectively settled, the Company must also estimate the likelihood that a taxing authority would review a tax position after a tax examination had otherwise been completed. The Company must also determine when it is reasonably possible that the amount of unrecognized tax benefits will significantly increase or decrease in the 12 months after each reporting date. These judgments are difficult because a taxing authority may change its behavior as a result of the Company's disclosures in its financial statements that are based on the requirements of FIN No. 48. The Company must re-evaluate its income tax positions on a quarterly basis to consider factors such as changes in facts or circumstances, changes in tax law, effectively settled issues under audit, and new audit activity. Such a change in recognition or measurement would result in recognition of a tax benefit or an additional charge to the tax provision.

The Company must make significant assumptions, judgments and estimates to determine its current provision for income taxes, its deferred tax assets and liabilities and any valuation allowance to be recorded against its deferred tax assets. The Company's judgments, assumptions and estimates relating to the current provision for income taxes take into account current tax laws, its interpretation of current tax laws and possible outcomes of current and future audits conducted by foreign and domestic tax authorities. Changes in tax laws or our interpretation of tax laws, and developments in current and future tax audits, could significantly impact the amounts provided for income taxes in the Company's results of operations, financial position or cash flows. The Company's assumptions, judgments and estimates relating to the value of its net deferred tax assets take into account predictions of the amount and category of future taxable income from potential sources, including tax planning strategies that would, if necessary, be implemented to prevent a loss carry-forward or tax credit carry-forward from expiring unused. Actual operating results and the underlying amount and category of income in future years could render the Company's current assumptions, judgments and estimates of recoverable net deferred taxes inaccurate, thus materially affecting its consolidated financial position or results of operations.

***Sales Taxes***

The Company presents its revenues net of sales tax in its Consolidated Statements of Income.

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**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)*****Foreign Currency Translation***

The functional currency of each of the Company's foreign subsidiaries is the foreign subsidiary's local currency except for the Company's Cayman subsidiary, whose books and records are maintained in U.S. dollars, and accordingly its functional currency is the U.S. dollar. Actuate translates the assets and liabilities of its international non-U.S. functional currency subsidiaries into U.S. dollars at the rates of exchange in effect at the end of the period. Revenues and expenses are translated using rates that approximate those in effect during the period. Gains and losses from currency translation are included in Accumulated Other Comprehensive Income (Loss) in the Consolidated Balance Sheet. Currency transaction gains or losses are recorded in interest and other income, net in the accompanying Consolidated Financial Statements.

***Net Income Per Share***

The Company computes basic net income per share using the weighted-average number of common shares outstanding during the period, less weighted average shares subject to repurchase. The Company computes diluted net income per share using the weighted-average number of common shares and dilutive stock options outstanding during the period determined by using the treasury stock method.

The table below reconciles the weighted-average common shares used to calculate basic net income per share with the weighted-average common shares used to calculate diluted net income per share (in thousands).

|   | <b>Year ended December 31,</b> |             |             |
|---|--------------------------------|-------------|-------------|
|   | <b>2008</b>                    | <b>2007</b> | <b>2006</b> |
| Weighted-average shares of common stock outstanding                                 | 60,025                         | 60,838      | 60,375      |
| Weighted-average dilutive stock options outstanding under the treasury stock method | 5,024                          | 7,884       | 6,439       |
| Weighted-average common shares used in computing diluted net income per share       | 65,049                         | 68,722      | 66,814      |

The weighted-average number of common shares excluded from the calculation of diluted net income per share was, 6,440,639, 2,947,917 and 4,601,010 in fiscal years 2008, 2007 and 2006, respectively. These shares were excluded from Actuate's calculation of weighted-average common shares used in computing dilutive net income per share as they were anti-dilutive. These anti-dilutive options could be dilutive in the future.

The weighted average exercise price of excluded stock options was \$6.09, \$6.62 and \$5.05 for the years ended December 31, 2008, 2007 and 2006, respectively.

*Segment Information*

Actuate provides software and services for Business Intelligence, Performance Management and Reporting applications. Actuate's chief operating decision maker (the Chief Executive Officer) reviews financial information presented on a consolidated basis, accompanied by disaggregated information showing revenues by geographic region for purposes of making operating decisions and assessing financial performance. Actuate considers itself to be in a single reportable segment, specifically the license, implementation and support of its software products.

Actuate evaluates the performance of its geographic regions based primarily on revenues. Actuate does not regularly assess the performance of its geographic regions on other measures of income or expense, such as operating income or net income. In addition, as Actuate's assets are primarily located in its corporate office in the

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**ACTUATE CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

United States and not allocated to any specific region, Actuate does not produce reports for, or measure the performance of, its geographic regions based on any asset-based metrics. Therefore, geographic information is presented only for revenues in Note 13.

***Recent Accounting Pronouncements***

In May 2008, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles* ( SFAS No. 162 ). SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (the GAAP hierarchy). SFAS No. 162 will become effective 60 days following the SEC 's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, *The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles*. The Company does not expect the adoption of SFAS No. 162 to have a material effect on its consolidated results of operations and financial condition.

In April 2008, the FASB issued FSP FAS No. 142-3, *Determination of the Useful Life of Intangible Assets*. FSP FAS 142-3 amends the factors an entity should consider in developing renewal or extension assumptions used in determining the useful life of recognized intangible assets under SFAS No. 142. This new guidance applies prospectively to intangible assets that are acquired individually or with a group of other assets in business combinations and asset acquisitions. FSP FAS 142-3 is effective for financial statements issued for fiscal years and interim periods beginning after December 15, 2008. Early adoption is prohibited. Since this guidance will be applied prospectively, on adoption, there will be no impact to our Consolidated Financial Statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities* ( SFAS 161 ). SFAS 161 requires companies with derivative instruments to disclose information that should enable financial-statement users to understand how and why a company uses derivative instruments, how derivative instruments and related hedged items are accounted for under SFAS No. 133 *Accounting for Derivative Instruments and Hedging Activities* and how derivative instruments and related hedged items affect a company 's financial position, financial performance and cash flows. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The Company will provide required disclosure, if applicable, upon adoption.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* ( SFAS 159 ). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. Entities that elect the fair value option will report unrealized gains and losses in earnings at each subsequent reporting date. The fair value option may be elected on an instrument-by-instrument basis, with few exceptions. SFAS 159 also establishes presentation and disclosure requirements to facilitate comparisons between companies that choose different measurement attributes for similar assets and liabilities. The requirements of SFAS 159 are effective for our fiscal year which began January 1, 2008. However, the Company did not elect to apply the fair value option to any of its financial instruments or other items upon adoption of SFAS 159 during the fiscal year ended December 31, 2008. Therefore, the adoption of SFAS 159 did not impact the Company 's consolidated financial position, results of operations or cash flows.



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In December 2007, the FASB issued SFAS No. 141 (revised), *Business Combinations* ( SFAS 141(R) ). The standard changes the accounting for business combinations including the measurement of acquirer shares issued in consideration for a business combination, the recognition of contingent consideration, the accounting for pre-acquisition gain and loss contingencies, the recognition of capitalized in-process research and

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development, the accounting for acquisition-related restructuring cost accruals, the treatment of acquisition related transaction costs and the recognition of changes in the acquirer's income tax valuation allowance. SFAS 141(R) is effective for fiscal years beginning after December 15, 2008, with early adoption prohibited. Actuate will apply the provisions of SFAS 141(R) to business combinations completed after the date that SFAS 141(R) becomes effective.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurement* ( SFAS 157 ). SFAS 157 defines fair value, establishes a framework for measuring fair value, and also expands disclosures about fair value measurements. SFAS 157 is effective for periods beginning after November 15, 2007. The Company adopted this standard with respect to its financial assets effective January 1, 2008. In February 2008, the FASB issued FASB Staff Position SFAS No. 157-2 Effective Date of FASB Statement No. 157 delaying the effective date of SFAS 157 for one year for all non financial assets and non financial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). See Footnote 4 of the Notes to the Consolidated Financial Statements for further detail regarding the impact of our adoption of SFAS 157 for financial assets.

***Reclassifications***

The operating activities section of the 2006 Consolidated Statement of Cash Flows was expanded to be consistent with the current year presentation. In addition, Cash Flows relating to deferred tax assets were reclassified in fiscal 2006 from financing activities to operating activities to conform to the current year presentation. This reclassification resulted in an increase of approximately \$1.8 million to cash generated by operating activities and a similar decrease to cash generated by financing activities. Such reclassifications had no impact on the results of operations and the stockholders' equity for the years presented.

**2. Investment in Actuate Japan**

The minority shareholders of Actuate Japan have the non-expiring option to put their equity interest ( Minority Interest ) in Actuate Japan to the Company and the Company has the option to call the Minority Interest. The Minority Interest as of December 31, 2008 was approximately 12% of the total equity interest. If the Minority Interest Shareholder chose to put these remaining shares to the Company, Actuate would be required to pay approximately \$584,000 to purchase these shares. The Company will record a liability, if any, at the time that the put or call is probable of being exercised. Should an indicator arise that the Minority Interest has declined in value below the exercise price of the put and call option, the Company would conclude that exercise is probable at that point in time and recognize a liability for the intrinsic value of the option. The Company performs a periodic review of the value of the Minority Interest. This review may include assumptions regarding projected future cash flows and discount rates. Variances in these assumptions could have a significant impact on the Company's conclusion as to whether it is necessary to record a liability. As of December 31, 2008, the Company concluded that it was not necessary to record a liability. The Company consolidated 100% of the operating results of Actuate Japan and all investments in the subsidiary are eliminated in consolidation. As of the date of this filing, the remaining minority shareholder has not notified the Company of any intent to exercise its put option.

**3. Acquisitions**

*Performancesoft, Inc.*

On January 5, 2006, the Company acquired all of the outstanding stock of performancesoft, Inc. The acquisition principally consisted of an initial cash purchase price of \$15.3 million and additional contingent cash

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**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

consideration of up to \$13.5 million based on the achievement of certain revenue and operating margin targets for fiscal year 2006. Due to the fact that the contingent consideration was not determinable at the time of acquisition, the Company did not include this contingent consideration in the acquisition cost at that time. Rather, it was recorded in the fourth quarter of 2006, when the Company was able to determine the estimated amount of the payout. The Company determined that the initial earnout payment would be approximately \$4.9 million and the Company recorded this amount as additional cost of the acquired enterprise and this additional consideration was allocated to goodwill at that time. This earnout payment was increased by an additional \$616,000 in the third quarter of fiscal year 2007 when the final settlement agreement was signed. This agreement represented the final earnout settlement amount along with accrued interest. The Company recorded this amount as additional cost of the acquired enterprise and this additional consideration was allocated to goodwill in the third quarter of fiscal year 2007. The total amount of the contingent consideration was paid out to the former shareholders on October 5, 2007.

In accordance with criteria stipulated in the acquisition agreement, funds previously held in escrow totaling \$201,000 were released to Actuate in October 2007. The Company had previously included these funds held in escrow as part of the final purchase price, and accordingly, it recorded this release of funds from escrow of \$201,000, as a reduction in the cost of the acquired enterprise and a reduction of goodwill in the third quarter of fiscal year 2007.

The total \$20.9 million purchase price is comprised of the following:

|                             |                      |
|-----------------------------|----------------------|
| Cash                        | \$ 20,831,620        |
| Direct transaction costs    | 92,044               |
| <b>Final purchase price</b> | <b>\$ 20,923,664</b> |

Direct transaction costs of \$92,044 include legal and accounting fees, appraisal fees, and other external costs directly related to the acquisition.

**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)***Purchase Price Allocation*

The following represents the allocation of the final purchase price to the acquired net assets of performancesoft and the associated estimated useful lives, inclusive of the two contingent consideration payments discussed above (in thousands):

|                                      | Amount    | Estimated Useful Life |
|--------------------------------------|-----------|-----------------------|
| Net tangible assets and liabilities: |           |                       |
| Accounts receivable, net             | 1,048     | N/A                   |
| Recoverable income tax               | 1,595     | N/A                   |
| Accounts payable                     | (1,665)   | N/A                   |
| Deferred revenue                     | (1,657)   | N/A                   |
| Other net assets and liabilities     | (315)     | N/A                   |
|                                      | (994)     | N/A                   |
| Identifiable intangible assets:      |           |                       |
| Existing technology                  | 1,100     | 5 years               |
| Customer and partner relationships   | 3,400     | 5 years               |
| In-process research and development  | 900       | N/A                   |
| Tradenname                           | 800       | 3 years               |
| Goodwill                             | 15,718    | N/A                   |
| Final purchase price                 | \$ 20,924 |                       |

As of the acquisition date, \$900,000 was allocated to in-process research and development. In-process research and development is dependent on the status of new projects on the date the acquisition is consummated. At the date of acquisition the acquired company had two development projects that were in process, relating to its Views product and a new product offering called Track. Both of these projects were completed by the end of the third quarter of fiscal year 2006. The value of in-process research and development was determined using the excess earnings approach. The discount rates used were 18% to 19% and they take into consideration the stage of completion and the risk surrounding the successful development and commercialization of each of the purchased in-process technology projects that were valued. The Company expensed the total value of these in-process research and development projects at the time of acquisition as they were determined to have no alternative future use. This expense was shown as a separate line item in the fiscal year 2006 Consolidated Statement of Income.

In connection with the performancesoft acquisition, Actuate's Board of Directors duly authorized the issuance of stock options to eligible performancesoft employees from the Company's 1998 Equity Incentive Plan. A total of 530,200 non-statutory stock options were issued in January 2006 under the 1998 Equity Incentive Plan at an exercise price of \$3.36. Each grant vests in four years with 25% vesting at the end of year one and the remaining balance vesting in thirty-six equal monthly installments. These options were valued at their fair value in accordance with SFAS 123R and are being amortized over their vesting period using the accelerated amortization method as provided under Financial Accounting Standards Board Interpretation Number 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Awards Plans* (FIN 28).

**4. Cash, Cash Equivalents and Investments**

The Company adopted the provisions of SFAS 157 effective January 1, 2008. Under this standard, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

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**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The Company has investments that are valued in accordance with the provisions of SFAS 157. SFAS 157 establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

Level 1 Valuations based on quoted prices in active markets for identical assets that the Company has the ability to access.

Level 2 Valuations based inputs on other than quoted prices included within level 1, for which all significant inputs are observable, either directly or indirectly.

Level 3 Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

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

|                                   | Fair value of investments as of December 31, 2008 |   |   |  |
|-----------------------------------|---|---|---|--|
|                                   | Total   | Quoted Prices<br>In Active<br>Markets for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| Money market funds                | \$ 1,050  | \$ 1,050  | \$  | \$   |
| Corporate bonds                   | 11,673  |   | 11,673  |  |
| Federal and municipal obligations | 7,379   |   | 7,379   |  |
| ARS                               | 13,882  |   |   | 13,882   |
| Put Option                        | 2,509   |   |   | 2,509  |
|                                   | \$ 36,493   | \$ 1,050  | \$ 19,052   | \$ 16,391  |

Certain items in the table above are classified as Level 2 items because quoted prices in an active market are not readily accessible for those specific financial assets, and the Company may have relied on alternative pricing methods that do not rely exclusively on quoted prices to determine the fair value of the investments.

As of December 31, 2008, the Company had approximately \$16.5 million in ARS at par value. Since February 2008, substantially all auctions for ARS have failed as a result of the negative overall capital market conditions, meaning that there is not enough demand to sell the securities at auction. At December 31, 2008, the Company has classified its entire ARS investment balance as non-current on its Consolidated Balance Sheet because of the Company's inability to determine when its investments in ARS will settle. Typically the fair value of ARS investments approximates par value due to frequent interest rate resets through the auction process. While the Company continues to earn interest on its ARS

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investments at the maximum contractual rate, these investments are not currently trading and therefore do not currently have a readily determinable market value.

In November 2008, the Company elected to participate in a rights offering by UBS, the Company's investment broker, which provides Actuate with rights (the Put Option) to sell UBS \$16.5 million of its ARS portfolio at par value, at any time during a two-year sale period beginning June 30, 2010. By electing to participate in the rights offering, the Company granted UBS the right, exercisable at any time prior to June 30, 2010 or during the two-year sale period, to purchase or cause the sale of our ARS (the Call Right). UBS has stated that it will only exercise the Call Right for the purpose of restructurings, dispositions or other solutions that will provide their clients with par value for their ARS. UBS has agreed to pay their clients the par value of

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## ACTUATE CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

their ARS within one day of settlement of any Call Right transaction. Notwithstanding the Call Right, the Company is permitted to sell ARS to parties other than UBS, in which case the Put Option attached to the ARS that are sold would be extinguished. The Company has classified the Put Option as a non-current investment and has valued the Put Option at the present value of the difference between the fair market value and the par value of the ARS. As such, the Company recorded a realized loss of approximately \$84,000 related to the difference between the gain recognized on the Put Option and the realized loss on the \$16.5 million (par value) portion of the ARS portfolio.

The Company has no reason to believe that any of the underlying issuers of its ARS are presently at risk of default. Through December 31, 2008, the Company has continued to receive interest payments on the ARS in accordance with their terms. The Company believes that it will ultimately be able to liquidate its ARS related investments without significant loss primarily due to the collateral securing ARS and the legal settlements it has entered into with UBS. However, it could take until final maturity of the ARS (up to 39 years) to realize its investments' par value. Due to the changes and uncertainty in the ARS market, the Company believes the recovery period for these investments is likely to be longer than 12 months and as a result, the Company has classified these investments as long-term as of December 31, 2008.

The estimated fair value of ARS no longer approximates par value. The Company has used a discounted cash flow model to determine the estimated fair value of its investment in ARS as of December 31, 2008. The assumptions used in preparing the discounted cash flow model include estimates for interest rates, timing and amount of cash flows and expected holding periods of the ARS. Based on this assessment of fair value, as of December 31, 2008 the Company determined there was a decline in the fair value of its ARS investments of \$2.6 million. The Company considered the guidance contained in SEC Staff Accounting Bulletin No. 59, *Other Than Temporary Impairment of Certain Investments in Debt and Equity Securities* (SAB 59) and EITF 03-1 *The Meaning of Other-Than-Temporary Investments and its Application to Certain Investments*, and determined that 100% of this impairment was other-than-temporary at December 31, 2008. An other-than-temporary impairment charge is recorded as a realized loss in the Consolidated Statement of Income and reduces net income for the applicable accounting period. Prior to December 31, 2008, the ARS were classified as available-for-sale and all temporary changes in fair value were recognized in Accumulated Other Comprehensive Income (Loss) on the Company's Consolidated Balance Sheet. The main driving factor in Actuate's reclassification of the impairment to other-than-temporary was the UBS Settlement Agreement.

The following table represents the reconciliation of the beginning and ending balances of the Company's ARS and Put Option measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for fiscal year 2008 (in thousands).

|   | Fair Value<br>Measurements<br>Using Significant<br>Unobservable<br>Inputs<br>(Level 3)<br>ARS |
|---|---|
| Balance at December 31, 2007:                         | \$ 14,550   |
| Unrealized loss included in earnings                  | (2,593)   |
| Gain on fair value of Put Option included in earnings | 2,509   |
| Purchases of ARS                                      | 1,925   |
| Balance at December 31, 2008:                         | \$ 16,391   |



**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The Company's cash, cash equivalents, short-term investments and non-current investments are as follows (in thousands):

|  | Cost             | Net Gains<br>(losses) | Estimated<br>Fair Value |
|--|------------------|-----------------------|-------------------------|
| Balance at December 31, 2008             |                  |                       |                         |
| Classified as cash and cash equivalents: |                  |                       |                         |
| Cash                                     | \$ 21,947        | \$                    | \$ 21,947               |
| Money market funds                       | 1,050            |                       | 1,050                   |
| Federal and municipal obligations        | 1,775            |                       | 1,775                   |
|  | 24,772           |                       | 24,772                  |
| Classified as short-term investments:    |                  |                       |                         |
| Corporate bonds                          | 11,668           | 5                     | 11,673                  |
| Federal and municipal obligations        | 5,570            | 35                    | 5,605                   |
|  | 17,238           | 40                    | 17,278                  |
| Classified as non-current investments:   |                  |                       |                         |
| ARS                                      | 16,475           | (2,593)               | 13,882                  |
| Put Option                               |                  | 2,509                 | 2,509                   |
|  | 16,475           | (84)                  | 16,391                  |
| <b>Total</b>                             | <b>\$ 58,485</b> | <b>\$ (44)</b>        | <b>\$ 58,441</b>        |
|  |                  |                       |                         |
|  | Cost             | Net Gains<br>(losses) | Estimated<br>Fair Value |
| Balance at December 31, 2007             |                  |                       |                         |
| Classified as cash and cash equivalents: |                  |                       |                         |
| Cash                                     | \$ 16,525        | \$                    | \$ 16,525               |
| Money market funds                       | 4,943            |                       | 4,943                   |
|  | 21,468           |                       | 21,468                  |
| Classified as short-term investments:    |                  |                       |                         |
| Auction rate securities (ARS)            | 14,550           |                       | 14,550                  |
| Commercial paper                         | 13,903           | 9                     | 13,912                  |
| Corporate bonds                          | 12,972           | (9)                   | 12,963                  |
| Federal and municipal obligations        | 5,509            | 13                    | 5,522                   |
|  | 46,934           | 13                    | 46,947                  |
| <b>Total</b>                             | <b>\$ 68,402</b> | <b>\$ 13</b>          | <b>\$ 68,415</b>        |

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Any individual security in the above tables with an unrealized loss has been in a continuous unrealized loss position for less than twelve months. At this time, the Company believes that, due to the nature of the Company's investments, the financial condition of the issuer and the Company's ability to hold these investments through these short-term loss positions, factors would not indicate that these unrealized losses on investments, other than ARS and the Put Option, should be viewed as other-than-temporary.

As of December 31, 2008, the stated maturities of the Company's cash equivalents and short-term investments are \$2.8 million within 90 days and \$17.3 million beyond 90 days. Short-term investments are generally classified as available-for-sale and are recorded on the Company's Consolidated Balance Sheet at fair market value with unrealized gains or losses reported as a separate component of Accumulated Other

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**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Comprehensive Income (Loss). At December 31, 2008, Actuate has classified all of its marketable securities (other than ARS and the Put Option) as short-term investments, even though the stated maturity dates may be one year or more beyond the current balance sheet date as these investments are highly liquid and available for use in current operations.

**5. Property and Equipment**

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

|   | December 31, |          |
|---|--------------|----------|
|   | 2008         | 2007     |
| Furniture and fixtures                          | \$ 1,075     | \$ 1,521 |
| Computers and purchased software                | 8,465        | 8,542    |
| Leasehold improvements                          | 3,714        | 3,588    |
| Total   | 13,254       | 13,651   |
| Less: accumulated depreciation and amortization | (8,525)      | (8,382)  |
| Property and equipment, net                     | \$ 4,729     | \$ 5,269 |

**6. Goodwill and Purchased Intangible Assets**

In accordance with Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* ( SFAS 142 ), the Company performs its annual impairment test of goodwill on October 1st of each year. SFAS 142 requires that goodwill be tested at least annually using a two-step process that begins with identifying potential impairment. The potential impairment is identified if the fair value of the reporting unit to which goodwill applies is less than the recognized or book value of the related reporting entity, including such goodwill. Where the book value of a reporting entity, including related goodwill, is greater than the reporting entity's fair value, the second step of the goodwill impairment test is performed to measure the amount of impairment loss, if any. There have been no significant events or circumstances affecting the valuation of goodwill subsequent to the impairment test performed on October 1, 2008. As a result, the Company did not record any impairment related to its goodwill for the twelve months ended December 31, 2008.

Following is a roll-forward of the activity that affected goodwill during the fiscal year 2008 (in thousands):

|                                     |           |
|-------------------------------------|-----------|
| Goodwill as of December 31, 2007    | \$ 35,594 |
| Adjustment to tax benefits acquired | 520       |

Goodwill as of December 31, 2008

\$ 36,114

During fiscal year 2008, the Company recorded an immaterial correction from the prior fiscal year which resulted in adjustments to goodwill and purchased technology related to the tax benefits acquired from the performancesoft acquisition and the tax affected portion of the net operating losses utilized with respect to the Nimble acquisition, respectively. These adjustments resulted in a net increase of approximately \$520,000 to the Company's goodwill, and a decrease of approximately \$428,000 to the Company's purchased intangibles balance. There was an insignificant impact on the Company's Consolidated Statement of Income for the fiscal year ended December 31, 2008 as a result of this correction.

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**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)***Intangibles*

Other purchased intangible assets consist of the following (in thousands):

|                        | December 31, 2008           |                             |  | December 31, 2007 |                             |                             |                |
|------------------------|-----------------------------|-----------------------------|--|-------------------|-----------------------------|-----------------------------|----------------|
|                        | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Adjustment<br>to Purchase<br>Price<br>Allocation | Net<br>Balance    | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Net<br>Balance |
| Customer lists         | \$ 14,000                   | \$ (12,640)                 | \$   | \$ 1,360          | \$ 14,000                   | \$ (11,960)                 | \$ 2,040       |
| Purchased technologies | 8,430                       | (7,562)                     | (428)  | 440               | 8,430                       | (7,089)                     | 1,341          |
| Trademark              | 1,500                       | (1,500)                     |  |                   | 1,500                       | (1,233)                     | 267            |
|                        | \$ 23,930                   | \$ (21,702)                 | \$ (428)   | \$ 1,800          | \$ 23,930                   | \$ (20,282)                 | \$ 3,648       |

Amortization of purchased intangible assets was approximately \$1.4 million, \$1.9 million and \$2.0 million for years ended December 31, 2008, 2007 and 2006, respectively. These charges are included in cost of license fees and amortization of purchased intangibles in the accompanying Consolidated Statements of Income. The expected remaining annual amortization expense is summarized as follows (in thousands):

| Fiscal Year | Purchased<br>Technology and<br>Intangibles |
|-------------|--|
| 2009        | 900  |
| 2010        | 900  |
|             | \$ 1,800                                   |

**7. Deferred Revenue**

Deferred revenue consists of the following (in thousands):

|                         | December 31,<br>2008 | December 31,<br>2007 |
|-------------------------|----------------------|----------------------|
| Maintenance and support | \$ 38,070            | \$ 37,847            |
| Other                   | 5,302                | 6,004                |

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|                            |    |          |    |          |
|----------------------------|----|----------|----|----------|
|                            | \$ | 43,372   | \$ | 43,851   |
| Less: Current portion      |    | (40,900) |    | (40,352) |
| Long-term deferred revenue | \$ | 2,472    | \$ | 3,499    |

Maintenance and support consists of first year maintenance and support services associated with the initial purchase of Actuate's software, and the renewal of annual maintenance and support services from customers who purchased Actuate's software in prior periods. The maintenance and support period is generally 12 months and revenues are typically recognized on a straight-line basis over the term of the maintenance and support period.

Other deferred revenue consists of deferred license, training and consulting fees generated from arrangements, which did not meet some or all of the revenue recognition criteria of SOP No. 97-2 and are, therefore, deferred until all revenue recognition criteria have been met.

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**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****8. Contractual Obligations and Commercial Commitments***Revolving credit line*

In November 2008, the Company entered into a four year revolving line of credit agreement with Wells Fargo, LLC ( *Credit Agreement* ). The *Credit Agreement* was effective as of November 3, 2008 and allows for cash borrowings and letters of credit under a secured revolving credit facility of up to a maximum of \$50.0 million, but not to exceed 80% of the Company's trailing four quarters of recurring maintenance revenue. Interest is based on a floating rate plus an applicable margin based on the outstanding balance of the amount drawn under the *Credit Agreement*. The floating rate is determined at the Company's election and may either be (i) London Interbank Offered Rate ( *LIBOR* ) or (ii) the greater of the Federal Funds Rate plus an applicable margin and the Prime Rate. If the Company's usage of the credit line exceeds 80% of its trailing four quarters of recurring maintenance revenue, or if the sum of available funds under the *Credit Agreement* plus available cash is less than \$10.0 million the Company is required to meet certain minimum income targets and be subject to a limit on annual capital expenditures. The Company is required to make interest payments and pay an unused commitment fee on a monthly basis. The Company incurred approximately \$68,000 of interest expense associated with the credit facility during fiscal year 2008. The *Credit Agreement* also requires that the Company pay a closing fee based on a percentage of the overall available facility. Total costs associated with the facility including legal and closing fees amount to approximately \$1.2 million. Of these total costs, approximately \$400,000 was paid as of December 31, 2008. The remaining balance is comprised of legal fees totaling approximately \$400,000 payable during the first quarter of fiscal year 2009 and commitment fees of which \$250,000 are due and payable on the first anniversary of the credit facility in November of fiscal year 2009 and \$125,000 is due and payable on the third anniversary in November of fiscal year 2011. These costs are being capitalized and amortized over four years in accordance with SFAS 91, *Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases* . These costs are classified as current assets if payable within one year or non-current assets if payable beyond one year in the Company's Consolidated Balance Sheet at December 31, 2008.

Because of the Company's indebtedness, a significant portion of the Company's cash flow from operations is and will be required for debt service. The Company's levels of debt could have negative consequences. It should be noted that:

A substantial portion of the Company's cash flow is, and will be, dedicated to debt service and is not, and will not be, available for other purposes;

The Company's ability to obtain additional financing for working capital, capital expenditures, acquisitions and general corporate or other purposes may be impaired in the future;

The Company's borrowings are, and will be, at variable rates of interest, which may expose the Company to the risk of increases in interest rates;

The Company's level of indebtedness could make it more vulnerable to economic downturns, limit its ability to withstand competitive pressures and reduce the Company's flexibility in responding to changing business and economic conditions.

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The Credit Agreement contains financial covenants, which, among other things, require the Company to maintain specified financial ratios and impose certain limitations with respect to lines of business, mergers, investments and acquisitions, additional indebtedness, distributions, guarantees, liens and encumbrances. The Company was in compliance with these financial and non-financial covenants at December 31, 2008. The Company's indebtedness under the Credit Agreement is secured by a lien on (i) substantially all of its assets and the assets of Actuate International Corporation and (ii) by a pledge of all of its stock and a portion of the stock of each of its subsidiaries.

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**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The Company believes that cash flows from operations will be sufficient to meet its current debt service requirements for interest and any required prepayments under the Credit Agreement. However, if such cash flow is not sufficient, the Company may be required to issue additional debt or equity securities, refinance its obligations, or take other actions in order to make such scheduled payments. The Company cannot be sure that it would be able to effect any such transactions on favorable terms, if at all and failure to do so may cause an event of default under the Credit Agreement, which will have a material adverse effect on the Company's business, operating results and financial conditions.

***Operating Lease Commitments***

The Company reached the end of its lease term on its previous corporate headquarters located at 701 Gateway, in South San Francisco in February 2008. In anticipation of this event, on June 1, 2007, the Company entered into a five year sublease agreement with Oracle Corporation for approximately 83,000 square feet of office space in the Bridgepointe Campus in San Mateo, California. This lease is operating in nature, commenced on August 1, 2007 and ends on July 31, 2012. In addition, the lease provides for approximately nine months of free rent (rent holiday) and approximately \$600,000 in landlord incentives to be applied by Actuate towards construction of improvements. The incentives were applied to leasehold improvements completed during the fourth quarter of fiscal year 2007. The Company accounts for and recognizes the rent holidays in its operating lease on a straight-line basis over the lease term (including any rent holiday period) in accordance with paragraph 2 of FASB Technical Bulletin 85-3 ( FTB 85-3 ), *Accounting for Operating Leases with Scheduled Rent Increases*. The Company accounts for the amortization of its leasehold improvements over the duration of the lease consistent with SFAS 13 ( SFAS 13 ), *Accounting for Leases, as amended*. Leasehold improvements made by the Company that are funded by landlord incentives or allowances under an operating lease are recorded by the Company as leasehold improvement assets and amortized over the term of the lease. The incentives are recorded as deferred rent and amortized as reductions to lease expense over the lease term in accordance with SFAS 13.

As of December 31, 2008, Actuate pledged \$655,000 of restricted cash as collateral for a standby letters of credit that guarantees its contractual obligations relating to certain sublease agreements including its new corporate headquarter facilities located at the Bridgepointe Campus in San Mateo, California. This restricted cash is classified as Other Assets in the accompanying Consolidated Balance Sheet.

The following table summarizes our contractual lease obligations as of December 31, 2008 (in thousands):

| Fiscal Year | Future<br>Minimum<br>Lease<br>Payments(1) |
|-------------|---|
| 2009        | 5,256                                     |
| 2010        | 4,535                                     |
| 2011        | 3,081                                     |
| 2012        | 1,661                                     |
| Thereafter  | 993                                       |
| Total       | \$ 15,526                                 |

- (1) Our future contractual obligations include minimum lease payments under operating leases at December 31, 2008, net of contractual sublease proceeds. Of the remaining net future minimum lease payments, approximately \$4.5 million is included in restructuring liabilities on the Company's Consolidated Balance Sheet as of December 31, 2008.

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**ACTUATE CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Indemnification*

Our license agreements include indemnification for infringement of third party intellectual property rights and certain warranties. Historically, the Company has not experienced significant claims under these contractual rights. Therefore, no amounts have been accrued relating to those indemnities and warranties.

**9. Stockholders Equity**

*Preferred Stock*

Under the terms of the certificate of incorporation, the Board of Directors is authorized, subject to any limitations prescribed by law, to issue preferred stock in one or more series. Each series shall have the rights, preferences, privileges and restrictions, related to dividend rights, dividend rates, conversion rights, voting rights, terms of redemption, redemption prices, liquidation preferences and the right to increase or decrease the number of shares of any series, as the Board of Directors shall determine. The Board of Directors may issue preferred stock with voting or conversion rights that may have the effect of delaying, deferring or preventing a change in control of Actuate and could adversely affect the market price of the common stock and the voting and other rights of the holders of common stock. The Company currently has no plans to issue any preferred stock.

*Stock Option Plans*

*Amended and Restated 1998 Equity Incentive Plan.* In May 1998, the Amended and Restated 1998 Equity Incentive Plan (the 1998 Plan ) was adopted by the Board of Directors and approved by the stockholders in July 1998. Employees, consultants and directors are eligible for awards under the 1998 Plan. Initially, a total of 5,200,000 shares of common stock were reserved for issuance under the 1998 Plan. As of January 1 of each year, the number of shares reserved for issuance under the 1998 Plan is increased automatically by the lesser of (i) 5% of the total number of shares of common stock then outstanding or (ii) 2,800,000 shares. The 1998 Plan has been amended and restated to account for stock splits.

Under the 1998 Plan, eligible participants may be awarded options to purchase shares of common stock, stock appreciation rights ( SARs ), restricted shares or stock units (collectively, the Awards ). Options under the 1998 Plan may be incentive stock options designed to satisfy Section 422 of the Internal Revenue Code of 1986, as amended (the Code ) or non-statutory stock options not designed to meet such requirements. If restricted shares or shares issued upon the exercise of options granted under the 1998 Plan are forfeited, then such shares will again become available for Awards under the 1998 Plan. If stock units, options or SARs granted under the 1998 Plan are forfeited or terminated for any other reason before being exercised, then the corresponding shares will again become available for Awards under the 1998 Plan. The exercise price for non-statutory and incentive stock options granted under the 1998 Plan may not be less than 85% or 100%, respectively, of the fair market value of the common stock on the option grant date. The Board may amend or terminate the 1998 Plan at any time. Amendments may be subject to stockholder approval to the extent required by applicable laws.

Options granted under the 1998 Plan are exercisable when vested. Shares generally vest at the rate of 20% or 25% after one year from the date of grant with the remaining balance vesting monthly over the next four or three years, with a maximum contractual life of ten years. Upon a change in control, an Award under the 1998 Plan will become fully vested as to all shares subject to such Award if such Award is not assumed by the surviving corporation or its parent and the surviving corporation or its parent does not substitute such Award with another Award of substantially the same terms. In the event of an involuntary termination of a participant within 12 months following a change in control, the vesting of an Award under the 1998 Plan will accelerate in full. All outstanding repurchase rights under the 1998 Plan shall terminate automatically upon the occurrence of

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**ACTUATE CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

any merger, consolidation, or disposition of all or substantially all of the Company's assets, except to the extent the repurchase rights are expressly assigned to the successor corporation. As of December 31, 2008, 14,383,895 shares of common stock were reserved and available for future grants under the 1998 Option Plan.

*2001 Supplemental Stock Plan.* In January 2001, the Board of Directors adopted the 2001 Supplemental Stock Plan (the 2001 Plan). A total of 2,700,000 shares of common stock were reserved for issuance under the 2001 Plan. Employees and consultants are eligible for awards under the 2001 Plan. Members of the Board of Directors and officers of Actuate are not eligible to receive awards under the 2001 Plan.

Under the 2001 Plan, eligible participants may be awarded options to purchase shares of common stock and restricted shares only. All options granted under the 2001 Plan are non-statutory stock options. If restricted shares or shares issued upon the exercise of options granted under the 2001 Plan are forfeited, then such shares will again become available for awards under the 2001 Plan. The exercise price for non-statutory and incentive stock options granted under the 2001 Plan may not be less than 85% or 100%, respectively, of the fair market value of the common stock on the option grant date. The Board may amend or terminate the 2001 Plan at any time. Amendments may be subject to stockholder approval to the extent required by applicable laws.

Options granted under the 2001 Plan are exercisable when vested. Shares generally vest at the rate of 25% after one year from the date of grant with the remaining balance vesting monthly over the next four years, with a maximum contractual life of ten years. Upon a change in control, an award under the 2001 Plan will become fully vested as to all shares subject to such award if such award is not assumed by the surviving corporation or its parent and the surviving corporation or its parent does not substitute such award with another award of substantially the same terms. In the event of an involuntary termination of a participant within 12 months following a change in control, the vesting of an award under the 2001 Plan will accelerate in full. All outstanding repurchase rights under the 2001 Plan shall terminate automatically upon the occurrence of any merger, consolidation, or disposition of all or substantially all of the Company's assets, except to the extent the repurchase rights are expressly assigned to the successor corporation. As of December 31, 2008, 714,600 shares of common stock were reserved and available for future grants under the 2001 Option Plan.

*Tidestone Technologies Stock Option Plans.* Tidestone Technologies, Inc.'s 1998 Incentive Stock Option Plan (T-98 Option Plan) and Non-qualified Stock Option Plan of 1999 (T-99 Option Plan) were assumed by the Company on May 30, 2001, in connection with the acquisition of Tidestone. The T-98 Option Plan and the T-99 Option Plan are collectively known as the Tidestone Option Plans. Each option under the Tidestone Option Plans was converted into a right to receive an option to purchase shares of Actuate's common stock. As of December 31, 2008, a total of 77,968 and 70,509 shares of common stock have been authorized for issuance under the T-98 Option Plan and T-99 Option Plan, respectively.

All options granted under the T-98 Option Plan are incentive stock options qualified under Section 422 of the Code, with a vesting term of five years while the options granted under the T-99 Option Plan are non-statutory stock options with a vesting term of three years. All options have a maximum contractual life of ten years. Options granted under the Tidestone Option Plans are generally exercisable upon grant and are subject to repurchase rights by us until vested. Under the T-99 Option Plan, shares generally vest at the rate 33% annually. Under the T-98 Option Plan, shares generally vest at the rate of 20% annually. Upon a change in control, an award under the Tidestone Option Plans will become fully vested as to all shares subject to such award if such award is not assumed by the surviving corporation or its parent and the surviving corporation or its

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parent does not substitute such award with another award of substantially the same terms. The T-98 Option Plan reached its maximum contractual ten year life on July 23, 2008 and employee options are no longer available for issuance under this Plan. As of December 31, 2008, 2,055 shares of common stock were reserved and available for future grants under the T-99 Option Plan.

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**ACTUATE CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*1998 Non-Employee Director Option Plan.* The 1998 Non-Employee Directors Option Plan (the Directors Option Plan ) was adopted by the Board of Directors in May 1998, and approved by the stockholders in July 1998. The Director Option Plan provides for non-employee members of the Board of Directors to be eligible for automatic option grants. 800,000 shares of common stock have been authorized for issuance under the Directors Option Plan. Each individual who first joins the Board as a non-employee director, whether through election or appointment, will receive at that time an automatic option grant for 80,000 shares of common stock. With respect to the initial automatic option grant, the option will become exercisable as to 25% of the shares after one year of Board service, with the balance of the shares becoming exercisable ratably in 36 monthly installments over the remaining period of optionee's Board service. At each annual stockholders meeting beginning in fiscal year 1999, each current non-employee director will automatically be granted a stock option to purchase 10,000 shares of common stock, whether or not he or she is standing for re-election at that particular meeting, which will become fully vested and exercisable on the first anniversary of such meeting. Each option will have an exercise price equal to the fair market value of the common stock on the automatic grant date and a maximum term of ten years, subject to earlier termination following the optionee's cessation of Board service.

In March 2007, the Board of Directors amended the automatic stock option grant program for non-employee directors under the Directors Plan to change the number of shares covered by the initial and annual awards to non-employee directors, beginning with the grants to be made at the 2007 Annual Meeting. The amendment reduced the number of option shares which will automatically be granted to each individual who first joins the Board as a non-employee director from 80,000 to 40,000 option shares and increased the number of option shares which will be automatically granted to each continuing non-employee Board member at each Annual Stockholders Meeting from 10,000 option shares to 25,000 option shares. All other terms of the program including vesting schedules for the initial grant and the annual grant remain unchanged.

All Directors are eligible to receive option awards under Actuate's Amended and Restated 1998 Equity Incentive Plan (the 1998 Plan ). In January 2008, the Board of Directors resolved that starting with the grant awards to be made at the 2008 Annual Meeting, all grant awards to the non-employee directors shall be made under the 1998 Plan rather than the Directors Plan. All other terms of the non-employee director program, including vesting schedules for the initial grant award and the automatic annual award remain unchanged.

As of December 31, 2008, 230,000 shares of common stock were reserved and available for future grants under the Directors Option Plan.

Shares issued as a result of the exercise of options under any of our plans would be fulfilled through shares currently in our existing pools. Total authorized but unissued shares of common stock were 32,207,163 as of December 31, 2008.

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Activity under all option plans was as follows:

|                                 | Shares Available For Grant | Outstanding Options |                 | Weighted-Average Exercise Price |
|---------------------------------|----------------------------|---------------------|-----------------|---------------------------------|
|                                 |                            | Number of Shares    | Price Per Share |                                 |
| Balance at December 31, 2005    | 11,573,471                 | 19,292,404          | \$ 0.16-\$31.19 | \$ 2.83                         |
| Additional authorization        | 2,800,000                  |                     |                 |                                 |
| Options granted                 | (3,141,200)                | 3,141,200           | \$ 3.16-\$5.94  | \$ 3.70                         |
| Options exercised               |                            | (1,640,855)         | \$ 0.16-\$5.26  | \$ 2.11                         |
| Options forfeited and cancelled | 1,245,831                  | (1,245,831)         | \$ 1.04-\$17.25 | \$ 3.55                         |
| Balance at December 31, 2006    | 12,478,102                 | 19,546,918          | \$ 0.16-\$31.19 | \$ 2.98                         |
| Additional authorization        | 2,800,000                  |                     |                 |                                 |
| Options granted                 | (3,364,700)                | 3,364,700           | \$ 4.99-\$8.39  | \$ 5.53                         |
| Options exercised               |                            | (3,282,257)         | \$ 0.16-\$5.90  | \$ 2.53                         |
| Options forfeited and cancelled | 880,215                    | (880,215)           | \$ 1.27-\$21.63 | \$ 4.40                         |
| Balance at December 31, 2007    | 12,793,617                 | 18,749,146          | \$ 0.75-\$31.19 | \$ 3.45                         |
| Additional authorization        | 2,800,000                  |                     |                 |                                 |
| Options granted                 | (2,441,280)                | 2,441,280           | \$ 2.20-\$7.81  | \$ 5.78                         |
| Options exercised               |                            | (2,100,088)         | \$ 0.75-\$5.11  | \$ 2.36                         |
| Options forfeited and cancelled | 2,213,725                  | (2,213,725)         | \$ 1.80-\$8.39  | \$ 4.30                         |
| Plan shares expired             | (35,512)                   |                     |                 |                                 |
| Balance at December 31, 2008    | 15,330,550                 | 16,876,613          | \$ 0.78-\$31.19 | \$ 3.82                         |

The weighted-average grant date fair value of stock options granted was \$3.58 in fiscal year 2008, \$3.75 in fiscal year 2007 and \$2.40 in fiscal year 2006. Upon the exercise of options, the Company issues new common stock from its authorized shares. The total intrinsic value of options exercised during fiscal year 2008, 2007 and 2006 was \$3.5 million, \$14.0 million and \$4.3 million, respectively.

| Range of Exercise Prices | Number of Shares | Options Outstanding                         |                                 | Options Exercisable |                                 |
|--------------------------|------------------|---|---------------------------------|---------------------|---------------------------------|
|                          |                  | Weighted-Average Remaining Contractual Life | Weighted-Average Exercise Price | Number of Shares    | Weighted-Average Exercise Price |
| \$0.78-\$1.49            | 4,423,164        | 4.17 years                                  | \$ 1.49                         | 4,423,164           | \$ 1.49                         |
| \$1.56-\$2.99            | 2,818,479        | 5.56 years                                  | \$ 2.61                         | 2,712,719           | \$ 2.62                         |
| \$3.00-\$3.89            | 3,223,923        | 5.18 years                                  | \$ 3.63                         | 2,732,076           | \$ 3.65                         |
| \$3.90-\$5.27            | 3,354,831        | 6.63 years                                  | \$ 4.83                         | 2,016,087           | \$ 4.78                         |
| \$5.30-\$31.19           | 3,056,216        | 7.64 years                                  | \$ 7.37                         | 738,010             | \$ 10.99                        |
| \$0.78-\$31.19           | 16,876,613       | 5.71 years                                  | \$ 3.82                         | 12,622,056          | \$ 3.28                         |



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|   | December 31,<br>2008 | December 31,<br>2007 |
|---|----------------------|----------------------|
| Options Outstanding Vested and Expected to Vest                           |                      |                      |
| Vested and expected to vest, net of expected forfeitures                  | 16,626,377           | 18,309,895           |
| Aggregate intrinsic value (in thousands)                                  | \$ 7,499             | \$ 82,530            |
| Weighted average exercise price per share                                 | \$ 3.79              | \$ 3.43              |
| Weighted average remaining contractual term (in years)                    | 5.67                 | 5.77                 |
| Options Exercisable   |                      |                      |
| Options currently exercisable   | 12,622,056           | 13,787,490           |
| Aggregate intrinsic value of currently exercisable options (in thousands) | \$ 7,437             | \$ 68,429            |
| Weighted average exercise price per share                                 | \$ 3.28              | \$ 3.02              |
| Weighted average remaining contractual term (in years)                    | 4.81                 | 4.88                 |

***Amended and Restated 1998 Employee Stock Purchase Plan***

The 1998 Amended and Restated Employee Stock Purchase Plan (the Purchase Plan) was adopted by the Board of Directors in May 1998, and approved by the stockholders in July 1998. A total of 1,000,000 shares of common stock were initially reserved for issuance under the Purchase Plan. On January 1 of each year, the number of shares reserved for issuance under the Purchase Plan is automatically increased by 600,000 shares. The Purchase Plan is intended to qualify under Section 423 of the Code. Each calendar year, two overlapping 24-month offering periods will commence on February 1 and August 1. Each offering period contains four six-month accumulation periods, with purchases occurring at the end of each six-month accumulation period. If the market price of Actuate's stock at the end of any six-month purchase period is lower than the stock price at the original grant date, the offering period is cancelled immediately after that purchase date. A new 24-month offering period is established using the then-current stock price as the base purchase price. The Purchase Plan permits each eligible employee to purchase common stock through payroll deductions, which may not exceed 15% of an employee's cash compensation. Employees enrolled prior to August 1, 2006 may purchase up to 500 shares per accumulation period until the end of their current accumulation period at which time they may purchase up to 1000 shares per accumulation period. New participants starting in the August 1 offering period may purchase up to 1000 shares per accumulation period. The price of each share of common stock purchased under the Purchase Plan will be 85% of the lower of (i) the fair market value per share of common stock on the date immediately prior to the first date of the applicable offering period or (ii) the date at the end of the applicable accumulation period. Employees may end their participation in the Purchase Plan at any time during the accumulation period, and participation ends automatically upon termination of employment with the Company. The Purchase Plan has been amended and restated to account for stock splits. During fiscal year 2008, 2007 and 2006, the Company issued 422,863, 311,718 and 219,629 common shares, respectively under the Purchase Plan, with a weighted-average purchase price of \$4.11, \$2.82 and \$2.10, respectively. As of December 31, 2008, 5,293,637 shares had been purchased under the Purchase Plan and 1,706,363 shares of common stock were reserved and available for future issuance.

As of December 31, 2008, the number of shares of common stock reserved for future issuance of stock options under all option plans and the Purchase Plan was 17,036,913.

***Valuation and Expense Information under SFAS 123(R)***

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Beginning January 1, 2006, the Company adopted SFAS 123R. The Company currently uses the Black-Scholes-Merton option pricing model to determine the fair value of stock options and employee stock purchase plan shares. The determination of the fair value of stock-based payment awards on the date of grant using an

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option-pricing model is affected by the Company's stock price as well as assumptions regarding a number of complex and subjective variables. These variables include expected stock price volatility over the term of the award, actual and projected employee stock option exercise behaviors, risk-free interest rate and expected dividends.

Compensation cost for all share-based payments granted is based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R. The Company amortizes its stock-based compensation expense for all awards in accordance with the method described in Financial Accounting Standards Board Interpretation 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans*.

Share-based compensation expense and the related income tax benefit recognized under Statement of Financial Accounting Standards, or SFAS No. 123R, *Share-Based Payment* in the Consolidated Statements of Income in connection with stock options and the Employee Stock Purchase Plan ( ESPP ) for the fiscal years ended December 31, 2008, 2007 and 2006 were as follows (in thousands):

|                                       | <b>Year ended December 31,</b> |                 |                 |
|---------------------------------------|--------------------------------|-----------------|-----------------|
|                                       | <b>2008</b>                    | <b>2007</b>     | <b>2006</b>     |
| Stock options                         | \$ 7,974                       | \$ 8,367        | \$ 6,111        |
| ESPP                                  | 1,148                          | 619             | 381             |
| <b>Total stock-based compensation</b> | <b>\$ 9,122</b>                | <b>\$ 8,986</b> | <b>\$ 6,492</b> |
| Income tax benefit                    | \$ 948                         | \$ 4,760        | \$ 2,274        |

We estimate the expected term of options granted by analyzing actual historical experience of exercises and cancellations under our plans. We also look at the average length of time in which our current outstanding options are expected to be exercised or cancelled based on past experience and the vesting and contractual term. We estimate the volatility of our common stock by using historical volatility over the expected term. We base the risk-free interest rate that we use in the option valuation model on the published Treasury rate. We do not anticipate paying any cash dividends in the foreseeable future and therefore use an expected dividend yield of zero in the option valuation model. The assumptions we use to estimate the fair value of stock options granted and stock purchase rights granted under our ESPP program for the fiscal years 2008, 2007 and 2006 are as follows:

|                          | <b>Options</b>                 |        |             |        |             |        |
|--------------------------|--------------------------------|--------|-------------|--------|-------------|--------|
|                          | <b>Year ended December 31,</b> |        |             |        |             |        |
|                          | <b>2008</b>                    |        | <b>2007</b> |        | <b>2006</b> |        |
| Dividends                | 0%                             |        | 0%          |        | 0%          |        |
| Forfeiture rate          | 3                              | 4%     | 3           | 4%     | 4           | %      |
| Risk-free interest rate  | 1.50                           | 3.50%  | 3.625       | 4.75%  | 4.50        | 4.88%  |
| Expected life (in years) | 5.48                           | 5.70   | 5.31        | 5.50   | 4.16        | 4.60   |
| Expected volatility      | 57.75                          | 71.49% | 75.36       | 80.41% | 80.88       | 86.82% |

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|                          | ESPP                    |        |       |        |       |        |
|--------------------------|-------------------------|--------|-------|--------|-------|--------|
|                          | 2008                    |        | 2007  |        | 2006  |        |
|                          | Year ended December 31, |        |       |        |       |        |
| Dividends                | 0%                      |        | 0%    |        | 0%    |        |
| Risk-free interest rate  | 2.05                    | 2.18%  | 4.47  | 5.05%  | 4.68  | 5.08%  |
| Expected life (in years) | 0.5                     |        | 0.5   |        | 0.5   |        |
| Expected volatility      | 43.13                   | 55.79% | 35.78 | 38.66% | 42.58 | 46.05% |

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**ACTUATE CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The weighted-average grant date fair value of stock options granted was \$3.58 in fiscal year 2008, \$3.75 in fiscal year 2007 and \$2.40 in fiscal year 2006.

During fiscal years 2008, 2007 and 2006, Actuate issued 422,863 shares, 311,718 shares and 219,629 shares, respectively, under the Purchase Plan. The weighted-average fair value of employees' stock purchase rights under the Purchase Plan during fiscal years 2008, 2007 and 2006 was \$1.90, \$1.91 and \$1.44, respectively.

The total compensation cost for share-based payments and the related tax benefits was \$9.1 million and \$948,000, respectively in fiscal year 2008. The total compensation cost for share-based payments and the related tax benefits was \$9.0 million and \$4.8 million, respectively in fiscal year 2007.

***Stock Repurchase Program***

On October 24, 2007, the Company's Board of Directors authorized an acceleration of its existing stock repurchase program. As of October 24, 2007, the Company was authorized to repurchase shares in an amount not to exceed approximately \$6.3 million per quarter, and the cumulative amount not to exceed \$50.0 million over a two year period. On February 4, 2008, the Company's Board of Directors authorized a further acceleration of the Company's existing stock repurchase program which allowed for the repurchase of 2,638,560 shares of Actuate common stock at a cost of approximately \$10.0 million in the first half of fiscal year 2008.

On November 3, 2008, the Company announced its intention to commence a modified Dutch auction tender offer to purchase up to \$60.0 million worth of its common stock, at a price per share not less than \$3.15 and not greater than \$3.50. On December 29, 2008, the Company announced the final results of its tender offer and agreed to purchase and pay \$3.50 per share for 17,142,857 of these shares at a total cost of \$60.0 million. This repurchase was completed in fiscal year 2008 and was funded by \$30.0 million in cash and an additional \$30.0 million drawn under the Company's credit facility. The Company has subsequently suspended its stock repurchase program.

**10. Actuate 401(k) Plan**

The Company sponsors a salary deferral 401(k) plan for all of its eligible domestic employees. This plan allows employees to contribute up to 60% of their pretax salary up to the maximum dollar limitation prescribed by the Internal Revenue Code. Beginning in fiscal year 2007, the Company started to match 50% of the employee's first 3% contribution. The maximum match in any given plan year is the lower of 3% of the employee's eligible compensation or the then current IRS compensation wage limit. In 2007 the IRS wage limit was \$225,000 and the maximum match was \$3,375 per employee. The Company's contributions under the plan were charged to operations and totaled approximately \$400,000 in fiscal 2007. In 2008 the IRS wage limit was \$230,000 and the maximum match was \$3,450 per employee. The Company's contributions under the plan were charged to operations and totaled approximately \$382,000 in fiscal year 2008.



**11. Restructuring Charges**

During the first half of fiscal year 2007, the Company evaluated the consolidation of its facilities as a result of the performance soft acquisition and determined that a \$297,000 facility-related restructuring charge was required. This charge was directly related to the consolidation of its three offices located in the United Kingdom into one office. These restructuring charges were accounted for in accordance with FAS 146, which requires the recognition of costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan.

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During the second half of fiscal year 2007, the Company recorded a restructuring charge related to the relocation of its headquarters facility from South San Francisco to San Mateo, California and the closure of its service facility in Iselin, New Jersey. These charges were primarily comprised of rent and operating expenses through the end of the lease term for the fully vacated portion of the South San Francisco facility, impairment of fixed assets and leasehold improvements considered abandoned, and relocation costs to the new facility. The Company also recorded restructuring charges for rent and operating expenses for the Company's Iselin, New Jersey facility. As a result of these relocations, the Company recorded a total restructuring charge of approximately \$1.4 million in the second half of fiscal year 2007 in accordance with FAS 146.

During the first half of fiscal year 2008, the Company recorded facility related restructuring charges totaling \$271,000. These charges primarily related to additional lease exit costs associated with the Company's South San Francisco facility; the closure of one of the three floors in our Toronto, Canada facility and the consolidation of our Vienna, Virginia facilities into one location. The Company also incurred approximately \$132,000 in legal fees related to a previous restructuring which involved the terminations of former employees in one of our European subsidiaries.

In order to size the operations to meet the expected business and economic environment for its products, the Company implemented an additional restructuring plan during the second half of fiscal year 2008 to eliminate 46 positions held by Actuate employees, primarily in North America. The reduction in force was completed in fiscal year 2008 and impacted all functional areas. The restructuring plan also included costs related to the world-wide consolidation of facilities, the cancellation of certain contracts and the write-off of fixed assets located at facilities that have been vacated.

The following table summarizes the restructuring accrual activity for the fiscal years ended December 31, 2006, 2007 and 2008 (in thousands):

|                                 | <b>Severance<br/>&amp; Benefits</b> | <b>Facility<br/>Related</b> | <b>Total</b> |
|---------------------------------|-------------------------------------|-----------------------------|--------------|
| Balance at December 31, 2005    | \$ 465                              | \$ 12,368                   | \$ 12,833    |
| Restructuring charges           | 45                                  | (29)                        | 16           |
| Cash payments                   | (89)                                | (3,450)                     | (3,539)      |
| Changes in estimate             | 29                                  | 1                           | 30           |
| Rents collected on the sublease |                                     | 1,318                       | 1,318        |
| Balance at December 31, 2006    | 450                                 | 10,208                      | 10,658       |
| Restructuring charges           |                                     | 1,686                       | 1,686        |
| Cash payments                   |                                     | (4,967)                     | (4,967)      |
| Loss on disposal of assets      |                                     | (244)                       | (244)        |
| Changes in estimate             | 14                                  | (9)                         | 5            |
| Rents collected on the sublease |                                     | 1,669                       | 1,669        |
| Balance at December 31, 2007    | 464                                 | 8,343                       | 8,807        |
| Restructuring charges           | 1,101                               | 405                         | 1,506        |
| Cash payments                   | (1,027)                             | (4,666)                     | (5,693)      |
| Changes in estimate             | 23                                  | (66)                        | (43)         |

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|  |       |          |          |
|--|-------|----------|----------|
| Rents collected on the sublease        |       | 1,721    | 1,721    |
|  | 561   | 5,737    | 6,298    |
| Less: Current portion                  | (561) | (2,645)  | (3,206)  |
| Long-term balance at December 31, 2008 | \$    | \$ 3,092 | \$ 3,092 |

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**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****12. Income Taxes**

The following table presents the profit before income taxes for domestic and foreign operations (in thousands):

|                            | Year ended December 31, |           |           |
|----------------------------|-------------------------|-----------|-----------|
|                            | 2008                    | 2007      | 2006      |
| Domestic                   | \$ 4,500                | \$ 11,900 | \$ 8,300  |
| Foreign                    | 8,000                   | 7,400     | 4,500     |
| Profit before income taxes | \$ 12,500               | \$ 19,300 | \$ 12,800 |

The benefit from income taxes consists of the following (in thousands):

|                           | Year ended December 31, |          |          |
|---------------------------|-------------------------|----------|----------|
|                           | 2008                    | 2007     | 2006     |
| Federal:                  |                         |          |          |
| Current                   | \$ 66                   | \$ 4,720 | \$ 3,174 |
| Deferred                  | (2,056)                 | (5,728)  | (3,556)  |
|                           | (1,990)                 | (1,008)  | (382)    |
| State:                    |                         |          |          |
| Current                   | 70                      | 698      | 1051     |
| Deferred                  | (1,196)                 | (897)    | (2,013)  |
|                           | (1,126)                 | (199)    | (962)    |
| Foreign:                  |                         |          |          |
| Current                   | 1,447                   | 219      | 402      |
| Deferred                  | 351                     | 125      | (32)     |
|                           | 1,798                   | 344      | 370      |
| Benefit from income taxes | \$ (1,318)              | \$ (863) | \$ (974) |

The tax benefits associated with exercises of stock options reduced taxes currently payable by approximately \$948,000, \$4.8 million and \$2.3 million for the years ended December 31, 2008, 2007 and 2006, respectively. Such benefits were credited to additional paid-in capital. Tax expense associated with the increase of tax reserves increased taxes currently payable by approximately \$1.2 million in fiscal year 2008,

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\$164,000 in 2007 and \$275,000 in fiscal year 2006.

The tax expense associated with the utilization of acquired deferred tax assets and the release of the valuation allowance increased goodwill and intangibles by approximately \$92,000 and \$70,000 in fiscal year 2008 and 2007, respectively. For 2006, the tax benefits associated with the utilization of acquired deferred tax assets and the valuation allowance release reduced goodwill and intangibles by \$1.5 million.

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**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following table represents the tax expenses /(benefits) associated with the utilization of acquired deferred tax assets and the release of the valuation allowance (in thousands):

|  | Year ended December 31, |        |            |
|--|-------------------------|--------|------------|
|  | 2008                    | 2007   | 2006       |
| Purchased Technology   | \$ (428)                | \$ 139 | \$ (149)   |
| Goodwill   | 520                     | (69)   | (1,398)    |
| Tax/ Expense (benefit) from acquired deferred tax assets and valuation allowance release | \$ 92                   | \$ 70  | \$ (1,547) |

During fiscal year 2008, the Company recorded the correction of an error from the prior fiscal year which resulted in adjustments to goodwill and purchased technology related to the tax benefits acquired from the performancesoft acquisition and the deferred tax assets utilized with respect to the Nimble acquisition. The correction resulted in a reversal of tax benefit previously credited to goodwill and intangibles of approximately \$237,000 in fiscal year 2008. In addition, the current year tax benefits from the utilization of performancesoft deferred tax assets and the related valuation allowance release of approximately \$145,000 were credited to goodwill.

The difference between the benefit from income taxes and the amount computed by applying the federal statutory rate (35 percent) to income before taxes is explained below (in thousands):

|   | Year ended December 31, |          |          |
|---|-------------------------|----------|----------|
|   | 2008                    | 2007     | 2006     |
| Income taxes at federal statutory rate      | \$ 4,377                | \$ 6,755 | \$ 4,488 |
| Permanent differences                       | 175                     | (34)     | 942      |
| Foreign tax rate differential               | (866)                   | (1,871)  | (1,097)  |
| Valuation allowance release                 | (1,270)                 | (6,757)  | (5,406)  |
| State tax, net of federal benefit           | (1,150)                 | 1,260    | 695      |
| Tax benefit related to a foreign subsidiary | (3,403)                 | 0        | 0        |
| Tax credits                                 | (354)                   | (381)    | (909)    |
| Increase of tax reserves                    | 1,147                   | 164      | 275      |
| Other                                       | 26                      | 1        | 38       |
| Benefit from income taxes                   | \$ (1,318)              | \$ (863) | \$ (974) |

As of December 31, 2008, the Company had federal net operating loss carry-forwards of approximately \$3.5 million. Of this amount, \$1.5 million can be carried back two years and the remaining federal net operating loss carry-forwards will expire in 2023 if not utilized. As of December 31, 2008, the Company had federal and state research tax credit carry-forwards of approximately \$2.7 million and \$8.2 million, respectively. The federal research credits will expire at various dates beginning in the year 2018 through 2028, if not utilized. The state research

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credits can be carried forward indefinitely. The Company also had approximately \$159,000 of foreign tax credits which are due to expire at various dates beginning in the year 2010 through 2014.

Utilization of the net operating losses and the research tax credits may be subject to a substantial annual limitation due to the ownership change limitations provided by Section 382 and 383 of the Internal Revenue Code and similar state provisions. The annual limitation may result in the expiration of net operating losses and tax credits before utilization.

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**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

United States income and foreign withholding taxes have not been provided on undistributed earnings for certain non-U.S. subsidiaries. The undistributed earnings on a book basis for the non-U.S. subsidiaries are approximately \$10.6 million. The Company intends to reinvest these earnings indefinitely in its operations outside the U.S. If the undistributed earnings are remitted to the U.S. these amounts would be taxable in the U.S. at the current federal and state tax rates net of foreign tax credits. Also, depending on the jurisdiction any distribution may be subject to withholding taxes at rates applicable for that jurisdiction. During the fiscal year ended December 31, 2008, the Company benefited from the terms of a tax holiday in Switzerland which is due to expire in 2010.

Significant components of deferred tax assets and liabilities for federal and states are as follows (in thousands):

|  | <b>December 31,</b> |               |
|--|---------------------|---------------|
|  | <b>2008</b>         | <b>2007</b>   |
| <b>Deferred tax assets</b>                           |                     |               |
| Net operating loss carry-forwards                    | \$ 3,463            | \$ 6,541      |
| Research credit carry-forwards                       | 7,103               | 6,636         |
| performancesoft deferred tax assets                  | 2,402               | 1,839         |
| Depreciation and amortization                        | 951                 | 226           |
| Accruals and allowances not currently tax deductible | 5,707               | 6,344         |
| Non-qualified stock options (SFAS 123R)              | 6,736               | 4,321         |
| <br>Total deferred tax assets                        | <br>\$ 26,362       | <br>\$ 25,907 |
| <br>Valuation allowance                              | <br>(8,093)         | <br>(10,667)  |
| <br>Net deferred tax assets                          | <br>\$ 18,269       | <br>\$ 15,240 |
| <br><b>Deferred tax liabilities</b>                  |                     |               |
| Acquired intangible assets                           | \$ 1,898            | \$ 2,339      |
| <br>Net deferred tax assets                          | <br>\$ 16,371       | <br>\$ 12,901 |

SFAS No. 109, *Accounting for Income Taxes*, provides for the recognition of deferred tax assets if realization of such assets is more likely than not. The net valuation allowance decreased by approximately \$2.6 million and \$6.6 million during the years ended December 31, 2008 and 2007, respectively. The \$2.6 million decrease in the valuation allowance in fiscal year 2008 resulted from the release of the valuation allowance from the write off of the deferred tax assets associated with a foreign subsidiary of \$1.4 million and the release of the valuation allowance of \$1.2 million related to the utilization of net operating losses, tax credits, change in tax rates and foreign exchange rates. The \$6.6 million decrease in fiscal year 2007 mostly related to temporary differences, utilization of net operating losses and tax credits. As of December 31, 2008, approximately \$4.2 million of the valuation allowance reflected above relates to the tax benefits of stock option deductions that will be credited to additional paid-in capital when realized, approximately \$2.4 million of the valuation allowance reflected above relates to the tax attributes from acquisitions that will be credited to intangibles and goodwill, when realized and the remaining \$1.5 million is related to foreign net operating losses which will be credited to tax expense when realized.



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In July 2006, the Financial Accounting Standards Board (the FASB ) issued Interpretation No. 48 ( FIN 48 ), Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109. FIN 48 clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on

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**Table of Contents****ACTUATE CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

de-recognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 applies to all tax positions related to income taxes.

On January 1, 2007, the Company adopted the provisions of FIN 48. The adoption and implementation of FIN 48 resulted in federal, state, and foreign unrecognized tax benefits of \$2.2 million. Of that total, approximately \$320,000 of the unrecognized tax benefits, if recognized would affect the effective tax rate. The \$2.2 million of unrecognized tax benefits was accounted for as a reduction of \$1.8 million to deferred tax assets and the corresponding valuation allowance, an increase in the long term liability of approximately \$320,000 which includes a transfer of \$275,000 from current tax liability to long term tax liability and approximately \$45,000 to the January 1, 2007 balance of retained earnings.

A reconciliation of the January 1, 2007 through December 31, 2008 amount of unrecognized tax benefits are as follows (in thousands):

|  |          |
|--|----------|
| Beginning balance at January 1, 2007                         | \$ 2,168 |
| Additions based on tax positions related to the current year | 164      |
| Ending balance at December 31, 2007                          | \$ 2,332 |
| Additions based on tax positions related to the current year | 1,588    |
| Ending balance at December 31, 2008                          | \$ 3,920 |

As of December 31, 2008, the Company had total federal, state, and foreign unrecognized tax benefits of \$3.9 million. Of that total, approximately \$1.7 million of the unrecognized tax benefits, if recognized would affect the effective tax rate.

Upon adoption of FIN 48, the Company adopted an accounting policy to classify interest and penalties on unrecognized tax benefits as income tax expense. During its fiscal years for 2003 through 2007, the Company has not recognized any interest and penalties in its Consolidated Statement of Income and Consolidated Statement of Financial Position. During 2008, approximately \$229,000 was accrued for the payment of interest and penalties.

As of December 31, 2008, the Company does not expect any material changes to uncertain tax positions within the next twelve months.

The Company files income tax returns in the U.S. federal, states, and various foreign jurisdictions. Management believes that its accrual for tax liabilities is adequate for all open audit years based on its assessment of many factors including past experience and interpretations of tax law. This assessment relies on estimates and assumptions and may involve a series of complex judgments about future events. The 2003 to 2008 tax years generally remain subject to U.S. federal, state, or non-U.S. income tax examinations.

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During fiscal year 2008, the Company also completed a Texas income tax audit which resulted in no change in the income tax due. The Company has a California income tax audit in process for the 2005 and 2006 tax years. The audit is in its initial stages and no issues have been identified at this point. No other federal, state or foreign income tax audits are in progress.

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**Table of Contents****13. Geographic Information**

Actuate's primary operations are located in the United States. Revenues from international sources relate to export sales, primarily to Europe. Actuate's revenues by geographic area are as follows (in thousands):

|                         | Year ended December 31, |            |            |
|-------------------------|-------------------------|------------|------------|
|                         | 2008                    | 2007       | 2006       |
| Revenues:               |                         |            |            |
| North America           | \$ 94,109               | \$ 102,610 | \$ 96,955  |
| Europe                  | 32,479                  | 33,839     | 26,679     |
| Asia Pacific and others | 4,402                   | 4,177      | 4,935      |
| Total revenue           | \$ 130,990              | \$ 140,626 | \$ 128,569 |

**14. Contingencies**

Actuate is engaged in certain legal actions arising in the ordinary course of business. Although there can be no assurance as to the outcome of such litigation, Actuate believes that the ultimate outcome of these actions will not have a material effect on its Consolidated Financial Position and results of operations.

**15. Subsequent Events**

On January 30, 2009, the Company amended and restated its Bylaws. Key changes made to the Bylaws addressed the following subjects:

Advance Notice Provisions,

Calling Special Meetings of Stockholders,

Quorum at Stockholder Meetings,

Voting Requirement at Stockholder Meetings,

Officers, and

Indemnification.

**Table of Contents****16. Selected Quarterly Financial Data (Unaudited)**

The following tables set forth certain unaudited financial data for the eight quarters ended December 31, 2008 (in thousands, except per share data).

|                               | Quarter Ended     |                  |                       |                      |
|-------------------------------|-------------------|------------------|-----------------------|----------------------|
|                               | March 31,<br>2008 | June 30,<br>2008 | September 30,<br>2008 | December 31,<br>2008 |
| Revenues                      | \$ 29,521         | \$ 34,600        | \$ 33,681             | \$ 33,188            |
| Income (loss) from operations | \$ (949)          | \$ 3,296         | \$ 3,443              | \$ 5,685             |
| Net income                    | \$ 2,907          | \$ 2,895         | \$ 3,105              | \$ 4,671             |
| Net income per share:         |                   |                  |                       |                      |
| Basic                         | \$ 0.05           | \$ 0.05          | \$ 0.05               | \$ 0.08              |
| Diluted                       | \$ 0.04           | \$ 0.04          | \$ 0.05               | \$ 0.08              |

|                        | Quarter Ended     |                  |                       |                      |
|------------------------|-------------------|------------------|-----------------------|----------------------|
|                        | March 31,<br>2007 | June 30,<br>2007 | September 30,<br>2007 | December 31,<br>2007 |
| Revenues               | \$ 31,975         | \$ 34,700        | \$ 34,739             | \$ 39,212            |
| Income from operations | \$ 1,580          | \$ 4,118         | \$ 3,820              | \$ 6,628             |
| Net income             | \$ 1,396          | \$ 3,383         | \$ 4,607              | \$ 10,778            |
| Net income per share:  |                   |                  |                       |                      |
| Basic                  | \$ 0.02           | \$ 0.06          | \$ 0.08               | \$ 0.18              |
| Diluted                | \$ 0.02           | \$ 0.05          | \$ 0.07               | \$ 0.16              |

**Table of Contents****SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS****(In thousands)**

|                                  | <b>Balance at<br/>beginning<br/>of period</b> | <b>Acquired<br/>through<br/>acquisition</b> | <b>Additions<br/>(reductions)<br/>charged to<br/>costs and<br/>expenses</b> | <b>Additions<br/>charged<br/>to<br/>other<br/>accounts(1)</b> | <b>Deductions(2)</b> | <b>Balance at<br/>end of period</b> |
|----------------------------------|---|---|---|---|----------------------|-------------------------------------|
| Allowance for doubtful accounts: |   |   |   |   |                      |                                     |
| Year ended December 31, 2008     | \$ 1,141                                      | \$  | \$ 239  | \$ (557)  | \$ (217)             | \$ 606                              |
| Year ended December 31, 2007     | 826   | \$  | \$ 159  | \$ 472  | \$ (316)             | \$ 1,141                            |
| Year ended December 31, 2006     | 1,318   | 405   | (184)   | (235)   | (478)                | 826                                 |

(1) Represents amounts charged to revenue and deferred revenue for sales returns and other revenue related items.

(2) Deductions are primarily comprised of write-offs of receivable balances against the allowance for doubtful accounts.