

PROS Holdings, Inc.
Form 10-Q
May 08, 2012
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2012

OR

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

Commission File Number: 001-33554

PROS HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Edgar Filing: PROS Holdings, Inc. - Form 10-Q

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

76-0168604
(I.R.S. Employer
Identification No.)

**3100 Main Street, Suite 900,
Houston, TX 77002; (713) 335-5151**

(Address and telephone number of Principal Executive Offices)

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

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

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

Large Accelerated Filer Accelerated Filer

Non-Accelerated Filer (do not check if a smaller reporting company) Smaller Reporting Company

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

The number of shares outstanding of the Registrant's Common Stock, \$0.001 par value, was 27,337,577 as of May 3, 2012.

Table of Contents

PROS Holdings, Inc.

Form 10-Q

For the Quarterly Period Ended March 31, 2012

Table of Contents

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Interim Condensed Consolidated Financial Statements (Unaudited)</u>	
<u>Condensed Consolidated Balance Sheets</u>	3
<u>Condensed Consolidated Statements of Comprehensive Income</u>	4
<u>Condensed Consolidated Statements of Cash Flows</u>	5
<u>Notes to Consolidated Financial Statements</u>	6
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	12
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	16
<u>Item 4. Controls and Procedures</u>	17
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	17
<u>Item 1A. Risk Factors</u>	17
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	29
<u>Item 3. Defaults Upon Senior Securities</u>	29
<u>Item 4. Mine Safety Disclosure</u>	29
<u>Item 5. Other Information</u>	29
<u>Item 6. Exhibits</u>	29
<u>Signatures</u>	31

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements relate to future events or our future financial performance. These forward-looking statements regarding future events and our future results are based on current expectations, estimates, forecasts and projections, and the beliefs and assumptions of our management including, without limitation, our expectations regarding the following: the sales of our software products and services; the impact of our revenue recognition policies; our belief that our current assets, including cash, cash equivalents, and expected cash flows from operating activities, will be sufficient to fund our operations; our anticipated additions to property, plant and equipment; our belief that our facilities are suitable and adequate to meet our current operating needs; our belief that we do not have any material exposure to changes in the fair value of our investment portfolio as a result of changes in interest rates. Words such as we expect, anticipate, target, project, believe, goals, estimate, potential, predict, may, might, could, intend, and variations of these types of words and similar expressions are intended to identify these forward-looking statements.

Table of Contents**PART I. Financial Information****ITEM 1. INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****PROS Holdings, Inc.****Condensed Consolidated Balance Sheets****(In thousands, except share amounts)****(Unaudited)**

	March 31, 2012	December 31, 2011
Assets:		
Current assets:		
Cash and cash equivalents	\$ 70,913	\$ 68,457
Accounts and unbilled receivables, net of allowance of \$910 and \$1,130, respectively	27,865	33,864
Prepaid and other current assets	8,525	8,353
Total current assets	107,303	110,674
Restricted cash	329	329
Property and equipment, net	5,319	4,703
Other long term assets, net	5,700	5,553
Total assets	\$ 118,651	\$ 121,259
Liabilities and Stockholders Equity:		
Current liabilities:		
Accounts payable	\$ 4,717	\$ 4,915
Accrued liabilities	1,118	1,318
Accrued payroll and other employee benefits	2,080	5,139
Deferred revenue	30,732	33,094
Total current liabilities	38,647	44,466
Long-term deferred revenue	2,810	2,850
Total liabilities	41,457	47,316
Commitments and contingencies (Note 5)		
Stockholders' equity:		
Preferred stock, \$0.001 par value, 5,000,000 shares authorized none issued		
Common stock, \$0.001 par value, 75,000,000 shares authorized, 31,753,002 and 31,432,430 shares issued, respectively,		
27,335,417 and 27,014,845 shares outstanding, respectively	32	31
Additional paid-in capital	79,993	77,934
Treasury stock, 4,417,585 common shares, at cost	(13,938)	(13,938)
Accumulated other comprehensive loss	(11)	(11)
Retained earnings	11,118	9,927
Total stockholders equity	77,194	73,943
Total liabilities and stockholders equity	\$ 118,651	\$ 121,259

Edgar Filing: PROS Holdings, Inc. - Form 10-Q

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

Table of Contents**PROS Holdings, Inc.****Condensed Consolidated Statements of Comprehensive Income****(In thousands, except share and per share data)****(Unaudited)**

	For the Three Months Ended March 31,	
	2012	2011
Revenue:		
License and implementation	\$ 17,796	\$ 13,793
Maintenance and support	9,225	7,613
Total revenue	27,021	21,406
Cost of revenue:		
License and implementation	5,986	4,623
Maintenance and support	1,935	1,710
Total cost of revenue	7,921	6,333
Gross profit	19,100	15,073
Operating expenses:		
Selling, marketing, general and administrative	10,252	7,871
Research and development	6,697	5,960
Income from operations	2,151	1,242
Other income:		
Interest income	1	18
Income before income tax provision	2,152	1,260
Income tax provision	961	404
Net income	\$ 1,191	\$ 856
Net earnings per share:		
Basic	\$ 0.04	\$ 0.03
Diluted	\$ 0.04	\$ 0.03
Weighted average number of shares:		
Basic	27,166,973	26,594,083
Diluted	28,284,044	27,447,436
Other comprehensive income, net of tax:		
Other comprehensive income		
Comprehensive income	\$ 1,191	\$ 856

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

Table of Contents**PROS Holdings, Inc.****Condensed Consolidated Statements of Cash Flows****(In thousands)****(Unaudited)**

	For the Three Months Ended March 31,	
	2012	2011
Operating activities:		
Net income	\$ 1,191	\$ 856
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	427	367
Share-based compensation	2,032	1,756
Excess tax benefits on share-based compensation	(1,395)	(852)
Deferred income tax		(201)
Provision for doubtful accounts	(220)	38
Changes in operating assets and liabilities:		
Accounts and unbilled receivables	6,219	4,471
Prepaid expenses and other assets	1,040	(203)
Accounts payable	(183)	(706)
Accrued liabilities	(226)	(641)
Accrued payroll and other employee benefits	(3,059)	(669)
Deferred revenue	(2,402)	1,716
Net cash provided by operating activities	3,424	5,932
Investing activities:		
Purchases of property and equipment	(1,031)	(697)
Increase in restricted cash		(36)
Increase in short-term investment		(292)
Net cash used in investing activities	(1,031)	(1,025)
Financing activities:		
Exercise of stock options	488	1,066
Excess tax benefits on share-based compensation	1,395	852
Tax withholding related to net share settlement of restricted stock units	(1,820)	(1,171)
Net cash provided by financing activities	63	747
Net increase in cash and cash equivalents	2,456	5,654
Cash and cash equivalents:		
Beginning of period	68,457	55,845
End of period	\$ 70,913	\$ 61,499

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

Table of Contents

PROS Holdings, Inc.

Notes to Condensed Consolidated Financial Statements

(Unaudited)

1. Organization and Nature of Operations

PROS Holdings, Inc., a Delaware corporation, through its operating subsidiaries (the Company), is a leading global provider of profitability management and optimization software. This software is an emerging category of enterprise applications designed to allow business to make better sales decisions to significantly improve business agility in dynamic markets. The Company offers its large enterprise and mid-market customers secure and scalable software solutions which optimize pricing and product mix on a real-time basis by applying advanced forecasting and optimization technologies to their relevant enterprise and market data. The Company's software solutions are engineered to work together with existing customer information technology, including private and public cloud environments, and support the real-time, high volume transaction processing and database requirements of some of the world's largest and most sophisticated businesses. The Company also provides professional services to configure its software solutions to meet the specific integration and process needs of each customer. The Company provides its software solutions to enterprises across a range of industries, including manufacturing, distribution, services and travel.

2. Summary of Significant Accounting Policies

The accompanying unaudited condensed consolidated financial statements reflect the application of significant accounting policies as described below and elsewhere in these notes to the condensed consolidated financial statements.

Basis of presentation

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial reporting and applicable quarterly reporting regulations of the Securities and Exchange Commission (SEC). In management's opinion, the accompanying interim unaudited condensed consolidated financial statements include all adjustments necessary for a fair statement of the financial position of the Company as of March 31, 2012, the results of operations for the three months ended March 31, 2012 and cash flows for the three months ended March 31, 2012. Certain information and disclosures normally included in the notes to the annual financial statements prepared in accordance with GAAP have been omitted from these interim unaudited condensed consolidated financial statements pursuant to the rules and regulations of the SEC. Accordingly, these unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2011 (Annual Report) filed with the SEC. The condensed consolidated balance sheet as of December 31, 2011 was derived from the Company's audited consolidated financial statements, but does not include all disclosures required by GAAP.

Basis of consolidation

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

Dollar amounts

The dollar amounts presented in the tabular data within these footnote disclosures are stated in thousands of dollars, except per unit amounts, or as noted within the context of each footnote disclosure.

Use of estimates

The Company's management prepares the unaudited condensed consolidated financial statements in accordance with GAAP. The Company makes estimates and assumptions in the preparation of its unaudited condensed consolidated financial statements, and its estimates and assumptions may affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the unaudited condensed consolidated financial statements, and the reported amounts of revenue and expenses during the reporting periods. Actual results could differ from those estimates. The complexity and judgment required in the Company's estimation process and issues related to the assumptions, risks and uncertainties inherent

Table of Contents

in the application of the percentage-of-completion method of accounting affect the amounts of revenue, expenses, unbilled receivables and deferred revenue. Estimates are also used for, but not limited to, receivables, allowance for doubtful accounts, useful lives of assets, depreciation, income taxes and deferred tax asset valuation, valuation of stock options, other current liabilities and accrued liabilities. Numerous internal and external factors can affect estimates. The critical accounting policies related to the estimates and judgments are discussed in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 under management's discussion and analysis of financial condition and results of operations. There have been no significant changes to the Company's critical accounting policies as described in the Company's Annual Report.

Revenue recognition

The Company derives its revenue from the licensing and implementation of software solutions and associated software maintenance and support. To a lesser extent, the Company's revenue includes non-software related hosting services. The Company's arrangements with customers typically include: (a) license fees paid for the use of our solutions either in perpetuity or over a specified term and implementation fees for configuration, implementation and training services and (b) maintenance and support fees related to technical support and software updates. If there is significant uncertainty about contract completion or collectability is not reasonably assured, revenue is deferred until the uncertainty is sufficiently resolved or collectability is reasonably assured. In addition, revenue is recognized when persuasive evidence of an arrangement exists and fees are fixed or determinable. For certain arrangements, we engage an independent contractor or a system integrator to assist in the implementation of our software solutions. These arrangements are analyzed based on numerous factors to determine the amount of revenue to be recognized.

The Company's software license arrangements typically include implementation services that are considered essential to the customer's usability of the licensed software solutions and therefore new perpetual software license revenue is generally recognized with the implementation services using the percentage-of-completion method. The percentage-of-completion computation is measured by the percentage of man-days incurred during the reporting period as compared to the estimated total man-days necessary for each contract for implementation of the software solutions. The Company measures performance under the percentage-of-completion method using total man-day method based on current estimates of man-days to complete the project. The Company believes that for each such project, man-days expended in proportion to total estimated man-days at completion represents the most reliable and meaningful measure for determining a project's progress toward completion. Under our fixed-fee arrangements, should a loss be anticipated on a contract, the full amount is recorded when the loss is determinable.

The Company also licenses software solutions under term license agreements that typically include maintenance during the license term. When maintenance is included for the entire term of the license, there is no renewal rate and the Company has not established vendor specific objective evidence (VSOE) of fair value for the maintenance. For term license agreements, revenue and the associated costs are deferred until the delivery of the solution and recognized ratably over the remaining license term.

For arrangements that include hosting services we allocate the arrangement consideration between the hosting service and other elements and recognize the hosting fee ratably beginning on the date the customer commences use of our services and continuing through the end of the customer term.

The Company's customer arrangements typically contain multiple elements that include software license, implementation services and post-implementation maintenance and support. In October 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2009-13, Multiple-Deliverable Revenue Arrangements, (amendments to FASB Accounting Standards Codification (ASC)) Topic 605, Revenue Recognition), which amended the accounting standards for certain multiple deliverable revenue arrangements that contain non-software related elements to:

provide updated guidance on whether multiple deliverables exist, how the deliverables in an arrangement should be separated, and how the consideration should be allocated;

require an entity to allocate revenue in an arrangement using best estimated selling price, (BESP) of deliverables if a vendor does not have VSOE of selling price; and

eliminate the use of the residual method and require an entity to allocate revenue using the relative selling price method.

Edgar Filing: PROS Holdings, Inc. - Form 10-Q

For multiple element arrangements containing our non-software services, the Company must (1) determine whether and when each element has been delivered; (2) determine fair value of each element using the selling price hierarchy of VSOE of fair value, third party evidence (TPE), or BESP, as applicable, and (3) allocate the total price among the various elements based on the relative selling price method.

For multiple-element arrangements that contain software and non-software elements such as the Company's hosted offerings, we allocate revenue to software or software related elements as a group and any non-software elements separately based on the selling price hierarchy. The Company determines the selling price for each deliverable using VSOE of selling price, if it exists.

In certain instances, the Company may not be able to establish VSOE for all deliverables in an arrangement with multiple elements. This may be due to infrequently selling each element separately, not pricing solutions or services within a narrow range, or only having a limited sales history. In addition, third party evidence may not be available. When the Company is unable to establish selling prices using VSOE or TPE, it uses BESP in our allocation of arrangement consideration. The objective of BESP is to determine the price at which the Company would transact a sale if the product or service were sold on a stand-alone basis. Revenue is then recognized when the basic revenue recognition criteria are met for each element. For transactions that only include software and software-related elements the Company continues to account for such arrangements under the software revenue recognition standards which require it to establish VSOE of fair value to allocate arrangement consideration to multiple deliverables.

Maintenance and support revenue includes post-implementation customer support and the right to unspecified software updates and enhancements on a when and if available basis. The Company generally invoices for maintenance and support services on a monthly, quarterly or on an annual basis through the maintenance and support period. The Company recognizes revenue from maintenance arrangements ratably over the period in which the services are provided.

Software license and implementation revenue that has been recognized, but for which the Company has not invoiced the customer, is recorded as unbilled receivables. Invoices that have been issued before software license, implementation and maintenance and support revenue has been recognized are recorded as deferred revenue in the accompanying unaudited condensed consolidated balance sheets.

Internal-use software

Costs incurred to date to develop internal-use software during the application development stage are capitalized, stated at cost, and depreciated using the straight-line method over the estimated useful lives of the assets. Application development stage costs generally include costs associated with internal-use software configuration, coding, installation and testing. During the three months ended March 31, 2012, the Company capitalized internal-use software development costs of \$0.4 million related to its cloud-based product offerings and \$0.3 million related to the implementation of a new enterprise resource planning system. Capitalized software for internal use is included in property and equipment, net in the condensed consolidated balance sheets.

Noncash share-based compensation

The Company measures all share-based payments to its employees based on the grant date fair value of the awards and recognizes expense in the Company's unaudited consolidated statement of comprehensive income on a straight-line basis over the period during which the recipient is required to perform service (generally over the vesting period of the awards). To date, the Company has granted Stock Options, Stock Appreciation Rights (SARs), Restricted Stock Units (RSUs) and Market Stock Units (MSUs). The MSUs are performance-based awards that vest based upon the Company's relative shareholder return.

Table of Contents

The following table presents the number of awards outstanding for each award type as of March 31, 2012 and December 31, 2011, respectively (in thousands).

Award type	At March 31, 2012	At December 31, 2011
Stock options	1,539	1,581
Restricted stock units	1,331	1,153
Stock appreciation rights	825	836
Market share units	205	

Stock options, SARs and RSUs vest ratably between three and four years. The actual number of MSUs that will be eligible to vest is based on the total shareholder return of the Company relative to the total shareholder return of the Russell 2000 Index (Index) over a two year period ending December 31, 2013 (performance period). The MSUs vest on January 1, 2014, and the maximum number of shares issuable upon vesting is 200% of the MSUs initially granted.

The fair value of the restricted stock units is based on the closing price of the Company's stock on the date of grant.

The Company estimates the fair value of MSUs on the date of grant using a Monte Carlo simulation model. The determination of fair value of the MSUs is affected by the Company's stock price and a number of assumptions including the expected volatilities of the Company's stock and the Index, its risk-free interest rate and expected dividends. The Company's expected volatility at the date of grant was based on the historical volatilities of the Company and the Index over the performance period. The Company did not estimate a forfeiture rate for the MSUs due to the limited size, the vesting period and nature of the grantee population and the lack of history of granting this type of award.

The assumptions used to value the MSUs granted during the three months ended March 31, 2012 were as follows:

	2012
Volatility	61%
Risk-free interest rate	0.28%
Expected option life in years	1.88
Dividend yield	0

Earnings per share

The Company computes basic earnings per share by dividing net income by the weighted average number of common shares outstanding. Diluted earnings per share is computed by dividing net income by the weighted average number of common shares and dilutive potential common shares then outstanding. Potential common shares consist of shares issuable upon the exercise of stock options and SARs or the vesting of share-based awards. Diluted earnings per share reflects the assumed conversion of all dilutive share-based awards using the treasury stock method.

Fair value measurement

The Company's financial assets that are measured at fair value on a recurring basis consisted of \$58.0 million invested in treasury money market funds at March 31, 2012 and December 31, 2011, respectively. The fair value of these accounts is determined based on quoted market prices, which represents level 1 in the fair value hierarchy as defined by Accounting Standard Codification, (ASC), 820, *Fair Value Measurement and Disclosure*. The Company's treasury money market funds have a fair value that is not materially different from its carrying amount.

Deferred revenue and unbilled receivables

Software license and implementation services that have been performed, but for which the Company has not invoiced the customer, are recorded as unbilled receivables, and invoices that have been issued before the software license and implementation services have been performed are recorded as deferred revenue in the accompanying unaudited condensed consolidated balance sheets. The Company generally invoices for maintenance and support services on a monthly, a quarterly or an annual basis through the maintenance and support period.

Table of Contents

Income taxes

At the end of each interim reporting period, the Company estimates its annual effective tax rate to calculate its income tax provision. The estimated effective tax rate includes U.S. federal, state and foreign income taxes and is based on the application of an estimated annual income tax rate applied to the current quarter's year-to-date pre-tax income. This estimated effective tax rate is used in providing for income taxes on a year-to-date basis and may change in subsequent interim reporting periods. The effective tax rate for the three months ended March 31, 2012 and 2011 was 45% and 32%, respectively. The increase in the effective tax rate in three months ended March 31, 2012 compared to the three months ended March 31, 2011 is due primarily to nondeductible share-based compensation expense and the effect of the nonrenewal of the R&E tax credit effective in 2012. The difference between the effective tax rate and the federal statutory rate of 34% for the three months ended March 31, 2012 was due primarily to nondeductible share-based compensation expense.

Recent accounting pronouncements

In December 2011, the FASB issued ASU 2011-12, *Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassification of Items Out of Accumulated Other Comprehensive Income in ASU 2011-5*. ASU 2011-12 defers the effective date pertaining to reclassification adjustments out of accumulated other comprehensive income in ASU 2011-5, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income*. The Company adopted the standard on January 1, 2012, reporting comprehensive income in a single continuous financial statement in its unaudited condensed statements of comprehensive income. For the three months ending March 31, 2012 and 2011, the Company did not report other comprehensive income in its unaudited consolidated statements of comprehensive income. In previous periods, the Company has reported cumulative foreign currency translation adjustments in other comprehensive income related to a wholly-owned foreign subsidiary. Since this standard affects disclosure requirements only, its adoption did not have a material impact on the Company's consolidated financial statements.

Table of Contents**3. Earnings per Share**

The following table sets forth the computation of basic and diluted earnings per share for the three months ended March 31, 2012 and 2011:

	For the Three Months Ended March 31,	
	2012	2011
Numerator:		
Net income	\$ 1,191	\$ 856
Denominator:		
Weighted average shares (basic)	27,167	26,594
Dilutive effect of potential common shares	1,117	853
Weighted average shares (diluted)	28,284	27,447
Basic earnings per share	\$ 0.04	\$ 0.03
Diluted earnings per share	\$ 0.04	\$ 0.03

Dilutive potential common shares consist of shares issuable upon the exercise of stock options, settlement of SARs, and vesting of RSUs. The MSUs are not included in dilutive potential common shares outstanding as they were determined to be antidilutive for the three months ended March 31, 2012. Potential common shares determined to be antidilutive and excluded from diluted weighted average shares outstanding were approximately 413,000 and 960,000 for the three months ended March 31, 2012 and 2011, respectively.

4. Noncash Share-based Compensation

The Company granted 552,300 shares of RSUs with a weighted average grant-date fair value of \$19.04 during the three months ended March 31, 2012. During the three months ended March 31, 2012, the Company granted 205,000 MSUs with a weighted average grant-date fair value of \$26.08 to certain executive officers and non-executive employees. The Company did not grant any stock options or SARs during the three months ended March 31, 2012.

The following table summarizes share-based compensation expense included in the Company's unaudited condensed consolidated statements of comprehensive income for the three months ended March 31, 2012 and 2011:

	For the Three Months Ended March 31,	
	2012	2011
Share-based compensation:		
Cost of revenue:		
License and implementation	\$ 329	\$ 334
Total included in cost of revenue	329	334
Operating expenses:		
Selling, marketing, general and administrative	1,268	1,072
Research and development	435	350
Total included in operating expenses	1,703	1,422
Total share-based compensation expense	\$ 2,032	\$ 1,756

Edgar Filing: PROS Holdings, Inc. - Form 10-Q

In February 2012, the Company increased the number of shares available for issuance by 900,000 to 6,368,000 under an evergreen provision in the Company's 2007 Equity Incentive Plan (" Plan "). As of March 31, 2012, 665,891 shares remained available for issuance under the Plan. At March 31, 2012, there was an estimated \$25.7 million of total unrecognized compensation costs related to share-based compensation arrangements. These costs will be recognized over a weighted average period of 3.0 years.

Table of Contents

5. Commitments and Contingencies

Litigation:

In the ordinary course of the Company's business, the Company regularly becomes involved in contract and other negotiations and, in more limited circumstances, becomes involved in legal proceedings, claims and litigation. The outcomes of these matters are inherently unpredictable. The Company is not currently involved in any outstanding litigation that it believes, individually or in the aggregate, will have a material adverse effect on its business, results of operations or financial condition.

Table of Contents

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

The terms we, us and our refer to PROS Holdings, Inc. and all of its subsidiaries that are consolidated in conformity with accounting principles generally accepted in the United States of America.

This management's discussion and analysis of financial condition and results of operations should be read along with the unaudited condensed consolidated financial statements and unaudited notes to condensed consolidated financial statements included in Item 1 of this Quarterly Report on Form 10-Q, as well as the audited consolidated financial statements and notes to consolidated financial statements and management's discussion and analysis of financial condition and results of operations set forth in our Annual Report on Form 10-K for the year ended December 31, 2011.

Overview

We are a leading provider of enterprise pricing and margin optimization software to enterprises across a range of industries, including manufacturing, distribution, services and travel. These products are an emerging category of enterprise applications designed to allow companies to improve financial performance by implementing pricing excellence best practices. Enterprises use our software to gain insight into their pricing strategies, identify detrimental pricing practices, optimize their pricing decision-making and improve their business processes and financial performance. Our software incorporates advanced pricing science, which includes operations research, forecasting and statistics. Our innovative science-based software products analyze, execute and optimize pricing strategies using data elements determined using pricing algorithms, including the pocket price, pocket margin, customer willingness-to-pay, customer cost-to-serve, win-loss ratios, market price, stretch price, as well as data from traditional enterprise applications often augmenting it with real-time and historical data and external data sources. Our high performance software architecture supports real-time high volume transaction processing and allows us to handle the processing and database requirements of the most sophisticated and largest customers, including customers with hundreds of simultaneous users and sub-second electronic transactions. We provide professional services to configure, integrate and customize our solutions to meet the specific pricing needs of each customer.

Many of our customers process large volumes of individually priced business-to-consumer and business-to-business transactions every day. Our high-performance, real-time, dynamic pricing products differ from static retail pricing products by delivering the relevant pricing information at the time the price is quoted, the deal is negotiated and the sale transaction is made. Our software products are also used to provide optimized price lists and goal-driven price guidance. While companies in our target industries differ in the wide range of business-to-business and business-to-customer products and services that they provide, many are similar in their need to improve pricing agility in dynamic markets, improve control of their pricing processes and optimally price each individual transaction. Since inception, we have implemented over 500 solutions across a range of industries in more than 50 countries.

Opportunities, Trends and Uncertainties

We have noted opportunities, trends and uncertainties that we believe are particularly significant to understand our financial results and condition.

Growth opportunities. We believe the market for pricing and revenue management software is underpenetrated. Market interest for our software has increased over the past several years providing us with a growth opportunity. We are investing in our businesses to more effectively address these opportunities through significant investment in research and development, sales, marketing and back office. In addition to organic growth, we may acquire companies or technology that can contribute to the strategic, operational and financial growth of our business. We expect to continue to explore both organic and other strategic growth opportunities.

Difficult economic conditions. The current global economic conditions continue to be challenging and have had and may continue to have a negative impact on the adoption of pricing and revenue management software and may increase the volatility in our business. Due to the difficult economic conditions, we continue to experience long sales cycles, increased scrutiny on purchasing decisions and overall cautiousness taken by customers. In addition, certain foreign countries are also facing significant economic crisis and it is possible that these crises could result in economic deterioration in the markets in which we operate. We believe our solutions provide value to our customers during periods of growth as well as in recessions, but it is uncertain the extent to which the difficult economic conditions will further affect our business.

Table of Contents

Variability in revenue. Our revenue recognition policy provides visibility into a significant portion of our revenue in the near-term quarters, although the actual timing of recognition of revenue varies based on the nature and requirements of our contracts. For the substantial majority of our arrangements, we have not historically recognized license revenue upon customer contract signature and software delivery because we consider implementation services to be essential to the customers' usability of our licensed software. We evaluate our contract terms and conditions as well as our implementation performance obligations in making our revenue recognition determination for each contract. In the future, as the market for pricing and margin optimization software evolves and more third party system integrators and resellers independently deploy our software, we believe the nature and scope of our implementation performance obligations will be materially reduced. Such a reduction in our implementation performance obligations would materially impact the timing of recognition of license revenue and results of operations. Our revenue could also vary based on our customer mix and customer geographic location. We sell our solutions to customers in the manufacturing, distribution, services and travel industries. From a geographical standpoint, approximately 60% of our consolidated revenues were derived from customers outside the United States for each of the three months ended March 31, 2012 and 2011, respectively. The economic and political environments around the world could change our concentration of revenue within industries and across geographies.

Income taxes. During the three months ended March 31, 2012, the effective income tax rate was 45% as compared to the federal rate of 34%. The increase in the effective tax rate is due primarily to nondeductible share-based compensation expense. We expect our effective tax rate to be higher than the federal rate in 2012 and 2013. The research and experimentation (R&E) tax credit was not reinstated for 2012 and, accordingly, our federal income tax provision for the three months ended March 31, 2012 excludes the effect of the R&E tax credit. If the R&E tax credit is reinstated during 2012, our annual effective tax rate will be favorably impacted, resulting in a reduction to our 2012 tax provision on a cumulative basis.

Results of Operations*Comparison of three months ended March 31, 2012 with three months ended March 31, 2011**Revenue:*

(Dollars in thousands)	For the Three Months Ended March 31, 2012		2011		Variance \$	Variance %
	Amount	As a percentage of total revenue	Amount	As a percentage of total revenue		
License and implementation	\$ 17,796	66%	\$ 13,793	64%	\$ 4,003	29%
Maintenance and support	9,225	34%	7,613	36%	1,612	21%
Total	\$ 27,021	100%	\$ 21,406	100%	\$ 5,615	26%

License and implementation. License and implementation revenue increased \$4.0 million to \$17.8 million for the three months ended March 31, 2012 from \$13.8 million for the three months ended March 31, 2011, representing a 29% increase. The increase in license and implementation revenue in the three months ended March 31, 2012 was principally due to a 8% increase in the number of implementations from 78 to 84, and a 33% increase in the average revenue recognized per man-day as compared to the corresponding period of 2011. These increases were offset by a 3% decrease in the number of man-days expended that generated license and implementation revenue.

License and implementation revenue includes revenue from both term licenses and hosting services. Revenue from term licenses represented approximately 5.5% and 5.4% of total revenue for the three months ended March 31, 2012 and 2011, respectively. Revenue from hosting services represented approximately 2.5% and 1.4% of total revenue for the three months ended March 31, 2012 and 2011, respectively.

Maintenance and support. Maintenance and support revenue increased \$1.6 million to \$9.2 million for the three months ended March 31, 2012 from \$7.6 million for the three months ended March 31, 2011, representing a 21% increase. The increase in maintenance and support revenue is principally the result of an increase in the number of customers for which we are providing maintenance and support services.

Table of Contents*Cost of revenue and gross profit:*

(Dollars in thousands)	For the Three Months Ended March 31, 2012		For the Three Months Ended March 31, 2011		Variance \$	Variance %
	Amount	As a percentage of related revenue	Amount	As a percentage of related revenue		
Cost of license and implementation	\$ 5,986	34%	\$ 4,623	34%	\$ 1,363	29%
Cost of maintenance and support	1,935	21%	1,710	22%	225	13%
Total cost of revenue	\$ 7,921	29%	\$ 6,333	30%	\$ 1,588	25%
Gross profit	\$ 19,100	71%	\$ 15,073	70%	\$ 4,027	27%

Cost of license and implementation. Cost of license and implementation increased \$1.4 million to \$6.0 million for the three months ended March 31, 2012 from \$4.6 million for the three months ended March 31, 2011, representing a 29% increase. The increase in cost of license and implementation is principally attributable to an increase of \$1.5 million of human resources costs. Human resources costs increased as a result of an increase in headcount to support the increased number of active implementations and salary merit increases. In addition, there was an increase of \$0.1 million of travel expense. These increases were partially offset by a decrease of \$0.3 million related to a reduction in the use of system integrators.

License and implementation gross margins were 66% for both of the three months ended March 31, 2012 and 2011. License and implementation margins may vary from period to period depending on different factors, including the amount of implementation services required to deploy our products relative to the total contract price.

Cost of maintenance and support. Cost of maintenance and support increased \$0.2 million to \$1.9 million for the three months ended March 31, 2012 from \$1.7 million for the three months ended March 31, 2011, representing a 13% increase. The increase in cost of maintenance in the first three months of 2012 when compared to the corresponding period in 2011 is attributable to an increase in expenses associated with the continued growth in our customer maintenance and support function commensurate with maintenance and support revenue growth. Maintenance and support gross margins were 79% for the three months ended March 31, 2012 as compared to 78% for the three months ended March 31, 2011.

Gross profit. Gross profit increased \$4.0 million to \$19.1 million for the three months ended March 31, 2012 from \$15.1 million for the three months ended March 31, 2011, representing a 27% increase. The increase in overall gross profit was attributable to the increase in overall revenue.

Operating expenses:

(Dollars in thousands)	For the Three Months Ended March 31, 2012		For the Three Months Ended March 31, 2011		Variance \$	Variance %
	Amount	As a percentage of total revenue	Amount	As a percentage of total revenue		
Selling, marketing, general and administrative	\$ 10,252	38%	\$ 7,871	37%	\$ 2,381	30%
Research and development	6,697	25%	5,960	28%	737	12%
Total operating expenses	\$ 16,949	63%	\$ 13,831	65%	\$ 3,118	23%

Selling, marketing, general and administrative expenses. Selling, marketing, general and administrative expenses increased \$2.4 million to \$10.3 million for the three months ended March 31, 2012 from \$7.9 million for the three months ended March 31, 2011, representing a 30% increase. The increase was principally due to an increase of \$1.5 million in sales, marketing, general and administrative human resources costs and third party contractor expenses as a result of an increase in headcount to support our planned growth objectives. In addition, there was an increase of \$0.6 million of marketing expenses resulting from increases in marketing initiatives, an increase of \$0.3 million of travel expense and an

Edgar Filing: PROS Holdings, Inc. - Form 10-Q

increase of \$0.2 million of overhead and other expenses. These increases were partially offset by a \$0.2 million decrease in bad debt expense.

Research and development expenses. Research and development expenses increased \$0.7 million to \$6.7 million for the three months ended March 31, 2012 from \$6.0 million for the three months ended March 31, 2011, representing a 12% increase. The increase was principally attributed to an increase of \$0.5 million in human resources costs and third party contractor expenses as a result of increased headcount and salary merit increases. In addition, there was an increase of \$0.2 million in overhead costs.

Table of Contents*Income tax provision:*

(Dollars in thousands)	For the Three Months Ended March 31,		Variance \$	Variance %
	2012	2011		
Effective tax rate	45%	32%	n/a	13%
Income tax provision	\$ 961	\$ 404	\$ 557	138%

Income tax provision. Our income tax provision increased \$0.6 million to \$1.0 million for the three months ended March 31, 2012 from \$0.4 million for the three months ended March 31, 2011. The effective tax rate was 45% and 32% for the three months ended March 31, 2012 and 2011, respectively. The increase in the effective tax rate is due primarily to nondeductible share-based compensation expense and the effect of the nonrenewal of the R&E tax credit effective in 2012.

Liquidity and Capital Resources*Liquidity*

At March 31, 2012, we had \$70.9 million of cash and cash equivalents and \$68.6 million of working capital as compared to \$68.5 million of cash and cash equivalents and \$66.2 million of working capital at December 31, 2011. Our principal source of liquidity is our cash and cash equivalents. Our material drivers or variants of operating cash flow are net income, non-cash expenses (principally share-based compensation) and the timing of periodic billings and collections related to the sale of our software and related services. The primary source of operating cash flows is the collection of accounts receivable from our customers. 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.

Based on existing cash and cash equivalents balances and our current estimates of revenues and expenses, we believe that we will have adequate liquidity and capital resources to meet our operational requirements and anticipated capital expenditures for the next twelve months. However, at some future date we may need to seek additional sources of capital to meet our requirements. Our future working capital requirements will depend on many factors, including the operations of our existing business, our potential strategic expansion, future acquisitions we might undertake, and the expansion into complementary businesses. If such need arises, we may need to raise additional funds through equity or debt financings. We do not currently have a bank line of credit. We can provide no assurance that bank lines of credit or other financing will be available on terms acceptable to us. If available, such financing may result in dilution to our stockholders and interest expense. At March 31, 2012, we had restricted cash of \$0.3 million related to letters of credit.

The following table presents key components of our unaudited condensed consolidated statements of cash flows for the three months ended March 31, 2012 and 2011.

(Dollars in thousands)	For the Three Months Ended March 31,	
	2012	2011
Net cash provided by operating activities	\$ 3,424	\$ 5,932
Net cash used in investing activities	(1,031)	(1,025)
Net cash provided by financing activities	63	747
Cash and cash equivalents (beginning of period)	68,457	55,845
Cash and cash equivalents (end of period)	\$ 70,913	\$ 61,499

Net cash provided by operating activities. Net cash provided by operating activities for the three months ended March 31, 2012 was \$3.4 million, which represents a decrease of \$2.5 million when compared to the corresponding period in 2011. In the first quarter of 2012, our cash flows from operations were derived principally from: (i) our earnings from on-going operations prior to non-cash expenses such as depreciation, excess tax benefits on share-based compensation and share-based compensation; and (ii) changes in our working capital. The decrease in net cash provided by operating activities in the first three months of 2012 as compared to the corresponding period in 2011 was

Table of Contents

due to net decreases of \$0.3 million in non-cash expenses and a decrease of \$2.5 million attributed to changes in operating assets and liabilities, which are composed of accounts receivable, unbilled receivables, prepaid and other assets, accounts payable, accrued expenses, accrued liabilities and accrued payroll and deferred revenue. These decreases were partially offset by an increase in net earnings of \$0.3 million.

Net cash used in investing activities. Net cash flow used in investing activities was \$1.0 million for both the three months ended March 31, 2012 and 2011. The net cash used in investing activities is primarily the result of purchases of software, computer and equipment.

Net cash provided by financing activities. Net cash flow provided by financing activities was \$0.1 million for the three months ended March 31, 2012 compared to net cash flow provided by financing activities of \$0.7 million for the three months ended March 31, 2011. The decrease is primarily the result of a tax withholding related to net share settlement of restricted stock units offset by the excess tax benefits on share-based compensation and the exercise of stock options and SARs.

Off-Balance Sheet Arrangements

We do not have any relationships with unconsolidated entities or financial partnerships, such as variable interest entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

Contractual Obligations

There have been no material changes to our contractual obligations as disclosed in our Annual Report on SEC Form 10-K for the year ended December 31, 2011.

Recent Accounting Pronouncements

In December 2011, the FASB issued ASU 2011-12, *Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassification of Items Out of Accumulated Other Comprehensive Income in ASU 2011-5*. ASU 2011-12 defers the effective date pertaining to reclassification adjustments out of accumulated other comprehensive income in ASU 2011-5, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income*. We adopted the standard on January 1, 2012, reporting comprehensive income in a single continuous financial statement in its unaudited condensed statements of comprehensive income. For the three months ending March 31, 2012 and 2011, we did not report other comprehensive income in our unaudited consolidated statements of comprehensive income. In previous periods, we have reported foreign currency translation adjustments in other comprehensive income related to a wholly owned foreign subsidiary. Since this standard affects disclosure requirements only, its adoption did not have a material impact on our consolidated financial statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Exchange Risk

We have contracts denominated in foreign currencies and therefore a portion of our revenue is subject to foreign currency risks. The primary market risk we face is from foreign currency exchange rate fluctuations. Our cash flows are subject to fluctuations due to changes in foreign currency exchange rates. The effect of an immediate 10% adverse change in exchange rates on foreign denominated receivables as of March 31, 2012 would have resulted in a \$0.2 million loss. Fluctuations in currency exchange rates could harm our results of operations in the future. We currently do not use derivative financial instruments to mitigate foreign currency exchange risks. We continue to review this issue and may consider hedging certain foreign exchange risks through the use of currency futures or options in future years.

Table of Contents

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as defined in Rules 13a-15(e) or 15d-15(e) under the Exchange Act of 1934, as amended (the Exchange Act) as of March 31, 2012. Based on our evaluation of our disclosure controls and procedures as of March 31, 2012, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act (i) is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and (ii) is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

We are in the process of implementing the financial management and reporting modules of a new enterprise resource planning (ERP) system on a company-wide basis. During the three months ended March 31, 2012, we implemented the financial reporting, fixed assets, time-keeping, accounts receivable and accounts payable modules. The implementation of these ERP modules represents a change in internal control over financial reporting. Once the implementation is completed, we believe our internal control over financial reporting will be enhanced. We have taken steps to implement appropriate internal control over financial reporting during this period of change and will continue to evaluate the design and operating effectiveness of our internal controls during subsequent periods. We believe during the periods of implementation we have maintained effective internal control over financial reporting.

Other than the internal controls affected by the implementation of the ERP components, there have been no changes in, our internal control over financial reporting during the three months ended March 31, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, we are a party to legal proceedings and claims arising in the ordinary course of business. We are not currently aware of any such proceedings or claims that we believe will have, individually or in the aggregate, a material adverse effect on our business, financial condition or results of operations.

ITEM 1A. RISK FACTORS

We operate in a dynamic environment that involves numerous risks and uncertainties. The following section describes some of the risks that may adversely affect our business, financial condition or results of operations, and the trading price of our common stock; these are not necessarily listed in terms of their importance or level of risk.

Risks relating to our business and industry:

The deterioration of general U.S. and global economic conditions could adversely affect our sales and operating results.

We are a global company with customers around the world. As widely reported, global financial markets have experienced extreme disruption, including, among other things, extreme volatility in security prices, limited ability to raise capital in public and private financial markets, severely diminished liquidity, credit unavailability and company rating downgrades. These conditions have a negative impact on our prospects and customers ability to raise capital and operate their businesses.

The implementation of our software solutions, which is often accompanied by third party hardware purchases and other capital commitments, involves significant capital expenditure by our customers. Customers may reduce or defer their spending on technology. In addition, the weak and uncertain U.S. and global economic conditions could impair our customers ability to pay for our products or services. Any of these factors could delay our revenue recognition or otherwise adversely impact our business, quarterly or annual operating results and financial condition.

Table of Contents

Periodic fluctuations in the U.S. Dollar and other currencies, corporate profits, lower spending, the availability of credit, the impact of conflicts throughout the world, terrorist acts, natural disasters, volatile energy costs, the outbreak of diseases and other geopolitical factors have had, and may continue to have, a negative impact on the U.S. and global economies. Our customers and prospects may experience consolidation or bankruptcies in their industries which may result in project delays or cancellations. We are unable to predict the strength or duration of current market conditions or effects of consolidation. Uncertainties in anticipated spending levels or further consolidation may adversely affect our business, financial condition and results of operations.

A significant or prolonged economic downturn in industries in which we focus may result in our customers or prospects reducing or postponing spending on the solutions we offer.

There are a number of factors, other than our performance, that could affect the size, frequency and renewal rates of our customer contracts. For instance, if economic conditions weaken in any industry in which we focus, our customers or prospects may reduce or postpone their spending significantly which may, in turn, lower the demand for our solutions and negatively affect our revenue and profitability. As a way of dealing with a challenging economic environment, customers may be changing their purchasing strategies, including, in some instances, requesting term licenses or SaaS agreements as opposed to perpetual license agreements, increased negotiation of price, deciding to license one solution rather than multiple solutions or licensing solutions for portions of their business. Customers could also terminate or delay their implementations or maintenance contracts. Change in license terms or the loss of, or any significant decline in business from, one or more of our customers may lead to a significant decline in our revenue and operating margins, particularly if we are unable to make corresponding reductions in our expenses in the event of any such loss or decline. Moreover, a significant change in the liquidity or financial position of any of these customers could have a material adverse effect on the collectability of our accounts receivable, liquidity and future operating results.

A weakening economy and changing business conditions could result in substantial defaults or slowing of payments by our customers on our accounts receivable which could have a significant negative impact on our business, results of operations, financial condition or liquidity.

A significant portion of our working capital consists of accounts receivable from customers. If customers responsible for a significant amount of accounts receivable were to become insolvent or otherwise unable to pay for solutions and services, or were to become unwilling or unable to make payments in a timely manner, our business, results of operations, financial condition or liquidity could be adversely affected.

Our global growth is subject to economic and political risks.

We are a global company with customers around the world. In 2011, approximately 64% of our revenues were attributable to activities outside the United States. Our operations are subject to the effects of global competition. They are also affected by local economic environments, including inflation, recession and currency volatility. Political changes, some of which may be disruptive, may interfere with our customers and our activities in a particular location.

We are subject to a lengthy sales cycle and delays or failures to complete sales may harm our business and cause our revenue and operating income to decline in the future.

Our sales cycle may take several months to over a year. To sell our solutions successfully and obtain an executed contract, we generally have to educate our potential customers about the use and benefits of our solutions, which can require significant time and expense without the ability to realize any revenue. During this sales cycle, we expend substantial resources with no assurance that a sale will ultimately result. The length of a customer's sales cycle depends on a number of factors, many of which we may not be able to control. These factors include the customer's product and technical requirements and the level of competition we face for that customer's business. Any unexpected lengthening of the sales cycle or failure to secure anticipated orders would negatively affect our revenue. Furthermore, a delay in our ability to obtain a signed agreement or to complete certain contract requirements in a particular quarter could reduce our revenue in that quarter. Any significant failure to generate revenue or delays in recognizing revenue after incurring costs related to our sales or services process could have a material adverse effect on our business, financial condition and results of operations.

Table of Contents

We focus exclusively on the pricing and revenue management software market, and if this market develops more slowly than we expect, our business will be harmed.

We derive, and expect to continue to derive, all of our revenue from providing pricing and revenue management software solutions, implementation services and ongoing customer support. The pricing and revenue management software market is relatively new and still evolving, and it is uncertain whether this software will achieve and sustain high levels of demand and market acceptance. Our success will depend on the willingness of businesses in the manufacturing, distribution, services, and travel industries to use pricing and revenue management software.

Some businesses may be reluctant or unwilling to implement pricing and revenue management software for a number of reasons, including failure to understand the potential returns of improving their pricing processes and lack of knowledge about the potential benefits that such software may provide. Even if businesses recognize the need for improved pricing processes, they may not select our pricing and revenue management software solutions because they previously have made investments in internally developed pricing and revenue management solutions. Some businesses may elect to improve their pricing processes through solutions obtained from their existing enterprise software providers, whose solutions are designed principally to address one or more functional areas other than pricing. These enterprise solutions may appeal to customers that wish to limit the number of software vendors on which they rely and the number of different types of solutions used to run their businesses.

If businesses do not embrace the benefits of pricing and revenue management software, the pricing and revenue management software market may not continue to develop or may develop more slowly than we expect, either of which would significantly and adversely affect our revenue and operating results. Because the pricing and revenue management software market is developing and the manner of its development is difficult to predict, we may make errors in predicting and reacting to relevant business trends, which could harm our operating results.

Any downturn in sales to our target markets of manufacturing, distribution, services, and travel would adversely affect our operating results.

Our success is highly dependent upon our ability to sell our software solutions to customers in the manufacturing, distribution, services, and travel industries. If we are unable to market and sell our software solutions effectively to customers in these industries, we may not be able to grow our business. It is uncertain whether our software solutions will achieve and sustain the levels of demand and market acceptance that we anticipate. Such uncertainty is attributable to, among other factors, the following:

it may be more difficult than we currently anticipate to implement our software solutions in our target industries;

it may be more difficult than we currently anticipate to increase our customer base in our target industries; and

it may take more time than we currently anticipate to train our personnel in the implementation of our software solutions in our target industries

Our revenue growth has been derived principally from customers in the manufacturing, distribution, services, and travel industries. Our revenue growth is highly dependent upon continued growth of market acceptance in these industries, and there can be no assurance our solutions will achieve or sustain widespread acceptance among customers in these industries. Failure to expand market acceptance of our solutions in the manufacturing, distribution, services industries or to maintain sales in the manufacturing, distribution, services, and travel industries would adversely affect our operating results and financial condition.

Our software solutions require implementation projects that are subject to significant risks and delays, which if any occurred could negatively impact the effectiveness of our software, resulting in harm to our reputation, business and financial performance.

The implementation of our software solutions can involve complex, large-scale projects that require substantial support operations, significant resources and reliance on factors that are beyond our control. For example, the success of our implementation projects is heavily dependent upon the quality of data used by our software solutions, the commitment of customers' resources and personnel to the projects and the stability, functionality and scalability of the customer's information technology infrastructure. We may not be able to correct or compensate for weaknesses or problems in infrastructure or data, or our customers' commitment and investment in personnel and resources. In addition, implementation of our software solutions can

Table of Contents

be highly complex and require substantial efforts and cooperation on the part of our customers. If we are unable to successfully manage the implementation of our software solutions such that those products do not meet customer needs or expectations, we may become involved in disputes with our customers and our business, reputation and financial performance may be significantly harmed. For projects accounted for under percentage-of-completion, we recognize our license and implementation revenues as implementation services are performed. Any delays in an implementation project or changes in the scope or timing of an implementation project would delay or alter the corresponding revenue recognition and could adversely affect our operating results. In addition, any delays or changes in scope could result in estimated project costs exceeding contracted revenue of which a loss reserve would need to be established which would have an adverse effect on our operating results. If an implementation project for a large customer or a number of customers is substantially delayed or cancelled, our ability to recognize the associated revenue and our operating results would be adversely affected.

Competition from vendors of pricing solutions and enterprise applications as well as from companies internally developing their own solutions could adversely affect our ability to sell our software solutions and could result in pressure to price our software solutions in a manner that reduces our margins and harms our operating results.

The pricing and revenue management software market is competitive, fragmented and rapidly evolving. Our software solutions compete with both solutions developed internally by businesses as well as those solutions offered by competitors. Our principal competition consists of:

pricing and revenue management software vendors, including a number of vendors that provide pricing and revenue management software for specific industries; and

large enterprise application providers that have developed offerings that include pricing and revenue management functionality. We expect additional competition from other established and emerging companies to the extent the pricing and revenue management software market continues to develop and expand. We also expect competition to increase as a result of the entrance of new competitors in the market and industry consolidation, including through a merger or partnership of two or more of our competitors or the acquisition of a competitor by a larger company. A number of our current and potential competitors have larger installed bases of users, longer operating histories and greater name recognition than we have. In addition, many of these companies have significantly greater financial, technical, marketing, service and other resources than we have. As a result, these companies may be able to respond more quickly to new or emerging technologies and changes in customer demands and devote greater resources to the development, promotion and sale of their products.

Competition could seriously impede our ability to sell additional software solutions and related services on terms favorable to us. We do not know how our competition will set prices for their products. Businesses may internally develop solutions, rather than investing in commercially-available solutions. Our current and potential competitors may develop and market new technologies that render our existing or future solutions obsolete, unmarketable or less competitive. In addition, if these competitors develop solutions with similar or superior functionality to our solutions, or if they offer solutions with similar functionality at a substantially lower price than our solutions, we may need to decrease the prices for our solutions in order to remain competitive. If we are unable to maintain our current solution, services and maintenance pricing due to competitive pressures, our margins will be reduced and our operating results will be adversely affected. We cannot provide assurance that we will be able to compete successfully against current or future competitors or that competitive pressures will not materially and adversely affect our business, financial condition and operating results.

Our revenue recognition is primarily based upon our ability to estimate the efforts required to complete our implementation projects, which may be difficult to estimate.

We generally recognize revenue from our software licenses and implementation services over the period during which such services are performed using the percentage-of-completion method. The length of this period depends on the number of licensed software solutions and the scope and complexity of the customer's deployment requirements. Under the percentage-of-completion method, the revenue we recognize during a reporting period is based on the resources expended during the reporting period as compared to the estimated total resources required to implement our software solutions. If we are unable to accurately estimate the overall total man-days required to implement our software solutions, such inaccuracies could have a material effect on the timing of our revenue. Any change in the timing of revenue recognition as a result of inaccurate estimates could adversely impact our quarterly or annual operating results.

Table of Contents

Failure to sustain our historical maintenance and support renewal rates and pricing would adversely affect our operating results.

Maintenance and support agreements are typically for a term of one to two years. Historically, maintenance and support revenue has represented a significant portion of our total revenue, including approximately 35%, 41% and 36% of our total revenue for the years ended December 31, 2011, 2010 and 2009, respectively. If our customers choose not to renew their maintenance and support agreements with us on favorable terms or at all, our business, operating results and financial condition could be harmed.

We might not generate increased business from our current customers, which could limit our revenue in the future.

We sell our software solutions to both new customers and existing customers. Many of our existing customers initially purchase our software solutions for a specific business segment or a specific geographic location within their organization and later purchase additional software solutions for the same or other business segments and geographic locations within their organization. These customers might not choose to make additional purchases of our software solutions or to expand their existing software solutions to other business segments. In addition, as we deploy new applications and features for our software solutions or introduce new software solutions, our current customers could choose not to purchase these new offerings. If we fail to generate additional business from our existing customers, our revenue could grow at a slower rate or even decrease.

If our cost estimates for fixed-fee arrangements do not accurately anticipate the cost and complexity of implementing our software solutions, our profitability could be reduced and we could experience losses on these arrangements.

A material portion of our license and implementation arrangements are priced on a fixed-fee basis. If we underestimate the amount of effort required to implement our software solutions, our profitability could be reduced. Moreover, if the actual costs of completing the implementation exceed the agreed upon fixed price, we would incur a loss on the arrangement.

Our revenue recognition policy may cause any decreases in sales not to be reflected in our revenue immediately.

The period over which we recognize license and implementation revenue for an implementation depends on the number of licensed software solutions and the scope and complexity of the customer's deployment requirements which may range from six months to several years. As a result, a significant majority of our revenue is recognized on arrangements that were executed in previous periods. Any shortfall in new sales of our software solutions may not be reflected in our revenue for several quarters, and as such the adverse impact on our business may not be readily apparent.

We may enter into acquisitions that may be difficult to integrate, fail to achieve our strategic objectives, disrupt our business, dilute stockholder value or divert management attention.

In the future we may pursue acquisitions of businesses, technologies and products that we intend to complement our existing business, solutions, services and technologies. We cannot provide assurance that any acquisition we make in the future will provide us with the benefits we anticipated in entering into the transaction. Acquisitions are typically accompanied by a number of risks, including:

difficulties in integrating the operations and personnel of the acquired companies;

difficulties in maintaining acceptable standards, controls, procedures and policies;

potential disruption of ongoing business and distraction of management;

inability to maintain relationships with customers of the acquired business;

Edgar Filing: PROS Holdings, Inc. - Form 10-Q

impairment of relationships with employees and customers as a result of any integration of new management and other personnel;

difficulties in incorporating acquired technology and rights into our solutions and services;

unexpected expenses resulting from the acquisition; and

potential unknown liabilities associated with acquired businesses.

Table of Contents

In addition, acquisitions may result in the incurrence of debt, acquisition related costs and expenses, restructuring charges and write-offs. Acquisitions may also result in goodwill and other intangible assets that are subject to impairment tests, which could result in future impairment charges.

We may enter into negotiations for acquisitions that are not ultimately consummated. Those negotiations could result in diversion of management time and significant out-of-pocket costs. If we fail to evaluate and execute acquisitions successfully, we may not be able to achieve our anticipated level of growth and our business and operating results could be adversely affected.

If we fail to develop or acquire new pricing and revenue management functionality to enhance our existing software solutions, we will not be able to grow our business and it could be harmed.

The pricing and revenue management software market is characterized by:

rapid technological developments;

newly emerging and changing customer requirements; and

frequent solution introductions, updates and functional enhancements.

We must introduce new pricing and revenue management functionality that enhances our existing software solutions in order to meet our business plan, maintain or improve our competitive position, keep pace with technological developments, satisfy increasing customer requirements and increase awareness of pricing and revenue management software generally and of our software solutions in particular. Any new functionality we develop may not be introduced in a timely manner and may not achieve market acceptance sufficient to generate material revenue. Furthermore, we believe our competitors are heavily investing in research and development, and may develop and market new solutions that will compete with, and may reduce the demand for, our software solutions. We cannot provide assurance that we will be successful in developing or otherwise acquiring, marketing and licensing new functionality, or delivering updates and upgrades that meet changing industry standards and customer demands. In addition, we may experience difficulties that could delay or prevent the successful development, marketing and licensing of such functionality. If we are unable to develop or acquire new functionality, enhance our existing software solutions or adapt to changing industry requirements to meet market demand, we may not be able to grow our business and our revenue and operating results would be adversely affected.

In addition, because our software solutions are intended to operate on a variety of technology platforms, we must continue to modify and enhance our software solutions to keep pace with changes in these platforms. Any inability of our software solutions to operate effectively with existing or future platforms could reduce the demand for our software solutions, result in customer dissatisfaction and limit our revenue.

Our software solutions require hardware to operate which may be difficult for our customers to obtain.

The implementation of our software solutions often requires specific hardware to operate. The inability of our customers to access and secure such hardware could impact the effectiveness of our software and result in harm to our reputation if the software does not operate properly due to the unavailability of the necessary hardware. Moreover, if our customers are unable to obtain such hardware, they may not purchase our software or purchase software from a competitor or enterprise software, which may not require specific hardware. If businesses do not implement our software due to their inability to obtain the hardware needed for our software, our business, results of operations and financial condition could be adversely affected.

Defects or errors in our software solutions could harm our reputation, impair our ability to sell our solutions and result in significant costs to us.

Our pricing and revenue management software solutions are complex and may contain undetected defects or errors. Several of our solutions have recently been developed and may therefore be more likely to contain undetected defects or errors. In addition, we frequently develop enhancements to our software solutions that may contain defects. We have not suffered significant harm from any defects or errors to date, but we have found defects in our software solutions from time to time. We may discover additional defects in the future, and such defects could be material. We may not be able to detect and correct defects or errors before the final implementation of our software solutions. Consequently, we

Edgar Filing: PROS Holdings, Inc. - Form 10-Q

or our customers may discover defects or errors after our software solutions have been implemented. We have in the past issued, and may in the future need to issue, corrective releases of our solutions to correct defects or errors. The occurrence of any defects or errors could result in:

Table of Contents

lost or delayed market acceptance and sales of our software solutions;

delays in payment to us by customers;

injury to our reputation;

diversion of our resources;

legal claims, including product liability claims, against us;

increased maintenance and support expenses; and

increased insurance costs.

Our license agreements with our customers typically contain provisions designed to limit our liability for defects and errors in our software solutions and damages relating to such defects and errors, but these provisions may not be enforced by a court or otherwise effectively protect us from legal claims. Our liability insurance may not be adequate to cover all of the costs resulting from these legal claims. Moreover, we cannot provide assurance that our current liability insurance coverage will continue to be available on acceptable terms. In addition, the insurer may deny coverage on any future claim. The successful assertion against us of one or more large claims that exceeds available insurance coverage, or the occurrence of changes in our insurance policies, including premium increases or the imposition of large deductible or co-insurance requirements, could have a material adverse effect on our business and operating results. Furthermore, even if we prevail in any litigation, we are likely to incur substantial costs and our management's attention will be diverted from our operations.

If our executives and other key personnel are unable to effectively manage our business, or if we fail to attract additional qualified personnel, our operating results could be adversely affected.

Our future success depends upon the performance and service of our executive officers and other key sales, development, science and professional services staff. The failure of our executives and key personnel to effectively manage our business or the loss of the services of our executive officers and other key personnel would harm our operations. In addition, our future success will depend in large part on our ability to attract and retain a sufficient number of highly qualified personnel, and there can be no assurance that we will be able to do so. We've recently added a significant number of new personnel, and their ability to learn our business and manage it effectively will be important to our continued growth and expansion. In addition, given the highly sophisticated pricing science included in our solutions, the pool of scientists and software developers qualified to work on our solutions is limited, and the implementation of our software solutions requires highly-qualified personnel, and hiring and retaining such personnel to support our growth may be challenging. Competition for such qualified personnel is intense, and we compete for these individuals with other companies that have greater financial, technical, marketing, service and other resources than we do. If our key personnel are unable to effectively manage our business, or if we fail to attract additional qualified personnel, our operating results could be adversely affected.

Intellectual property litigation and infringement claims may cause us to incur significant expense or prevent us from selling our software solutions.

Our industry is characterized by the existence of a large number of patents, trademarks and copyrights, and by frequent litigation based on allegations of infringement or other violations of intellectual property rights. A third party may assert that our technology violates its intellectual property rights, or we may become the subject of a material intellectual property dispute. Pricing and revenue management solutions may become increasingly subject to infringement claims as the number of commercially available pricing and revenue management solutions increases and the functionality of these solutions overlaps. In addition, changes in patent laws in the U.S. such as the recently adopted America Invents Act of 2011 may affect the scope, strength and enforceability of our patent rights or the nature of proceedings which may be brought by us related to our patent rights. Future litigation may involve patent holding companies or other adverse patent owners who have no relevant product revenue and against whom our own potential patents may therefore provide little or no deterrence. Regardless of the merit of any particular claim that our technology violates the intellectual property rights of others, responding to such claims may require us to:

Table of Contents

incur substantial expenses and expend significant management efforts to defend such claims;

pay damages, potentially including treble damages, if we are found to have willfully infringed such parties' patents or copyrights;

cease making, licensing or using products that are alleged to incorporate the intellectual property of others;

distract management and other key personnel from performing their duties for us;

enter into potentially unfavorable royalty or license agreements in order to obtain the right to use necessary technologies; and

expend additional development resources to redesign our solutions.

Any license required as a result of litigation under any patent may not be made available on commercially acceptable terms, if at all. In addition, some licenses may be nonexclusive, and therefore our competitors may have access to the same technology licensed to us. If we fail to obtain a required license or are unable to design around a patent, we may be unable to effectively develop or market our solutions, which could limit our ability to generate revenue or maintain profitability.

Contract terms generally obligate us to indemnify our customers for their use of the intellectual property associated with our software or for other third-party products that are incorporated into our solutions and that infringe the intellectual property rights of others. If we are unable to resolve our legal obligations by settling or paying an infringement claim or a related indemnification claim as described above, we may be required to compensate our customers under the contractual arrangement with such customers. Some of our intellectual property indemnification obligations are contractually capped at a very high amount or not capped at all.

If we fail to protect our proprietary rights and intellectual property adequately, our business and prospects may be harmed.

Our success will depend in part on our ability to protect our proprietary methodologies and intellectual property. We rely upon a combination of trade secrets, confidentiality policies, nondisclosure and other contractual arrangements, and patent, copyright and trademark laws to protect our intellectual property rights. We cannot, however, be certain that steps we take to protect our proprietary rights will prevent misappropriation of our intellectual property, or the development and marketing of similar and competing products and services by third parties.

We rely, in some circumstances, on trade secrets to protect our technology. Trade secrets, however, are difficult to protect. In addition, our trade secrets may otherwise become known or be independently discovered by competitors, and in such cases, we could not assert such trade secret rights against such parties. We seek to protect our proprietary technology and processes, in part, by confidentiality agreements with our employees, consultants, customers, scientific advisors and other contractors. These agreements may be breached, and we may not have adequate remedies for any breach. To the extent that our employees, consultants or contractors use intellectual property owned by others in their work for us, disputes may arise as to the rights in related or resulting know-how and inventions.

As of the date of this filing, we have five issued U.S. patents and three pending U.S. patent applications. We have not pursued patent protection in any foreign countries. Our pending patent applications may not result in issued patents. The patent position of technology-oriented companies, including ours, is generally uncertain and involves complex legal and factual considerations. The standards that the United States Patent and Trademark Office use to grant patents are not always applied predictably or uniformly and can change. Accordingly, we do not know the degree of future protection for our proprietary rights or the breadth of claims allowed in any patents that may be issued to us or to others. Our patents may not contain claims sufficiently broad to protect us against third parties with similar technologies or products, or provide us with any competitive advantage. Moreover, our patents and any patent for which we have licensed or may license rights may be challenged, narrowed, invalidated or circumvented. If our patents are invalidated or otherwise limited, other companies will be better able to develop products that compete with ours, which could adversely affect our competitive business position, business prospects and financial condition.

Table of Contents

Patent applications in the U.S. are typically not published until, at least, 18 months after filing or in some cases not at all, and publications of discoveries in industry-related literature lag behind actual discoveries. We cannot be certain that we were the first to invent the inventions claimed in our pending patent applications or that we were the first to file for patent protection. Additionally, the process of obtaining patent protection is expensive and time-consuming, and we may not be able to prosecute all necessary or desirable patent applications at a reasonable cost or in a timely manner. As a result, we may not be able to obtain adequate patent protection.

In addition, despite our efforts to protect our proprietary rights, unauthorized parties may be able to obtain and use information that we regard as proprietary. The issuance of a patent does not guarantee that it is valid or enforceable. As such, even if we obtain patents, they may not be valid or enforceable against third parties. In addition, the issuance of a patent does not guarantee that we have a right to practice the patented invention. Third parties may have blocking patents that could be used to prevent us from marketing or practicing our potentially patented products. As a result, we may be required to obtain licenses under these third-party patents. If licenses are not available to us on acceptable terms, or at all, we will not be able to make and sell our software solutions and competitors would be more easily able to compete with us.

We use open source software in our solutions that may subject our software solutions to general release or require us to re-engineer our solutions, which may cause harm to our business.

We use open source software in our solutions and may use more open source software in the future. From time to time, there have been claims challenging the ownership of open source software against companies that incorporate open source software into their products. As a result, we could be subject to suits by parties claiming ownership of what we believe to be open source software. Some open source licenses contain requirements that we make available source code for modifications or derivative works we create based upon the open source software and that we license such modifications or derivative works under the terms of a particular open source license or other license granting third parties certain rights of further use. If we combine our proprietary software solutions with open source software in a certain manner, we could, under certain of the open source licenses, be required to release the source code of our proprietary software solutions. In addition to risks related to license requirements, usage of open source software can lead to greater risks than use of third party commercial software, as open source licensors generally do not provide warranties or controls on origin of the software. In addition, open source license terms may be ambiguous and many of the risks associated with usage of open source cannot be eliminated, and could, if not properly addressed, negatively affect our business. If we were found to have inappropriately used open source software, we may be required to seek licenses from third parties in order to continue offering our software, to re-engineer our solutions, to discontinue the sale of our solutions in the event re-engineering cannot be accomplished on a timely basis or take other remedial action that may divert resources away from our development efforts, any of which could adversely affect our business, operating results and financial condition.

We utilize third-party software that we incorporate into our software solutions, and impaired relations with these third parties, defects in third-party software or a third party's inability or failure to enhance their software over time could adversely affect our operating performance and financial condition.

We incorporate and include third-party software into our software solutions. If our relations with any of these third parties are impaired, or if we are unable to obtain or develop a replacement for the software, our business could be harmed. The operation of our solutions could be impaired if errors occur in the third-party software that we utilize. It may be more difficult for us to correct any defects in third-party software because the software is not within our control. Accordingly, our business could be adversely affected in the event of any errors in this software. There can be no assurance that these third parties will continue to invest the appropriate levels of resources in their products and services to maintain and enhance the capabilities of their software.

New accounting standards or interpretations of existing accounting standards, including those related to revenue recognition, could adversely affect our operating results.

GAAP in the United States are subject to interpretation by the Financial Accounting Standards Board, the American Institute of Certified Public Accountants, the SEC and various bodies formed to promulgate and interpret appropriate accounting principles. We adopted new accounting standards for multiple-element arrangements effective from January 1, 2010 and standard setters have proposed further changes to revenue recognition accounting standards, among others. A change in principles or interpretations, in particular those related to revenue recognition, could have an adverse effect on our reported financial results.

Table of Contents

The expiration of the research and experimentation tax credit or other general business credit could have a negative impact on our business, results of operations, financial condition or liquidity.

Our federal effective tax rate historically has been lower than the statutory rate of 34% largely due to tax credit incentives under the U.S. research and experimentation tax credit extended to taxpayers engaged in qualified research and experimental activities. This tax credit is designed to stimulate qualifying company research and development over time by reducing after-tax costs. By qualifying for the tax credit, we have been able to use general business tax credits to reduce our federal income tax liability. In December 2010, the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 was enacted which extended the research and experimentation tax credit until December 31, 2011. Since its enactment in 1981, Congress has reinstated on a retroactive basis the research and experimentation tax credit several times. Unless the research and experimentation tax credit is reinstated for 2012, we will record federal income taxes in 2012 at the enacted federal rate of 34%, net of other tax credits.

Our international sales subject us to risks that may adversely affect our operating results.

Over the last several years, we derived a significant portion of our revenue from customers outside the United States. For the year ended December 31, 2011, 2010, and 2009, approximately 64%, 60% and 59% of our total revenue, respectively, was derived from outside the United States. We may not be able to maintain or increase international market demand for our solutions. Managing overseas growth could require significant resources and management attention and may subject us to new or larger levels of regulatory, economic, foreign currency exchange, tax and political risks. Among the risks we believe are most likely to affect us with respect to our international sales and operations are:

economic conditions in various parts of the world;

unexpected changes in regulatory requirements;

less protection for intellectual property rights in some countries;

new and different sources of competition;

multiple, conflicting and changing tax laws and regulations that may affect both our international and domestic tax liabilities and result in increased complexity and costs;

if we were to establish international offices, the difficulty of managing and staffing such international offices and the increased travel, infrastructure and legal compliance costs associated with multiple international locations;

difficulties in enforcing contracts and collecting accounts receivable, especially in developing countries;

if more contracts become denominated in local currency, fluctuations in exchange rates; and

tariffs and trade barriers, import/export controls and other regulatory or contractual limitations on our ability to sell or develop our solutions in certain foreign markets.

If we continue to expand our business globally, our success will depend, in large part, on our ability to anticipate and effectively manage these and other risks associated with our international operations. Our failure to manage any of these risks successfully could harm our international operations and reduce our international sales, adversely affecting our business, operating results and financial condition.

Security breaches, cyber attacks or fraudulent activity could result in damage to our operations or lead to reputational damage.

A security breach or cyber attack of our computer systems could interrupt or damage our operations or harm our reputation. Despite the implementation of security measures, our systems may still be vulnerable to data theft, computer viruses, malicious software programs, programming errors, attacks by third parties or similar disruptive problems. If we were to experience a security breach or cyber attack, we could be required to incur substantial costs and liabilities, including:

Table of Contents

expenses to rectify the consequences of the security breach or cyber attack,

liability for stolen assets or information,

costs of repairing damage to our systems,

increased costs of cyber security protection, and

damage to our reputation causing customers and investors to lose confidence in us.

Our operations might be affected by the occurrence of a natural disaster or other catastrophic event in Houston, Texas.

Our headquarters are located in Houston, Texas, from which we base our operations. Although we have contingency plans in effect for natural disasters or other catastrophic events, these events, including terrorist attacks and natural disasters such as hurricanes, could disrupt our operations. Even though we carry business interruption insurance and typically have provisions in our contracts that protect us in certain events, we might suffer losses as a result of business interruptions that exceed the coverage available under our insurance policies or for which we do not have coverage. For example, even a temporary disruption to our business operations may create a negative perception in the marketplace. Any natural disaster or catastrophic event affecting us could have a significant negative impact on our operations.

Our ability to raise capital in the future may be limited, and our failure to raise capital when needed could prevent us from executing our strategy.

We believe that our existing cash and cash equivalents and our cash flow from future operating activities will be sufficient to meet our anticipated cash needs for the next twelve months and the foreseeable future. The timing and amount of our working capital and capital expenditure requirements may vary significantly depending on numerous factors, including the other risk factors described in this Annual Report on Form 10-K. In addition, we may require additional capital to fund acquisitions. Additional capital may not be available on terms favorable to us, or at all. If we are unable to obtain adequate financing or financing on terms satisfactory to us, when we require it, our ability to continue to invest in our business growth could be limited. Any additional capital raised through the sale of equity or convertible debt securities may dilute your percentage ownership of our common stock. Furthermore, any new debt or equity securities we issue could have rights, preferences and privileges superior to our common stock. If we raise capital by issuing convertible debt or equity securities, our existing stockholders may be diluted and earnings per share may decrease. Capital raised through debt financings could require us to make periodic interest payments and could impose restrictive covenants on the conduct of our business that make it more difficult for us to obtain additional capital and to pursue business opportunities, including potential acquisitions.

We incur significant costs as a result of operating as a public company, and our management is required to devote substantial time to compliance initiatives.

As a public company, we incur significant legal, accounting and other expenses. The Sarbanes-Oxley Act of 2002 and the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), and rules currently proposed or subsequently implemented by the SEC and NYSE impose heightened requirements on public companies. Our management and other personnel devote a substantial amount of time to these compliance initiatives. We may also need to hire additional personnel to support our compliance requirements. Moreover, these rules and regulations increase our legal and financial costs and make some activities more time-consuming.

Risks relating to ownership of our common stock:

Market volatility may affect our stock price and the value of your investment.

The market price for our common stock has been and is likely to continue to be volatile. Volatility could make it difficult to trade shares of our common stock at predictable prices or times.

Many factors could cause the market price of our common stock to be volatile, including the following:

variations in our quarterly or annual operating results;

decreases in market valuations of comparable companies;

fluctuations in stock market prices and volumes;

Table of Contents

decreases in financial estimates by equity research analysts;

announcements by our competitors of significant contracts, new solutions or enhancements, acquisitions, distribution partnerships, joint ventures or capital commitments;

departure of key personnel;

changes in governmental regulations and standards affecting the software industry and our solutions;

sales of common stock or other securities by us in the future;

damages, settlements, legal fees and other costs related to litigation, claims and other contingencies;

deterioration of the general U. S. and global economic condition; and

other risks described elsewhere in this section.

In the past, securities class action litigation often has been initiated against a company following a period of volatility in the market price of the company's securities. If class action litigation is initiated against us, we will incur substantial costs and our management's attention will be diverted from our operations. All of these factors could cause the market price of our stock to decline, and you may lose some or all of your investment.

Shares of our common stock are relatively illiquid and trading of our shares could adversely affect the market price of our common stock.

Our common stock is thinly traded and we have a relatively small public float. For the quarterly period ended December 31, 2011, the average daily trading volume of our common stock on the New York Stock Exchange was 88,952 shares. Our common stock may be less liquid than the stock of companies with a broader public ownership. In addition, sales of a large volume of our common stock by us or our current stockholders, or the perception that sales could occur, may also have a significant impact on its trading price.

If equity research analysts cease to publish research or reports about us or if they issue unfavorable commentary or downgrade our common stock, the price of our common stock could decline.

The trading market for our common stock relies in part on the research and reports that equity research analysts publish about us and our business. The price of our stock could decline if one or more equity research analysts downgrade our stock or if those analysts issue other unfavorable commentary or cease publishing reports about our business.

Anti-takeover provisions in our Certificate of Incorporation and Bylaws and under Delaware law could make an acquisition of us, which may be beneficial to our stockholders, more difficult and may prevent attempts by our stockholders to replace or remove our current management.

Our Certificate of Incorporation and by-laws and Section 203 of the Delaware General Corporation Law contain provisions that might enable our management to resist a takeover of our company. These provisions include the following:

the division of our board of directors into three classes to be elected on a staggered basis, one class each year;

Edgar Filing: PROS Holdings, Inc. - Form 10-Q

a prohibition on actions by written consent of our stockholders;

the elimination of the right of stockholders to call a special meeting of stockholders;

a requirement that stockholders provide advance notice of any stockholder nominations of directors or any proposal of new business to be considered at any meeting of stockholders;

a requirement that a supermajority vote be obtained to amend or repeal certain provisions of our certificate of incorporation;
and

the ability of our board of directors to issue preferred stock without stockholder approval.

Table of Contents

In addition, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which limits the ability of stockholders owning in excess of 15% of our outstanding voting stock to merge or combine with us. Although we believe these provisions collectively provide for an opportunity to obtain higher bids by requiring potential acquirors to negotiate with our board of directors, they would apply even if an offer were considered beneficial by some stockholders. In addition, these provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management.

We do not intend to pay dividends on our common stock in the foreseeable future.

We do not currently anticipate paying any cash dividends on our common stock in the foreseeable future. We currently anticipate that we will retain all of our available cash, if any, for use as working capital and for other general corporate purposes. Any payment of future dividends will be at the discretion of our board of directors and will depend upon, among other things, our earnings, financial condition, capital requirements, level of indebtedness, statutory and contractual restrictions applying to the payment of dividends and other considerations that the board of directors deems relevant. Investors seeking cash dividends should not purchase our common stock.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

We have an ongoing authorization from our Board of Directors to repurchase up to \$15.0 million in shares of our common stock in the open market or through privately negotiated transactions. As of March 31, 2012, \$10.0 million remained available for repurchase under the existing repurchase authorization.

We did not make any purchases of our common stock under this program for the three months ended March 31, 2012.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 4. MINE SAFETY DISCLOSURE

None.

Item 5. Other information.

None.

ITEM 6. EXHIBITS.

Number	Description
10.13	Form of Market Stock Unit Agreement under the PROS Holdings, Inc. 2007 Equity Incentive Plan.
31.1	Certification of Chief Executive Officer Pursuant to Exchange Act Rule 13a-14(a)/15d-14(a).
31.2	Certification of Chief Financial Officer Pursuant to Exchange Act Rule 13a-14(a)/ 15d-14(a).
32.1*	Certifications of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.

Edgar Filing: PROS Holdings, Inc. - Form 10-Q

* This certification shall not be deemed filed for purposes of Section 18 of the Securities Act of 1934, or otherwise subject to the liability of that Section, nor shall it be deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934

Table of Contents

SIGNATURES

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

Date: May 8, 2012

PROS HOLDINGS, INC.

By: /s/ Andres Reiner
Andres Reiner
President and Chief Executive Officer

(Principal Executive Officer)

Date: May 8, 2012

By: /s/ Charles H. Murphy
Charles H. Murphy
Executive Vice President and Chief Financial Officer

(Principal Financial and Accounting Officer)