

SERENA SOFTWARE INC
Form 10-Q
September 14, 2012
Table of Contents

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

FORM 10-Q

(MARK ONE)

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

FOR THE QUARTERLY PERIOD ENDED July 31, 2012

OR

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NO. 000-25285

SERENA SOFTWARE, INC.

(Exact name of registrant as specified in its charter)

Edgar Filing: SERENA SOFTWARE INC - Form 10-Q

DELAWARE
(State or other jurisdiction of
incorporation or organization)
1850 GATEWAY DRIVE, SAN MATEO, CALIFORNIA 94404-4060

94-2669809
(I.R.S. Employer
Identification No.)
650-481-3400

(Address of principal executive offices, including zip code)

650-481-3400

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer (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

As of July 31, 2012, 98,446,007 shares of the registrant's common stock, \$0.01 par value per share, were outstanding.

Table of Contents

INDEX

	Page
<u>PART I FINANCIAL INFORMATION</u>	
Item 1	
<u>Financial Statements:</u>	
<u>Condensed Consolidated Balance Sheets as of July 31, 2012 and January 31, 2012</u>	3
<u>Condensed Consolidated Statements of Comprehensive Loss for the Three and Six Months Ended July 31, 2012 and 2011</u>	4
<u>Condensed Consolidated Statements of Cash Flows for the Six Months Ended July 31, 2012 and 2011</u>	5
<u>Notes to Condensed Consolidated Financial Statements</u>	6
Item 2	15
<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	
Item 3	24
<u>Quantitative and Qualitative Disclosures About Market Risk</u>	
Item 4	24
<u>Controls and Procedures</u>	
<u>PART II OTHER INFORMATION</u>	
Item 1	25
<u>Legal Proceedings</u>	
Item 1A	25
<u>Risk Factors</u>	
Item 2	25
<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	
Item 3	25
<u>Defaults Upon Senior Securities</u>	
Item 4	25
<u>Mine Safety Disclosures</u>	
Item 5	25
<u>Other Information</u>	
Item 6	26
<u>Exhibits</u>	
<u>SIGNATURES</u>	27

Table of Contents**PART I FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****SERENA SOFTWARE, INC.****Condensed Consolidated Balance Sheets****(In thousands, except share data)****(Unaudited)**

	July 31, 2012	January 31, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 102,160	\$ 109,688
Accounts receivable, net of allowance of \$973 and \$963 at July 31, 2012 and January 31, 2012, respectively	19,717	23,747
Deferred taxes, net	5,013	5,015
Prepaid expenses and other current assets	7,873	7,779
Total current assets	134,763	146,229
Property and equipment, net	4,741	4,879
Goodwill	462,400	462,400
Other intangible assets, net	58,910	77,264
Other assets	9,268	3,600
TOTAL ASSETS	\$ 670,082	\$ 694,372
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 2,051	\$ 1,515
Income taxes payable	1,257	683
Accrued expenses	16,027	18,916
Accrued interest on term loan and subordinated notes	5,823	7,030
Deferred revenue	66,290	68,861
Total current liabilities	91,448	97,005
Deferred revenue, less current portion	8,508	9,443
Long-term liabilities	5,379	5,423
Deferred taxes	13,711	20,835
Term loans	308,500	308,500
Senior subordinated notes	126,542	134,265
Total liabilities	554,088	575,471
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.01 par value; 10,000,000 shares authorized and no shares issued and outstanding at July 31, 2012 and January 31, 2012		
Series A Preferred stock, \$0.01 par value; 1 share authorized, issued and outstanding at July 31, 2012 and January 31, 2012		

Edgar Filing: SERENA SOFTWARE INC - Form 10-Q

Common stock, \$0.01 par value; 200,000,000 shares authorized; 98,446,007 and 98,392,478 shares issued and outstanding at July 31, 2012 and January 31, 2012, respectively	984	984
Additional paid-in capital	517,483	516,578
Accumulated other comprehensive loss	(1,958)	(1,573)
Accumulated deficit	(400,515)	(397,088)
Total stockholders' equity	115,994	118,901
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 670,082	\$ 694,372

See accompanying notes to condensed consolidated financial statements.

Table of Contents**SERENA SOFTWARE, INC.****Condensed Consolidated Statements of Comprehensive Loss****For the Three and Six Months Ended July 31, 2012 and 2011****(In thousands)****(Unaudited)**

	Three Months Ended July 31,		Six Months Ended July 31,	
	2012	2011	2012	2011
Revenue:				
Software licenses	\$ 11,590	\$ 14,860	\$ 19,519	\$ 23,710
Maintenance	34,575	36,361	68,937	71,016
Professional services	6,283	5,938	11,911	11,625
Total revenue	52,448	57,159	100,367	106,351
Cost of revenue:				
Software licenses	425	462	972	797
Maintenance	2,783	2,888	5,657	5,713
Professional services	5,785	5,808	11,319	11,162
Amortization of acquired technology		43		3,651
Total cost of revenue	8,993	9,201	17,948	21,323
Gross profit	43,455	47,958	82,419	85,028
Operating expenses:				
Sales and marketing	14,315	15,762	29,148	30,200
Research and development	6,735	6,841	13,710	13,539
General and administrative	4,352	3,640	8,267	7,167
Amortization of intangible assets	9,076	9,198	18,259	18,401
Restructuring, acquisition and other charges	1,617	1,057	2,009	1,669
Total operating expenses	36,095	36,498	71,393	70,976
Operating income	7,360	11,460	11,026	14,052
Other income (expense):				
Interest income	46	29	98	71
Loss on early extinguishment of debt	(154)		(154)	
Interest expense	(6,965)	(6,518)	(13,584)	(12,717)
Amortization and write off of debt issuance costs	(533)	(315)	(1,082)	(675)
Amend and extend transaction fees			(577)	(1,487)
Total other income (expense)	(7,606)	(6,804)	(15,299)	(14,808)
(Loss) income before income taxes	(246)	4,656	(4,273)	(756)
Income tax expense (benefit)	68	57	(846)	(461)

Edgar Filing: SERENA SOFTWARE INC - Form 10-Q

Net (loss) income	(314)	4,599	(3,427)	(295)
Other comprehensive (loss) income- foreign currency translation adjustments	(142)	198	(385)	(28)
Comprehensive (loss) income	\$ (456)	\$ 4,797	\$ (3,812)	\$ (323)

See accompanying notes to condensed consolidated financial statements.

Table of Contents**SERENA SOFTWARE, INC.****Condensed Consolidated Statements of Cash Flows****For the Six Months Ended July 31, 2012 and 2011****(In thousands)****(Unaudited)**

	Six Months Ended July 31,	
	2012	2011
Cash flows from operating activities:		
Net loss	\$ (3,427)	\$ (295)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization of acquired technology and other intangible assets	19,565	23,489
Deferred income taxes	(7,122)	(8,629)
Interest expense on term credit facility and subordinated notes, net of interest paid	(1,245)	567
Loss on early extinguishment of debt	154	
Amortization and write off of debt issuance costs	1,082	675
Amend and extend transaction fees	577	1,487
Stock-based compensation	1,009	491
Changes in operating assets and liabilities:		
Accounts receivable	4,030	(736)
Prepaid expenses and other assets	396	(1,466)
Accounts payable	447	(416)
Income taxes payable	358	(315)
Accrued expenses and other liabilities	(2,341)	(4,411)
Deferred revenue	(3,506)	(6,690)
Net cash provided by operating activities	9,977	3,751
Cash flows from investing activities:		
Capital expenditures	(908)	(2,605)
Purchased software	(4,216)	(319)
Net cash used in investing activities	(5,124)	(2,924)
Cash flows from financing activities:		
Exercise of stock options under employee stock option plan	67	2
Repurchase of option rights under employee stock option plan	(149)	(2)
Principal borrowings under term credit facility and senior subordinated notes	84,400	
Principal payments and early extinguishments under the term credit facility and senior subordinated notes	(92,507)	(7,500)
Debt issuance costs paid	(3,807)	(1,958)
Net cash used in financing activities	(11,996)	(9,458)
Effect of exchange rate changes on cash	(385)	(28)
Net increase (decrease) in cash and cash equivalents	(7,528)	(8,659)
Cash and cash equivalents at beginning of period	109,688	126,374
Cash and cash equivalents at end of period	\$ 102,160	\$ 117,715

Supplemental disclosures of cash flow information:

Income taxes paid, net of refunds	\$ 5,739	\$ 8,680
Interest expense paid	\$ 14,816	\$ 12,150

See accompanying notes to condensed consolidated financial statements.

Table of Contents

SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

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

(a) Description of Business

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

(b) Basis of Presentation

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

(c) Significant Accounting Policies

The Company's significant accounting policies are described in the notes to the Company's consolidated financial statements, included in the Company's Annual Report on Form 10-K for the fiscal year ended January 31, 2012 filed with the Securities and Exchange Commission (SEC) on April 30, 2012. There have been no changes to the Company's significant accounting policies.

(d) Spyglass Merger Corp.

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

(e) Immaterial Correction of Prior Period Errors

Prior to the filing of the Company's Form 10-Q for the second quarter of fiscal 2013, the Company identified errors related to its interest accrual calculations in fiscal 2007 through fiscal 2011. As a result, the Company's historical interest expense and the related accrued interest on term loan and subordinated notes were overstated. Management evaluated the materiality of the errors from a qualitative and quantitative perspective, and concluded that the errors were immaterial to each of the prior periods but could have been material if corrected in the second quarter of fiscal 2013.

Consequently, in this Form 10-Q, consolidated balance sheet data as of January 31, 2012 has been revised to reflect the correction of these errors by decreasing accrued interest on the term loan and subordinated notes by approximately \$1.8 million and decreasing accumulated deficit by approximately \$1.8 million. The impact of the errors prior to fiscal 2010 would decrease accumulated deficit as of the beginning of fiscal 2010 by approximately \$1.3 million. The impact of the errors in fiscal 2010 and 2011 is a decrease in interest expense of approximately \$0.2 million

Edgar Filing: SERENA SOFTWARE INC - Form 10-Q

and \$0.3 million for the year ended January 31, 2010 and 2011, respectively, and a decrease in accrued interest on the term loan and subordinated notes of approximately \$0.2 million and \$0.5 million as of January 31, 2010 and 2011, respectively. The revised financial data will be reflected when those periods are published again in future filings.

Table of Contents**(2) Stock-Based Compensation***General Stock Option Information*

The following table sets forth the summary of option activity under our stock option programs for the six months ended July 31, 2012:

	Options Available for Grant	Number of Options Outstanding	Weighted Average Exercise Price
Balances as of January 31, 2012	3,970,302	8,582,511	\$ 2.79
Granted	(800,000)	800,000	\$ 3.72
Exercised		(121,854)	\$ 1.25
Cancelled (1)		(233,742)	\$ 1.25
Cancelled	361,352	(361,352)	\$ 2.39
 Balances as of July 31, 2012(2)	 3,531,654	 8,665,563	 \$ 2.92

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

(2) The number of options vested and expected to vest, net of estimated forfeitures, as of July 31, 2012 was 5,347,619 and has a weighted average exercise price of \$2.78.

The aggregate intrinsic value for options outstanding and options exercisable as of July 31, 2012 was \$6.9 million and \$4.7 million, respectively.

To assist management in determining the estimated fair value of the Company's common stock, the Company engages a third-party valuation specialist to perform a valuation on a semi-annual basis as of January 31 and July 31. In estimating the fair value of the Company's common stock, the external valuation firm employs a two-step approach that first estimates the fair value of the Company as a whole, and then allocates the adjusted value of shareholders' equity to the Company's common stock.

The fair value of each stock option grant under the stock option plans is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants in the three and six months ended July 31, 2012 and 2011:

	Three Months Ended July 31,		Six Months Ended July 31,	
	2012	2011	2012	2011
Expected term (in years)	2.7 to 3.0	3.0	2.7 to 3.0	3.0
Risk-free interest rate	0.1% to 0.4%	0.2% to 1.2%	0.1% to 0.4%	0.2% to 1.2%
Volatility	25% to 28%	19% to 33%	25% to 28%	19% to 33%

Table of Contents

The expected term is based on observed and expected time to post vesting exercise or cancellation of options. The risk-free interest rates are derived from the average U.S. Treasury constant maturity rates and approximate the rates in effect at the time of grant for the respective expected term. Volatility is based on the volatility of the Company's peer group's common stock over the period commensurate with the expected term of the options. The Company does not anticipate paying any cash dividends in the foreseeable future and therefore uses an expected dividend yield of zero. The Company estimates forfeitures at the time of grant and revises those estimates in subsequent periods if actual forfeitures differ from those estimates. The Company records stock-based compensation expense only for those awards that are expected to vest.

Information regarding the stock options outstanding at July 31, 2012 is summarized as follows:

Exercise Price	Number Outstanding(1)	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable(1)	Weighted Average Exercise Price
\$1.25	1,033,860	1.36	\$ 1.25	1,033,860	\$ 1.25
\$3.00	4,822,538	7.10	\$ 3.00	2,563,829	\$ 3.00
\$3.08	780,000	7.72	\$ 3.08	269,231	\$ 3.08
\$3.19	500,000	8.17	\$ 3.19	214,853	\$ 3.19
\$3.54	478,749	9.02	\$ 3.54	114,959	\$ 3.54
\$3.58	275,416	8.25	\$ 3.58	93,050	\$ 3.58
\$3.72	775,000	9.83	\$ 3.72	0	\$ 0.00
	8,665,563	6.92	\$ 2.92	4,289,782	\$ 2.62

(1) The table shows options without consideration of expected forfeitures.

Restricted Stock Units

The following table sets forth the summary of restricted stock units activity under our restricted stock purchase agreements for the six months ended July 31, 2012:

	Shares	Weighted Average Grant Date Fair Value
Balances as of January 31, 2012	1,315,000	\$ 3.04
Granted	100,000	\$ 3.72
Cancelled	(25,000)	\$ 3.00
Balances as of July 31, 2012	1,390,000	\$ 3.14

The aggregate fair value of restricted stock units outstanding as of July 31, 2012 was \$5.2 million. There were no restricted stock units vested as of July 31, 2012.

As of July 31, 2012, total unrecognized compensation costs related to unvested stock options and restricted stock was \$4.1 million. Costs related to unvested stock options are expected to be recognized over a period of 3 to 3.5 years and costs related to the restricted stock are expected to be

recognized over a period of 3 to 4 years from grant date.

Table of Contents

Stock-based compensation expense for the three and six months ended July 31, 2012 and 2011 is categorized as follows (in thousands):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2012	2011	2012	2011
Cost of maintenance	\$ 14	\$ 17	\$ 30	\$ 30
Cost of professional services	(3)	15	6	53
Stock-based compensation expense in cost of revenue	11	32	36	83
Sales and marketing	75	156	212	366
Research and development	60	50	124	(247)
General and administrative	379	(106)	637	289
Stock-based compensation expense (benefit) in operating expense	514	100	973	408
Total stock-based compensation expense	525	132	1,009	491
Income tax benefit	(204)	(51)	(392)	(190)
Total stock-based compensation expense, net of tax	\$ 321	\$ 81	\$ 617	\$ 301

Restructuring, acquisition and other charges are categorized as follows for the three and six months ended July 31, 2012 and 2011 (in thousands):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2012	2011	2012	2011
Sponsor fees, administration fees and other costs related to the Merger and the issuance of debt	\$ 311	\$ 313	\$ 622	\$ 622
Restructuring and other charges consisting principally of severance, payroll taxes and other employee benefits, facilities closures and legal and other miscellaneous costs	480		480	162
Other costs not related to our restructuring plans including severance and other employee related costs, costs to establish or liquidate entities, and other costs not part of ongoing operations	826	744	907	885
Total restructuring, acquisition and other charges	\$ 1,617	\$ 1,057	\$ 2,009	\$ 1,669

The agreements underlying the Company's senior subordinated notes and the credit facility include financial covenants based on Adjusted EBITDA. Restructuring, acquisition and other charges are a component of that computation. Restructuring, acquisition and other charges include employee payroll, severance and other employee related costs and other costs that are not part of our ongoing operations. These charges have been included as a separate line within operating expenses in the Company's unaudited condensed consolidated statements of comprehensive loss.

(3) Goodwill and Other Intangible Assets*(a) Goodwill:*

Goodwill is not amortized but instead is periodically tested for impairment. The required annual impairment test is performed in the fourth fiscal quarter each year. The Company has concluded that there were no indicators of impairment of goodwill as of July 31, 2012.

There were no changes in the carrying amount of goodwill during the three and six months ended July 31, 2012.

Table of Contents*(b) Other Intangible Assets:*

	Gross Carrying Amount	As of July 31, 2012 Accumulated Amortization	Net Carrying Amount
Amortizing intangible assets:			
Acquired technology	\$ 178,699	\$ (178,699)	\$
Customer relationships	278,900	(223,399)	55,501
Trademark/Trade name portfolio	14,300	(11,447)	2,853
Capitalized software	6,799	(6,243)	556
Total	\$ 478,698	\$ (419,788)	\$ 58,910

	Gross Carrying Amount	As of January 31, 2012 Accumulated Amortization	Net Carrying Amount
Amortizing intangible assets:			
Acquired technology	\$ 178,699	\$ (178,699)	\$
Customer relationships	278,900	(206,030)	72,870
Trademark and trade name portfolio	14,300	(10,559)	3,741
Capitalized software	6,649	(5,996)	653
Total	\$ 478,548	\$ (401,284)	\$ 77,264

As of July 31, 2012, the Company expects amortization expense in future periods as follows (in thousands):

For remaining six months of year ending January 31, 2013	\$ 18,243
For year ending January 31, 2014	36,486
For year ending January 31, 2015	4,089
For year ending January 31, 2016	92
Total	\$ 58,910

As of July 31, 2012, the weighted average remaining amortization periods for customer relationships, trademark/trade name portfolio, and capitalized software are 19 months, 19 months and 18 months, respectively. The aggregate amortization expense of acquired technology and other intangible assets was \$9.1 million and \$18.3 million in the three months and six months ended July 31, 2012, respectively, as compared to \$9.2 million and \$22.1 million in the three months and six months ended July 31, 2011, respectively.

The Company tests its long-lived assets for recoverability whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. A long-lived asset is not recoverable, and therefore subject to an impairment charge, if its carrying amount exceeds the undiscounted cash flows associated with it. There were no impairment charges in the three and six month periods ended July 31, 2012 and 2011.

Table of Contents**(4) Debt**

Debt as of July 31, 2012 and January 31, 2012 consisted of the following (in thousands):

	July 31, 2012	January 31, 2012
2016 Tranche B Term Loans, due March 10, 2016, LIBOR plus 4.00% with a 1.00% LIBOR floor	\$ 117,399	\$
2013 Term Loans, due March 10, 2013, LIBOR plus 2.00%		117,399
2016 Extended Term Loans, due March 10, 2016, LIBOR plus 4.00%	191,101	191,101
Senior Subordinated Notes, due March 15, 2016, 10.375%	126,542	134,265
Total long-term debt	\$ 435,042	\$ 442,765

Senior Secured Credit Agreement

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

First Amend and Extend Transaction

On March 2, 2011, the Company entered into an amendment to our Credit Facility to extend the final maturity date for the repayment of a portion of outstanding term loans, extend the commitment termination date of the commitments for a portion of the revolving credit facility and provide for additional flexibility in the financial covenants under the Credit Facility (the First Amend and Extend Transaction). As a result of the amendment, \$191.1 million of the existing term loans were extended and will mature on March 10, 2016 (the 2016 Extended Term Loans), and \$20.0 million of the existing revolving credit commitments were extended and will terminate on March 10, 2015 (the Extended Revolving Credit Commitments). The \$124.9 million of the existing term loans that were not extended (the 2013 Term Loans), and the \$55.0 million of the existing revolving credit commitments that were not extended, would continue to mature on March 10, 2013 and March 10, 2012, respectively. As a result of the amendment, the interest rate margins were increased by 200 basis points for the extended facilities. In addition, the maximum total leverage ratio stepped up to 5.50x beginning with the fiscal quarter ended April 30, 2011 and through the test periods ending on July 31, 2012 and will step down to 5.00x thereafter for both the extended facilities and non-extended facilities. After giving effect to the amendment, the aggregate principal amount outstanding under the senior secured credit agreement did not change, and the principal amount of the term loans would continue to amortize at a rate of 1.00% per year on a quarterly basis.

Second Amend and Extend Transaction

On April 12, 2012, the Company entered into an Extension Agreement and Amendment No. 1 (the Second Amend and Extend Transaction) to its Credit Facility to extend the final maturity date of its 2013 Term Loans, that were not extended in the First Amend and Extend Transaction. As a result of the Second Amend and Extend Transaction \$117.4 million of the 2013 Term Loans were extended through a combination of the establishment of a series of term loans to new and existing lenders and the repayment of certain amounts to existing and departing lenders. This resulted in \$84.4 million of the 2013 Term Loans being effectively repaid or extinguished and the same amount being considered new borrowings. The Company refers to the incremental term loans and the newly extended term loans as the 2016 Tranche B Term Loans. The 2016 Tranche B Term Loans have an applicable margin for London Interbank Offered Rate, or LIBOR, -based loans of 4.0% (or, if we exceed a specified leverage ratio, 4.25%) (which is 200 basis points higher than the interest rate under the 2013 Term Loans) and a LIBOR floor of 1.0%. The other terms and conditions of the 2016 Tranche B Term Loans are the same as those for the 2016 Extended Term Loans. After giving effect to the Second Amend and Extend Transaction and the repayment of the remaining 2013 Term Loans, all of the Company's outstanding term loans under the Credit Facility have a final maturity date of March 10, 2016 and the aggregate principal amount of the term loans outstanding under the Credit Facility did not change. The Company paid each lender holding 2016 Tranche B Term Loans an original issuer discount equal to 1.5% of the principal amount of 2016 Tranche B Term Loans held by such lender.

The Credit Facility bears an annual commitment fee on the undrawn portion of that facility commencing on the date of execution and delivery of the senior secured credit agreement. As a result of the cancellation of the non-extended 2012 revolving credit commitment totaling \$55.0 million during the quarter ended October 31, 2011, the annual commitment fee is limited to the Extended Revolving Credit Commitments. Effective February 1, 2011, the annual commitment fee is 0.375% per annum.

Table of Contents*Senior Subordinated Notes*

The Company has outstanding \$126.5 million principal amount of senior subordinated notes, which bear interest at a rate of 10.375%, payable semi-annually on March 15 and September 15, and which mature on March 15, 2016. Each of our domestic subsidiaries that guarantees the obligations under the Company's Credit Facility will jointly, severally and unconditionally guarantee the notes on an unsecured senior subordinated basis. The Company does not have any domestic subsidiaries and, accordingly, there are no guarantors. The notes are the Company's unsecured, senior subordinated obligations, and the guarantees, if any, will be unsecured, senior subordinated obligations of the guarantors. The notes are subject to redemption at the Company's option under terms and conditions specified in the indenture related to the notes, and may be redeemed at the option of the holders at 101% of their face amount, plus accrued and unpaid interest, upon certain change of control events.

During the quarter ended July 31, 2012, the Company repurchased \$7.7 million of the 10.375% senior subordinated notes. The total cost including accrued interest of \$0.2 million was \$8.1 million, resulting in a loss on the early extinguishment of this debt of \$0.2 million during the three and six months ended July 31, 2012.

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

Debt Covenants

The senior subordinated notes and the credit facility contain various covenants including limitations on additional indebtedness, capital expenditures, restricted payments, the incurrence of liens, transactions with affiliates and sales of assets. In addition, the credit facility requires the Company to comply with certain financial covenants, including leverage and interest coverage ratios and capital expenditure limitations. The Company was in compliance with all of the covenants of the credit facility as of July 31, 2012.

The Company's senior secured credit agreement requires the Company to maintain a rolling twelve-month consolidated Adjusted EBITDA to consolidated Interest Expense ratio of a minimum of 2.00x at the end of each quarter beginning with the fiscal year ending January 31, 2010. Consolidated Interest Expense is defined in the senior secured credit agreement as consolidated cash interest expense less cash interest income and is further adjusted for certain non-cash interest expenses and other items. The Company is also required to maintain a rolling twelve-month consolidated Total Debt to consolidated Adjusted EBITDA ratio of a maximum of 5.00x at the end of each quarter beginning with the fiscal year ending January 31, 2011. Under the terms of the Amended and Restated Senior Secured Credit Agreement, the maximum total leverage ratio stepped up to 5.50x beginning with the fiscal quarter ending April 30, 2011 and through the test period ending on July 31, 2012 and will step down to 5.00x thereafter. Consolidated Total Debt is defined in the senior secured credit agreement as total debt other than certain indebtedness and is reduced by the amount of cash and cash equivalents on our consolidated balance sheet in excess of \$5.0 million. As of July 31, 2012, our consolidated Total Debt was \$337.8 million, consisting of total debt other than certain indebtedness totaling \$435.0 million, net of cash and cash equivalents in excess of \$5.0 million totaling \$97.2 million. Failure to satisfy these ratio requirements would constitute a default under the senior secured credit agreement. If the Company's lenders failed to waive any such default, our repayment obligations under the senior secured credit agreement could be accelerated, which would also constitute a default under the indenture governing the senior subordinated notes.

The Company's ability to incur additional debt and make certain restricted payments under the indenture governing the senior subordinated notes, subject to specified exceptions, is tied to an Adjusted EBITDA to fixed charges ratio of at least 2.0x, except that we may incur certain debt and make certain restricted payments and certain permitted investments without regard to the ratio, such as the Company's ability to incur up to an aggregate principal amount of \$625.0 million under our senior secured credit agreement (subject to reduction for mandatory prepayments under our senior secured credit agreement and inclusive of amounts outstanding under our senior secured credit agreement from time to time; as of July 31, 2012, we had \$308.5 million outstanding under our term loan and \$0.0 million under our revolving credit facility), to acquire persons engaged in a similar business that become restricted subsidiaries and to make other investments equal to the greater of \$25.0 million or 2% of our consolidated assets. Fixed charges is defined in the indenture governing the senior subordinated notes as consolidated Interest Expense less interest income, adjusted for acquisitions, and further adjusted for non-cash interest expense.

(5) Income Taxes

Income tax expense was \$0.1 million and income tax benefit was \$0.8 million in the three and six months ended July 31, 2012, respectively, as compared to income tax expense of \$0.1 million and income tax benefit of \$0.5 million in the three and six months ended July 31, 2011, respectively. The Company's projected effective income tax rate for fiscal year 2013 is 15%. The Company's effective income tax rate for fiscal year 2012 was 9%. The Company's effective income tax rate differs from the federal statutory rate of 35% primarily due to the impacts of

Edgar Filing: SERENA SOFTWARE INC - Form 10-Q

permanently reinvested foreign earnings and the domestic production deduction. During periods where the Company experiences losses, these items will generally increase the effective income tax rate above the statutory rate, whereas, they will reduce the effective income tax rate below the statutory rate during periods where the Company has income.

Table of Contents

At January 31, 2012, the Company had total federal, state and foreign unrecognized tax benefits of \$4.6 million, including interest of \$1.0 million. During the six months ended July 31, 2012 there were no material changes to the total unrecognized tax benefit, and the Company accrued immaterial amounts in interest.

The Company files tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. The statute of limitations on the Company's federal tax return filings remains open for the years ended January 31, 2009 through January 31, 2012. The statute of limitations on the Company's major state tax return filings remains open for the years ended January 31, 2007 through January 31, 2012. The statute of limitations on the Company's U.K. income tax filings remains open for the years ended January 31, 1999 through January 31, 2012. Over the next twelve months, the Company expects a decrease of \$1.2 million in our unrecognized tax benefits primarily as a result of expiring statutes of limitation and audit settlements.

(6) Fair Value Measurement

The following table presents the Company's assets and liabilities that are measured at fair value on a recurring basis at July 31, 2012 and January 31, 2012 (in thousands):

Description	Estimated Fair Value at July 31, 2012	Fair Value Measurement at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets	Significant Other Observable Inputs	Significant Unobservable Inputs
Assets:				
Money market funds	\$ 76,720	\$ 76,720	\$	\$
Total Assets	\$ 76,720	\$ 76,720	\$	\$
Total Liabilities	\$	\$	\$	\$

Description	Estimated Fair Value at January 31, 2012	Fair Value Measurement at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets	Significant Other Observable Inputs	Significant Unobservable Inputs
Assets:				
Money market funds	\$ 78,669	\$ 78,669	\$	\$
Total Assets	\$ 78,669	\$ 78,669	\$	\$
Total Liabilities	\$	\$	\$	\$

At July 31, 2012 and January 31, 2012, the Company did not have any assets or liabilities measured at fair value on a recurring basis using significant other observable inputs or significant unobservable inputs.

Fair Value of Financial Instruments

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

Table of Contents

The estimated fair values of certain of the Company's long-term debt obligations, as of July 31, 2012 and January 31, 2012 are as follows:

	Carrying Amount	Fair Value(1)
	(In thousands)	
As of July 31, 2012:		
5.00000% 2016 Tranche B Term Loans due March 10, 2016	\$ 117,399	\$ 116,812
4.47455% 2016 Extended Term Loans due March 10, 2016	\$ 191,101	\$ 186,801
10.375% Senior Subordinated Notes due March 15, 2016	\$ 126,542	\$ 128,756
As of January 31, 2012:		
2.53775% 2013 Non-Extended Term Loans due March 10, 2013	\$ 117,399	\$ 115,932
4.53775% 2016 Extended Term Loans due March 10, 2016	\$ 191,101	\$ 187,279
10.375% Senior Subordinated Notes due March 15, 2016	\$ 134,265	\$ 138,293

- (1) The term loans and senior subordinated notes are measured at fair value using level 2 inputs. These measurements consider inputs such as observable prices for similar instruments, quoted prices in markets that are not active, or other inputs that are observable, either directly or indirectly, including price quotes from independent pricing vendors and broker-dealers and available trade, bid and other market information.

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

(7) Litigation

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

Table of Contents

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

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that are subject to safe harbors under the Securities Act of 1933 and the Securities Exchange Act of 1934. These forward-looking statements include, but are not limited to, statements about financial projections, operational plans and objectives, future economic performance and other projections and estimates contained in this report. When used in this report, the words expects, anticipates, intends, plans, believes, seeks, estimates and similar expressions identify forward-looking statements. Because these forward-looking statements involve risks and uncertainties, they are subject to important factors that could cause actual results to differ materially from those expressed or implied by the forward-looking statements, including those risk factors discussed in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended January 31, 2012. We assume no obligation to update any forward-looking statements contained in this report. It is important that the discussion below be read together with the attached unaudited condensed consolidated financial statements and notes thereto and the risk factors discussed in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended January 31, 2012.

Overview

We are the largest global independent software company in terms of revenue solely focused on managing change and processes across information technology, or IT, environments. Our products and services address the complexity of application lifecycle management, or ALM, and are used by our customers to manage the development of, and control change in, mission critical applications within both mainframe and distributed systems environments. In addition, we provide products and services to enable customers to rapidly address IT service management, or ITSM, and business process challenges through the use of visually designed process workflows.

Our products and services allow customers to orchestrate and manage their application development, IT and business processes by automating and integrating disparate ALM and ITSM products and processes, improving process visibility and consistency, enhancing software integrity, mitigating application development risks, supporting auditability and regulatory compliance, and boosting productivity. Our revenue is generated by software licenses, maintenance contracts and professional services. Our software products are typically installed within customer IT environments and generally accompanied by renewable annual maintenance contracts.

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

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

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

Executive Summary

The following is a summary of the analysis of our results contained in this Management's Discussion and Analysis of Financial Condition and Results of Operations section.

Total revenue for the second quarter of fiscal 2013 decreased 8% to \$52.4 million as compared to \$57.2 million in the second quarter of fiscal 2012, primarily due to a decrease in mainframe software license revenue.

Total cost of revenue was 17% of total revenue for the second quarter of fiscal 2013 as compared to 18% of total revenue for the second quarter of fiscal 2012.

Edgar Filing: SERENA SOFTWARE INC - Form 10-Q

Total operating expense was \$36.1 million for the second quarter of fiscal 2013 and decreased by 1% from \$36.4 million in the second quarter of fiscal 2012.

We recorded a net loss for the second quarter of fiscal 2013 of \$(0.3) million as compared to net income of \$4.7 million for the second quarter of fiscal 2012.

Income tax expense was \$0.1 million for the second quarter of fiscal 2013 and for the second quarter of fiscal 2012.

Net cash provided by operating activities increased to \$10.0 million for the six months ended July 31, 2012 from \$3.8 million for the six months ended July 31, 2011.

Table of Contents

During the quarter ended July 31, 2012, we repurchased \$7.7 million of the 10.375% subordinated notes. For a description of this transaction and its effect on our consolidated financial statements, see Note 4 Debt in the notes to our unaudited condensed consolidated financial statements.

Historically, our revenue has been generally attributable to sales in North America, Europe and to a lesser extent Asia Pacific and South America. Revenue attributable to sales in North America accounted for approximately 66% and 67% of our total revenue in the three and six months ended July 31, 2012, respectively, as compared to 64% and 65% of our total revenue in the three and six months ended July 31, 2011, respectively. Our international revenue is attributable principally to our European operations and to a lesser extent Asia Pacific and South America. International revenue accounted for approximately 34% and 33% of our total revenue in the three and six months ended July 31, 2012, respectively, as compared to 36% and 35% of our total revenue in the three and six months ended July 31, 2011, respectively.

Critical Accounting Policies and Estimates

This discussion is based upon our consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosures of contingent assets and liabilities. In many instances, we could have reasonably used different accounting estimates, and in other instances changes in the accounting estimates are reasonably likely to occur from period to period. Accordingly, actual results could differ significantly from the estimates made by us. To the extent that there are material differences between these estimates and actual results, our future financial statement presentation of our financial condition or results of operations could be affected.

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

In addition to these estimates and assumptions utilized in the preparation of historical financial statements, the inability to properly estimate the timing and amount of future revenue could significantly affect our future operations. We must make assumptions and estimates as to the timing and amount of future revenue. Specifically, our sales personnel monitor the status of all proposals, such as the estimated closing date and potential dollar amount of such transactions. We aggregate these estimates to generate a sales pipeline and then evaluate the pipeline to identify trends in our business. This pipeline analysis and related estimates of revenue may differ significantly from actual revenue in a particular reporting period as the estimates and assumptions were made using the best available data at the time, which is subject to change. Specifically, slowdowns in the global economy and information technology spending has caused and may continue to cause customer purchasing decisions to be delayed, reduced in amount or cancelled, all of which have reduced and could continue to reduce the rate of conversion of the pipeline into contracts. A variation in the pipeline or the conversion rate of the pipeline into contracts could cause us to plan or budget inaccurately and thereby could adversely affect our business, financial condition or results of operations. In addition, because a substantial portion of our software license contracts close in the latter part of a quarter, we may not be able to adjust our cost structure to respond to a variation in the conversion of the pipeline in a timely manner, and thereby the delays may adversely and materially affect our business, financial condition or results of operations.

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

Revenue recognition,

Stock-based compensation,

Valuation of long-lived assets, including goodwill, and

Accounting for income taxes

Edgar Filing: SERENA SOFTWARE INC - Form 10-Q

In the six months ended July 31, 2012, there has been no significant change in the above critical accounting policies or the underlying assumptions and estimates used in their application. See our Annual Report on Form 10-K for the fiscal year ended January 31, 2012 filed with the SEC on April 30, 2012 for further information regarding our critical accounting policies and estimates.

Table of Contents**Historical Results of Operations**

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

	Three Months Ended July 31,		Six Months Ended July 31,	
	2012	2011	2012	2011
Revenue:				
Software licenses	22%	26%	19%	22%
Maintenance	66%	64%	69%	67%
Professional services	12%	10%	12%	11%
Total revenue	100%	100%	100%	100%
Cost of revenue:				
Software licenses	1%	1%	1%	1%
Maintenance	6%	5%	6%	5%
Professional services	11%	10%	12%	11%
Amortization of acquired technology	0%	0%	0%	3%
Total cost of revenue	17%	16%	18%	20%
Gross profit	83%	84%	82%	80%
Operating expenses:				
Sales and marketing	28%	28%	29%	28%
Research and development	12%	12%	13%	13%
General and administrative	8%	6%	8%	7%
Amortization of intangible assets	17%	16%	18%	17%
Restructuring, acquisition and other charges	3%	2%	2%	2%
Total operating expenses	68%	64%	70%	67%
Operating income	14%	20%	11%	13%
Other income (expense):				
Interest income	0%	0%	0%	0%
Loss on early extinguishment of debt	0%	0%	0%	0%
Interest expense	(13)%	(11)%	(14)%	(12)%
Amortization of debt issuance costs	(1)%	(1)%	(1)%	(1)%
Amend and extend transaction fees	0%	0%	(1)%	(1)%
Total other income (expense)	(15)%	(12)%	(15)%	(14)%
(Loss) income before income taxes	(1)%	8%	(4)%	(1)%
Income tax expense (benefit)	0%	0%	(1)%	1%
Net loss (income)	(1)%	8%	(3)%	0%
Other comprehensive loss-foreign currency translation adjustments	0%	0%	0%	0%
Comprehensive (loss) income	(1)%	8%	(3)%	0%

Revenue

Edgar Filing: SERENA SOFTWARE INC - Form 10-Q

We derive revenue from software licenses, maintenance and professional services. Our total revenue decreased \$4.7 million, or 8%, to \$52.4 million in the three months ended July 31, 2012 from \$57.2 million in the same quarter a year ago. For the six months ended July 31, 2012, total revenue decreased \$6.0 million, or 6%, as compared to the same period a year ago. The decrease was primarily the result of decreases in mainframe software license revenue, driven primarily from lower sales of our *ChangeMan ZMF* and other mainframe products, offset in part by higher sales of our distributed systems products, most predominantly *Dimensions*. Maintenance revenues were impacted by the decline in total license revenues in the current quarter, when compared to the same quarter a year ago. Professional services revenue increased in the three months ended July 31, 2012 by \$0.3 million as compared to the same quarter a year ago. This is due in part to the fact that our professional services revenue is driven by solution-oriented sales initiated in prior periods.

Table of Contents

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

	Three Months Ended July 31,				Six Months Ended July 31,			
	2012	2011	Increase/(Decrease)		2012	2011	Increase/(Decrease)	
			In Dollars	In %			In Dollars	In %
Revenue:								
Software licenses	\$ 11,590	\$ 14,860	\$ (3,270)	(22)%	\$ 19,519	\$ 23,710	\$ (4,191)	(18)%
Maintenance	34,575	36,361	(1,786)	(5)%	68,937	71,016	(2,079)	(3)%
Professional services	6,283	5,938	345	6%	11,911	11,625	286	2%
Total revenue	\$ 52,448	\$ 57,159	\$ (4,711)	(8)%	\$ 100,367	\$ 106,351	\$ (5,984)	(6)%

Software Licenses. Software license revenue as a percentage of total revenue was 22% and 19% for the three and six months ended July 31, 2012, respectively, as compared to 26% and 22% for the three and six months ended July 31, 2011, respectively. The decrease in software licenses revenue, in both absolute dollars and as a percentage of total revenue, for the three and six months ended July 31, 2012 as compared to the same period a year ago, was primarily due to lower sales of our *ChangeMan ZMF* and other mainframe products, partially offset by higher sales of our distributed systems products, primarily *Dimensions*. In addition, the continuing adverse worldwide economic conditions, particularly in Europe, continued to negatively impact revenues. Our core ALM products continue to make up nearly all of our total software licenses revenue. Combined, our core ALM products accounted for \$10.6 million or 92% and \$18.3 million or 94% of total software license revenue in the three and six months ended July 31, 2012, respectively, as compared to \$13.5 million or 91% and \$21.3 million or 90%, in the three and six months ended July 31, 2011, respectively. Distributed systems products accounted for \$8.7 million or 75% and \$14.5 million or 75%, of total software licenses revenue in the three and six months ended July 31, 2012, as compared to \$ 8.1 million or 54% and \$12.3 million or 52%, in the three and six months ended July 31, 2011, respectively. We expect that our *Serena Release Manager* and *Serena Service Manager* products will account for a substantial portion of our software licenses revenue growth in the future as our sales organization becomes more familiar with selling these products. We also expect that *Dimensions*, *Professional* and *Serena Business Manager* family of products will account for a substantial portion of our software licenses revenue in the future. We expect our software licenses revenue for the fiscal quarter ending October 31, 2012 to increase sequentially when compared to the fiscal quarter ended July 31, 2012.

Maintenance. Maintenance revenue as a percentage of total revenue was 66% and 69% for the three and six months ended July 31, 2012, respectively, as compared to 64% and 67% for the three and six months ended July 31, 2011, respectively. For the three and six months ended July 31, 2012, when compared to the same periods a year ago, the decrease in maintenance revenue in absolute dollar terms is primarily due to the decrease in software license revenues as well as the impact of maintenance contracts that were not renewed. We expect maintenance revenue to remain generally flat in the near term as maintenance contracts continue to renew at consistent rates and we continue to sell software licenses.

Professional Services. Professional services revenue as a percentage of total revenue was 12% for both the three and six months ended July 31, 2012 as compared to 10% and 11% for the three and six months ended July 31, 2011, respectively. The increase in professional services revenue in the three and six months ended July 31, 2012 as compared to the same periods a year ago, is predominantly due to an increase in the number of consulting service engagements particularly in Asia as well as our focus on solution-oriented sales and the expansion of our professional services organization. In general, professional services revenue is attributable to both consulting opportunities in our installed customer base and to the expansion of our consulting service capabilities. We expect professional services revenue to remain generally flat in the near term. We continue to focus on selling solution-oriented offerings based on our ALM products and *Serena Business Manager* and *Serena Service Manager* family of products.

Cost of Revenue

Cost of revenue, consisting of cost of software licenses, cost of maintenance, cost of professional services and amortization of acquired technology, was 17% and 18% of total revenue in the three and six months ended July 31, 2012, respectively, as compared to 16% and 20% in the three and six months ended July 31, 2011, respectively.

Table of Contents

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

	Three Months Ended July 31,				Six Months Ended July 31,			
	2012	2011	Increase/(Decrease)		2012	2011	Increase/(Decrease)	
			In Dollars	In %			In Dollars	In %
Cost of revenue:								
Software licenses	\$ 425	\$ 462	\$ (37)	(8)%	\$ 972	\$ 797	\$ 175	22%
Maintenance	2,783	2,888	(105)	(4)%	5,657	5,713	(56)	(1)%
Professional services	5,785	5,808	(23)	0%	11,319	11,162	157	1%
Amortization of acquired technology		43	(43)	(100)%	0	3,651	(3,651)	(100)%
Total cost of revenue	\$ 8,993	\$ 9,201	\$ (208)	(2)%	\$ 17,948	\$ 21,323	\$ (3,375)	(16)%
Percentage of total revenue	17%	16%			18%	20%		

Software Licenses. Cost of software licenses consist principally of fees associated with integrating third party technology into our *Serena Release Automation* and *Dimensions* distributed systems products. Cost of software licenses as a percentage of total software licenses revenue was 4% and 5% for the three and six months ended July 31, 2012, respectively, as compared to 3% for both the three and six months ended July 31, 2011. The increase in both absolute dollars and as a percentage of total software license revenue for the three and six months ended July 31, 2012, when compared to the same periods a year ago, was primarily due to an increase in sales of our distributed systems products such as our *Serena Release Automation* product and certain other distributed system products that have fees associated with distributing a third party product and integrating third party technology into our products.

Maintenance. Cost of maintenance consists primarily of salaries, bonuses and other costs associated with our customer support organization. Cost of maintenance as a percentage of total maintenance revenue was 8% for both the three and six months ended July 31, 2012, respectively, and 8% for both the three and six months ended July 31, 2011, respectively. Cost of maintenance remained generally flat in both absolute dollars and as a percentage of maintenance revenue as general cost increases associated with our customer support organization were offset by decreases in expenses associated with our prior cost cutting initiatives.

Professional Services. Cost of professional services consists of salaries, bonuses and other costs associated with supporting our professional services organization. Cost of professional services as a percentage of total professional services revenue was 11% and 12% for the three and six months ended July 31, 2012, respectively, as compared to 10% and 11% for the three and six months ended July 31, 2011, respectively. The cost of professional services in absolute dollars was generally flat as cost increases associated with the build out of our professional services organization were offset by decreases in expenses associated with cost cutting initiatives.

Amortization of Acquired Technology. Our acquired technology became fully amortized in the first quarter of fiscal 2012. Amortization expense was predominantly due to the acquired technology recorded in connection with our merger in March 2006.

Operating Expenses

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

	Three Months Ended July 31,				Six Months Ended July 31,			
	2012	2011	Increase/(Decrease)		2012	2011	Increase/(Decrease)	
			In Dollars	In %			In Dollars	In %
Operating expenses:								
Sales and marketing	\$ 14,315	\$ 15,762	\$ (1,447)	(9)%	\$ 29,148	\$ 30,200	\$ (1,052)	(3)%
Research and development	6,735	6,841	(106)	(2)%	13,710	13,539	171	1%
General and administrative	4,352	3,640	712	20%	8,267	7,167	1,100	15%
Amortization of intangible assets	9,076	9,198	(122)	(1)%	18,259	18,401	(142)	(1)%
Restructuring, acquisition & other charges	1,617	1,057	560	53%	2,009	1,669	340	20%
Total operating expenses	\$ 36,095	\$ 36,498	\$ (403)	(1)%	\$ 71,393	\$ 70,976	\$ 417	1%

Percentage of total revenue	68%	64%	70%	67%
-----------------------------	-----	-----	-----	-----

Table of Contents

Sales and Marketing. Sales and marketing expenses consist primarily of salaries, commissions and bonuses, payroll taxes and employee benefits as well as travel, entertainment and marketing expenses. Sales and marketing expenses as a percentage of total revenue were 28% and 29% for the three and six months ended July 31, 2012, respectively, as compared to 28% for both the three and six months ended July 31, 2011. The decrease in selling and marketing expenses in absolute dollars was primarily attributable to a decrease in commission expenses during the three and six months ended July 31, 2012, when compared to the three and six months ended July 31, 2011, as a result of lower revenues. In absolute dollar terms, we expect sales and marketing expenses to increase over the near term as a result of increased commissions attributable to increased software license revenue.

Research and Development. Research and development expenses consist primarily of salaries, bonuses, payroll taxes, employee benefits and costs attributable to research and development activities. Research and development expenses as a percentage of total revenue were 12% and 13% for the three and six months ended July 31, 2012, respectively, as compared to 12% and 13% for the three and six months ended July 31, 2011, respectively. Research and development expenses for the three and six months ended July 31, 2012, were consistent with the three and six months ended July 31, 2011. We expect research and development expenses to increase slightly in the near term.

General and Administrative. General and administrative expenses consist primarily of salaries, bonuses, payroll taxes, benefits and certain other administrative costs, including legal and accounting fees and bad debt. General and administrative expenses as a percentage of total revenue were 8% for both the three and six months ended July 31, 2012, as compared to 6% and 7% for the three and six months ended July 31, 2011, respectively. The increase in general and administrative expenses in both absolute dollars and as a percentage of total revenue was primarily attributable to growing our general and administrative organizations to support our business and fluctuations in foreign currency rates, all partially offset by restructuring and other ongoing cost cutting initiatives put in place in the first quarter of fiscal 2012. We expect general and administrative expenses to remain generally flat in the near term.

Amortization of Intangible Assets. For the three and six months ended July 31, 2012 and 2011, amortization expense was predominantly due to the identifiable intangible assets recorded in connection with the merger. Assuming there are no impairments and no acquisitions, we expect to record \$9.1 million in amortization expense in each of the next six fiscal quarters, and finally, \$3.9 million in amortization expense in the first quarter of fiscal 2015.

Restructuring, Acquisition and Other Charges. Restructuring, acquisition and other charges are mainly comprised of severance and other employee related costs, sponsor fees and other charges not part of ongoing operations. We recorded \$1.6 million and \$2.0 million in restructuring, acquisition and other charges in the three and six months ended July 31, 2012, respectively, as compared to \$1.1 million and \$1.7 million in the three and six months ended July 31, 2011, respectively.

Restructuring, acquisition and other charges for the three and six months ended July 31, 2012 and 2011 are categorized as follows (in thousands):

	Three Months Ended July 31,		Six Months Ended July 31,	
	2012	2011	2012	2011
Sponsor fees, administration fees and other costs related to the Merger and the issuance of debt	\$ 311	\$ 313	\$ 622	\$ 622
Restructuring charges consisting principally of severance, payroll taxes and other employee benefits, facilities closures and legal and other miscellaneous costs	480		480	162
Other costs not related to our restructuring plans including severance and other employee related costs, costs to establish or liquidate entities, and other costs not part of ongoing operations	826	744	907	885
Total restructuring, acquisition and other charges	\$ 1,617	\$ 1,057	\$ 2,009	\$ 1,669

Table of Contents**Other Income (Expense)**

The following table summarizes other income (expense) for the periods indicated (in thousands, except percentages):

	Three Months Ended July 31,				Six Months Ended July 31,			
	2012	2011	Increase/(Decrease)		2012	2011	Increase/(Decrease)	
			In Dollars	In %			In Dollars	In %
Other income (expense):								
Interest income	\$ 46	\$ 29	\$ 17	59%	\$ 98	\$ 71	\$ 27	39%
Loss on early extinguishment of debt	(154)		(154)		(154)		(154)	
Interest expense	(6,965)	(6,518)	(447)	7%	(13,584)	(12,717)	(867)	7%
Amortization and write-off of debt issuance costs	(533)	(315)	(218)	69%	(1,082)	(675)	(407)	60%
Amend and extend transaction fees					(577)	(1,487)	910	(61)%
Total other income (expense)	\$ (7,606)	\$ (6,804)	\$ (802)	12%	\$ (15,299)	\$ (14,808)	\$ (491)	2%

Interest Income. Interest income for the three and six months ended July 31, 2012, as compared to the three and six months ended July 31, 2011, increased mainly as a result of increases in cash balances resulting from the accumulation of free cash flows from operations.

Interest Expense. Interest expense for the three and six months ended July 31, 2012, as compared to the three and six months ended July 31, 2011, increased in both dollar terms and percentage terms. This was mainly due to the fact that our interest rates on our term loans increased as a result of the Second Amend and Extend Transaction.

Amortization and Write-Off of Debt Issuance Costs. We recorded \$0.5 million and \$1.0 million in amortization and write-off of debt issuance costs in the in the three and six months ended July 31, 2012, respectively, as compared to \$0.3 million and \$0.7 million in the three and six months ended July 31, 2011, respectively. During the quarter ended July 31, 2012, we repurchased \$7.7 million of the 10.375% senior subordinated notes for a total cost of \$8.1 million. We amortized an additional \$0.1 million in capitalized debt issuance costs as a result of the repurchase.

Income Tax Expense (Benefit)

The following table summarizes income tax expense (benefit) for the periods indicated (in thousands, except percentages):

	Three Months Ended July 31,				Six Months Ended July 31,			
	2012	2011	Increase (Decrease)		2012	2011	Increase (Decrease)	
			In Dollars	In %			In Dollars	In %
Income tax expense (benefit)	\$ 68	\$ 57	\$ 11	19%	\$ (846)	\$ (461)	\$ (385)	84%
Percentage of total revenue	0%	0%			(1)%	(1)%		

Table of Contents

Income Tax Expense (Benefit). The income tax expense was \$0.1 million in the quarter ended July 31, 2012, as compared to \$0.1 million in the same quarter a year ago. Income tax benefit was \$0.8 million for the six months ended July 31, 2012, as compared to \$0.5 million for the six months ended July 31, 2011. Our projected effective income tax rate for fiscal year 2013 is 15%. Our effective income tax rate for fiscal year 2012 was 9%. Our effective income tax rate differs from the federal statutory rate of 35% primarily due to the impacts of permanently reinvested foreign earnings and the domestic production deduction. During periods where we experience losses, these items will generally increase the effective income tax rate above the statutory rate, whereas, they will reduce the effective income tax rate below the statutory rate during periods where we have income. See Note 5 of the notes to our unaudited condensed consolidated financial statements included elsewhere in this report for further information regarding income taxes and its impact on our results of operations and financial position.

Liquidity and Capital Resources

Cash and Cash Equivalents. Since our inception, we have financed our operations and met our capital expenditure requirements through cash flows from operations. As of July 31, 2012, we had \$102.2 million in cash and cash equivalents. Approximately 24% of our cash and cash equivalents were held by foreign subsidiaries as of July 31, 2012. Our intent is to permanently reinvest our earnings from certain foreign operations. We do not anticipate a need to repatriate dividends from foreign operations that are permanently reinvested in order to fund operations.

Net Cash Provided by Operating Activities. Cash flows provided by operating activities were \$10.0 million and \$3.8 million in the six months ended July 31, 2012 and 2011, respectively. In the six months ended July 31, 2012, our cash flows provided by operating activities exceeded our net loss principally due to the adjustment for non-cash expenses reflected in our net loss of \$14.0 million, offset by an increase in operating net assets of \$0.7 million. In the six months ended July 31, 2011, our cash flows provided by operating activities exceeded our net loss principally due to the adjustment for non-cash expenses in net loss of \$18.1 million, offset by an increase in operating net assets of \$14.0 million.

Net Cash Used in Investing Activities. Net cash used in investing activities was \$5.1 million and \$2.9 million in the six months ended July 31, 2012 and 2011, respectively. In the six months ended July 31, 2012, net cash used in investing activities of \$5.1 million, was comprised of \$4.2 million for the purchase of software and \$0.9 million for the purchase of computer equipment and office furniture and equipment. In the six months ended July 31, 2011, net cash used in investing activities of \$2.9 million, was comprised of \$2.6 million for the purchase of computer equipment and office furniture and equipment and \$0.3 million for the purchase of internal use software.

Net Cash Used in Financing Activities. Net cash used in financing activities was \$12.0 million and \$9.5 million in the six months ended July 31, 2012 and 2011, respectively. In the six months ended July 31, 2012, net cash used in financing activities of \$12.0 million was mainly comprised of \$8.1 million related to the extinguishment of senior subordinated notes and \$3.8 million of debt issuance costs associated with the Second Amend and Extend Transaction in April 2012. In the six months ended July 31, 2011, net cash used in financing activities of \$9.5 million was principally related to principal payments made on the term loan totaling \$7.5 million and debt issuance costs associated with the First Amend and Extend Transaction in March 2011 totaling \$2.0 million.

Contractual Obligations and Commitments

As a result of the acquisition transactions related to the merger in March 2006, we became highly leveraged. As of July 31, 2012, we had outstanding \$435.0 million in aggregate indebtedness. Our liquidity requirements are significant, primarily due to debt service obligations. Our cash interest paid in the three and six months ended July 31, 2012 was \$4.8 million and \$14.8 million, respectively, as compared to \$6.5 million and \$12.7 million for the three and six months ended July 31, 2011, respectively.

We believe that current cash and cash equivalents, and cash flows from operations will satisfy our working capital and capital expenditure requirements for the twelve months ending July 31, 2013. At some point in the future, we may require additional funds for either operating or strategic purposes or to refinance our existing indebtedness and may seek to raise additional funds through public or private debt or equity financing. If we are required to seek additional financing in the future through public or private debt or equity financing, there is no assurance that this additional financing will be available or, if available, will be upon reasonable terms and not legally or structurally senior to or on parity with our existing debt obligations.

Table of Contents

The following is a summary of our various contractual commitments as of July 31, 2012, including non-cancelable operating lease agreements for office space that expire between calendar years 2012 and 2018. All periods start from May 1, 2012.

	Total	Payments Due by Period(2)			Thereafter
		Less than 1 year	1-3 years (in thousands)	3-5 years	
Operating lease obligations	\$ 12,647	\$ 2,494	\$ 4,612	\$ 3,227	\$ 2,314
Credit Facility:					
2016 Tranche B Term Loans due March 10, 2016	117,399			117,399	
2016 Extended Term Loans due March 10, 2016	191,101			191,101	
Senior Subordinated Notes due March 15, 2016	126,542			126,542	
Scheduled interest on debt(1)	106,961	28,064	56,127	22,770	
	\$ 554,650	\$ 30,558	\$ 60,739	\$ 461,039	\$ 2,314

- (1) Scheduled interest on debt is calculated through each instrument's due date and assumes no unscheduled principal pay downs or borrowings. Scheduled interest on debt includes the 2016 Tranche B term loan due March 10, 2016 at an annual rate of 5.0%, which is the rate in effect as of July 31, 2012, the 2016 extended term loan due March 10, 2016 at an annual rate of 4.24575%, which is the rate in effect as of July 31, 2012, the commitment fee on the unutilized amount of the revolving term credit facility due March 10, 2015 at the annual rate of 0.375%, which is the rate in effect as of July 31, 2012, and the ten-year senior subordinated notes due March 15, 2016 at the stated annual rate of 10.375%.
- (2) This table excludes our unrecognized tax benefits totaling \$4.6 million as of July 31, 2012 since we have determined that the timing of payments with respect to this liability cannot be reasonably estimated.

Off-Balance Sheet Arrangements. As part of our ongoing operations, we do not participate in transactions that generate relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, or SPEs, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. As of July 31, 2012, we were not involved in any unconsolidated SPE transactions.

Senior Secured Credit Agreement

In connection with the consummation of the Merger in March 2006, we entered into a senior secured credit agreement pursuant to a debt commitment that we obtained from affiliates of the initial purchasers of our senior subordinated notes (the Credit Facility).

First Amend and Extend Transaction. On March 2, 2011, we entered into an amendment to our Credit Facility to extend the final maturity date for the repayment of a portion of outstanding term loans, extend the commitment termination date of the commitments for a portion of the revolving credit facility and provide for additional flexibility in the financial covenants under the Credit Facility (the First Amend and Extend Transaction). As a result of the amendment, \$191.1 million of the existing term loans were extended and will mature on March 10, 2016 (the 2016 Extended Term Loans), and \$20.0 million of the existing revolving credit commitments were extended and will terminate on March 10, 2015 (the Extended Revolving Credit Commitments). The \$124.9 million of the existing term loans that were not extended (the 2013 Term Loans), and the \$55.0 million of the existing revolving credit commitments that were not extended, would continue to mature on March 10, 2013 and March 10, 2012, respectively. As a result of the amendment, the interest rate margins were increased by 200 basis points for the extended facilities. In addition, the maximum total leverage ratio stepped up to 5.50x beginning with the fiscal quarter ended April 30, 2011 and through the test periods ending on July 31, 2012 and will step down to 5.00x thereafter for both the extended facilities and non-extended facilities. After giving effect to the amendment, the aggregate principal amount outstanding under the senior secured credit agreement did not change, and the principal amount of the term loans would continue to amortize at a rate of 1.00% per year on a quarterly basis.

Second Amend and Extend Transaction. On April 12, 2012, we entered into an Extension Agreement and Amendment No. 1 (the Second Amend and Extend Transaction) to our Credit Facility to extend the final maturity date of the 2013 Term Loans that were not extended in the First Amend and Extend Transaction. As a result of the Second Amend and Extend Transaction, \$117.4 million of the 2013 Term Loans were extended through a combination of the establishment of a new series of term loans and borrowing of incremental term loans under the Credit

Edgar Filing: SERENA SOFTWARE INC - Form 10-Q

Facility. In connection with the Second Amend and Extend Transaction, certain holders of 2013 Term Loans that did not elect to extend their loans were repaid and replaced with new lenders, and certain holders had their holdings reallocated. We refer to the incremental term loans and the newly extended term loans as the 2016 Tranche B Term Loans. The 2016 Tranche B Term Loans have an applicable margin for London Interbank Offered Rate, or LIBOR, -based loans of 4.0% (or, if we exceed a specified leverage ratio, 4.25%) (which is 200 basis points higher than the interest rate under the 2013 Term Loans) and a LIBOR floor of 1.0%. The other terms and conditions of the 2016 Tranche B Term Loans are the same as those for the 2016 Extended Term Loans. After giving effect to the Second Amend and Extend Transaction and the repayment of the remaining 2013 Term Loans, all of our outstanding term loans under the Credit Facility have a final maturity date of March 10, 2016, and the aggregate principal amount of the term loans outstanding under the Credit Facility did not change. We paid each lender holding 2016 Tranche B Term Loans an original issuer discount equal to 1.5% of the principal amount of 2016 Tranche B Term Loans held by such lender.

Interest Rates and Fees. As of July 31, 2012, the aggregate principal amount outstanding under our Credit Facility was \$308.5 million, which consisted of \$191.1 million of 2016 Extended Term Loans and \$117.4 million of the 2016 Tranche B Term Loans. The 2016 Extended Term Loans bear interest at a rate equal to LIBOR plus 4.00%. That rate was 4.24575% as of July 31, 2012. The 2016 Tranche B Term Loans bear interest at a rate equal to LIBOR plus 4.00% with a 1.00% LIBOR floor. That rate was 5.00% as of July 31, 2012. The Extended Revolving Credit Commitments, of which \$0.0 million was outstanding as of July 31, 2012, bear interest at a rate equal to three-month LIBOR plus 3.75%.

The Credit Facility bears an annual commitment fee on the undrawn portion of that facility commencing on the date of execution and delivery of the senior secured credit agreement. As a result of the cancellation of the non-extended 2012 revolving credit commitment totaling \$55.0 million during the quarter ended October 31, 2011, the annual commitment fee is limited to the Extended Revolving Credit Commitments. Effective February 1, 2011, the annual commitment fee is 0.375% per annum.

Senior Subordinated Notes

We have outstanding \$126.5 million principal amount of senior subordinated notes, which bear interest at a rate of 10.375%, payable semi-annually on March 15 and September 15, and which mature on March 15, 2016. Each of our domestic subsidiaries that guarantees our obligations under our Credit Facility will jointly, severally and unconditionally guarantee the notes on an unsecured senior subordinated basis. We do not have any domestic subsidiaries and, accordingly, there are no guarantors. The notes are our unsecured, senior subordinated obligations, and the guarantees, if any, will be unsecured, senior subordinated obligations of the guarantors. The notes are subject to redemption at our option under terms and conditions specified in the indenture related to the notes, and may be redeemed at the option of the holders at 101% of their face amount, plus accrued and unpaid interest, upon certain change of control events.

During the quarter ended July 31, 2012, we repurchased \$7.7 million of the 10.375% senior subordinated notes. The total cost including accrued interest of \$0.2 million was \$8.1 million resulting in a loss on the early extinguishment of this debt of \$0.2 million during the three and six months ended July 31, 2012.

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

Covenant Compliance

Under our Credit Facility, we are required to satisfy and maintain specified financial ratios and other financial condition tests, including a minimum interest coverage ratio and a maximum total leverage ratio. We were in compliance with all of the covenants under the Credit Facility and indenture as of July 31, 2012. Our ability to meet those financial ratios and tests can be affected by events beyond our control, and we cannot assure you that we will meet those ratios and tests in the future. A breach of any of these covenants would result in a default (which, if not cured, could mature into an event of default) and in certain cases an immediate event of default under our Credit Facility. Upon the occurrence of an event of default under our Credit Facility, all amounts outstanding under our Credit Facility could be declared to be (or could automatically become) immediately due and payable and all commitments to extend further credit could be terminated.

Earnings before interest, taxes, depreciation and amortization, or EBITDA, is a non-GAAP financial measure used to determine our compliance with certain covenants contained in our Credit Facility. Adjusted EBITDA represents EBITDA further adjusted to exclude certain defined unusual items and other adjustments permitted in calculating covenant compliance under our Credit Facility. We believe that the presentation of Adjusted EBITDA is appropriate to provide additional information to investors regarding our compliance with the financial covenants under our Credit Facility.

Adjusted EBITDA does not represent net income (loss) or cash flow from operations as those terms are defined by GAAP and does not necessarily indicate whether cash flows will be sufficient to fund cash needs. While Adjusted EBITDA and similar measures are frequently used as measures of operations and the ability to meet debt service requirements, these terms are not necessarily comparable to other similarly titled captions of other companies due to the potential inconsistencies in the method of calculation. Adjusted EBITDA does not reflect the impact of earnings or charges resulting from matters that we may consider not to be indicative of our ongoing operations. In particular, the definition of

Edgar Filing: SERENA SOFTWARE INC - Form 10-Q

Adjusted EBITDA in our Credit Facility allows us to add back certain defined non-cash, extraordinary, unusual or non-recurring charges that are deducted in calculating GAAP net income (loss). Our Credit Facility requires that Adjusted EBITDA be calculated for the most recent four fiscal quarters. As a result, Adjusted EBITDA can be disproportionately affected by a particularly strong or weak quarter and may not be comparable to Adjusted EBITDA for any subsequent four-quarter period or any complete fiscal year.

Table of Contents

The following is a reconciliation of net loss, a GAAP measure of our operating results, to Adjusted EBITDA as defined in our debt agreements.

	Three Months Ended July 31,		Six Months Ended July 31,	
	2012	2011	2012	2011
Net income (loss)	\$ (314)	\$ 4,599	\$ (3,427)	\$ (295)
Interest expense (income), net(1)	7,606	6,804	15,299	14,808
Income tax expense (benefit)	68	57	(846)	(461)
Depreciation and amortization expense(2)	10,277	10,102	20,575	23,980
EBITDA	17,637	21,562	31,601	38,032
Restructuring, acquisition and other charges(3)	1,617	1,057	2,009	1,669
Adjusted EBITDA	\$ 19,254	\$ 22,619	\$ 33,610	\$ 39,701

- (1) Interest expense (income), net includes interest income, interest expense, amortization and write off of debt issuance costs, and amend and extend transaction fees.
- (2) Depreciation and amortization expense includes depreciation of fixed assets, amortization of leasehold improvements, amortization of acquired technologies, amortization of other intangible assets and amortization of stock-based compensation. See Note 2 of notes to our unaudited condensed consolidated financial statements for additional information related to stock-based compensation.
- (3) Restructuring, acquisition and other charges include employee payroll, severance and other employee related costs associated with transitional activities that are not expected to be part of our ongoing operations.

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

We do not use derivative financial instruments in our investment portfolio and have no foreign exchange contracts. Our financial instruments consist of cash and cash equivalents, trade accounts receivable, accounts payable, term loan and secured indebtedness. We consider investments in highly liquid instruments purchased with an original maturity of 90 days or less to be cash equivalents. All of our cash equivalents principally consist of money market funds as of July 31, 2012. We are subject to interest rate risk related to the variable interest rate on the secured term loan. Management currently does not intend to enter into any swap contract to hedge any portion of the variable interest rate secured term loan. We do not believe that a hypothetical 25% fluctuation in the variable interest rate would have a material impact on our consolidated financial position or results of operations.

Interest Rate Risk. Historically, our exposure to market risk for changes in interest rates relates primarily to our short and long-term investments and short and long-term debt obligations.

As of July 31, 2012, we had \$308.5 million of debt under our senior secured credit agreement. A 1% increase in these floating rates would increase annual interest expense by \$3.1 million.

Foreign Exchange Risk. Sales to foreign countries accounted for approximately 34% and 33% of our total revenue in the three and six months ended July 31, 2012, respectively, as compared to 36% and 35% of our revenue in the three and six months ended July 31, 2011, respectively. Because we invoice certain foreign sales in currencies other than the United States dollar, predominantly the British pound sterling and euro, and do not hedge these transactions, fluctuations in exchange rates could adversely affect the translated results of operations of our foreign subsidiaries. Therefore, foreign exchange fluctuations could create a risk of significant balance sheet gains or losses on our consolidated financial statements. If the U.S. dollar strengthens against foreign currencies, our future net revenues could be adversely affected. However, given our foreign subsidiaries' net book values as of July 31, 2012 and net cash flows for the most recent fiscal quarter ended July 31, 2012, we do not believe that a hypothetical 25% fluctuation in foreign currency exchange rates would have a material impact on our consolidated financial position or results of operations.

ITEM 4. Controls and Procedures

Edgar Filing: SERENA SOFTWARE INC - Form 10-Q

Evaluation of Disclosure Controls and Procedures. Our Chief Executive Officer and Chief Financial Officer, with the assistance of senior management personnel, have conducted an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 15d-15(e) of the Securities Exchange Act of 1934, as amended (Exchange Act)) as of July 31, 2012. We perform this evaluation on a quarterly basis so that the conclusions concerning the effectiveness of our disclosure controls and procedures can be reported in our annual and quarterly reports filed under the Exchange Act. Based on this evaluation, and subject to the limitations described below, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of July 31, 2012.

Changes in Internal Control over Financial Reporting. There were no changes in our internal control over financial reporting during the quarter ended July 31, 2012 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Limitations on Effectiveness of Controls. Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or internal control over financial reporting will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can only provide reasonable, not absolute, assurances that the objectives of the control system are met. The design of a control system reflects resource constraints, and the benefits of controls must be considered relative to their costs. Because there are inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of error or fraud, if any, have been or will be detected.

Table of Contents

PART II OTHER INFORMATION

ITEM 1. Legal Proceedings

Information with respect to this Item may be found in Note 7 of notes to our unaudited condensed consolidated financial statements in Part I, Item I of this quarterly report, which information is incorporated into this Item 1 by reference.

ITEM 1A. Risk Factors

There have been no material changes from the risk factors associated with our business, financial condition and results of operations as set forth in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended January 31, 2012.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not Applicable

ITEM 3. Defaults Upon Senior Securities

Not Applicable

ITEM 4. Mine Safety Disclosures

Not Applicable

ITEM 5. Other Information

Not Applicable

Table of Contents

ITEM 6. Exhibits

See Exhibit Index on the page immediately preceding the exhibits for a list of exhibits filed as part of this Quarterly Report on Form 10-Q, which Exhibit Index is incorporated herein by reference.

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.

SERENA SOFTWARE, INC.

By: /s/ Joseph Passarello
Joseph Passarello
*Senior Vice President, Finance and Chief Financial
Officer (Principal Financial and Accounting
Officer)*

Date: September 14, 2012

Table of Contents**EXHIBIT INDEX****Exhibit**

No.	Exhibit Description
10.1*	Employment Agreement between Serena Software, Inc. and Joseph Passarello dated April 16, 2012
10.2*	Agreement and Release between Serena Software, Inc. and John Alves dated May 25, 2012
10.3*	Form of Time and Performance Option Agreement under the Amended and Restated 2006 Stock Incentive Plan
31.01	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.02	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.01	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.02	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	The following financial information from Serena Software, Inc.'s Quarterly Report on Form 10-Q for the fiscal quarter ended July 31, 2012, formatted in XBRL (eXtensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets as of July 31, 2012 (Unaudited) and January 31, 2012, (ii) Condensed Consolidated Statements of Operations (Unaudited) for the three and six months ended July 31, 2012 and 2011, (iii) Condensed Consolidated Statements of Cash Flows (Unaudited) for the three and six months ended July 31, 2012 and 2011 and (iv) the Notes to Condensed Consolidated Financial Statements (Unaudited)

- * Indicates a management contract or compensatory plan or arrangement.
 Exhibit is filed herewith.
 Exhibit is furnished rather than filed, and shall not be deemed incorporated by reference into any filing, in accordance with Item 601 of Regulation S-K.
 The information in these exhibits is furnished and deemed not filed or part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of section 18 of the Exchange Act of 1934, and is not subject to liability under these sections, in accordance with Rule 406T of Regulation S-T.