



UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the Fiscal Year Ended November 30, 2004

or

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

Commission File Number: 0-19417

PROGRESS SOFTWARE CORPORATION

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

MASSACHUSETTS

*(State or other jurisdiction of incorporation or organization)*

04-2746201

*(I.R.S. Employer Identification No.)*

14 Oak Park

Bedford, Massachusetts 01730

*(Address of principal executive offices)*

Telephone Number: (781) 280-4000

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

Securities registered pursuant to Section 12(g) of the Act:

Common Stock \$.01 par value

*Title of each class*

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2).

Yes  No

As of May 31, 2004 (the last business day of the registrant's most recently completed second fiscal quarter), the aggregate market value of voting stock held by non-affiliates of the registrant was approximately \$579,000,000.

As of January 31, 2005, there were 36,545,000 common shares outstanding.

Documents Incorporated by Reference

Portions of the definitive Proxy Statement for the Annual Meeting of Shareholders to be held on April 21, 2005 are incorporated by reference into Part III.

PROGRESS SOFTWARE CORPORATION

FORM 10-K

FOR THE FISCAL YEAR ENDED NOVEMBER 30, 2004

**PART I**

<a href="#"><u>Item 1. Business</u></a>	2
<a href="#"><u>Item 2. Properties</u></a>	11
<a href="#"><u>Item 3. Legal Proceedings</u></a>	11
<a href="#"><u>Item 4. Submission of Matters to a Vote of Security Holders</u></a>	11

**PART II**

<a href="#"><u>Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u></a>	12
<a href="#"><u>Item 6. Selected Financial Data</u></a>	13
<a href="#"><u>Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u></a>	13
<a href="#"><u>Item 7A. Quantitative and Qualitative Disclosures About Market Risk</u></a>	24
<a href="#"><u>Item 8. Financial Statements and Supplementary Data</u></a>	26
<a href="#"><u>Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure</u></a>	49
<a href="#"><u>Item 9A. Controls and Procedures</u></a>	49
<a href="#"><u>Item 9B. Other Information</u></a>	51

**PART III**

<a href="#"><u>Item 10. Directors and Executive Officers of the Registrant</u></a>	51
<a href="#"><u>Item 11. Executive Compensation</u></a>	51
<a href="#"><u>Item 12. Security Ownership of Certain Beneficial Owners and Management</u></a>	52
<a href="#"><u>Item 13. Certain Relationships and Related Transactions</u></a>	52
<a href="#"><u>Item 14. Principal Accounting Fees and Services</u></a>	52

**PART IV**

<a href="#"><u>Item 15. Exhibits, Financial Statement Schedules</u></a>	53
<a href="#"><u>Signatures</u></a>	56
<a href="#"><u>EX-10.10 Sonic Software Corporation 2001 Stock Incentive Plan, as amended</u></a>	
<a href="#"><u>EX-10.11 PeerDirect Corporation 2003 Stock Incentive Plan</u></a>	
<a href="#"><u>EX-10.12 2004 Inducement Stock Plan</u></a>	
<a href="#"><u>EX-21.1 List of Subsidiaries of the Registrant</u></a>	
<a href="#"><u>EX-23.1 Consent of Deloitte &amp; Touche LLP</u></a>	
<a href="#"><u>EX-31.1 Section 302 Certification of CEO</u></a>	
<a href="#"><u>EX-31.2 Section 302 Certification of CFO</u></a>	
<a href="#"><u>EX-32.1 Section 906 Certification of CEO &amp; CFO</u></a>	

## PART I

### CAUTIONARY STATEMENTS

The Private Securities Litigation Reform Act of 1995 contains certain safe harbor provisions regarding forward-looking statements. This Form 10-K, and other information provided by the Company or statements made by its directors, officers or employees from time to time, may contain “forward-looking” statements and information, which involve risks and uncertainties. Actual future results may differ materially. Statements indicating that the Company “expects,” “estimates,” “believes,” “is planning” or “plans to” are forward-looking, as are other statements concerning future financial results, product offerings or other events that have not yet occurred. There are several important factors that could cause actual results or events to differ materially from those anticipated by the forward-looking statements. Such factors are described in greater detail in Item 7 of this Form 10-K under the heading “Factors That May Affect Future Results” and include, but are not limited to, the timing of the receipt and shipment of new orders, the success of the Company’s distribution channels, the timely release of enhancements to the Company’s products, the growth rates of certain market segments, the positioning of the Company’s products in those market segments, success in the messaging and integration market, variations in the demand for professional services and product maintenance, including technical support, global economic conditions, pricing pressures and the competitive environment in the software industry, the impact of recent acquisitions and any future acquisitions on the Company’s business and the Company’s ability to penetrate international markets and manage its international operations. Although the Company has sought to identify the most significant risks to its business, the Company cannot predict whether, or to what extent, any of such risks may be realized, nor can there be any assurance that the Company has identified all possible issues which the Company might face. The Company undertakes no obligation to update any forward-looking statements it makes.

#### Item 1. Business

Progress Software Corporation (PSC or the Company) develops, markets and distributes software to simplify and accelerate the development, deployment, integration and management of business applications software. The mission of PSC is to deliver superior software products and services that empower partners and customers to dramatically improve their development, deployment, integration and management of quality applications worldwide. PSC seeks to achieve its mission by providing a robust set of software platforms, tools and services that simplify the process of delivering highly integrated and constantly evolving business applications that support an open, flexible and dynamic architecture. PSC’s products include development tools, databases, application servers, messaging servers, application management tools, data connectivity products and integration products for distributed and Web-based applications as well as for client/server applications.

PSC has four principal operating units. PSC’s largest operating unit conducts business as the Progress OpenEdge Division. The second operating unit is Sonic Software Corporation, which invented and is a leading provider of the enterprise service bus (ESB) and operates as a subsidiary of the Company. The third operating unit is ObjectStore, a division of PSC, providing advanced data management software for developing high performance real-time applications which require processing of large amounts of data. The ObjectStore division is also responsible for the PeerDirect product line and the products and people associated with the recently acquired business of Persistence Software, Inc. (Persistence). The fourth operating unit, DataDirect Technologies (DataDirect), was acquired in December 2003. DataDirect is a division of PSC and provides standards-based data connectivity software.

The Progress OpenEdge Division (OED) provides the Progress OpenEdge® platform, a set of development and deployment technologies, including the OpenEdge™ RDBMS, one of the leading embedded databases, that simplifies the job of building business applications. OED was formerly known as the Progress Company. OED released its latest version, OpenEdge 10, in December 2003. The goal of OED, in partnership with its more than 2,000 Application Partners (APs), is to enable end users to achieve a sustainable competitive advantage through AP developed business solutions that simplify end users’ operations, are fast to implement, provide one of the lowest total costs of ownership, and have unparalleled reliability.

Sonic Software Corporation provides distributed infrastructure products that integrate applications and orchestrate business processes across the extended enterprise.

## Table of Contents

PSC's ObjectStore division, acquired in December 2002 as part of the acquisition of eXcelon Corporation (eXcelon), provides advanced data management software for developing real-time, high performance operational applications. ObjectStore products enable complex relationships among data elements to be modeled identically in memory and on disk, providing fast storage and retrieval of complex data structures at in-memory speeds. ObjectStore's PeerDirect group supplies technology for distributed application and database deployment and management. Its flagship product suite, PeerDirect™ Distributed Enterprise, allows companies to centrally manage distributed applications and synchronize databases.

In December 2003, the Company completed its cash acquisition of certain assets and subsidiaries and the assumption of certain liabilities of DataDirect Technologies Limited for \$87.5 million, net of cash acquired. DataDirect operates as a division of PSC. DataDirect provides data connectivity middleware including ODBC and JDBC drivers, .Net data providers, and XML query products.

In November 2004, the Company completed its cash acquisition of Persistence for approximately \$11.8 million, net of cash acquired. The principal product of Persistence is data caching technology. The products and people associated with the Persistence business were combined with the ObjectStore operating unit.

Based upon the aggregation criteria for segment reporting within consolidated financial statements, PSC had two reportable segments in fiscal 2004: Application Development & Deployment, which primarily includes OED, ObjectStore and DataDirect, and Enterprise Application Integration, which principally represents Sonic Software.

More than half of PSC's worldwide revenue is realized through its relationships with indirect channel partners, principally APs, independent software vendors that develop and market applications utilizing the Company's technology. These APs sell business applications in diverse markets such as manufacturing, distribution, financial services, retail and health care. PSC also sells software products and services directly to the business groups and Information Technology (IT) organizations of businesses and governments. PSC operates in North America, Latin America, Europe, Middle East, Africa (EMEA) and the Asia/Pacific region through local subsidiaries as well as independent distributors. For financial information relating to business segments and international operations, see Note 11 of the Consolidated Financial Statements, included in this Annual Report on Form 10-K.

### **PSC Products**

PSC develops, markets and distributes software for the development, deployment, integration and management of business applications. PSC provides development tools that empower developers to deliver high-quality applications. PSC delivers reliable, high-performance deployment and integration products—such as application servers, databases, ESBs and messaging servers—that are essential to the successful use of an application, result in a low total cost of ownership and extend the application's lifecycle. The Company's product lines are designed to continually integrate open standards and to deliver high levels of performance and scalability. PSC's products are generally licensed under perpetual licenses.

OED's OpenEdge product suite is a flexible, reliable and comprehensive business application development and deployment platform whose components are designed to work together. OpenEdge 10, released in December 2003, supports the latest advance in software development and deployment: Service Oriented Architecture (SOA). Under a SOA, applications are built as reusable services that can interoperate dynamically through industry standard web services interfaces. OpenEdge delivers flexibility that allows developers to leverage existing technology, effectively adopt new technology and connect applications with customers, partners and suppliers. OpenEdge 10 provides backward compatibility to the Company's previous release, Progress Version 9.

Sonic Software Corporation is focused on providing infrastructure software for enterprise messaging, integration and interoperability. The core Sonic product, Sonic ESB®, enables the configuration, reliable connection, mediation and control of software services and their interactions. Sonic ESB is particularly well-suited for integrating large numbers of mission critical applications that must interoperate across a global enterprise and with its many business partners. Sonic Software also offers SonicMQ®, a highly scalable messaging server. The ObjectStore® product set from the ObjectStore division provides a technology solution for developing reliable, high performance data management and data caching support for applications. DataDirect's primary product for standards-based database connectivity is DataDirect Connect®.

## [Table of Contents](#)

The following descriptions, organized by technology groups, provide details about the Company's significant products:

### **Development Products**

#### ***OpenEdge™ Studio***

OpenEdge™ Studio provides developers with a unified, highly productive development environment for building complex distributed business applications. OpenEdge Studio presents one workbench and one set of tools for developing a range of applications from client/server models to transaction processing over the Internet. OpenEdge contains Progress® AppBuilder, a central workbench that provides visual tools for defining objects, laying out interfaces and linking data, and the 4GL Development System, a toolset for writing Progress applications that includes an editor, compiler, data dictionary and data administration utilities.

#### ***WebSpeed® Workshop***

WebSpeed® Workshop is a solution for building and deploying highly scalable, business Web applications that process large volumes of transactions. WebSpeed WorkShop combines a visual toolset, packaged Web objects, and SpeedScript, a scripting language specially purposed for internet applications to create a productive development environment.

#### ***Stylus Studio®***

Stylus Studio® is an advanced eXtensible Mark-up Language (XML) development environment. Stylus Studio includes numerous XML-related data maps, editors and debuggers. Stylus Studio has the capability to query and update relational data using the SQL/XML standard. Stylus Studio includes XQuery (XML Query) Tools, a standards-based, advanced XQuery development environment.

### **Deployment Products**

#### ***OpenEdge™ RDBMS***

The OpenEdge RDBMS products are high-performance relational databases that can scale from a single-user Windows system to symmetric multiprocessing (SMP) and cache coherent non-uniform memory access (ccNUMA) systems, supporting thousands of concurrent users. In addition to offering scalability and a low total cost of ownership, the OpenEdge RDBMS products offer high availability, reliability, performance, and platform portability. OpenEdge provides flexible data storage capabilities that allow multiple clients to access the same data via Progress 4GL or SQL access via Open DataBase Connectivity (ODBC) and Java DataBase Connectivity (JDBC). OpenEdge RDBMS products integrate with enterprise applications, tools and numerous third-party data management systems. The three OpenEdge RDBMS products – Enterprise, Workgroup and Personal — allow users to select a solution that satisfies their business objectives.

The OpenEdge Enterprise RDBMS is designed for mid-size and large user environments and the transaction processing throughput of high volume SQL-based and Progress 4GL-based on-line transaction processing (OLTP) applications. The OpenEdge Enterprise RDBMS was developed with a flexible, multithreaded, multiserver architecture. The OpenEdge Enterprise RDBMS is a powerful, open and large-scale enterprise database that can run across multiple hardware platforms and networks. The architecture of the OpenEdge storage engine lets applications take advantage of powerful computing systems. With support for over 10,000 concurrent users and numerous terabytes of data, it provides the capacity for large-scale, high-performance computing.

The OpenEdge Workgroup RDBMS, which offers many of the same powerful capabilities as the OpenEdge Enterprise RDBMS, is designed for deployment in a departmental or small business environment that involves a limited number of users (up to fifty). This department-level solution provides high performance, multi-user support and cross-platform interoperability. The OpenEdge Workgroup RDBMS runs on a wide variety of hardware and operating system platforms. The OpenEdge Personal RDBMS is bundled with OpenEdge development tools and is

## [Table of Contents](#)

suitable for deploying single-user SQL-based and 4GL-based applications and for developing, prototyping and testing applications.

### **OpenEdge™ Application Server**

OpenEdge™ Application Server supports an open, component-based model for partitioning applications and enables applications to be transformed into modular elements within an integrated environment. This enables business logic to be more easily distributed and reused. OpenEdge Application Server provides open, standards-based interoperability and integration to ensure that applications can support multiple user interface and integration methodologies. OpenEdge Application Server includes WebSpeed Transaction Server which is designed for high-throughput transaction processing over the Internet.

There are two editions of OpenEdge Application Server to address varying processing needs. OpenEdge Application Server Basic Edition provides a solution for deploying simple yet dynamic business applications for some small and mid-size businesses. OpenEdge Application Server Enterprise Edition provides an application server solution for mid-size and large businesses. The Enterprise Edition provides the foundation for delivering service-oriented architecture (SOA) and next-generation integration, including Web services, SonicMQ messaging and Sonic ESB.

### **OpenEdge™ DataServers**

OpenEdge DataServers provide developers with a transparent interface to a wide range of database management systems. These products offer full read, write, update, insert and delete capabilities to diverse data management systems and enable developers to write OpenEdge-based applications once and deploy them across numerous data sources. OpenEdge DataServers provide native access to Oracle and Microsoft SQL Server and access to a wide range of ODBC-compliant data sources, including IBM DB2, IBM Informix On-Line and Sybase.

### **ObjectStore®**

ObjectStore is a data management solution for enterprise e-Business, telecommunications and commercial software applications. This scalable, high-performance technology leverages its object-oriented data modeling and native support for Java® and C++ to provide the reliability, scalability and time-to-market demands required of mission-critical systems. ObjectStore provides developers with highly efficient data storage. An ObjectStore database is defined by the components' object model. ObjectStore's Cache-Forward™ architecture is designed to maximize the performance of an application through load balancing, cache affinity, transaction services, and overall component coordination and management. The Cache-Forward architecture creates local data caches for components from the ObjectStore server or other enterprise databases.

### **ObjectStore® EdgeXtend®**

ObjectStore® EdgeXtend® provides a distributed data caching infrastructure that is automatically generated using model-driven, object-relational mapping tools. This data access and caching layer is designed to minimize bottlenecks in custom enterprise applications by optimizing relational database access. ObjectStore EdgeXtend provides graphical object-relational mapping tools and model-driven, interactive code generation designed to accelerate development. Built-in intelligent cache design incorporates the object model and schema for high performance. Cache clustering capabilities provide scalability and high availability.

### **DataDirect Connect®**

DataDirect Connect for ODBC is a clientless wire protocol ODBC driver for all major databases, including IBM DB2, Informix, Oracle, Microsoft SQL Server, Progress OpenEdge and Sybase. Wire protocol drivers eliminate the need for the database vendor's client software, thereby making applications easier to configure, deploy and maintain, and increases data access speeds. DataDirect Connect for JDBC is a Type 4 JDBC driver for high-performance database connectivity. DataDirect Connect for JDBC drivers support the latest database features, such as JTA (Java Transaction API). Other products from DataDirect include Connect64 for ODBC, Connect for .NET, Connect for ADO and Connect for SQL/XML.

## **Integration and Messaging Products**

### ***Sonic ESB®***

Sonic ESB is an enterprise service bus which is designed to simplify the integration and flexible reuse of business components using a standards-based, service-oriented architecture. Sonic ESB is designed to allow architects to dynamically configure the reliable connection, mediation and control of services and their interactions. Sonic ESB spans clusters and security infrastructures to form a federated environment which can be managed from any point. With its configurable service interaction that eliminates hard-wired dependencies, Sonic ESB is designed to make it easier to deploy initial projects and, without recoding, evolve, scale, and extend them throughout the enterprise.

### ***SonicMQ®***

SonicMQ is a standards-based enterprise messaging system that is designed to deliver high performance, management capabilities and scalability for large enterprise deployments. The patent-pending Sonic Continuously Available Architecture (CAA™) is designed to ensure continuous system performance while the Dynamic Routing Architecture® and advanced clustering technologies are designed to ensure scalability to large numbers of messages, users and brokers. Sonic CAA provides high availability for SonicMQ message brokers, SonicMQ clients and the communications among clients, brokers, and destinations. The advanced distributed management and deployment infrastructure of SonicMQ simplifies operations and lowers the total cost of ownership for business-critical communication across the enterprise. SonicMQ is designed to have strong authentication, authorization, and encryption support to ensure that messages and systems are protected inside and outside the firewall. With its guaranteed message delivery system that ensures messages are not lost due to software, network, or hardware failure, SonicMQ is utilized for very complex business transactions and mission-critical communications.

### ***Sonic Orchestration Server™***

Sonic Orchestration Server™ extends the intelligent routing capabilities of the Sonic ESB to enable the modeling, automation, and management of complex, stateful business processes across the extended enterprise. The Orchestration Server leverages the reach of the ESB to include participating services in a coordinated and managed business process.

### ***Sonic XML Server™***

Sonic XML Server™ provides high-speed XML processing, storage, and query services for management of Sonic ESB operational data. By processing XML messages in their native XML format, Sonic XML Server is designed to be fast, without imposing restrictions on XML message schema. Sonic XML Server can be used as an operational data cache and aggregation service and it can be deployed anywhere on the Sonic ESB to enhance performance, or support data warehousing, business event management, auditing and non-repudiation applications.

## **Management Products**

### ***PeerDirect® Distributed Enterprise***

PeerDirect® Distributed Enterprise offers patented technology for two-way, read-write replication of databases and applications, supporting companies that need to manage data across multiple sites, geographies or systems. This technology enables enterprises to effectively distribute business applications within an enterprise or to remote offices and users, improving the quality of service and system availability. PeerDirect Mobilized Enterprise and PeerDirect Remote Office are products in the PeerDirect Distributed Enterprise suite that leverage patented technology for application distribution and data synchronization. PeerDirect Mobilized Enterprise enables centralized control of applications and their databases, while automatically provisioning the same application on mobile computers. PeerDirect Remote Office enables applications and associated data to be managed centrally even when deployed in remote offices.



## [Table of Contents](#)

### ***Progress® Fathom®***

Progress® Fathom™ is a set of enterprise-class application management tools designed to increase the availability and performance of business systems. Progress Fathom enhances the availability and performance of Progress-based applications through system monitoring, alerting and automatic handling of corrective actions.

### **Product Development**

Most of PSC's products have been developed by its internal product development staff or the internal staffs of acquired companies. PSC believes that the features and performance of its products are competitive with those of other available development and deployment tools and that none of the current versions of its products is approaching obsolescence. However, PSC believes that significant investments in new product development and continuing enhancements of its current products will be required to enable the Company to maintain its competitive position.

PSC's product development staff consisted of 381 employees as of November 30, 2004. The Company has six development offices in North America and one in Belgium. In fiscal years 2004, 2003 and 2002, PSC spent \$60.7 million, \$50.5 million and \$42.0 million, respectively, on product development, of which \$0.3 million in fiscal 2004 and \$0.4 million in fiscal 2003 was capitalized. No amounts were capitalized in fiscal 2002.

### **Customers**

PSC globally markets its products primarily through APs and, to some extent, directly to end users. Purchasers of Progress-based applications are generally either business managers or IT managers in corporations and government agencies. In addition, the DataDirect, ObjectStore and Sonic product lines are also marketed to OEMs who embed and resell these products as part of an integrated solution. International distributors are generally located in countries where PSC does not have a direct presence. No single customer has accounted for more than 10% of PSC's total revenue in any of its last three fiscal years.

### ***Application Partners***

The Company's APs cover a broad range of markets, offer an extensive library of business applications and are a source of follow-on revenue. PSC maintains on-line application catalogs and includes APs in trade shows and other marketing programs. PSC also has kept entry costs for APs low to encourage a wide variety of APs to build applications. An AP typically takes six to twelve months to develop an application. Although many of the Company's APs have developed successful applications and have large installed customer bases, others are engaged in earlier stages of product development and marketing and may not contribute follow-on revenue to PSC for some time, if at all. However, if an AP succeeds in marketing its applications, PSC obtains follow-on revenue as the AP licenses the Company's deployment products to allow its application to be installed and used by customers. OED offers a subscription model alternative to the traditional perpetual license model for APs who have chosen to enable their business applications under a "software as a service" business model.

### ***Direct End Users***

PSC licenses its products directly to corporations, government agencies and other organizations. Many end users who purchase AP applications also purchase PSC's development tools to supplement their internal application development or purchase add-on products directly from PSC. Like APs, end user customers also license deployment products for internal applications.

### **Sales and Marketing**

PSC sells its products through its direct sales force in the United States and in over 25 other countries and through independent distributors in over 30 countries outside North America. The sales, marketing and service groups are organized by operating company and by regions within each operating company as applicable. OED operates by region in North America, EMEA, Asia/Pacific and Latin America. DataDirect, ObjectStore and Sonic Software operate by region within North America, EMEA and Japan. PSC believes that this structure allows it to maintain

## [Table of Contents](#)

direct contact with and support the diverse market requirements of its customers. PSC's international operations provide focused local marketing efforts and are able to respond directly to changes in local conditions.

Sales personnel are responsible for developing direct end user accounts, recruiting new AP accounts, assisting APs in marketing, closing major accounts and servicing existing customers. PSC actively seeks to avoid conflict between the sales efforts of its APs and the Company's own direct sales efforts. PSC uses its inside sales and customer service groups to enhance its direct sales efforts and to generate new business and follow-on business from existing customers. These groups may provide evaluation copies to APs or end user organizations to help qualify them as prospective customers, and also sell additional development and deployment products to existing customers.

The marketing groups within PSC and each operating unit conduct a variety of marketing programs designed to ensure a stream of market-ready products, assist APs with marketing, raise general awareness of PSC and its operating companies, generate leads for the sales organization and promote the various product lines. These programs include public relations, direct mail, participation in trade shows, advertising and production of collateral literature. In fiscal 2004, the Company held three regional user conference events in the United States, Spain and Australia.

### **Customer Support**

PSC's technical support staff provides telephone support to application developers and end-users. Customers may purchase maintenance services entitling them to software updates, technical support and technical bulletins. First year maintenance and any subsequent annual renewals are not included with the Company's products and are purchased separately. PSC provides technical support to customers primarily through its technical support centers in Bedford, Massachusetts; Rotterdam, The Netherlands; Slough, United Kingdom; and Melbourne, Australia. Local technical support for specific products is provided in certain countries, primarily in Japan.

OED launched the Progress Software Developers Network (PSDN) to deliver information, education and software resources for creating business applications with Progress technology. PSDN facilitates the exchange of technical expertise within the Progress developer community. PSDN offers Progress partners access to Progress expertise via technical white papers, live chats with experts and Web seminars.

### **Professional Services**

PSC's global professional services organization delivers business solutions for customers through a combination of products, consulting and education. PSC's consulting organization offers project management, custom development, programming, application implementation, Internet migration and other services. PSC's consulting organization also provides services to Web-enable existing applications or to take advantage of the capabilities of new product releases. The Company's education organization offers numerous training options, from traditional instructor-led courses to advanced learning modules available on CDs. Personnel at PSC's international subsidiaries and distributors provide consulting and training services for customers located outside North America.

### **Competition**

The computer software industry is intensely competitive. PSC experiences significant competition from a variety of sources with respect to all its products. PSC believes that the breadth and integration of its product offerings have become increasingly important competitive advantages. Other factors affecting competition in the markets served by PSC include product performance in complex applications, application portability, vendor experience, ease of integration, price, training and support.

## [Table of Contents](#)

PSC competes in various markets with a number of entities including database vendors offering development tools in conjunction with their database systems, such as Microsoft Corporation, Oracle Corporation and IBM Corporation, as well as numerous enterprise application integration vendors, messaging vendors and application development tools vendors. PSC believes that Oracle, Microsoft and IBM currently dominate the database market and that IBM dominates the messaging market. PSC does not believe that there is a dominant application development tools vendor or enterprise application integration vendor. Some of PSC's competitors have greater financial, marketing or technical resources than PSC and may be able to adapt more quickly to new or emerging technologies and changes in customer requirements or to devote greater resources to the promotion and sale of their products than can the Company. Increased competition could make it more difficult for PSC to maintain its revenue and market presence.

### **Copyrights, Trademarks, Patents and Licenses**

PSC relies upon a combination of contractual provisions and copyright, patent, trademark and trade secret laws to protect its proprietary rights in its products. PSC distributes its products under software license agreements that grant customers a perpetual nonexclusive license to use the Company's products and contain terms and conditions prohibiting the unauthorized reproduction or transfer of the Company's products. In addition, PSC attempts to protect its trade secrets and other proprietary information through agreements with employees and consultants. Although PSC intends to protect its rights vigorously, there can be no assurance that these measures will be successful.

PSC seeks to protect the source code of its products as trade secrets and as unpublished copyrighted works. PSC owns twenty patents covering portions of its products. PSC also owns twenty-five patent applications for some of its other product technologies. Where possible, PSC seeks to obtain protection of its product names and service offerings through trademark registration and other similar procedures throughout the world.

DataDirect, DataDirect Connect, Dynamic Routing Architecture, EdgeXtend, ObjectStore, PeerDirect, Progress, Progress OpenEdge, Persistence, Sonic ESB, SonicMQ, Stylus Studio and WebSpeed are registered trademarks of Progress Software Corporation or one of its subsidiaries in the U.S. and/or other countries. Cache-Forward, DataDirect Connect64, Fathom, OpenEdge, Sonic Orchestration Server and Sonic XML Server are trademarks of Progress Software Corporation or one of its subsidiaries in the U.S. and other countries. Java and all Java-based marks are trademarks or registered trademarks of Sun Microsystems, Inc. in the U.S. and other countries. Any other trademarks or trade names appearing in this Form 10-K are the property of their respective owners.

PSC believes that due to the rapid pace of innovation within its industry, factors such as the technological and creative skills of its personnel are as important in establishing and maintaining a leadership position within the industry as are the various legal protections of its technology. In addition, PSC believes that the nature of its customers, the importance of PSC's products to them and their need for continuing product support may reduce the risk of unauthorized reproduction.

## [Table of Contents](#)

### Employees

As of November 30, 2004, PSC had 1,552 employees worldwide, including 612 in sales and marketing, 319 in customer support and services (including manufacturing and distribution), 381 in product development and 240 in administration. None of PSC's U.S. employees is subject to a collective bargaining agreement. Employees in certain foreign jurisdictions are represented by local workers' councils and/or collective bargaining agreements as may be customary or required in that jurisdiction. PSC has experienced no work stoppages and believes its relations with employees are good.

PSC has various equity incentive plans that permit the granting of options to eligible employees and the purchase of shares by eligible employees. The payment of cash bonuses and contributions to retirement plans is at the discretion of the compensation committee of the Board of Directors and the amounts depend on the level of attainment relative to PSC's financial plan. These programs are designed to reward employees for performance and reduce employee turnover, although there can be no assurance that such programs will be successful.

### Executive Officers of the Registrant

The following table sets forth certain information regarding the executive officers of the Company.

Name	Age	Position
Joseph W. Alsop	59	Co-Founder and Chief Executive Officer and Director
James D. Freedman	56	Senior Vice President and General Counsel
David G. Ireland	58	President, Progress OpenEdge
Gregory J. O'Connor	42	President, Sonic Software Corporation
Richard D. Reidy	45	President, DataDirect Technologies
Norman R. Robertson	56	Senior Vice President, Finance and Administration and Chief Financial Officer
Peter G. Sliwkowski	40	President, ObjectStore
Jeffrey R. Stamen	59	Senior Vice President, Corporate Strategy and Business Development

Mr. Alsop, a co-founder of PSC, has been a director and Chief Executive Officer since the Company's inception in 1981.

Mr. Freedman was appointed Vice President and General Counsel in 1995 and was appointed Senior Vice President and General Counsel in August 2004. Mr. Freedman joined PSC in 1992.

Mr. Ireland joined the Company in 1997 as Vice President, Core Products and Services and was appointed Vice President and General Manager, Core Products and Services in 1998, Vice President and General Manager, Worldwide Field Operations in 1999 and President, Progress OpenEdge in 2000.

Mr. O'Connor was appointed Vice President, Apptivity Engineering in 1998 and was appointed Vice President, Sonic Engineering in 1999 and President, Sonic Software Corporation in 2001. Mr. O'Connor joined PSC in 1992.

Mr. Reidy was appointed Vice President, Development Tools in 1996 and was appointed Vice President, Product Development in 1997, Vice President, Products in 1999, Senior Vice President, Products and Corporate Development in 2000 and President, DataDirect Technologies in May 2004. Mr. Reidy joined PSC in 1985.

## Table of Contents

Mr. Robertson joined PSC in 1996 as Vice President, Finance and Chief Financial Officer and was appointed Vice President, Finance and Administration and Chief Financial Officer in 1997 and Senior Vice President, Finance and Administration and Chief Financial Officer in 2000.

Mr. Sliwowski was appointed Vice President, Development in 1997 and President, ObjectStore in October 2004. Mr. Sliwowski joined PSC in 1988.

Mr. Stamen joined the Company in June 2004 as Senior Vice President, Corporate Strategy and Business Development. From 1999 to 2004, Mr. Stamen was CEO of Syncra Systems, Inc., a software developer.

### **Available Information**

The Company's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to reports filed or furnished pursuant to Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, as amended, are available free of charge on the Company's website at [www.progress.com](http://www.progress.com) as soon as reasonably practicable after such reports are electronically filed with, or furnished to, the Securities and Exchange Commission. The information posted on the Company's web site is not incorporated into this Annual Report.

### **Item 2. Properties**

PSC owns its principal administrative, sales, support, marketing and product development facility, which is located in a single building of approximately 165,000 square feet in Bedford, Massachusetts. In November 2004, PSC purchased an adjacent 40,000 square feet facility which will be used for office space and manufacturing and distribution. In addition, PSC maintains offices in leased facilities in approximately 20 other locations in North America and approximately 40 locations outside North America. The terms of leases generally range from one to seven years. PSC believes that its facilities are adequate for its current needs and that suitable additional space will be available as needed.

### **Item 3. Legal Proceedings**

The Company is subject to various legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. While the outcome of these claims cannot be predicted with certainty, management does not believe that the outcome of any of these legal matters will have a material adverse effect on the Company's consolidated financial position or results of operations.

### **Item 4. Submission of Matters to a Vote of Security Holders**

No matters were submitted to a vote of PSC's shareholders during the fourth quarter of the fiscal year ended November 30, 2004.

**PART II****Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

The following table sets forth, for the periods indicated, the range of high and low sale prices for the Company's common stock. The Company's common stock trades on the Nasdaq National Market under the symbol PRGS.

Year Ended November 30,	2004		2003	
	High	Low	High	Low
First Quarter	\$ 24.46	\$ 20.10	\$ 15.98	\$ 12.60
Second Quarter	24.75	17.87	20.43	13.76
Third Quarter	22.46	17.82	24.06	18.90
Fourth Quarter	23.33	18.97	24.00	20.33

The Company has not declared or paid cash dividends on its common stock and does not plan to pay cash dividends to its shareholders in the near future. As of December 31, 2004, the Company's common stock was held by approximately 8,500 shareholders of record or through nominee or street name accounts with brokers.

Information related to repurchases by the Company of its common stock by month in the fourth quarter of fiscal 2004 is as follows:

*(in thousands, except per share data)*

Period:	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs (2)
Sep. 1, 2004 – Sep. 30, 2004	24	\$ 19.28	24	9,357
Oct. 1, 2004 – Oct. 31, 2004	23	\$ 19.63	23	9,977
Nov. 1, 2004 – Nov. 30, 2004	—	—	—	9,977
	47	\$ 19.45	47	9,977

(1) All shares were purchased in open market transactions.

(2) In September 2003, the Board of Directors authorized, for the period from October 1, 2003 through September 30, 2004, the purchase of up to 10,000,000 shares of the Company's common stock. In September 2004, the Board of Directors authorized, for the period from October 1, 2004 through September 30, 2005, the purchase of up to 10,000,000 shares of the Company's common stock, at such times that the Company deems such purchases to be an effective use of cash.

## [Table of Contents](#)

### Item 6. Selected Financial Data

The following table sets forth selected financial data regarding the Company for the last five fiscal years.

*(In thousands, except per share data)*

Year ended November 30,	2004	2003	2002	2001	2000
Revenue	\$ 362,662	\$ 309,060	\$ 273,123	\$ 263,584	\$ 273,080
Income from operations	46,364	36,752	28,224	21,305	38,695
Net income	32,101	27,074	20,587	17,643	33,651
Basic earnings per share	0.89	0.79	0.58	0.50	0.94
Diluted earnings per share	0.82	0.72	0.54	0.46	0.85
Cash and short-term investments	191,267	219,131	177,193	174,516	158,106
Total assets	446,814	367,770	290,166	299,380	278,805
Long-term debt, including current portion	2,438	—	—	—	—
Shareholders' equity	266,978	222,041	172,963	185,176	166,813

As discussed below in Item 7 of this Annual Report on Form 10-K, the Company completed the acquisition of eXcelon in fiscal 2003 and the acquisitions of DataDirect and Persistence in fiscal 2004.

### Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

#### Overview

The Company develops, markets and distributes software to simplify and accelerate the development, deployment, integration and management of business applications. The mission of the Company is to deliver software products and services that empower partners and customers to improve their development, deployment, integration and management of quality applications worldwide. The Company's products include development tools, databases, application servers, messaging servers, application management tools, data connectivity products and integration products for distributed and Web-based applications as well as for client/server applications. The Company, through its various operating units, markets its products globally to a broad range of organizations in manufacturing, distribution, finance, retail, healthcare, telecommunications, government and many other fields.

A significant portion of the Company's revenue is derived from international operations. In fiscal 2004 as well as in fiscal years 2003 and 2002, the weakening of the U.S. dollar against most major currencies, primarily the euro and the British pound, positively affected the Company's results. Prior to that, the U.S. dollar was stronger and the Company's results were adversely affected.

The Company conducts business through four operating units. The Company's principal operating unit conducts business as the Progress OpenEdge Division (OED). OED provides the Progress® OpenEdge® platform, a set of development and deployment technologies, including the OpenEdge RDBMS, one of the leading embedded databases, for building business applications. Sonic Software Corporation is focused on enterprise application integration and the emerging market for enterprise service bus (ESB) and operates as a subsidiary of the Company. Sonic Software Corporation delivers a distributed, standards-based communications and integration infrastructure, built on an ESB that integrates existing business applications and orchestrates business processes across the extended enterprise. The third operating unit is ObjectStore, a division of PSC, providing advanced data management software for developing high performance real-time applications which require processing of large amounts of data. ObjectStore was acquired in December 2002 as part of the acquisition of eXcelon Corporation (eXcelon). The ObjectStore division is also responsible for the PeerDirect product line. The fourth operating unit, the DataDirect division of PSC, provides standards-based data connectivity software.

In December 2003, the Company completed its cash acquisition of certain assets and subsidiaries and the assumption of certain liabilities of DataDirect Technologies Limited for approximately \$87.5 million, net of cash acquired and subject to certain post-closing adjustments.

In November 2004, the Company completed its cash acquisition of Persistence for approximately \$11.8 million, net of cash acquired. The principal product of Persistence is data caching technology. The products and people associated with the Persistence business were combined with the ObjectStore operating unit.

## Critical Accounting Policies

Management's discussion and analysis of financial condition and results of operations are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The Company makes estimates and assumptions in the preparation of its consolidated financial statements that affect the reported amounts of assets and liabilities, revenue and expenses, and related disclosures of contingent assets and liabilities. The Company bases its estimates on historical experience and various other assumptions that are believed to be reasonable under the circumstances. However, actual results may differ from these estimates.

The Company has identified the following critical accounting policies that require the use of significant judgments and estimates in the preparation of its consolidated financial statements. This listing is not a comprehensive list of all of the Company's accounting policies. For further information regarding the application of these and other accounting policies, see Note 1 in the Notes to Consolidated Financial Statements in Item 8 of this Annual Report on Form 10-K.

**Revenue Recognition** — The Company's revenue recognition policy is significant because revenue is a key component affecting results of operations. In determining when to recognize revenue from a customer arrangement, the Company is often required to exercise judgment regarding the application of its accounting policies to a particular arrangement. For example, judgment is required in determining whether a customer arrangement has multiple elements. If such a situation exists, judgment is also involved in determining whether vendor-specific objective evidence (VSOE) of fair value for the undelivered elements exists. While the Company follows specific and detailed rules and guidelines related to revenue recognition, significant management judgments and estimates are made and used in connection with the revenue recognized in any reporting period, particularly in the areas described above as well as collectibility. If management made different estimates or judgments, material differences in the timing of the recognition of revenue could occur.

**Allowance for Doubtful Accounts** — The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of customers to make required payments. This allowance is established using estimates that the Company makes based on factors such as the composition of the accounts receivable aging, historical bad debts, changes in payment patterns, changes to customer creditworthiness and current economic trends. If the Company used different estimates, or if the financial condition of customers were to deteriorate, resulting in an impairment of their ability to make payments, additional provisions for doubtful accounts would be required and would increase bad debt expense.

**Goodwill and Intangible Assets** — The Company has goodwill and net intangible assets of \$107.4 million at November 30, 2004. The Company assesses the impairment of goodwill and identifiable intangible assets on an annual basis and whenever events or changes in circumstances indicate that the carrying value of the asset may not be recoverable. An impairment charge would be recorded if such an assessment were to indicate that the fair value of such assets was less than the carrying value. Judgment is required in determining whether an event has occurred that may impair the value of goodwill or identifiable intangible assets. Factors that could indicate that an impairment may exist include significant underperformance relative to plan or long-term projections, strategic changes in business strategy, significant negative industry or economic trends or a significant decline in the stock price of the Company for a sustained period of time. The Company utilizes discounted cash flow models or valuation reports from third-party firms to determine the fair value of its reporting units. The Company must make assumptions about future cash flows, future operating plans, discount rates and other factors in the models and valuation reports. Different assumptions and judgment determinations could yield different conclusions that would result in an impairment charge to income in the period that such change or determination was made.

**Deferred Income Taxes** — The Company had a net deferred tax asset of \$28.8 million at November 30, 2004. The Company records valuation allowances to reduce deferred tax assets to the amount that is more likely than not to be realized. The Company considers scheduled reversals of temporary differences, projected future taxable income, ongoing tax planning strategies and other matters in assessing the need for and the amount of a valuation allowance. If the Company were to change its assumptions or otherwise determine that it was unable to realize all or part of its net deferred tax asset in the future, an adjustment to the deferred tax asset would be charged to income in the period that such change or determination was made.



## [Table of Contents](#)

### Results of Operations

The following table sets forth certain income and expense items as a percentage of total revenue, and the percentage change in dollar amounts of such items compared with the corresponding period in the previous fiscal year.

Year Ended November 30,	Percentage of Total Revenue			Period-to-Period Change	
	2004	2003	2002	2004 Compared to 2003	2003 Compared to 2002
<b>Revenue:</b>					
Software licenses	39%	35%	34%	28%	17%
Maintenance and services	61	65	66	11	11
Total revenue	100	100	100	17	13
<b>Costs and expenses:</b>					
Cost of software licenses	2	3	4	6	(20)
Cost of maintenance and services	14	17	21	0	(8)
Sales and marketing	40	40	39	16	20
Product development	17	16	15	21	19
General and administrative	11	11	11	17	11
Amortization of acquired intangibles	2	1	0	209	358
In-process research and development	1	0	—	*	*
Total costs and expenses	87	88	90	16	11
Income from operations	13	12	10	26	30
Other income (expense), net	0	1	1	(56)	62
Income before provision for income taxes	13	13	11	22	32
Provision for income taxes	4	4	3	30	32
Net income	9%	9%	8%	19%	32%

\* not meaningful

### Fiscal 2004 Compared to Fiscal 2003

The Company's total revenue increased 17% from \$309.1 million in fiscal 2003 to \$362.7 million in fiscal 2004. Total revenue would have increased by approximately 11% if exchange rates had been constant in fiscal 2004 as compared to the exchange rates in effect in fiscal 2003. In addition to the positive effect of changes in exchange rates, the Company's revenue increased due to software license and maintenance revenue derived from the products acquired as part of the DataDirect acquisition and software license and maintenance revenue growth of all of the Company's major product lines including Progress OpenEdge, Sonic and ObjectStore.

Total revenue from the Progress OpenEdge product line increased 7% from \$272.5 million in fiscal 2003 to \$290.3 million in fiscal 2004. Total revenue derived from the Sonic product line increased 14% from \$23.0 million in fiscal 2003 to \$26.2 million in fiscal 2004. Revenue from the ObjectStore product line increased 32% from \$13.5 million in fiscal 2003 to \$17.9 million in fiscal 2004. Revenue from the DataDirect product line, which was acquired in the December 2003 acquisition of DataDirect Technologies, contributed \$28.2 million of revenue in fiscal 2004.

Software license revenue increased 28% from \$109.7 million in fiscal 2003 to \$140.5 million in fiscal 2004. Software license revenue would have increased by approximately 22% if exchange rates had been constant in fiscal 2004 as compared to the exchange rates in effect in fiscal 2003. The increase in software license revenue was positively affected by the addition of DataDirect, which accounted for 13% of software license revenue in fiscal 2004. Software license revenue from indirect channels, including application partners which have written software applications utilizing Progress Software technology and which resell the Company's products in conjunction with the sale of their applications and OEMs, and from sales to direct end users, both increased in fiscal 2004 as compared to fiscal 2003. Software license revenue from the Progress OpenEdge product set increased year over year, primarily within the database products. Software license revenue also increased from newer products such as the Sonic and ObjectStore product lines.

## [Table of Contents](#)

Maintenance and services revenue increased 11% from \$199.4 million in fiscal 2003 to \$222.2 million in fiscal 2004. Maintenance and services revenue would have increased by approximately 5% if exchange rates had been constant in fiscal 2004 as compared to the exchange rates in effect in fiscal 2003. The increase in maintenance and services revenue was also the result of growth in the Company's installed customer base, renewal of maintenance agreements and the acquisition of DataDirect, partially offset by a decline in professional services revenue. The decline in professional services revenue was primarily the result of a continued decrease in consulting revenue in the Europe, Middle East and Africa (EMEA) region as a result of economic conditions and a slower overall market for professional services.

Total revenue generated in markets outside North America increased 12% from \$187.0 million in fiscal 2003 to \$208.9 million in fiscal 2004 and represented 61% of total revenue in fiscal 2003 and 58% of total revenue in fiscal 2004. Revenue from the three major regions outside of North America, consisting of EMEA, Latin America and Asia Pacific, each increased in fiscal 2004 as compared to fiscal 2003. Total revenue generated in markets outside North America would have represented 55% of total revenue if exchange rates had been constant in fiscal 2004 as compared to the exchange rates in effect in fiscal 2003. The decrease in the percentage of business derived from international operations in fiscal 2004 is primarily the result of the addition of DataDirect. The customer base for DataDirect is more concentrated within North America.

The Company anticipates total revenue in fiscal 2005 to be in the range of \$390 million to \$400 million, representing an increase of 8% to 10% as compared to fiscal 2004. This revenue expectation assumes the continued success of the Company's application partners and other channel partners, continued improvement in the Company's ability to generate new business in end user accounts and continued growth and success from the newer product lines of DataDirect, ObjectStore and Sonic. However, many factors, including external factors such as geopolitical issues or a significant strengthening of the U.S. dollar against currencies from which the Company derives a significant portion of its business, could negatively impact this revenue expectation.

Cost of software licenses consists primarily of cost of product media, documentation, duplication, packaging, electronic software distribution, royalties and amortization of capitalized software costs. Cost of software licenses increased 6% from \$8.4 million in fiscal 2003 to \$9.0 million in fiscal 2004, but decreased as a percentage of software license revenue from 8% to 6%. The dollar increase was primarily due to higher royalty expense for products and technologies licensed from third parties. Cost of software licenses as a percentage of software license revenue may vary from period to period depending upon the relative product mix. However, the Company expects the cost of software licenses for fiscal 2005 to remain at the lower end of the past few years' historical range of 6% to 10% of the related software license revenue.

Cost of maintenance and services consists primarily of costs of providing customer technical support, education and consulting. Cost of maintenance and services decreased less than 1% from \$52.6 million in fiscal 2003 to \$52.4 million in fiscal 2004, but decreased as a percentage of maintenance and services revenue from 26% to 24%. The maintenance and services revenue margin improvement was due to maintenance revenue, which has a substantially higher margin than professional services revenue, representing a greater proportion of the total maintenance and services revenue in 2004. The total dollar amount in fiscal 2004 increased due to the impact of year-over-year changes in exchange rates and additional technical support personnel and related costs associated with DataDirect, but were offset by lower outside contractor expenses in professional services. The Company's technical support, education and consulting headcount increased by 5% from the end of fiscal 2003 to the end of fiscal 2004.

Sales and marketing expenses increased 16% from \$125.7 million in fiscal 2003 to \$146.2 million in fiscal 2004, but remained the same percentage of total revenue at 40%. The increase in sales and marketing expenses was due to the addition of sales and marketing personnel and related expenses resulting from the acquisition of DataDirect as well as a slight increase in the level of discretionary marketing spending for trade shows, advertising campaigns, lead generation, direct mail solicitations and other events. Expenses also increased due to the impact of year-over-year changes in exchange rates as a significant percentage of sales and marketing expenses are incurred outside of North America. The Company's sales, sales support and marketing headcount increased by 7% from the end of fiscal 2003 to the end of fiscal 2004.

Product development expenses increased 21% from \$50.1 million in fiscal 2003 to \$60.4 million in fiscal 2004 and increased as a percentage of revenue from 16% to 17%. The most significant development efforts in fiscal 2004 related to the release of Progress OpenEdge 10, new releases of Sonic ESB and SonicMQ and updated versions of

## [Table of Contents](#)

the DataDirect and ObjectStore product lines. The dollar increase was primarily due to an increase in headcount and related expenses resulting from the acquisition of DataDirect. Capitalized software costs associated with Progress OpenEdge 10 totaled \$0.3 million in fiscal 2004 as compared to \$0.4 million in fiscal 2003. Amounts capitalized represented less than 1% of total product development spending. The Company's product development headcount increased 29% from the end of fiscal 2003 to the end of fiscal 2004.

General and administrative expenses include the costs of the finance, human resources, legal, information systems and administrative departments of the Company. General and administrative expenses increased 17% from \$33.1 million in fiscal 2003 to \$38.8 million in fiscal 2004, but remained the same percentage of revenue at 11%. The dollar increase was primarily due to headcount related costs, transition and integration costs associated with acquisitions, higher professional services fees and the impact of changes in exchange rates. The Company's administrative headcount increased 10% from the end of fiscal 2003 to the end of fiscal 2004.

Amortization of acquired intangibles primarily represents the assigned value of intangible assets obtained in business combinations. Amortization of acquired intangibles increased from \$2.3 million in fiscal 2003 to \$7.1 million in fiscal 2004. The increase was due to amortization expense associated with the acquisition of DataDirect. The Company expects amortization of acquired intangibles to total approximately \$7.9 million for fiscal 2005.

Acquired in-process research and development from the acquisition of DataDirect totaled \$2.6 million in fiscal 2004 and was expensed when the acquisition was consummated because the technological feasibility of several products under development at the time of the acquisition had not been achieved and no alternate future uses had been established. Research and development costs to bring the acquired products to technological feasibility are not expected to have a material impact on the Company's future results of operations or cash flows. At the date of the acquisition, the Company anticipated the completed product being released in the first half of fiscal 2005. The value of in-process research and development was determined based on an independent appraisal from a third party. In fiscal 2003, the Company incurred \$0.2 million of in-process research and development related to the acquisition of eXcelon.

Income from operations increased 26% from \$36.8 million in fiscal 2003 to \$46.4 million in fiscal 2004 and increased as a percentage of total revenue from 12% in fiscal 2003 to 13% in fiscal 2004. Noncash charges for amortization of purchased intangibles and in-process research and development increased from 1% of total revenue in fiscal 2003 to 3% of total revenue in fiscal 2004. If the Company is able to meet its forecasted revenue target and expenses occur as planned in fiscal 2005, the Company expects operating income as a percentage of revenue to be between 13% and 14% for fiscal 2005.

Other income decreased 56% from \$1.9 million in fiscal 2003 to \$0.8 million in fiscal 2004. The decrease was primarily due to lower interest income, resulting from lower interest rates and the reduction in cash and short-term investment balances due to the acquisition of DataDirect.

The Company's effective tax rate was 30% in fiscal 2003 as compared to 32% in fiscal 2004. The increase in the effective tax rate was due to a change in expected rates for state taxes on deferred taxes and lower benefits from tax-exempt interest. See Note 9 of Notes to Consolidated Financial Statements. The IRS is currently examining the Company's United States income tax returns for fiscal years through 2002. The Company has provided reserves for certain tax matters, both domestic and foreign, which it believes could result in additional tax being due. Any additional assessment or reduction of these contingent liabilities will be reflected in the Company's effective tax rate in the period when the audit is completed. Excluding the impact of the results of the IRS audit, the Company estimates that its effective tax rate will remain at approximately 32% in fiscal 2005.

### **Fiscal 2003 Compared to Fiscal 2002**

The Company's total revenue increased 13% from \$273.1 million in fiscal 2002 to \$309.1 million in fiscal 2003. Total revenue would have increased by 5% in fiscal 2003 if exchange rates had been constant in fiscal 2003 as compared to the exchange rates in effect in fiscal 2002.

Total revenue from the Progress OpenEdge product line increased 6% from \$258.2 million in fiscal 2002 to \$272.5 million in fiscal 2003. Total revenue derived from the Sonic product line, including the XML-based products acquired as part of the eXcelon acquisition, increased 54% from \$15.0 million in fiscal 2002 to \$23.0 million in

## [Table of Contents](#)

fiscal 2003. Revenue from the ObjectStore product line, acquired as part of the eXcelon acquisition, totaled \$13.5 million in fiscal 2003.

Software license revenue increased 17% from \$93.5 million in fiscal 2002 to \$109.7 million in fiscal 2003. Software license revenue would have increased by 10% in fiscal 2003 if exchange rates had been constant in fiscal 2003 as compared to the exchange rates in effect in fiscal 2002. The increase in software license revenue in fiscal 2003 was due to an increase in revenue from sales to direct end users and, to a lesser extent, APs. Software license revenue from the Progress product set increased year over year, primarily within the database product and other deployment and management products. Software license revenue also increased from new products, such as the Sonic product line, as well as from ObjectStore.

Maintenance and services revenue increased 11% from \$179.7 million in fiscal 2002 to \$199.4 million in fiscal 2003. Maintenance and services revenue would have increased by 3% in fiscal 2003 if exchange rates had been constant in fiscal 2003 as compared to the exchange rates in effect in fiscal 2002. The increase in maintenance and services revenue was the result of growth in the Company's installed customer base and renewal of maintenance contracts, partially offset by a decline in services revenue. The decline in professional services revenue was primarily the result of decreases in consulting revenue in EMEA and the Latin America region due to fewer projects as a result of economic conditions and a slower overall market for professional services. Education revenue also decreased in fiscal 2003 as compared to fiscal 2002.

Total revenue generated in markets outside North America increased 15% from \$163.3 million in fiscal 2002 to \$187.0 million in fiscal 2003 and represented 61% of total revenue in fiscal 2003 as compared to 60% of total revenue in fiscal 2002. The increase was the result of higher revenue from EMEA and Asia Pacific, partially offset by a continued decline in revenue from Latin America in fiscal 2003. The decrease in this region was due to an overall market slowdown in the purchase of packaged applications, especially in the government sector in various countries within Latin America. Total revenue generated in markets outside North America as a percentage of total revenue in fiscal 2003 would have been 58% if exchange rates had been constant in fiscal 2003 as compared to the exchange rates in effect in fiscal 2002.

Cost of software licenses decreased 20% from \$10.5 million in fiscal 2002 to \$8.4 million in fiscal 2003 and decreased as a percentage of software license revenue from 11% to 8%. The dollar and percentage decreases were primarily due to lower royalty expense for products and technologies licensed from third parties and lower amortization expense from previously capitalized software costs.

Cost of maintenance and services decreased 8% from \$56.9 million in fiscal 2002 to \$52.6 million in fiscal 2003 and decreased as a percentage of maintenance and services revenue from 32% to 26%. The maintenance and services revenue margin improvement was due to a change in the mix of maintenance and services revenue. Maintenance revenue, which has a substantially higher margin than professional services revenue, represented a greater proportion of the total maintenance and services revenue in fiscal 2003. The dollar decrease was due to lower usage of third-party contractors for service engagements, partially offset by increased headcount-related expenses primarily in technical support assumed in the acquisition of eXcelon. The Company increased its technical support, education and consulting staff by 8% from the end of fiscal 2002 to the end of fiscal 2003.

Sales and marketing expenses increased 20% from \$105.1 million in fiscal 2002 to \$125.7 million in fiscal 2003 and increased as a percentage of total revenue from 39% to 40%. The dollar and percentage increases in sales and marketing expenses were due to the addition of sales and marketing personnel and related expenses assumed in the acquisition of eXcelon, as well as an increase in the level of discretionary marketing spending for trade shows, advertising campaigns, lead generation, direct mail solicitations and other events. Expenses also increased in fiscal 2003 due to year-over-year changes in exchange rates as a significant percentage of sales and marketing expenses are incurred outside of North America. The Company increased its sales, sales support and marketing staff by 4% from the end of fiscal 2002 to the end of fiscal 2003.

Product development expenses increased 19% from \$42.0 million in fiscal 2002 to \$50.1 million in fiscal 2003 and increased as a percentage of total revenue from 15% to 16%. The dollar and percentage increases were primarily due to the addition of development personnel for the ObjectStore and XML product groups from the eXcelon acquisition. The major product development efforts in fiscal 2003 primarily related to the development and enhancement of the next release of the OpenEdge platform, the Company's principal product line, a new release of

## [Table of Contents](#)

ObjectStore and new products such as SonicESB, SonicMQ, Dynamics, Fathom and PeerDirect Replication Engine. The Company capitalized \$0.4 million of software development costs in fiscal 2003 and none in fiscal 2002. The amount capitalized in fiscal 2003 represented less than 1% of total product development costs that year. The Company increased its product development staff by 19% from the end of fiscal 2002 to the end of fiscal 2003.

General and administrative expenses increased 11% from \$29.8 million in fiscal 2002 to \$33.1 million in fiscal 2003, but remained the same percentage of total revenue at 11%. General and administrative expenses increased primarily due to higher headcount-related costs, the impact of changes in exchange rates and an increase in amortization expense from acquired intangible assets. The expense increase in fiscal 2003 also was due to transition and integration costs associated with the acquisition of eXcelon. The Company increased its administrative staff by 5% from the end of fiscal 2002 to the end of fiscal 2003.

Amortization of acquired intangibles increased from \$0.5 million in fiscal 2002 to \$2.3 million in fiscal 2003. The increase was due to amortization expense associated with the acquisition of eXcelon.

Acquired in-process research and development of \$0.2 million was expensed when the acquisition of eXcelon was consummated because the technological feasibility of several products under development at the time of the acquisition had not been achieved and no alternate future uses had been established. Research and development costs to bring the acquired products to technological feasibility are not expected to have a material impact on the Company's future results of operations or cash flows. At the date of the acquisition, the Company anticipated the completed product being released in the second half of fiscal 2003.

Income from operations increased as a percentage of total revenue from 10% in fiscal 2002 to 12% in fiscal 2003. The dollar increase and the increase in operating income as a percentage of revenue were primarily due to higher revenue during the year, partially offset by continued investment in new business opportunities such as Sonic Software and PeerDirect. In addition, the Company's total headcount increased throughout fiscal 2003, primarily due to the personnel acquired from eXcelon.

Other income increased 62% from \$1.2 million in fiscal 2002 to \$1.9 million in fiscal 2003. Excluding a noncash impairment charge of \$1.0 million related to the Company's investment in a related party, EasyAsk, Inc., in fiscal 2002, the Company's other income would have decreased 12% primarily due to lower interest income earned on cash balances, partially offset by lower foreign exchange transaction losses. The decrease in interest income was due to lower interest rates.

The Company's effective tax rate was 30% in each of fiscal 2002 and fiscal 2003.

### **Liquidity and Capital Resources**

The Company's cash and short-term investments totaled \$191.3 million at November 30, 2004. The decrease of \$27.8 million since the end of fiscal 2003 resulted primarily from the acquisitions of DataDirect and Persistence and stock repurchases, partially offset by cash generated from operations and proceeds from exercises of stock options and stock issuances under the Company's stock purchase plan.

In fiscal years 2004, 2003 and 2002, the Company generated \$72.2 million, \$57.7 million and \$44.4 million, respectively, in cash from operations. The increase in cash generated from operations in each year was due to higher net income and increases in deferred revenue, primarily the result of increased billings for maintenance.

Accounts receivable at November 30, 2004 increased by \$11.4 million from the end of fiscal 2003. The increase was primarily the result of higher revenue. Accounts receivable days sales outstanding (DSO) increased by 2 days to 59 days at the end of fiscal 2004 as compared to 57 days at the end of fiscal 2003 and 61 days at the end of fiscal 2002. The Company targets a DSO range of 60 to 80 days.

In fiscal years 2004, 2003 and 2002, the Company purchased \$13.1 million (including amounts associated with the assumption of a mortgage of \$2.4 million), \$7.1 million and \$6.8 million, respectively, of property and equipment. The amount for fiscal 2004 included the purchase of a building adjacent to the Company's headquarters for \$4.7 million. The remaining amounts in fiscal 2004 and in each of fiscal years 2003 and 2002 consisted primarily of computer equipment, software and building and leasehold improvements. The Company financed these purchases

## [Table of Contents](#)

primarily from cash generated from operations, except with respect to the building purchase which included the required assumption of an existing mortgage.

In fiscal years 2004, 2003 and 2002, the Company purchased and retired 646,618 shares, 686,237 shares and 3,386,676 shares, respectively, of its common stock for \$13.0 million, \$12.1 million and \$45.1 million, respectively. Since beginning its stock repurchase program in 1996, the Company has purchased and retired 18,258,379 shares at a cost of \$190.8 million. In September 2004, the Board of Directors authorized, for the period from October 1, 2004 through September 30, 2005, the purchase of up to 10,000,000 shares of the Company's common stock, at such times that the Company deems such purchases to be an effective use of cash. Shares that are repurchased may be used for various purposes, including the issuance of shares pursuant to the Company's stock option and stock purchase plans.

In November 2004, the Company completed its acquisition of Persistence. The acquisition was accounted for as a purchase, and accordingly, the results of operations of Persistence are included in the Company's operating results from the date of acquisition. The acquisition was structured as a merger of a wholly owned subsidiary of the Company with and into Persistence. Pursuant to the terms of the acquisition, each outstanding share of Persistence common stock was converted into the right to receive \$5.70 in cash, without interest. In addition, as a result of the acquisition, holders of exercisable options and warrants to purchase Persistence common stock with an exercise price of less than \$5.70 per share were entitled to receive a cash payment equal to the number of shares of Persistence common stock subject to such option or warrant multiplied by the amount by which \$5.70 exceeded the exercise price per share of such option or warrant. The aggregate purchase price, net of cash acquired, of approximately \$11.8 million included \$0.3 million for direct transaction costs. The purchase price was paid in cash from available funds.

In December 2003, the Company, through a wholly owned subsidiary, acquired substantially all of the assets and certain subsidiaries and assumed certain liabilities of DataDirect Technologies Limited, a private company incorporated under the laws of Ireland, for an aggregate purchase price of approximately \$87.5 million, net of cash acquired and subject to certain post-closing adjustments. The aggregate purchase price included \$0.7 million of direct transaction costs. The acquisition was accounted for as a purchase, and accordingly, the results of operations of DataDirect are included in the Company's operating results from the date of acquisition. The purchase price was paid in cash from available funds.

In December 2002, the Company completed its acquisition of eXcelon, a provider of data management software. The acquisition was accounted for as a purchase, and accordingly, the results of operations of eXcelon are included in the Company's operating results from the date of acquisition. The acquisition was structured as a merger of a wholly owned subsidiary of the Company with and into eXcelon. Pursuant to the terms of the acquisition, each outstanding share of eXcelon common stock was converted into the right to receive \$3.19 in cash, without interest. In addition, as a result of the acquisition, holders of outstanding options to purchase eXcelon common stock with an exercise price of less than \$3.19 per share were entitled to receive a cash payment equal to the number of shares of eXcelon common stock subject to such option multiplied by the amount by which \$3.19 exceeded the exercise price per share of such option. The aggregate purchase price of approximately \$33.7 million included \$9.1 million for facilities closures and employee severance and \$0.7 million for direct transaction costs. The purchase price was paid in cash from available funds.

The Company includes standard intellectual property indemnification provisions in its licensing agreements in the ordinary course of business. Pursuant to the Company's product license agreements, the Company will indemnify, hold harmless, and agree to reimburse the indemnified party for losses suffered or incurred by the indemnified party, generally business partners or customers, in connection with certain patent, copyright or other intellectual property infringement claims by third parties with respect to the Company's products. Other agreements with the Company's customers provide indemnification for claims relating to property damage or personal injury resulting from the performance of services by the Company or its subcontractors. Historically, the Company's costs to defend lawsuits or settle claims relating to such indemnity agreements have been insignificant. Accordingly, the estimated fair value of these indemnification provisions is immaterial.

The Company is subject to various legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. While the outcome of these claims cannot be predicted with certainty, management does not believe that the outcome of any of these legal matters will have a material adverse effect on the Company's consolidated financial position or results of operations.

## [Table of Contents](#)

In connection with the purchase of a building adjacent to the Company's headquarters, the Company was required to assume long-term debt, including the current portion, of \$2.4 million. The Company believes that existing cash balances together with funds generated from operations will be sufficient to finance the Company's operations and meet its foreseeable cash requirements (including planned capital expenditures, lease commitments, debt payments, potential cash acquisitions and other long-term obligations) through at least the next twelve months.

### **Contractual Obligations**

The Company has no off-balance sheet arrangements as defined in Item 303(a)(4) of Regulation S-K. The following table details the Company's contractual obligations as of November 30, 2004:

*(In thousands)*

Contractual Obligations	Total	Payments Due by Period			
		Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Long-term debt	\$ 2,438	\$ 238	\$ 541	\$ 635	\$ 1,024
Operating leases	21,994	10,508	8,853	2,174	459
Total	\$ 24,432	\$ 10,746	\$ 9,394	\$ 2,809	\$ 1,483

### **New Accounting Pronouncements**

In December 2004, the Financial Accounting Standards Board issued SFAS No. 123R, "Share-Based Payment" (SFAS 123R). This Statement is a revision of SFAS No. 123, Accounting for Stock-Based Compensation, and supersedes Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and its related implementation guidance. SFAS 123R requires a company to measure the grant-date fair value of equity awards given to employees in exchange for services and recognize that cost over the period that such services are performed. SFAS 123R is effective for the first interim or annual reporting period that begins after June 15, 2005.

The Company is currently evaluating the two methods of adoption allowed by SFAS 123R: the modified-prospective transition method and the modified-retrospective transition method. Adoption of SFAS 123R will materially increase stock compensation expense and decrease net income. In addition, SFAS 123R requires that the excess tax benefits related to stock compensation be reported as a cash inflow from financing activities rather than as a reduction of taxes paid in cash from operations.

### **Factors That May Affect Future Results**

The Company operates in a rapidly changing environment that involves certain risks and uncertainties, some of which are beyond the Company's control. The following discussion highlights some of these risks.

**Fluctuations in Revenue and Quarterly Results** — The Company may experience significant fluctuations in future quarterly operating results that may be caused by many factors. Some of these factors include changes in demand for the Company's products, introduction, enhancement or announcement of products by the Company and its competitors, market acceptance of new products, the growth rates of certain market segments including enterprise application integration and messaging, size and timing of significant orders, budgeting cycles of customers, mix of distribution channels, mix of products and services sold, mix of international and North American revenues, fluctuations in currency exchange rates, changes in the level of operating expenses, changes in the Company's sales incentive plans, customer order deferrals in anticipation of new products announced by the Company or its competitors and general economic conditions in regions in which the Company conducts business. Revenue forecasting is uncertain, in large part, because the Company generally ships its products shortly after receipt of orders. Most of the Company's expenses are relatively fixed, including costs of personnel and facilities, and are not easily reduced. Thus, an unexpected reduction in the Company's revenue, or failure to achieve the anticipated rate of growth, would have a material adverse effect on the profitability of the Company.

**Global Economic and Political Conditions** — The global economic and political environment and the current business climate could impact the Company's revenue and net income in the near term. Political instability, oil price shocks



## Table of Contents

and armed conflict in various regions of the world also contribute to economic uncertainty. If customers' buying patterns, such as decision-making processes, timing of expected deliveries and timing of new projects, unfavorably change due to economic or political conditions, there will be a material adverse effect on the Company's business, financial condition and operating results.

**Products** — Ongoing enhancements to the Company's various product sets will be required to enable the Company to maintain its competitive position. There can be no assurance that the Company will be successful in developing and marketing enhancements to its products on a timely basis, or that the enhancements will adequately address the changing needs of the marketplace. Failure to develop enhancements that meet market needs in a timely manner could have a material adverse effect on the Company's business, financial condition and operating results.

Overlaying the risks associated with the Company's existing products and enhancements are ongoing technological developments and rapid changes in customer requirements. The Company's future success will depend upon its ability to develop and introduce in a timely manner new products that take advantage of technological advances and respond to new customer requirements. The development of new products is increasingly complex and uncertain, which increases the risk of delays. There can be no assurance that the Company will be successful in developing new products incorporating new technology on a timely basis, or that its new products will adequately address the changing needs of the marketplace.

The Company derives a significant portion of its revenue from its core product line, Progress OpenEdge, and other products that complement OpenEdge and are generally licensed only in conjunction with OpenEdge. Accordingly, the Company's future results depend on continued market acceptance of OpenEdge and any factor adversely affecting the market for OpenEdge could have a material adverse effect on the Company's business, financial condition and operating results.

Some of the Company's newer products, such as the Sonic and PeerDirect product sets, require a higher level of development, distribution and support expenditures, on a percentage of revenue basis, than the OpenEdge, ObjectStore or DataDirect product lines. If revenue generated from these products becomes a greater percentage of the Company's total revenue and if the expenses associated with these products do not decrease on a percentage of revenue basis, then the Company's operating margins will be adversely affected.

**International Operations** – The Company typically generates between 55% and 60% of its total revenue from sales outside of North America. Because a majority of the Company's total revenue is derived from international operations that are primarily conducted in foreign currencies, changes in the value of these foreign currencies relative to the U.S. dollar may affect the Company's results of operations and financial position. In the past two years, the U.S. dollar has been significantly weaker than in the previous few years against most major foreign currencies, which has positively affected the Company's revenue and results of operations. This trend may not continue. There can be no assurance that the Company's currency hedging transactions will materially reduce the effect of fluctuations in foreign currency exchange rates on such results. If for any reason exchange or price controls or other restrictions on the conversion of foreign currencies were imposed, the Company's business could be adversely affected.

Other potential risks inherent in the Company's international business include longer payment cycles, greater difficulties in accounts receivable collection, unexpected changes in regulatory requirements, export restrictions, tariffs and other trade barriers, difficulties in staffing and managing foreign operations, political instability, reduced protection for intellectual property rights in some countries, seasonal reductions in business activity during the summer months in Europe and certain other parts of the world, economic instability in emerging markets and potentially adverse tax consequences. Any one of these factors could adversely impact the success of the Company's international operations. There can be no assurance that one or more of such factors will not have a material adverse effect on the Company's future international operations, and, consequently, on the Company's business, financial condition and operating results.

**Acquisitions** — As part of its business strategy, the Company has made and expects to continue to make acquisitions of businesses or investments in companies that offer complementary products, services and technologies, such as the acquisitions of DataDirect and Persistence in fiscal 2004. Such acquisitions or investments involve a number of risks, including the risks of assimilating the operations and personnel of acquired companies, realizing the value of the acquired assets relative to the price paid, distraction of management from the Company's ongoing businesses



## [Table of Contents](#)

and potential product disruptions associated with the sale of the acquired company's products. These factors could have a material adverse effect on the Company's business, financial condition and operating results. Consideration paid for any future acquisitions could include company stock. As a result, future acquisitions could cause dilution to existing shareholders and to earnings per share.

**Distribution Channels and New Markets** — Future results also depend upon the Company's continued successful distribution of its products through its AP and OEM channels and may be impacted by downward pressure on pricing, which may not be offset by increases in volume. APs utilize technology from the Company to create their applications and resell the Company's products along with their own applications. OEMs embed the Company's products within their software product or technology device. Any adverse effect on the APs' or OEMs' businesses related to competition, pricing and other factors could also have a material adverse effect on the Company's business, financial condition and operating results.

Sonic Software is currently developing and enhancing the Sonic product set and other new products and services. The market for enterprise application integration, Web services, messaging products and other Internet business-to-business products is highly competitive. Many potential customers have made significant investments in proprietary or internally developed systems and would incur significant costs in switching to the Sonic product set or other third-party products. Global e-commerce and online exchange of information on the Internet and other similar open wide area networks continue to evolve. There can be no assurance that the Company's products will be successful in penetrating these evolving markets.

**Competition** — The Company experiences significant competition from a variety of sources with respect to the marketing and distribution of its products. Many of the Company's competitors have greater financial, marketing or technical resources than the Company and may be able to adapt more quickly to new or emerging technologies and changes in customer requirements or to devote greater resources to the promotion and sale of their products than can the Company. Increased competition could make it more difficult for the Company to maintain its market presence. The marketplace for new products is intensely competitive and characterized by low barriers to entry. As a result, new competitors possessing technological, marketing or other competitive advantages may emerge and rapidly acquire market share.

In addition, current and potential competitors may make strategic acquisitions or establish cooperative relationships among themselves or with third parties, thereby increasing their ability to deliver products that better address the needs of the Company's prospective customers. Current and potential competitors also may be more successful than the Company in having their products or technologies widely accepted. There can be no assurance that the Company will be able to compete successfully against current and future competitors, and its failure to do so could have a material adverse effect upon the Company's business, prospects, financial condition and operating results.

**Hiring and Retention of Skilled Employees** — The Company's future success will depend in large part upon its ability to attract and retain highly skilled technical, managerial and marketing personnel. There is significant competition for such personnel in the software industry. There can be no assurance that the Company will continue to be successful in attracting and retaining the personnel it requires to develop new and enhanced products and to continue to grow and operate profitably.

**Intellectual Property and Proprietary Rights** — The Company's success is heavily dependent upon its proprietary software technology. The Company relies principally on a combination of contract provisions and copyright, trademark, patent and trade secret laws to protect its proprietary technology. Despite the Company's efforts to protect its proprietary rights, unauthorized parties may attempt to copy aspects of the Company's products or to obtain and use information that the Company regards as proprietary. Policing unauthorized use of the Company's products is difficult. There can be no assurance that the steps taken by the Company to protect its proprietary rights will be adequate to prevent misappropriation of its technology or independent development by others of similar technology.

In addition, litigation may be necessary in the future to enforce the Company's intellectual property rights, to protect the Company's trade secrets, to determine the validity and scope of the proprietary rights of others, or to defend against claims of infringement. Although the Company believes that its products and technology do not infringe on any existing proprietary rights of others, there can be no assurance that third parties will not assert infringement claims in the future or that any such claims will not be successful. Such litigation could result in substantial costs

## [Table of Contents](#)

and diversion of resources, whether or not the Company ultimately prevails on the merits, and could have a material adverse effect on the Company's business, financial condition and operating results. Such litigation could also result in the Company being prohibited from selling one or more of its products or cause reluctance by potential customers to purchase the Company's products.

**Third-Party Technology** — The Company also utilizes certain technology which it licenses from third parties, including software which is integrated with internally developed software and used in the Company's products to perform key functions. There can be no assurance that functionally similar technology will continue to be available on commercially reasonable terms in the future, or at all.

**Stock Price Volatility** — The market price of the Company's common stock, like that of other technology companies, is highly volatile and is subject to wide fluctuations in response to quarterly variations in operating results, announcements of technological innovations or new products by the Company or its competitors, changes in financial estimates by securities analysts or other events or factors. The Company's stock price may also be affected by broader market trends unrelated to the Company's performance.

### **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

The Company is exposed to a variety of risks, including changes in interest rates affecting the return on its investments and foreign currency fluctuations. The Company has established policies and procedures to manage its exposure to fluctuations in interest rates and foreign currency exchange rates.

Exposure to market rate risk for changes in interest rates relates to the Company's investment portfolio. The Company has not used derivative financial instruments in its investment portfolio. The Company places its investments with high-quality issuers and has policies limiting, among other things, the amount of credit exposure to any one issuer. The Company limits default risk by purchasing only investment-grade securities. The Company's investments have an average remaining maturity of less than two years and are primarily fixed-rate instruments. In addition, the Company has classified all its debt securities as available for sale. This classification reduces the income statement exposure to interest rate risk if such investments are held until their maturity date. Based on a hypothetical 10% adverse movement in interest rates, the potential losses in future earnings, fair value of risk-sensitive instruments, and cash flows are immaterial.

The Company has entered into foreign exchange option and forward contracts to hedge certain transactions of selected foreign currencies (mainly in Europe and Asia Pacific) against fluctuations in exchange rates. The Company has not entered into foreign exchange option and forward contracts for speculative or trading purposes. The Company's accounting policies for these contracts are based on the designation of the contracts as hedging instruments. The criteria the Company uses for designating a contract as a hedge include the contract's effectiveness in risk reduction and matching of derivative instruments to the underlying transactions. Market value increases and decreases on the foreign exchange option and forward contracts are generally recognized in income in the same period as gains and losses on the underlying transactions. The Company operates in certain countries where there are limited forward currency exchange markets and thus the Company has unhedged transaction exposures in these currencies. The Company generally does not hedge the net assets of its international subsidiaries. The notional principal amount of outstanding foreign exchange option contracts at November 30, 2004 was \$89.3 million. Unrealized market value gains on such contracts were immaterial at November 30, 2004. Based on a hypothetical 10% adverse movement in all foreign currency exchange rates, the Company's revenue would be adversely affected by approximately 6% and the Company's net income would be adversely affected by approximately 20% (excluding any offsetting positive impact from the Company's ongoing hedging programs), although the actual effects may differ materially from the hypothetical analysis.

## Table of Contents

The table below details outstanding forward contracts, which mature in ninety days or less, at November 30, 2004 where the notional amount is determined using contract exchange rates:

*(In thousands, except exchange rate data)*

Functional Currency:	Exchange Foreign Currency for U.S. Dollars (Notional Amount)	Exchange U.S. Dollars for Foreign Currency (Notional Amount)	Notional Weighted Average Exchange Rate*
Australian dollar	—	\$ 78	1.28
Brazilian real	\$ 1,940	—	2.78
Euro	—	7,179	0.75
Japanese yen	5,055	—	102.87
South African rand	776	—	5.80
U.K. pound	3,589	—	0.53
	\$ 11,360	\$ 7,257	

\*expressed as local currency unit per U.S. dollar

**Item 8. Financial Statements and Supplementary Data**

**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders of Progress Software Corporation:

We have audited the accompanying consolidated balance sheets of Progress Software Corporation and its subsidiaries as of November 30, 2004 and 2003, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended November 30, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Progress Software Corporation and its subsidiaries as of November 30, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended November 30, 2004, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of November 30, 2004, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 11, 2005 expressed an unqualified opinion on management's assessment of the effectiveness of the Company's internal control over financial reporting and an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ DELOITTE & TOUCHE LLP

Boston, Massachusetts  
February 11, 2005

[Table of Contents](#)**Consolidated Financial Statements****Consolidated Balance Sheets***(In thousands, except share data)*

November 30,	2004	2003
<b>Assets</b>		
Current assets:		
Cash and equivalents	\$ 141,449	\$ 152,117
Short-term investments	49,818	67,014
Accounts receivable (less allowances of \$8,710 in 2004 and \$8,561 in 2003)	63,503	52,065
Other current assets	11,909	11,387
Deferred income taxes	11,576	10,592
Total current assets	278,255	293,175
Property and equipment, net	40,658	35,572
Intangible assets, net	40,233	7,217
Goodwill	67,130	14,313
Deferred income taxes	17,176	14,654
Other assets	3,362	2,839
Total	\$ 446,814	\$ 367,770
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities:		
Current portion, long-term debt	\$ 238	\$ —
Accounts payable	11,953	11,593
Accrued compensation and related taxes	34,907	28,773
Income taxes payable	3,018	5,001
Other accrued liabilities	20,553	17,748
Short-term deferred revenue	101,106	80,039
Total current liabilities	171,775	143,154
Long-term debt, less current portion	2,200	—
Long-term deferred revenue	5,861	2,575
Commitments and contingencies (note 10)		
Shareholders' equity:		
Preferred stock, \$.01 par value; authorized, 1,000,000 shares; issued, none		
Common stock, \$.01 par value, and additional paid-in capital; authorized, 100,000,000 shares; issued and outstanding, 36,421,700 in 2004 and 35,238,895 in 2003	70,085	53,102
Retained earnings, including accumulated other comprehensive loss of \$1,913 in 2004 and \$1,825 in 2003	196,893	168,939
Total shareholders' equity	266,978	222,041
Total	\$ 446,814	\$ 367,770

See notes to consolidated financial statements.

[Table of Contents](#)**Consolidated Statements of Operations***(In thousands, except per share data)*

Year Ended November 30,	2004	2003	2002
<b>Revenue:</b>			
Software licenses	\$ 140,462	\$ 109,666	\$ 93,468
Maintenance and services	222,200	199,394	179,655
Total revenue	362,662	309,060	273,123
<b>Costs and expenses:</b>			
Cost of software licenses	8,973	8,435	10,501
Cost of maintenance and services	52,354	52,599	56,934
Sales and marketing	146,171	125,650	105,068
Product development	60,371	50,054	42,047
General and administrative	38,753	33,080	29,849
Amortization of acquired intangibles	7,076	2,290	500
In-process research and development	2,600	200	—
Total costs and expenses	316,298	272,308	244,899
Income from operations	46,364	36,752	28,224
<b>Other income (expense):</b>			
Interest income	2,805	3,617	4,672
Foreign currency loss	(1,942)	(1,433)	(2,559)
Investment impairment charge	—	—	(1,000)
Other income (expense)	(20)	(259)	73
Total other income, net	843	1,925	1,186
Income before provision for income taxes	47,207	38,677	29,410
Provision for income taxes	15,106	11,603	8,823
Net income	\$ 32,101	\$ 27,074	\$ 20,587
<b>Earnings per share:</b>			
Basic	\$ 0.89	\$ 0.79	\$ 0.58
Diluted	\$ 0.82	\$ 0.72	\$ 0.54
<b>Weighted average shares outstanding:</b>			
Basic	36,031	34,217	35,419
Diluted	39,010	37,554	38,132

See notes to consolidated financial statements.

**Consolidated Statements of Shareholders' Equity***(In thousands)*

Year Ended November 30,	2004	2003	2002
<b>Common stock and additional paid-in capital:</b>			
Balance, beginning of year	\$ 53,102	\$ 27,743	\$ 42,382
Exercise of employee stock options	16,173	23,209	6,411
Issuance of stock under the employee stock purchase plan	4,932	3,496	2,946
Repurchase of common stock	(8,907)	(8,330)	(26,516)
Issuance of stock by subsidiaries	40	56	67
Tax benefit from stock plans	4,745	6,928	2,453
Balance, end of year	70,085	53,102	27,743
<b>Retained earnings:</b>			
Balance, beginning of year	168,939	145,220	142,794
Net income	32,101	27,074	20,587
Other comprehensive income:			
Unrealized losses on investments, net of tax	(418)	(254)	(124)
Unrealized losses on foreign exchange hedging contracts, net of tax	(332)	(261)	—
Translation adjustments, net of tax	662	946	588
Comprehensive income	32,013	27,505	21,051
Repurchase of common stock	(4,059)	(3,786)	(18,625)
Balance, end of year	196,893	168,939	145,220
Total shareholders' equity	\$ 266,978	\$ 222,041	\$ 172,963

See notes to consolidated financial statements.

**Consolidated Statements of Cash Flows***(In thousands)*

Year Ended November 30,	2004	2003	2002
<b>Cash flows from operating activities:</b>			
Net income	\$ 32,101	\$ 27,074	\$ 20,587
<b>Adjustments to reconcile net income to net cash provided by operating activities:</b>			
Depreciation and amortization of property and equipment	9,134	8,389	9,981
Allowances for accounts receivable	922	1,725	2,589
Amortization of capitalized software costs	313	318	828
Amortization of intangible assets	7,076	2,290	500
Deferred income taxes	2,596	(1,905)	51
In-process research and development	2,600	200	—
Investment impairment charge	—	—	1,000
<b>Changes in operating assets and liabilities, net of effects from acquisitions:</b>			
Accounts receivable	(5,516)	5,233	5,193
Other assets	2,105	1,400	968
Accounts payable and accrued expenses	857	2,708	2,410
Income taxes payable	3,837	5,533	835
Deferred revenue	16,163	4,715	(530)
<b>Net cash provided by operating activities</b>	<b>72,188</b>	<b>57,680</b>	<b>44,412</b>
<b>Cash flows from investing activities:</b>			
Purchases of investments available for sale	(50,402)	(36,646)	(30,523)
Sales and maturities of investments available for sale	67,212	29,147	36,808
Purchases of property and equipment	(10,716)	(7,134)	(6,776)
Capitalized software costs	(300)	(400)	—
Acquisitions, net of cash acquired	(99,320)	(24,255)	—
Increase in other noncurrent assets	(88)	(463)	(785)
<b>Net cash used for investing activities</b>	<b>(93,614)</b>	<b>(39,751)</b>	<b>(1,276)</b>
<b>Cash flows from financing activities:</b>			
Proceeds from issuance of common stock	21,145	26,761	9,424
Repurchase of common stock	(12,966)	(12,116)	(45,141)
<b>Net cash provided by (used for) financing activities</b>	<b>8,179</b>	<b>14,645</b>	<b>(35,717)</b>
Effect of exchange rate changes on cash	2,579	2,118	1,669
<b>Net increase (decrease) in cash and equivalents</b>	<b>(10,668)</b>	<b>34,692</b>	<b>9,088</b>
Cash and equivalents, beginning of year	152,117	117,425	108,337
<b>Cash and equivalents, end of year</b>	<b>\$ 141,449</b>	<b>\$ 152,117</b>	<b>\$ 117,425</b>

See notes to consolidated financial statements.



## Notes to Consolidated Financial Statements

### Note 1: Nature of Business and Summary of Significant Accounting Policies

#### The Company

Progress Software Corporation (the Company) is a global supplier of software and services for the development, deployment, integration and management of business applications deployed in a distributed, Web-based or client/server environment. The Company develops, markets and distributes its products to business, industry and governments worldwide. The Company also provides consulting, education and technical support services.

#### Accounting Principles

The consolidated financial statements and accompanying notes have been prepared in conformity with accounting principles generally accepted in the United States of America.

Certain amounts for fiscal 2003 and fiscal 2002 have been reclassified to conform to the fiscal 2004 presentation.

#### Use of Estimates

The preparation of consolidated financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

#### Basis of Consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries. All intercompany balances and transactions have been eliminated.

#### Foreign Currency Translation

For foreign operations with the local currency as the functional currency, assets and liabilities are translated into U.S. dollars at the exchange rate on the balance sheet date. Income and expense items are translated at average rates of exchange prevailing during each period. Translation adjustments are accumulated in other comprehensive income (loss), a component of shareholders' equity.

For foreign operations with the U.S. dollar as the functional currency, monetary assets and liabilities are translated into U.S. dollars at the exchange rate on the balance sheet date. Nonmonetary assets and liabilities are remeasured into U.S. dollars at historical exchange rates. Income and expense items are translated at average rates of exchange prevailing during each period. Translation adjustments are recognized currently as a component of foreign currency gain or loss.

#### Revenue Recognition

Revenue is recognized when earned. Software license revenue is recognized upon shipment of the product or, if delivered electronically, when the customer has the right to access the software, provided that the license fee is fixed and determinable, persuasive evidence of an arrangement exists and collection is probable. The Company does not license its software with a right of return and generally does not license its software with conditions of acceptance. If an arrangement does contain conditions of acceptance, recognition of the revenue is deferred until the acceptance criteria are met or the period of acceptance has passed. The Company generally recognizes revenue for products distributed through application partners and distributors when sold through to the end user.

Software licenses are generally sold with maintenance services and, in some cases, also with consulting services. For the undelivered elements, vendor-specific objective evidence (VSOE) of fair value is determined to be the price charged when the undelivered element is sold separately. VSOE for maintenance sold in connection with a software license is determined based on the amount that will be separately charged for the maintenance renewal period.

## [Table of Contents](#)

VSOE for consulting services is determined by reference to the amount charged for similar engagements when a software license sale is not involved.

Revenue from software licenses sold together with maintenance and/or consulting services is generally recognized upon shipment using the residual method, provided that the above criteria have been met. If VSOE of fair value for the undelivered elements cannot be established, all revenue from the arrangement is deferred until the earlier of the point at which such sufficient VSOE does exist or all elements of the arrangement have been delivered or if the only undelivered element is maintenance, then the entire fee is recognized ratably. If payment of the software license fees is dependent upon the performance of consulting services or the consulting services are essential to the functionality of the licensed software, then both the software license and consulting fees are recognized under the percentage-of-completion method of contract accounting.

Maintenance revenue is recognized ratably over the term of the applicable agreement. Revenue from services, primarily consulting and customer education, is generally recognized as the related services are performed.

### **Warranty Costs**

The Company makes periodic provisions for expected warranty costs. Historically, warranty costs have been insignificant.

### **Allowance for Doubtful Accounts**

The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of customers to make required payments. This allowance is established using estimates that the Company makes based on factors such as the composition of the accounts receivable aging, historical bad debts, changes in payment patterns, changes to customer creditworthiness and current economic trends.

A summary of activity in the allowances against accounts receivable is as follows:

<i>(In thousands)</i>			
Year Ended November 30,	2004	2003	2002
Beginning balance	\$ 8,561	\$ 7,763	\$ 6,333
Charged to costs and expenses	922	1,725	2,589
Write-offs and other	(773)	(927)	(1,159)
Ending balance	\$ 8,710	\$ 8,561	\$ 7,763

### **Cash Equivalents and Short-Term Investments**

Cash equivalents include short-term, highly liquid investments purchased with remaining maturities of three months or less. Short-term investments, which consist primarily of municipal and U.S. government obligations and corporate debt securities purchased with remaining maturities of more than three months, are classified as investments available for sale and stated at fair value. Aggregate unrealized holding gains and losses are included as a component of accumulated other comprehensive income (loss) in shareholders' equity.

### **Supplemental Cash Flow Information**

In fiscal 2004, the Company purchased a building adjacent to its headquarters and assumed an existing mortgage of \$2.4 million as part of the total purchase price of \$4.7 million.

In fiscal years 2004, 2003 and 2002, the Company paid \$7.9 million, \$8.0 million and \$8.1 million in income taxes, respectively.

### **Concentration of Credit Risk**

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash, short-term investments and trade receivables. The Company has cash investment policies which, among other things, limit investments to investment-grade securities. The Company performs ongoing credit evaluations of its customers, and the risk with respect to trade receivables is further mitigated by the diversity, both by geography and by industry, of the customer base.

### **Fair Value of Financial Instruments**

The carrying amount of cash, accounts receivable and accounts payable approximates fair value due to the short-term nature of these instruments. The fair value of investments available for sale is based on current market value (Note 2). The carrying value of long-term debt approximates its fair value due to the short period of time that it was on the Company's balance sheet.

### **Property and Equipment**

Property and equipment are recorded at cost. Property and equipment purchased in business combinations are recorded at fair values which are then treated as the current cost. Depreciation and amortization are provided on the straight-line method over the estimated useful lives of the related assets or the remaining initial or current terms of leases, whichever is shorter. Useful lives by major asset class are as follows: computer equipment and software, three to five years; buildings and improvements, five to thirty-nine years; and furniture and fixtures, five to seven years.

### **Capitalization of Software Costs**

Product development costs, other than certain software-related costs, are expensed as incurred. The Company capitalizes certain internally generated software development costs after technological feasibility of the product has been established. Such costs are amortized over the estimated life of the product (generally four years) in an amount equal to the greater of the amount computed using the ratio of current revenue to total expected revenue in the product's life or the amount computed using the straight-line method. The Company periodically compares the unamortized costs of capitalized software to the expected future revenues for the products. If the unamortized costs exceed the expected future net realizable value, the excess amount is written off. Capitalized software costs, included in other assets, totaled \$0.6 million (net of accumulated amortization of \$13.2 million and \$12.9 million, respectively) at November 30, 2004 and 2003.

### **Goodwill, Other Intangible Assets and Long-lived Assets**

Goodwill is the amount by which the cost of acquired net assets in a business acquisition exceeded the fair value of net identifiable assets on the date of purchase. For purposes of the annual impairment test, goodwill of \$65.0 million has been assigned to the Application Development and Deployment operating segment and \$2.1 million has been assigned to the Enterprise Application Integration operating segment.

Under Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets," the Company evaluates goodwill or other intangible assets with indefinite useful lives for impairment annually. To conduct these impairment tests of goodwill and indefinite-lived intangible assets, the fair value of the reporting unit is compared to its carrying value. If the reporting unit's carrying value exceeds its fair value, the Company records an impairment loss to the extent that the carrying value of goodwill exceeds its implied fair value. The Company estimates the fair values of its reporting units using discounted cash flow valuation models and third-party valuation reports.

Long-lived assets primarily include property and equipment and intangible assets with finite lives (purchased software, capitalized software and customer-related intangibles). In accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," the Company periodically reviews long-lived assets for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable or that the useful lives of those assets are no longer appropriate. Each impairment test

## [Table of Contents](#)

is based on a comparison of the undiscounted cash flows to the recorded value of the asset. If impairment is indicated, the asset is written down to its estimated fair value based on a discounted cash flow analysis.

### Investment in Related Party

The Company holds a minority interest in EasyAsk, Inc., a privately-held software company whose chairman is a member of the Board of Directors of the Company. The Company regularly monitors the carrying value of its investment in EasyAsk. The investment was carried at \$0.3 million at November 30, 2004 and is included in other assets. During fiscal 2002, the Company recorded an impairment charge of \$1.0 million related to this investment.

### Stock-Based Compensation Plans

At November 30, 2004, the Company has three stock-based employee compensation plans, which are described more fully in Note 7. The Company accounts for those plans under the recognition and measurement principles of APB Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25), and related interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation" (SFAS 123), to stock-based employee compensation.

*(In thousands, except per share data)*

Year Ended November 30,	2004	2003	2002
Net income, as reported	\$ 32,101	\$ 27,074	\$ 20,587
Less: stock based compensation expense determined under fair value method for all awards, net of tax	(9,351)	(8,294)	(7,565)
Pro forma net income	\$ 22,750	\$ 18,780	\$ 13,022
Earnings per share:			
Basic, as reported	\$ 0.89	\$ 0.79	\$ 0.58
Basic, pro forma	\$ 0.63	\$ 0.55	\$ 0.37
Diluted, as reported	\$ 0.82	\$ 0.72	\$ 0.54
Diluted, pro forma	\$ 0.58	\$ 0.50	\$ 0.34

The fair value of options and Employee Stock Purchase Plan (ESPP) shares granted in fiscal years 2004, 2003 and 2002 has been estimated at the date of grant using the Black-Scholes option valuation model with the following weighted average assumptions:

Year Ended November 30,	2004	2003	2002
Stock Purchase Plan:			
Expected volatility	35.0%	33.0%	51.8%
Risk-free interest rate	1.7%	1.5%	5.1%
Expected life in years	1.7	0.9	1.6
Expected dividend yield	None	None	None
Stock Options:			
Expected volatility	43.7%	45.7%	48.6%
Risk-free interest rate	3.6%	3.5%	3.8%
Expected life in years	6.4	6.5	6.5
Expected dividend yield	None	None	None

Based on the above assumptions, the weighted average estimated fair value of options granted in fiscal years 2004, 2003 and 2002 was \$9.31, \$9.28 and \$7.51 per share, respectively. The weighted average estimated fair value for shares issued under the ESPP in fiscal years 2004, 2003 and 2002 was \$5.22, \$4.18 and \$6.68 per share,

## [Table of Contents](#)

respectively. For purposes of the pro forma disclosure above, the estimated fair value of options is amortized to expense over the vesting period.

### **Income Taxes**

The Company provides for deferred income taxes resulting from temporary differences between financial and taxable income. Such differences arise primarily from depreciation, accruals, deferred revenue, capitalized software costs, tax loss carryforwards and allowances for accounts receivable. The Company records valuation allowances to reduce deferred tax assets to the amount that is more likely than not to be realized. No provision for U.S. income taxes has been made for the undistributed earnings of non-U.S. subsidiaries, as these earnings have been permanently reinvested or would be principally offset by foreign tax credits. Cumulative undistributed foreign earnings were approximately \$30.6 million at November 30, 2004.

### **Comprehensive Income**

The components of comprehensive income include unrealized gains and losses on investments, unrealized gains and losses on foreign exchange hedging contracts and foreign currency translation adjustments. Accumulated foreign currency translation losses (net of taxes of approximately \$0.6 million and \$0.9 million at November 30, 2004 and 2003, respectively) were approximately \$1.2 million and \$1.9 million at November 30, 2004 and 2003, respectively. Accumulated unrealized foreign exchange hedging contracts losses (net of taxes of approximately \$0.3 million and \$0.1 million at November 30, 2004 and 2003, respectively) were approximately \$0.6 million and \$0.3 million at November 30, 2004 and 2003, respectively. Accumulated unrealized gains (losses) on short-term investments (net of taxes of approximately (\$0.1) million and \$0.1 million at November 30, 2004 and 2003, respectively) were approximately (\$0.1) million and \$0.3 million at November 30, 2004 and 2003, respectively.

### **New Accounting Pronouncements**

In December 2004, the Financial Accounting Standards Board issued SFAS No. 123R, "Share-Based Payment" (SFAS 123R). This Statement is a revision of SFAS 123 and supersedes APB 25 and its related implementation guidance. SFAS 123R requires a company to measure the grant-date fair value of equity awards given to employees in exchange for services and recognize that cost over the period that such services are performed. SFAS 123R is effective for the first interim or annual reporting period that begins after June 15, 2005.

The Company is currently evaluating the two methods of adoption allowed by SFAS 123R: the modified-prospective transition method and the modified-retrospective transition method. Adoption of SFAS 123R will materially increase stock compensation expense and decrease net income. In addition, SFAS 123R requires that the excess tax benefits related to stock compensation be reported as a cash inflow from financing activities rather than as a reduction of taxes paid in cash from operations.

### **Note 2: Cash and Short-Term Investments**

A summary of the Company's investments available for sale by major security type (including \$84.1 million classified as cash equivalents) at November 30, 2004 was as follows:

*(In thousands)*

Security Type	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Corporate debt securities	\$ 75,798	\$ —	\$ —	\$ 75,798
State and municipal obligations	58,192	28	(175)	58,045
Total	\$ 133,990	\$ 28	\$ 175	\$ 133,843

## [Table of Contents](#)

The fair value of debt securities at November 30, 2004, by contractual maturity, was as follows:

(In thousands)

Due in one year or less	\$ 113,761
Due after one year	20,082
Total	\$ 133,843

A summary of the Company's investments available for sale by major security type (including \$89.9 million classified as cash equivalents) at November 30, 2003 was as follows:

(In thousands)

Security Type	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Corporate debt securities	\$ 92,201	—	—	\$ 92,201
State and municipal obligations	56,134	\$ 400	\$ (52)	56,482
U.S. government obligations	8,122	149	—	8,271
Total	\$ 156,457	\$ 549	\$ (52)	\$ 156,954

In fiscal 2004, realized losses from the sale of available-for-sale securities totaled \$0.1 million. The cost basis used to determine the realized losses was the amortized cost on the date of sale. Such amounts in all other years were insignificant. Unrealized gains and losses that were reclassified from accumulated other comprehensive income to income were insignificant for all years presented.

### **Note 3: Derivative Instruments**

All derivatives, whether designated in hedging relationships or not, are recorded on the balance sheet at fair value. If the derivative is designated as a cash flow hedge, the effective portions of changes in the fair value of the derivative are recorded in other comprehensive income and are recognized in the income statement when the hedged item affects earnings. Ineffective portions of changes in the fair value of cash flow hedges are recognized immediately in earnings.

The Company uses derivative instruments to manage exposures to fluctuations in the value of foreign currencies. Certain forecasted transactions and assets are exposed to foreign currency risk. The Company's objective for holding derivatives is to eliminate or reduce the impact of these exposures. The Company periodically monitors its foreign currency exposures to enhance the overall effectiveness of its foreign currency hedge positions. Principal currencies hedged include the euro, British pound, and Australian dollar. Options used to hedge a portion of forecasted international intercompany revenue for up to one year in the future are designated as cash flow hedging instruments. Forward contracts not designated as hedging instruments under SFAS 133 are also used to hedge the impact of the variability in exchange rates on accounts receivable and collections denominated in certain foreign currencies. The notional principal amount of outstanding foreign exchange option contracts at November 30, 2004 was \$89.3 million. Unrealized market value gains on such contracts were immaterial at November 30, 2004 and 2003. Major U.S. multinational banks are counterparties to the option contracts.

For options designated as cash flow hedges, changes in the time value are excluded from the assessment of hedge effectiveness. In fiscal years 2004, 2003 and 2002, foreign currency loss included a net loss of \$1.0 million, \$0.8 million and \$0.9 million, respectively, for changes in the time value of options designated as cash flow hedges.

## Table of Contents

The table below details outstanding forward contracts, which mature in ninety days or less, at November 30, 2004 where the notional amount is determined using contract exchange rates:

(In thousands)

Functional Currency:	Exchange Foreign Currency For U.S. Dollars (Notional Amount)	Exchange U.S. Dollars For Foreign Currency (Notional Amount)	Notional Weighted Average Exchange Rate*
Australian dollar	—	\$ 78	1.28
Brazilian real	\$ 1,940	—	2.78
Euro	—	7,179	0.75
Japanese yen	5,055	—	102.87
South African rand	776	—	5.80
U.K. pound	3,589	—	0.53
	\$ 11,360	\$ 7,257	

\* expressed as local currency unit per U.S. dollar

The table below details outstanding forward contracts, which mature in ninety days or less, at November 30, 2003 where the notional amount is determined using contract exchange rates:

(In thousands)

Functional Currency:	Exchange Foreign Currency For U.S. Dollars (Notional Amount)	Exchange U.S. Dollars For Foreign Currency (Notional Amount)	Notional Weighted Average Exchange Rate*
Australian dollar	\$ 1,291	—	1.39
Brazilian real	432	—	3.01
Euro	—	\$ 7,800	0.85
Japanese yen	5,482	—	109.45
South African rand	848	—	6.61
U.K. pound	4,092	—	0.59
	\$ 12,145	\$ 7,800	

\* expressed as local currency unit per U.S. dollar

### Note 4: Property and Equipment

Property and equipment consisted of the following:

(In thousands)

November 30,	2004	2003
Computer equipment and software	\$ 83,195	\$ 75,121
Land, building and leasehold improvements	38,715	32,380
Furniture and fixtures	11,180	9,438
Total	133,090	116,939
Less accumulated depreciation and amortization	92,432	81,367
Property and equipment, net	\$ 40,658	\$ 35,572

**Note 5: Intangible Assets and Goodwill**

Intangible assets were composed of the following significant classes at November 30, 2004:

(In thousands)

	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Purchased technology	\$ 30,183	\$ 6,268	\$ 23,915
Customer-related and other	20,477	4,159	16,318
Total	\$ 50,660	\$ 10,427	\$ 40,233

Intangible assets were composed of the following significant classes at November 30, 2003:

(In thousands)

	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Purchased technology	\$ 5,310	\$ 2,218	\$ 3,092
Customer-related and other	5,307	1,182	4,125
Total	\$ 10,617	\$ 3,400	\$ 7,217

Intangible assets are being amortized with no expected residual value. The weighted average amortization period for all intangible assets was 6.4 years, including 6.5 years for purchased technology and 6.3 years for customer-related and other intangible assets. Amortization expense related to these intangible assets was \$7.1 million, \$2.3 million and \$0.5 million in fiscal years 2004, 2003 and 2002, respectively. Amortization expense is estimated to be approximately \$7.9 million, \$7.4 million, \$7.4 million, \$6.5 million and \$5.0 million in fiscal years 2005, 2006, 2007, 2008 and 2009, respectively.

During fiscal 2004, \$55.2 million was added to goodwill as a result of the acquisitions of DataDirect Technologies and Persistence Software. In addition, the Company adjusted the allocation of the purchase price related to its December 2002 acquisition of eXcelon by reducing goodwill by \$2.7 million to reflect an additional tax benefit not contemplated in the original allocation. During fiscal 2003, \$9.4 million was added to goodwill as a result of the acquisition of eXcelon. In addition, the carrying amount of goodwill in fiscal years 2004 and 2003 changed due to foreign currency translation adjustments related to those asset balances that are recorded in non-U.S. currencies. No goodwill was acquired in fiscal 2002. During fiscal years 2004, 2003 and 2002, no goodwill was impaired or written-off.



**Note 6: Earnings Per Share**

Basic earnings per share is computed using the weighted average number of common shares outstanding. Diluted earnings per share is computed using the weighted average number of common shares outstanding plus the effect of outstanding stock options using the treasury stock method. The following table sets forth the calculation of basic and diluted earnings per share for each fiscal year:

<i>(In thousands, except per share data)</i>			
Year Ended November 30,	2004	2003	2002
Net income	\$ 32,101	\$ 27,074	\$ 20,587
Weighted average shares outstanding	36,031	34,217	35,419
Dilutive impact from outstanding stock options	2,979	3,337	2,713
Diluted weighted average shares outstanding	39,010	37,554	38,132
Basic earnings per share	\$ 0.89	\$ 0.79	\$ 0.58
Diluted earnings per share	\$ 0.82	\$ 0.72	\$ 0.54

Stock options to purchase approximately 1,100,000 shares, 383,000 shares and 2,460,000 shares had exercise prices per share in excess of the average market price for the Company's common stock and were excluded from the calculation of diluted earnings per share in fiscal years 2004, 2003 and 2002, respectively, because these options were anti-dilutive. However, these options could be dilutive in the future.

**Note 7: Shareholders' Equity****Preferred Stock**

The Board of Directors is authorized to establish one or more series of preferred stock and to fix and determine the number and conditions of preferred shares, including dividend rates, redemption and/or conversion provisions, if any, preferences and voting rights. At November 30, 2004, the Board of Directors had not established any series of preferred stock.

**Common Stock**

A summary of share activity is as follows:

<i>(In thousands)</i>			
Year Ended November 30,	2004	2003	2002
Beginning balance	35,239	33,401	35,621
Shares issued	1,830	2,524	1,167
Shares repurchased	(647)	(686)	(3,387)
Ending balance	36,422	35,239	33,401

**Common Stock Repurchases**

In fiscal years 2004, 2003 and 2002, the Company purchased and retired 646,618 shares, 686,237 shares and 3,386,676 shares, respectively, of its common stock for \$13.0 million, \$12.1 million and \$45.1 million, respectively. Since beginning its stock repurchase program in 1996, the Company has purchased and retired 18,258,379 shares at a cost of \$190.8 million.

In September 2004, the Board of Directors authorized, for the period from October 1, 2004 through September 30, 2005, the purchase of up to 10,000,000 shares of the Company's common stock, at such times when the Company deems such purchases to be an effective use of cash. Shares that are repurchased may be used for various purposes, including the issuance of shares pursuant to the Company's stock option and stock purchase plans. At November 30, 2004, substantially all such shares of common stock remained available for repurchase under this authorization.

**Stock Options**

The Company has three shareholder-approved stock option plans: the 1992 Incentive and Nonqualified Stock Option Plan (1992 Plan), the 1994 Stock Incentive Plan (1994 Plan) and the 1997 Stock Incentive Plan (1997 Plan). These plans permit the granting of stock awards to officers, members of the Board of Directors, employees and consultants. Awards under the 1992, 1994 and 1997 Plans may include stock options (both incentive and nonqualified), grants of conditioned stock, unrestricted grants of stock, grants of stock contingent upon the attainment of performance goals and stock appreciation rights. No awards other than incentive and nonqualified stock options have been granted under the foregoing plans. The options generally vest over five years and have terms of ten years. A total of 19,540,000 shares are issuable under these plans, of which 743,000 shares were available for grant at November 30, 2004.

In 2002, the Board of Directors approved and adopted the 2002 Nonqualified Stock Plan (2002 Plan), for which the approval of shareholders was not required. Executive officers and members of the Board of Directors are not eligible for awards under the 2002 Plan. Awards under the 2002 Plan may include nonqualified stock options, grants of conditioned stock, unrestricted grants of stock, grants of stock contingent upon the attainment of performance goals and stock appreciation rights. No awards other than nonqualified stock options have been granted under the 2002 Plan. The options generally vest over five years and have terms of ten years. A total of 6,500,000 shares are issuable under the 2002 Plan, of which 943,000 shares were available for grant at November 30, 2004.

In 2004, the Board of Directors approved and adopted the 2004 Inducement Stock Plan (2004 Plan), for which approval of shareholders was not required. The Company intends that the 2004 Plan be reserved for persons to whom the Company may issue securities without shareholder approval as an inducement to become employed by the Company pursuant to the rules and regulations of the Nasdaq Stock Market. Awards under the 2004 Plan may include nonqualified stock options, grants of conditioned stock, unrestricted grants of stock, grants of stock contingent upon the attainment of performance goals and stock appreciation rights. No awards other than nonqualified stock options have been granted under the 2004 Plan. The options generally vest over five years and have terms of ten years. A total of 200,000 shares are issuable under the 2004 Plan, of which 75,000 shares were available for grant at November 30, 2004.

A summary of stock option activity under all plans is as follows:

*(In thousands, except per share data)*

	Number Of Shares	Weighted Average Exercise Price Per Share
Options outstanding, December 1, 2001	10,030	\$ 10.88
Granted	3,050	13.30
Exercised	(906)	7.07
Canceled	(625)	13.48
Options outstanding, November 30, 2002	11,549	11.67
Granted	3,129	18.42
Exercised	(2,201)	10.55
Canceled	(657)	13.49
Options outstanding, November 30, 2003	11,820	13.57
Granted	2,466	18.91
Exercised	(1,410)	11.47
Canceled	(430)	16.28
Options outstanding, November 30, 2004	12,446	\$ 14.77

## [Table of Contents](#)

For various exercise price ranges, characteristics of outstanding and exercisable stock options at November 30, 2004 were as follows:

(Number of shares in thousands)

Range of Exercise Price:	Options Outstanding			Options Exercisable	
	Number of Shares	Weighted Average Remaining Life (in years)	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
\$4.50- 7.23	1,265	2.18	\$ 5.98	1,263	\$ 5.98
9.00-12.94	2,485	5.24	12.05	2,146	11.96
13.00-16.87	4,347	7.63	13.77	2,122	13.60
18.15-21.86	4,349	8.88	19.88	1,420	20.01
<b>\$4.50-21.86</b>	<b>12,446</b>	<b>7.03</b>	<b>\$ 14.77</b>	<b>6,951</b>	<b>\$ 13.02</b>

At the end of fiscal years 2003 and 2002, the Company had 6,035,000 shares and 6,109,000 shares subject to exercisable options, respectively, with weighted average exercise prices of \$11.65 and \$10.28 per share, respectively.

### **Employee Stock Purchase Plan**

The 1991 Employee Stock Purchase Plan (ESPP), as amended in April 2004, April 2001 and April 1998, permits eligible employees to purchase up to a maximum of 3,200,000 shares of common stock of the Company at 85% of the lesser of the market value of such shares at the beginning of a 27-month offering period or the end of each three-month segment within such offering period. During fiscal years 2004, 2003 and 2002, 418,940 shares, 323,046 shares and 260,942 shares, respectively, were issued with weighted average purchase prices of \$11.77, \$10.82 and \$11.29 per share, respectively, under the ESPP. At November 30, 2004, approximately 870,000 shares were available and reserved for issuance under the ESPP.

### **Subsidiary Option Plans**

Sonic Software Corporation and PeerDirect Corporation, wholly-owned subsidiaries of the Company, have separate stock option plans for their employees. Options under these plans are granted at fair value based on valuation reports from an independent appraiser. The options vest over four years and have terms of ten years. These options are exercisable for stock of the respective subsidiary, and are not exercisable for or convertible into the Company's shares. The total number of common shares that may be granted under each of these stock option plans represents approximately 20% of the fully-diluted shares of each subsidiary. For PeerDirect Corporation, no options under the plan have been exercised as of November 30, 2004. For Sonic Software Corporation, options representing less than 1% of the outstanding shares of Sonic Software Corporation have been exercised at a total cost of approximately \$0.2 million at November 30, 2004. The exercise of stock options by employees results in the creation of minority interest in the subsidiaries. Such amounts were immaterial at November 30, 2004.

### **Note 8: Retirement Plan**

The Company maintains a retirement plan covering all U.S. employees under Section 401(k) of the Internal Revenue Code. Company contributions to the plan are at the discretion of the Board of Directors and totaled approximately \$4.2 million, \$3.5 million and \$2.8 million for fiscal years 2004, 2003 and 2002, respectively.

[Table of Contents](#)**Note 9: Income Taxes**

The components of pretax income were as follows:

(In thousands)

Year Ended November 30,	2004	2003	2002
United States	\$ 37,286	\$ 31,962	\$ 25,754
Non-U.S.	9,921	6,715	3,656
Total	\$ 47,207	\$ 38,677	\$ 29,410

The provisions for income taxes were comprised of the following:

(In thousands)

Year Ended November 30,	2004	2003	2002
Current:			
Federal	\$ 6,512	\$ 8,240	\$ 5,860
State	1,589	1,796	923
Foreign	4,409	3,472	1,989
Total current	12,510	13,508	8,772
Deferred:			
Federal	2,310	(1,367)	56
State	994	(271)	12
Foreign	(708)	(267)	(17)
Total deferred	2,596	(1,905)	51
Total	\$ 15,106	\$ 11,603	\$ 8,823

The tax effects of significant items comprising the Company's deferred taxes were as follows:

(In thousands)

November 30,	2004	2003
Deferred tax liabilities:		
Goodwill	\$ (1,488)	\$ (197)
Depreciation and amortization	(187)	—
Total deferred tax liabilities	(1,675)	(197)
Deferred tax assets:		
Accounts receivable	2,586	3,112
Depreciation and amortization	—	168
Capitalized research costs	4,584	4,801
Other current assets	488	673
Accrued compensation	1,478	739
Deferred revenue	1,877	972
Tax loss carryforwards	14,810	10,132
Accrued liabilities and other	5,468	5,682
Total deferred tax assets	31,291	26,279
Valuation allowance	(864)	(836)
Total	\$ 28,752	\$ 25,246

The valuation allowance primarily applies to net operating loss carryforwards in certain foreign jurisdictions where realization is not assured. The change in the valuation allowance of \$(0.3) million and \$0.3 million in fiscal years 2003 and 2002, respectively, primarily related to the utilization or creation of tax loss carryforwards.

## Table of Contents

At November 30, 2004, the Company has net operating loss carryforwards of \$34.1 million expiring on various dates through 2024 and \$5.5 million that may be carried forward indefinitely. The increase in net operating loss carryforwards in fiscal 2004 was primarily due to amounts acquired as part of the acquisition of Persistence.

A reconciliation of the U.S. federal statutory rate to the effective tax rate was as follows:

Year Ended November 30,	2004	2003	2002
Tax at U.S. federal statutory rate	35.0%	35.0%	35.0%
Foreign rate differences	0.9	1.5	2.7
Extraterritorial income exclusion	(4.8)	(5.1)	(5.6)
State income taxes, net	2.8	2.6	2.1
Research credits	(2.2)	(2.5)	(1.2)
Tax-exempt interest	(1.3)	(1.8)	(3.4)
Change in estimated state tax rates	1.1	—	—
Other	0.5	0.3	0.4
Total	32.0%	30.0%	30.0%

The IRS is currently examining the Company's United States income tax returns for fiscal years through 2002. The Company has provided reserves for certain tax matters, both domestic and foreign, which it believes could result in additional tax being due. Any additional assessment or reduction of these contingent liabilities will be reflected in the Company's effective tax rate in the period when the audit is completed.

### **Note 10: Long-term Debt, Commitments and Contingencies**

#### **Long-term Debt**

In connection with the purchase of a building adjacent to the Company's headquarters building, the Company was required to assume the existing mortgage under the terms of the agreement. The mortgage had a remaining principal balance of \$2.4 million with a fixed annual interest rate of 8.05% and is secured by the building. The Company, at its option, may repay the entire outstanding balance beginning in July 2006, subject to a potential penalty based on interest rates in effect at that time. The final payment is due in June 2012. Future principal and interest payments are as follows:

<i>(In thousands)</i>	Principal	Interest
2005	\$ 238	\$ 188
2006	260	168
2007	281	146
2008	305	122
2009	330	97
Thereafter	1,024	117
Total	\$ 2,438	\$ 838

## [Table of Contents](#)

### Leasing Arrangements

The Company leases certain facilities and equipment under noncancelable operating lease arrangements. Future minimum rental payments under these leases are as follows at November 30, 2004:

*(In thousands)*

2005	\$ 10,508
2006	5,647
2007	3,206
2008	1,490
2009	684
Thereafter	459
Total	\$ 21,994

Total rent expense under operating lease arrangements was approximately \$9.5 million, \$8.0 million and \$7.2 million in fiscal years 2004, 2003 and 2002, respectively.

### Guarantees and Indemnification Obligations

The Company includes standard intellectual property indemnification provisions in its licensing agreements in the ordinary course of business. Pursuant to the Company's product license agreements, the Company will indemnify, hold harmless, and agree to reimburse the indemnified party for losses suffered or incurred by the indemnified party, generally business partners or customers, in connection with certain patent, copyright or other intellectual property infringement claims by third parties with respect to the Company's products. Other agreements with the Company's customers provide indemnification for claims relating to property damage or personal injury resulting from the performance of services by the Company or its subcontractors. Historically, the Company's costs to defend lawsuits or settle claims relating to such indemnity agreements have been insignificant. Accordingly, the estimated fair value of these indemnification provisions is immaterial.

### Litigation

The Company is subject to various legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. While the outcome of these claims cannot be predicted with certainty, management does not believe that the outcome of any of these legal matters will have a material adverse effect on the Company's consolidated financial position or results of operations.

### Note 11: Business Segments and International Operations

During fiscal 2004, the Company conducted business through four principal operating units and a supporting research and business development unit. The first operating unit conducted business as the Progress OpenEdge Division (OED) and provided the OpenEdge platform, a set of development and deployment technologies, which includes the OpenEdge RDBMS, for building business applications. The second operating unit, Sonic Software Corporation, provided a set of standards-based integration products and services. The third operating unit, ObjectStore, acquired as part of the acquisition of eXcelon Corporation in December 2002, provided advanced data management software for developing real-time applications. The fourth operating unit, DataDirect Technologies (DataDirect), was acquired in December 2003. DataDirect provided standards-based data connectivity software. PeerDirect, which provides technology for managing distributed applications and synchronizing databases, was combined with ObjectStore in the fourth quarter of fiscal 2004. PSC Labs had responsibility for research and new business development activities.

Segment information is presented in accordance with SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information." This standard is based on a management approach, which requires segmentation based upon the Company's internal organization and disclosure of revenue and operating income based upon internal accounting methods.

Based upon the aggregation criteria for segment reporting, the Company has two reportable segments: Application Development & Deployment, which primarily includes OED, ObjectStore, DataDirect Technologies, PeerDirect and

## Table of Contents

PSC Labs, and Enterprise Application Integration, which includes Sonic Software and certain Sonic-related international sales and marketing functions within OED. The Company has aggregated its segment data based on similar utilization characteristics, such as deployment and integration, of the primary products in each operating unit. The Company does not internally report its assets, capital expenditures, interest income or provision for income taxes by segment.

The following table sets forth the Company's revenue and income from operations from the Company's reportable segments for fiscal years 2004, 2003 and 2002:

*(In thousands)*

	Application Development & Deployment	Enterprise Application Integration	Eliminations	Total
<b>Fiscal 2004:</b>				
Revenue	\$ 343,076	\$ 22,680	\$ (3,094)	\$ 362,662
Income (loss) from operations	\$ 74,242	\$ (24,784)	\$ (3,094)	\$ 46,364
<b>Fiscal 2003:</b>				
Revenue	\$ 293,294	\$ 19,440	\$ (3,674)	\$ 309,060
Income (loss) from operations	\$ 64,072	\$ (23,646)	\$ (3,674)	\$ 36,752
<b>Fiscal 2002:</b>				
Revenue	\$ 263,837	\$ 11,457	\$ (2,171)	\$ 273,123
Income (loss) from operations	\$ 47,843	\$ (17,448)	\$ (2,171)	\$ 28,224

Amounts included under Eliminations represent intersegment sales, which are accounted for as if sold under an equivalent arms-length basis arrangement.

Total revenue by significant product line, regardless of which segment generated the revenue, is as follows:

*(In thousands)*

Year Ended November 30,	2004	2003	2002
DataDirect	\$ 28,243	\$ —	\$ —
ObjectStore	17,889	13,543	—
Sonic	26,211	22,980	14,966
Progress OpenEdge and other	290,319	272,537	258,157
Total	\$ 362,662	\$ 309,060	\$ 273,123

The Company's revenues are derived from licensing its products, and from related services, which consist of maintenance and consulting and education. Information relating to product and service revenue from external customers is as follows:

*(In thousands)*

Year Ended November 30,	2004	2003	2002
Licenses	\$ 140,462	\$ 109,666	\$ 93,468
Maintenance	189,072	160,626	134,827
Consulting and education	33,128	38,768	44,828
Total	\$ 362,662	\$ 309,060	\$ 273,123

## Table of Contents

Revenue attributed to North America includes shipments to customers in the United States and Canada and licensing to certain multinational organizations. Revenue from Europe, Middle East and Africa (EMEA), Latin America and Asia Pacific includes shipments to customers in each region, not including certain multinational organizations, plus export shipments into each region that are billed from the United States. Information relating to revenue from external customers from different geographical areas is as follows:

(In thousands)

Year Ended November 30,	2004	2003	2002
North America	\$ 153,730	\$ 122,046	\$ 109,821
EMEA	170,870	153,345	130,368
Latin America	16,574	14,716	17,386
Asia Pacific	21,488	18,953	15,548
Total	\$ 362,662	\$ 309,060	\$ 273,123

Revenue from the United Kingdom totaled \$51.6 million, \$45.9 million and \$37.8 million for fiscal years 2004, 2003 and 2002, respectively. No other country outside of the United States exceeded 10% of the Company's consolidated total revenue in any year presented. Long-lived assets totaled \$37.9 million, \$32.5 million and \$31.3 million in the United States and \$5.3 million, \$5.4 million and \$5.0 million outside of the United States at the end of fiscal years 2004, 2003 and 2002, respectively. No individual country outside of the United States exceeded 10% of the Company's consolidated long-lived assets.

### **Note 12: Business Combinations**

On November 5, 2004, the Company completed its acquisition of Persistence Software, Inc. (Persistence), a provider of data caching software. The acquisition was accounted for as a purchase, and accordingly, the results of operations of Persistence are included in the Company's operating results from the date of acquisition. The purpose of the acquisition was to expand the product set of the ObjectStore operating unit. The acquisition was structured as a merger of a wholly owned subsidiary of the Company with and into Persistence. Pursuant to the terms of the acquisition, each outstanding share of Persistence common stock was converted into the right to receive \$5.70 in cash, without interest. In addition, as a result of the acquisition, holders of exercisable options and warrants to purchase Persistence common stock with an exercise price of less than \$5.70 per share were entitled to receive a cash payment equal to the number of shares of Persistence common stock subject to such option or warrant multiplied by the amount by which \$5.70 exceeded the exercise price per share of such option or warrant. The aggregate purchase price, net of cash acquired, of approximately \$11.8 million included \$0.3 million for direct transaction costs. The preliminary allocation of the purchase price was as follows:

(In thousands)

	Total	Life (in years)
Assets and liabilities, including cash	\$ 1,913	
Deferred income taxes	3,531	
Acquired intangible assets	4,207	1 to 6 years
Goodwill (not deductible for tax purposes)	6,357	
Total purchase price	16,008	
Less: cash acquired	(4,208)	
Net cash paid	\$ 11,800	

On December 23, 2003, the Company, through a wholly owned subsidiary, acquired substantially all of the assets and certain subsidiaries and assumed certain liabilities of DataDirect Technologies Limited (DataDirect), a private company incorporated under the laws of Ireland, for an aggregate purchase price of approximately \$87.5 million, net of cash acquired and subject to certain post-closing adjustments. The aggregate purchase price included \$0.7 million of direct transaction costs. The purpose of the acquisition was to expand the product sets and size of the Company. DataDirect is a provider of standards-based software for data connectivity. The acquisition was accounted for as a purchase, and accordingly, the results of operations of DataDirect are included in the Company's operating results from the date of acquisition. The purchase price was paid in cash from available funds.



## [Table of Contents](#)

Acquired in-process research and development (IPR&D) of \$2.6 million was expensed when the acquisition was consummated because the technological feasibility of several products under development at the time of the acquisition had not been achieved and no alternate future uses had been established. Research and development costs to bring the acquired products to technological feasibility are not expected to have a material impact on the Company's future results of operations or cash flows. At the date of the acquisition, the Company anticipated the completed product being released in the first half of fiscal 2005. The Company used an independent appraiser to calculate the amounts allocated to assets and liabilities acquired, including intangible assets and IPR&D. The allocation of the purchase price was as follows:

*(In thousands)*

	Total	Life (in years)
Assets and liabilities, including cash	\$ 6,045	
Acquired intangible assets	35,870	1 to 10 years
Goodwill (deductible for tax purposes)	48,817	
In-process research and development	2,600	
Total purchase price	93,332	
Less: cash acquired	(5,812)	
Net cash paid	\$ 87,520	

The following table sets forth supplemental unaudited pro forma financial information that assumes the acquisitions of Persistence and DataDirect were completed at the beginning of the fiscal 2003. The information for the twelve months ended November 30, 2004 includes the historical results of the Company for fiscal 2004 and the historical results of Persistence for the twelve-month period ended September 30, 2004, due to different fiscal period ends. The information for the twelve months ended November 30, 2003 includes the historical results of the Company for fiscal 2003 and the historical results of Persistence for the twelve-month period ended September 30, 2003, and the historical results of DataDirect for the twelve months ended October 31, 2003, due to different fiscal periods.

The unaudited pro forma results include estimates and assumptions regarding increased amortization of intangible assets related to the acquisition, a reduction in interest expense related to bank loans of DataDirect and decreased interest income related to cash paid for purchase price of the acquisitions, which the Company believes are reasonable. However, pro forma results are not necessarily indicative of the results that would have occurred if the acquisitions had occurred on the date indicated, or that may result in the future.

*(In thousands, except per share data, unaudited)*

Year Ended November 30,	2004	2003
Pro forma revenue	\$ 371,631	\$ 363,035
Pro forma net income	\$ 31,680	\$ 25,533
Pro forma diluted earnings per share	\$ 0.81	\$ 0.68

On December 19, 2002, the Company completed its acquisition of eXcelon Corporation (eXcelon), a provider of data management software. The acquisition was accounted for as a purchase, and accordingly, the results of operations of eXcelon are included in the Company's operating results from the date of acquisition. The purpose of the acquisition was to expand the product set of the Sonic Software operating unit and, in addition, increase the size of the Company with the ObjectStore product line. The acquisition was structured as a merger of a wholly owned subsidiary of the Company with and into eXcelon. Pursuant to the terms of the acquisition, each outstanding share of eXcelon common stock was converted into the right to receive \$3.19 in cash, without interest. In addition, as a result of the acquisition, holders of outstanding options to purchase eXcelon common stock with an exercise price of less than \$3.19 per share were entitled to receive a cash payment equal to the number of shares of eXcelon common stock subject to such option multiplied by the amount by which \$3.19 exceeded the exercise price per share of such option. The aggregate purchase price of approximately \$33.8 million included \$9.1 million for facilities closures and employee severance and \$0.7 million for direct transaction costs.

## [Table of Contents](#)

Acquired IPR&D of \$0.2 million was expensed when the acquisition was consummated because the technological feasibility of several products under development at the time of the acquisition had not been achieved and no alternate future uses had been established. Research and development costs to bring the acquired products to technological feasibility are not expected to have a material impact on the Company's future results of operations or cash flows. At the date of the acquisition, the Company anticipated the completed product being released in the second half of fiscal 2003. The Company used an independent appraiser to calculate the amounts allocated to assets and liabilities acquired including intangible assets, primarily customer-related and purchased technology, and IPR&D. In fiscal 2004, the Company adjusted the allocation of the purchase price by reducing goodwill by \$2.7 million to reflect an additional tax benefit not contemplated in the original allocation. The allocation of the purchase price was as follows:

*(In thousands, except share data)*

	Total	Life (in years)
Assets and liabilities, including cash	\$ 5,762	
Deferred income taxes	12,997	
Intangible assets	8,100	1 to 6 years
Goodwill (not deductible for tax purposes)	6,696	
In-process research and development	200	
Total purchase price	33,755	
Less: cash acquired	(9,200)	
Less: cash paid for 94,425 shares of eXcelon owned by PSC	(300)	
Net cash paid	\$ 24,255	

In connection with the acquisition of eXcelon, the Company established a reserve for exit costs related to facilities closures and related costs and employee severance. During fiscal 2004, the Company sublet portions of certain of the locations. The amounts included under cash disbursements are net of proceeds received from subrental agreements. A summary of activity is as follows:

*(In thousands)*

	Facilities Closures and Related Costs	Employee Severance and Related Benefits	Total
Balance, December 1, 2002	—	—	—
Establishment of reserve on date of acquisition	\$ 6,955	\$ 2,140	\$ 9,095
Cash disbursements	(2,580)	(2,140)	(4,720)
Balance, November 30, 2003	4,375	—	4,375
Cash disbursements	(2,023)	—	(2,023)
Balance, November 30, 2004	\$ 2,352	\$ —	\$ 2,352

[Table of Contents](#)**Selected Quarterly Financial Data (unaudited):***(In thousands, except per share data)*

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
<b>2004:</b>				
Revenue	\$ 86,375	\$ 90,777	\$ 89,316	\$ 96,194
Gross profit	70,957	74,519	74,398	81,461
Income from operations	6,333	11,470	12,698	15,863
Net income	4,640	8,085	8,520	10,856
Diluted earnings per share	0.12	0.21	0.22	0.28
<b>2003:</b>				
Revenue	\$ 71,822	\$ 77,550	\$ 77,695	\$ 81,993
Gross profit	56,542	62,518	62,700	66,266
Income from operations	5,262	9,165	10,063	12,262
Net income	4,238	6,690	7,329	8,817
Diluted earnings per share	0.12	0.18	0.19	0.23

**Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure**

None.

**Item 9A. Controls and Procedures****(a) Evaluation of disclosure controls and procedures**

The Company's management, including the chief executive officer and the chief financial officer, carried out an evaluation of the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based on this evaluation, the Company's chief executive officer and chief financial officer concluded that the Company's disclosure controls and procedures were effective to provide a reasonable level of assurance that the information required to be disclosed in the reports filed or submitted by the Company under the Securities Exchange Act of 1934 was recorded, processed, summarized and reported within the requisite time periods.

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

The management of Progress Software Corporation (PSC) is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). PSC's internal control system was designed to provide reasonable assurance to the Company's management and board of directors regarding the preparation and fair presentation of published financial statements.

PSC's management assessed the effectiveness of the Company's internal control over financial reporting as of November 30, 2004. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control—Integrated Framework. Based on our assessment we believe that, as of November 30, 2004, the Company's internal control over financial reporting is effective based on those criteria.

Management's assessment of the effectiveness of its internal control over financial reporting as of November 30, 2004 has been attested to by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report which is included herein.

**(c) Changes in internal control over financial reporting**

No changes in the Company's internal control over financial reporting occurred during the quarter ended November 30, 2004 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**(d) Scope of Management’s Annual Report on Internal Control Over Financial Reporting**

For purposes of evaluating the internal controls over financial reporting, management determined that the internal control over financial reporting of DataDirect and Persistence Software would be excluded from the fiscal 2004 internal control assessment, as permitted by the rules and regulations of the Securities and Exchange Commission.

In December 2003 DataDirect was acquired for an aggregate purchase price of approximately \$87.5 million, net of cash acquired. DataDirect contributed approximately 8% of the Company’s total revenue in fiscal 2004 and accounted for approximately 2% of its total assets at November 30, 2004. In November 2004 Persistence was acquired for an aggregate purchase price of approximately \$11.8 million, net of cash. Persistence contributed less than 1% of the Company’s total revenue in fiscal 2004 and accounted for approximately 1% of its total assets at November 30, 2004.

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders of  
Progress Software Corporation  
Bedford, Massachusetts

We have audited management’s assessment, included in the accompanying Management’s Annual Report on Internal Control Over Financial Reporting, included in Item 9A of the Annual Report on Form 10-K, that Progress Software Corporation and its subsidiaries maintained effective internal control over financial reporting as of November 30, 2004, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. As described in Management’s Annual Report on Internal Control Over Financial Reporting, management excluded from their assessment the internal control over financial reporting at DataDirect Technologies Limited (“DataDirect”) which was acquired on December 23, 2003 and whose financial statements reflect total assets and revenues constituting 2% and 8%, respectively, and Persistence Software, Inc. (“Persistence”) which was acquired on November 5, 2004 and whose financial statements reflect total assets and revenues constituting 1% and less than 1%, respectively, of the related consolidated financial statement amounts as of and for the year ended November 30, 2004. Accordingly, our audit did not include the internal control over financial reporting at DataDirect and Persistence. The Company’s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management’s assessment and an opinion on the effectiveness of the Company’s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management’s assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

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

## [Table of Contents](#)

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that the Company maintained effective internal control over financial reporting as of November 30, 2004 is fairly stated, in all material respects, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of November 30, 2004, based on the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended November 30, 2004 of the Company and our report dated February 11, 2005 expressed an unqualified opinion on those financial statements.

/s/ DELOITTE & TOUCHE LLP

Boston, Massachusetts  
February 11, 2005

### **Item 9B. Other Information**

None.

## **PART III**

### **Item 10. Directors and Executive Officers of the Registrant**

The information regarding executive officers set forth under the caption "Executive Officers of the Registrant" in Item 1 of this Annual Report is incorporated herein by reference.

The information regarding directors set forth under the caption "Election of Directors" appearing in the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held on April 21, 2005, which will be filed with the Securities and Exchange Commission (SEC) not later than 120 days after November 30, 2004, is incorporated herein by reference.

The information regarding the Company's code of ethics and audit committee set forth under the caption "Board of Directors and Committees of the Board" appearing in the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held on April 21, 2005, which will be filed with the SEC not later than 120 days after November 30, 2004, is incorporated herein by reference.

### **Item 11. Executive Compensation**

The information set forth under the caption "Executive Compensation" appearing in the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held on April 21, 2005, which will be filed with the SEC not later than 120 days after November 30, 2004, is incorporated herein by reference.

[Table of Contents](#)**Item 12. Security Ownership of Certain Beneficial Owners and Management**

The information set forth under the caption “Security Ownership of Certain Holders and Management” appearing in the Company’s definitive Proxy Statement for the Annual Meeting of Shareholders to be held on April 21, 2005, which will be filed with the SEC not later than 120 days after November 30, 2004, is incorporated herein by reference.

Information related to securities authorized for issuance under equity compensation plans as of November 30, 2004 is as follows:

*(In thousands, except per share data)*

Plan Category	Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights	Weighted-average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available For Future Issuance
Equity compensation plans approved by shareholders	7,397	\$ 13.02	743
Equity compensation plans not approved by shareholders	5,049	17.33	1,018
<b>Total</b>	<b>12,446</b>	<b>\$ 14.77</b>	<b>1,761</b>

The Company has adopted two equity compensation plans, the 2002 Nonqualified Stock Plan (2002 Plan) and the 2004 Inducement Stock Plan (2004 Plan), for which the approval of shareholders was not required. The Company intends that the 2004 Plan be reserved for persons to whom the Company may issue securities without shareholder approval as an inducement to become employed by the Company pursuant to the rules and regulations of the Nasdaq Stock Market. Executive officers and members of the Board of Directors are not eligible for awards under the 2002 Plan. An executive officer or director would be eligible to receive an award under the 2004 Plan only as an inducement to join the Company. Awards under the 2002 Plan and the 2004 Plan may include nonqualified stock options, grants of conditioned stock, unrestricted grants of stock, grants of stock contingent upon the attainment of performance goals and stock appreciation rights. No awards other than nonqualified stock options have been granted under either plan. A total of 6,700,000 shares are issuable under the two plans.

**Item 13. Certain Relationships and Related Transactions**

The information set forth under the caption “Certain Relationships and Related Transactions” appearing in the Company’s definitive Proxy Statement for the Annual Meeting of Shareholders to be held on April 21, 2005, which will be filed with the SEC not later than 120 days after November 30, 2004, is incorporated herein by reference.

**Item 14. Principal Accounting Fees and Services**

The information set forth under the caption “Principal Accounting Fees and Services” appearing in the Company’s definitive Proxy Statement for the Annual Meeting of Shareholders to be held on April 21, 2005, which will be filed with the SEC not later than 120 days after November 30, 2004, is incorporated herein by reference.

**PART IV**

**Item 15. Exhibits, Financial Statement Schedules**

**(a) Documents Filed as Part of this Form 10-K**

1. Financial Statements (included in Item 8 of this report on Form 10-K):

- Report of Independent Registered Public Accounting Firm
- Consolidated Balance Sheets as of November 30, 2004 and 2003
- Consolidated Statements of Operations for the years ending November 30, 2004, 2003 and 2002
- Consolidated Statements of Shareholders' Equity for the years ending November 30, 2004, 2003 and 2002
- Consolidated Statements of Cash Flows for the years ending November 30, 2004, 2003 and 2002
- Notes to Consolidated Financial Statements

2. Financial Statement Schedules

Financial statement schedules are omitted as they are either not required or the information is otherwise included.

**(b) Exhibits**

Documents listed below, except for documents followed by parenthetical numbers, are being filed as exhibits. Documents followed by parenthetical numbers are not being filed herewith and, pursuant to Rule 12b-32 of the General Rules and Regulations promulgated by the SEC under the Securities Exchange Act of 1934 (the Act), reference is made to such documents as previously filed as exhibits with the SEC. PSC's file number under the Act is 0-19417.

- 2.1 Agreement and Plan of Merger Among Progress Software Corporation, Chopin Merger Sub, Inc. and eXcelon Corporation (1)
- 2.2 Purchase Agreement Dated as of December 5, 2003 By and Among Progress Software Corporation, Diamond Acquisition Corp. and DataDirect Technologies Limited (2)
- 2.3 Agreement and Plan of Merger By and Among Progress Software Corporation, PSI Acquisition Sub, Inc. and Persistence Software, Inc. (3)
- 3.1 Restated Articles of Organization of the Company (4)
  - 3.1.1 Articles of Amendment to Restated Articles of Organization filed on January 19, 1995 (5)
  - 3.1.2 Articles of Amendment to Restated Articles of Organization filed on November 17, 1997 (6)
  - 3.1.3 Articles of Amendment to Restated Articles of Organization filed on May 6, 1999 (7)
  - 3.1.4 Articles of Amendment to Restated Articles of Organization filed on June 17, 2000 (8)
- 3.2 By-Laws of the Company, as amended and restated (9)
- 4.1 Specimen certificate for the Common Stock of the Company (10)
- 10.1\* Amended and Restated 1984 Incentive Stock Option Plan (11)
- 10.2\* 1991 Employee Stock Purchase Plan, as amended (12)
- 10.3\* 1992 Incentive and Nonqualified Stock Option Plan (13)
- 10.4\* 1994 Stock Incentive Plan (14)
- 10.5\* 1993 Directors' Stock Option Plan (15)
- 10.6\* 1997 Stock Incentive Plan, as amended (16)
- 10.7\* Employee Retention and Motivation Agreement executed by each of the Executive Officers (17)
- 10.8\* First amendment to Employee Retention and Motivation Agreement executed by each of the Executive Officers (18)
- 10.9\* 2002 Nonqualified Stock Plan (19)
- 10.10\* Sonic Software Corporation 2001 Stock Incentive Plan, as amended
- 10.11 PeerDirect Corporation 2003 Stock Incentive Plan

10.12 2004 Inducement Stock Plan

21.1 List of Subsidiaries of the Registrant

23.1 Consent of Deloitte & Touche LLP

31.1 Certification Pursuant to Section 302 of Sarbanes-Oxley Act of 2002 – Joseph W. Alsop

31.2 Certification Pursuant to Section 302 of Sarbanes-Oxley Act of 2002 – Norman R. Robertson



32.1 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

---

- (1) Incorporated by reference to Exhibit 1 of Schedule 13D filed October 28, 2002.
- (2) Incorporated by reference to Exhibit 2.1 of Form 8-K filed January 7, 2004
- (3) Incorporated by reference to Exhibit 99.1 of Form 8-K filed September 27, 2004.
- (4) Incorporated by reference to Exhibit 3.1 to the Company's Annual Report on Form 10-K for the fiscal year ended November 30, 1997.
- (5) Incorporated by reference to Exhibit 3.1.1 to the Company's Annual Report on Form 10-K for the fiscal year ended November 30, 1994.
- (6) Incorporated by reference to Exhibit 3.1.2 to the Company's Annual Report on Form 10-K for the fiscal year ended November 30, 1997.
- (7) Incorporated by reference to Exhibit 3.1.3 to the Company's Annual Report on Form 10-K for the fiscal year ended November 30, 1999.
- (8) Incorporated by reference to Exhibit 3.1.4 to the Company's Annual Report on Form 10-K for the fiscal year ended November 30, 2000.
- (9) Incorporated by reference to Exhibit 3.2 to the Company's Annual Report on Form 10-K for the fiscal year ended November 30, 1991.
- (10) Incorporated by reference to Exhibit 4.1 to the Company's Registration Statement on Form S-1, File No. 33-41223, as amended.
- (11) Incorporated by reference to Exhibit 10.12 to the Company's Registration Statement on Form S-1, File No. 33-41223, as amended.
- (12) Incorporated by reference to Exhibit 10.8 to the Company's Quarterly Report on Form 10-Q for the quarter ended May 31, 1998.
- (13) Incorporated by reference to Exhibit 10.12 to the Company's Quarterly Report on Form 10-Q for the quarter ended May 31, 1992.
- (14) Incorporated by reference to Exhibit 10.16 to the Company's Quarterly Report on Form 10-Q for the quarter ended August 31, 1994.
- (15) Incorporated by reference to Exhibit 10.17 to the Company's Quarterly Report on Form 10-Q for the quarter ended August 31, 1994.
- (16) Incorporated by reference to Exhibit 10.7 to the Company's Annual Report on Form 10-K for the fiscal year ended November 30, 2000.
- (17) Incorporated by reference to Exhibit 10.10 to the Company's Annual Report on Form 10-K for the fiscal year ended November 30, 1998.
- (18) Incorporated by reference to Exhibit 10.10.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended August 31, 1999.
- (19) Incorporated by reference to Exhibit 10.10 to the Company's Quarterly Report on Form 10-Q for the quarter ended May 31, 2002.

[Table of Contents](#)

\* Management contract or compensatory plan or arrangement in which an executive officer or director of PSC participates

**(c) Financial Statement Schedules**

All schedules are omitted because they are not applicable or the required information is shown on the financial statements or notes thereto.

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on the 11th day of February, 2005.

PROGRESS SOFTWARE CORPORATION

By: /s/ JOSEPH W. ALSOP

Joseph W. Alsop  
*Chief Executive Officer*

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

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ JOSEPH W. ALSOP</u> Joseph W. Alsop	Chief Executive Officer and Director (Principal Executive Officer)	February 11, 2005
<u>/s/ NORMAN R. ROBERTSON</u> Norman R. Robertson	Senior Vice President, Finance and Administration and Chief Financial Officer (Principal Financial Officer)	February 11, 2005
<u>/s/ DAVID H. BENTON, JR.</u> David H. Benton, Jr.	Vice President and Corporate Controller (Principal Accounting Officer)	February 11, 2005
<u>/s/ LARRY R. HARRIS</u> Larry R. Harris	Director	February 11, 2005
<u>/s/ ROGER J. HEINEN, JR.</u> Roger J. Heinen, Jr.	Director	February 11, 2005
<u>/s/ MICHAEL L. MARK</u> Michael L. Mark	Director	February 11, 2005
<u>/s/ SCOTT A. MCGREGOR</u> Scott A. McGregor	Director	February 11, 2005
<u>/s/ AMRAM RASIEL</u> Amram Rasiel	Director	February 11, 2005

SONIC SOFTWARE CORPORATION

2001 STOCK INCENTIVE PLAN

(AMENDED AND RESTATED AS OF NOVEMBER 12, 2003)

1. PURPOSE.

The purpose of this plan (the "Plan") is to secure for Sonic Software Corporation, a Delaware corporation (the "Company") and its shareholders the benefits arising from capital stock ownership by employees, officers and directors of, and consultants or advisors to, the Company and its parent and subsidiary corporations who are expected to contribute to the Company's future growth and success. Under the Plan recipients may be awarded both (i) Options (as defined in Section 2.1) to purchase the Company's common stock, par value \$.01 ("Common Stock"), and (ii) shares of the Company's Common Stock ("Restricted Stock Awards"). Except where the context otherwise requires, the term "Company" shall include the parent and all present and future subsidiaries of the Company as defined in Sections 424(e) and 424(f) of the Internal Revenue Code of 1986, as amended or replaced from time to time (the "Code"). Those provisions of the Plan which make express reference to Section 422 of the Code shall apply only to Incentive Stock Options (as that term is defined in the Plan). Appendix A to this Plan shall apply only to participants in the Plan who are residents of the State of California.

2. TYPES OF AWARDS AND ADMINISTRATION.

2.1 OPTIONS. Options granted pursuant to the Plan ("Options") shall be authorized by action of the Board of Directors of the Company and may be either incentive stock options ("Incentive Stock Options") meeting the requirements of Section 422 of the Code or non-statutory Options which are not intended to meet the requirements of Section 422. The vesting of Options may be conditioned upon the completion of a specified period of employment with the Company and/or such other conditions or events as the Board may determine. The Board may also provide that Options are immediately exercisable subject to certain repurchase rights in the Company dependent upon the continued employment of the optionee and/or such other conditions or event as the Board may determine.

2.1.1 INCENTIVE STOCK OPTIONS. All Options when granted are intended to be non-statutory Options, unless the applicable Option Agreement (as defined in Section 5.1) explicitly states that the Option is intended to be an Incentive Stock Option. Incentive Stock Options may only be granted to employees of the Company. For so long as the Code shall so provide, Options granted to any employee under the Plan (and any other incentive stock option plans of the Company) which are intended to constitute Incentive Stock Options shall not constitute Incentive Stock Options to the extent that such Options, in the aggregate, become exercisable for the first time in any one calendar year for shares of Common Stock with an aggregate fair market value (determined as of the respective date or dates of grant) of more than \$100,000. If an Option is intended to be an Incentive Stock Option, and if for any reason such Option (or any portion thereof) shall not qualify as an Incentive Stock Option, then, to the extent of such nonqualification, such Option (or portion thereof) shall be regarded as a non-statutory

Option appropriately granted under the Plan provided that such Option (or portion thereof) otherwise meets the Plan's requirements relating to non-statutory Options.

2.2 RESTRICTED STOCK AWARDS. The Board in its discretion may grant Restricted Stock Awards, entitling the recipient to acquire, for a purchase price determined by the Board, shares of Common Stock subject to such restrictions and conditions as the Board may determine at the time of grant ("Restricted Stock"), including continued employment and/or achievement of pre-established performance goals and objectives.

2.3 ADMINISTRATION. The Plan shall be administered by the Board of Directors of the Company, whose construction and interpretation of the terms and provisions of the Plan shall be final and conclusive. The Board of Directors may in its sole discretion issue Restricted Stock and grant Options to purchase shares of Common Stock, and issue shares upon exercise of such Options as provided in the Plan. The Board shall have authority, subject to the express provisions of the Plan, to construe Restricted Stock Agreements (as defined in Section 5.2), Option Agreements and the Plan, to prescribe, amend and rescind rules and regulations relating to the Plan, to determine the terms and provisions of Restricted Stock Agreements and Option Agreements, and to make all other determinations in the judgment of the Board of Directors necessary or desirable for the administration of the Plan. The Board of Directors may correct any defect or supply any omission or reconcile any inconsistency in the Plan or in any Restricted Stock Agreement or Option Agreement in the manner and to the extent it shall deem expedient to carry the Plan into effect and it shall be the sole and final judge of such expediency. No director or person acting pursuant to authority delegated by the Board of Directors shall be liable for any action or determination under the Plan made in good faith. The Board of Directors may, to the full extent permitted by or consistent with applicable laws or regulations (including, without limitation, applicable state law), delegate any or all of its powers under the Plan to a committee (the "Committee") appointed by the Board of Directors, and if the Committee is so appointed all references to the Board of Directors in the Plan shall mean and relate to such Committee.

### 3. ELIGIBILITY.

Options may be granted, and Restricted Stock may be issued, to persons who are, at the time of such grant or issuance, employees, officers or directors of, or consultants or advisors to, the Company; provided, that the class of persons to whom Incentive Stock Options may be granted shall be limited to employees of the Company.

3.1 10% SHAREHOLDER. If any employee to whom an Incentive Stock Option is to be granted is, at the time of the grant of such Option, the owner of stock possessing more than 10% of the total combined voting power of all classes of stock of the Company (after taking into account the attribution of stock ownership rules of Section 424(d) of the Code) ("10% Shareholder"), any Incentive Stock Option granted to such individual must: (i) have an exercise price per share of not less than 110% of the fair market value of one share of Common Stock at the time of grant; and (ii) expire by its terms not more than five years from the date of grant.

4. STOCK SUBJECT TO PLAN.

Subject to adjustment as provided in Section 14.2 below, the maximum number of shares of Common Stock which may be issued under the Plan is 12,950,000 shares. If an Option shall expire or terminate for any reason without having been exercised in full, the unpurchased shares subject to such Option shall again be available for subsequent Option grants or Restricted Stock awards under the Plan. If shares of Restricted Stock shall be forfeited to, or otherwise repurchased by, the Company pursuant to a Restricted Stock Agreement, such purchased shares shall again be available for subsequent Option grants or Restricted Stock awards under the Plan. If shares issued upon exercise of an Option are tendered to the Company in payment of the exercise price of an Option, such tendered shares shall again be available for subsequent Option grants or Restricted stock awards under the Plan.

5. FORMS OF RESTRICTED STOCK AGREEMENTS AND OPTION AGREEMENTS.

5.1 OPTION AGREEMENT. As a condition to the grant of an Option, each recipient of an Option shall execute an option agreement ("Option Agreement") in such form not inconsistent with the Plan as may be approved by the Board of Directors. Such Option Agreements may differ among recipients.

5.2 RESTRICTED STOCK AGREEMENT. As a condition to the issuance of Restricted Stock, each recipient thereof shall execute an agreement ("Restricted Stock Agreement") in such form not inconsistent with the Plan as may be approved by the Board of Directors. Such Restricted Stock Agreements may differ among recipients and need not be entitled "Restricted Stock Agreements."

5.3 "STAND-OFF" AGREEMENT. Unless the Board of Directors specifies otherwise, each Restricted Stock Agreement and Option Agreement shall provide that upon the request of the Company or the managing underwriter(s), the holder of any Option or the purchaser of any Restricted Stock shall, in connection with any registrations of securities of the Company, agree in writing that for a period of time (not to exceed 180 days) from the effective date of the Securities and Exchange Commission registration statement for such offering, the holder or purchaser will not sell, make any short sale of, loan, grant any option for the purchase of, or otherwise dispose of any shares of the common stock of the Company owned or controlled by him.

6. PURCHASE PRICE.

6.1 GENERAL. The purchase price per share of Restricted Stock and per share of stock deliverable upon the exercise of an Option shall be determined by the Board of Directors, provided, however, that in the case of an Incentive Stock Option, the exercise price shall not be less than 100% of the fair market value of such stock, as determined by the Board of Directors, at the time of grant of such Option, or less than 110% of such fair market value in the case of any Incentive Stock Option granted to a 10% Shareholder.

6.2 PAYMENT OF PURCHASE PRICE. Option Agreements may provide for the payment of the exercise price by (i) delivery of a personal, certified or bank check or postal money order payable to the order of the Company in an amount equal to the exercise price of

such Option, (ii) delivery to the Company of shares of Common Stock of the Company already owned by the optionee for a period of six months and having a fair market value equal in amount to the exercise price of the Option being exercised, (ii) a personal recourse note issued by the optionee to the Company in a principal amount equal to such aggregate exercise price and with such other terms, including interest rate and maturity, as the Company may determine in its discretion; provided, however, that the interest rate borne by such note shall not be less than the lowest applicable federal rate, as defined in Section 1274(d) of the Code, (iii) any other means which the Board of Directors determines are consistent with the purpose of the Plan and with applicable laws and regulations or (iv) any combination of such methods of payment. The fair market value of any shares of Common Stock or other non-cash consideration which may be delivered upon exercise of an Option shall be determined by the Board of Directors. Restricted Stock Agreements may provide for the payment of any purchase price in any manner approved by the Board of Directors at the time of authorizing the issuance thereof.

#### 7. OPTION PERIOD.

Notwithstanding any other provision of the Plan or any Option Agreement, each Option and all rights thereunder shall expire on the date specified in the applicable Option Agreement, provided that such date shall not be later than 10 years after the date on which the Option is granted (or five years in the case of an Incentive Stock Option granted to a 10% Shareholder), and in either case, shall be subject to earlier termination as provided in the Plan.

#### 8. EXERCISE OF OPTIONS.

8.1 GENERAL. Each Option shall be exercisable either in full or in installments at such time or times and during such period as shall be set forth in the agreement evidencing such Option, subject to the provisions of the Plan. To the extent not exercised, installments shall accumulate and be exercisable, in whole or in part, at any time after becoming exercisable, but not later than the date the Option expires.

8.2 NOTICE OF EXERCISE. Any option granted under the Plan may be exercised by the optionee by delivering to the Company on any business day a written notice specifying the number of Common Shares the optionee then desires to purchase (the "Notice"), accompanied by payment for such shares.

8.3 DELIVERY. As promptly as practicable after receipt of such written notification and payment, the Company shall deliver or cause to be delivered to the optionee certificates for the number of shares with respect to which such Option has been so exercised, issued in the optionee's name or, at the Company's election, the Company shall deposit such shares into an electronic share account maintained for the benefit of the optionee; provided, however, that such delivery of certificates shall be deemed effected for all purposes when the Company or a stock transfer agent shall have deposited such certificates in the United States mail, addressed to the optionee, at the address specified in the Notice; and that such deposit of shares shall be deemed effected for all purposes when the deposit is reflected in the optionee's account.

9. NONTRANSFERABILITY OF OPTIONS.

No Option shall be assignable or transferable by the person to whom it is granted, either voluntarily or by operation of law, except by will or the laws of descent and distribution. During the life of an optionee, an Option shall be exercisable only by the optionee.

10. TERMINATION OF EMPLOYMENT; DISABILITY; DEATH. Except as may be otherwise expressly provided in the terms and conditions of the Option Agreement, Options shall terminate on the earliest to occur of:

- (i) the date of expiration thereof;
- (ii) immediately upon termination of the optionee's employment with or services to the Company by the Company for Cause (as hereinafter defined), or upon voluntary termination of employment by the optionee (other than for death or permanent disability as defined below); or
- (iii) 90 days after the date of termination of the optionee's employment with or services to the Company by the Company without Cause (other than for death or permanent and total disability as defined below).

Until the date on which the Option so expires, the optionee may exercise that portion of his Option which is exercisable at the time of termination of the employment or service relationship.

An employment relationship between the Company and the optionee shall be deemed to exist during any period during which the optionee is employed by the Company or by a parent or any Subsidiary of the Company. Whether an authorized leave of absence or an absence due to military or government service shall constitute termination of the employment relationship between the Company and the optionee shall be determined by the Board at the time thereof.

For purposes of this Section 10, the term "Cause" shall mean (a) any material breach by the optionee of any agreement to which the optionee and the Company are both parties, (b) any act (other than retirement) or omission to act by the optionee which may have a material and adverse effect on the Company's business or on the optionee's ability to perform services for the Company, including, without limitation, the commission of any crime (other than minor traffic violations), or (c) any material misconduct or material neglect of duties by the optionee in connection with the business or affairs of the Company, its parent or any Subsidiary or affiliate of the Company.

In the event of the permanent and total disability or death of an optionee while in an employment or other relationship with the Company and before the date of expiration of such option, such option shall terminate on the earlier of such date of expiration or one year following the date of such disability or death. After disability or death, the optionee (or in the case of death, his executor, administrator or any person or persons to whom his option may be transferred by will or by laws of descent and distribution) shall have the right, at any time prior to such termination, to exercise the option to the extent the optionee was entitled to exercise such



option as of the date of his disability or death. An optionee is permanently and totally disabled if he is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to last for a continuous period of not less than 12 months; permanent and total disability shall be determined in accordance with Section 22(e)(3) of the Code and the regulations issued thereunder.

11. RIGHTS AS A SHAREHOLDER. The holder of an Option shall have no rights as a shareholder with respect to any shares covered by the Option (including, without limitation, any rights to receive dividends or non-cash distributions with respect to such shares) until the date of issue of a stock certificate to him or her for such shares or the date of deposit of such shares in an electronic deposit account for the benefit of him or her. No adjustment shall be made for dividends or other rights for which the record date is prior to the date such stock certificate is issued or such shares deposited.

12. ADDITIONAL PROVISIONS. The Board of Directors may, in its sole discretion, include additional provisions in Restricted Stock Agreements and Option Agreements, including, without limitation, restrictions on transfer, rights of the Company to repurchase shares of Restricted Stock or shares of Common Stock acquired upon exercise of Options, commitments to pay cash bonuses, to make, arrange for or guaranty loans or to transfer other property to optionees upon exercise of Options, or such other provisions as shall be determined by the Board of Directors; provided that such additional provisions shall not be inconsistent with any other term or condition of the Plan and such additional provisions shall not be such as to cause any Incentive Stock Option to fail to qualify as an Incentive Stock Option within the meaning of Section 422 of the Code.

13. ACCELERATION, EXTENSION, ETC. The Board of Directors may, in its sole discretion, (i) accelerate the date or dates on which all or any particular Option or Options may be exercised or (ii) extend the dates during which all, or any particular, Option or Options may be exercised.

#### 14. ADJUSTMENT UPON CHANGES IN CAPITALIZATION

14.1 NO EFFECT OF OPTIONS UPON CERTAIN CORPORATE TRANSACTIONS. The existence of outstanding Options shall not affect in any way the right or power of the Company to make or authorize any or all adjustments, recapitalizations, reorganizations or other changes in the Company's capital structure or its business, or any merger or consolidation, or any issue of Common Shares, or any issue of bonds, debentures, preferred or prior preference stock ahead of or affecting the Common Shares or the rights thereof, or the dissolution or liquidation of the Company, or any sale or transfer of all or any part of its assets or business, or any other corporate act or proceeding, whether of a similar character or otherwise.

14.2 ADJUSTMENT PROVISIONS. If, through or as a result of any merger, consolidation, sale of all or substantially all of the assets of the Company, reorganization, recapitalization, reclassification, stock dividend, stock split, reverse stock split or other similar transaction, (i) the outstanding shares of Common Stock are increased, decreased or exchanged for a different number or kind of shares or other securities of the Company, or (ii) additional shares or new or different shares or other securities of the Company or other non-cash assets are distributed with respect to such shares of Common Stock or other securities, an appropriate and

proportionate adjustment may be made in (x) the maximum number and kind of shares reserved for issuance under the Plan, (y) the number and kind of shares or other securities subject to any then outstanding Options, and (z) the price for each share subject to any then outstanding Options, without changing the aggregate purchase price as to which such Options remain exercisable. Notwithstanding the foregoing, no adjustment shall be made pursuant to this Section 14 if such adjustment would cause the Plan to fail to comply with Section 422 of the Code.

14.3 NO ADJUSTMENT IN CERTAIN CASES. Except as hereinbefore expressly provided, the issue by the Company of shares of stock of any class, or securities convertible into shares of stock of any class, for cash or property or for labor or services, either upon direct sale or upon the exercise of rights or warrants to subscribe therefore, or upon conversion of shares or obligations of the Company convertible into such shares or other securities, shall not affect, and no adjustment by reason thereof shall be made with respect to, the number or price of shares of Common Stock then subject to outstanding options.

14.4 BOARD AUTHORITY TO MAKE ADJUSTMENTS. Any adjustments under this Section 14 will be made by the Board of Directors, whose determination as to what adjustments, if any, will be made and the extent thereof will be final, binding and conclusive. No fractional shares will be issued under the Plan on account of any such adjustments.

#### 15. EFFECT OF CERTAIN TRANSACTIONS

15.1 GENERAL. In the event of a consolidation or merger or sale of all or substantially all of the assets of the Company in which outstanding shares of Common Stock are exchanged for securities, cash or other property of any other corporation or business entity, or in the event of a liquidation of the Company, the Board of Directors of the Company, or the board of directors of any corporation assuming the obligations of the Company, may, in its discretion, take any one or more of the following actions, as to some or all outstanding Options (and need not take the same action as to each such Option): (i) provide that such Options shall be assumed, or equivalent Options shall be substituted, by the acquiring or succeeding corporation (or an affiliate thereof), provided that any such Options substituted for Incentive Stock Options shall meet the requirements of Section 424(a) of the Code, (ii) upon written notice to the optionees, provide that all unexercised Options will terminate immediately prior to the consummation of such transaction unless exercised by the optionee (to the extent otherwise then exercisable) within a specified period following the date of such notice, (iii) in the event of a merger under the terms of which holders of the Common Stock of the Company will receive upon consummation thereof a cash payment for each share surrendered in the merger (the "Merger Price"), make or provide for a cash payment to the optionees equal to the difference between (A) the Merger Price times the number of shares of Common Stock subject to such outstanding Options (to the extent then exercisable at prices not in excess of the Merger Price) and (B) the aggregate exercise price of all such outstanding Options, in exchange for the termination of such Options, and (iv) provide that all or any outstanding Options shall become exercisable in full immediately prior to such event.

15.2 SUBSTITUTE OPTIONS. The Company may grant Options in substitution for Options held by employees of another corporation who become employees of the Company, or a

subsidiary of the Company, as the result of a merger or consolidation of the employing corporation with the Company or a subsidiary of the Company, or as a result of the acquisition by the Company, or one of its subsidiaries, of property or stock of the employing corporation. The Company may direct that substitute Options be granted on such terms and conditions as the Board of Directors considers appropriate in the circumstances.

15.3 RESTRICTED STOCK. In the event of a business combination or other transaction of the type detailed in Section 15.1, any securities, cash or other property received in exchange for shares of Restricted Stock shall continue to be governed by the provisions of any Restricted Stock Agreement pursuant to which they were issued, including any provision regarding vesting, and such securities, cash, or other property may be held in escrow on such terms as the Board of Directors may direct, to insure compliance with the terms of any such Restricted Stock Agreement.

16. NO SPECIAL EMPLOYMENT RIGHTS. Nothing contained in the Plan or in any Option or Restricted Stock Agreement shall confer upon any optionee any right with respect to the continuation of his or her employment by the Company or interfere in any way with the right of the Company at any time to terminate such employment or to increase or decrease the compensation of the optionee.

17. OTHER EMPLOYEE BENEFITS. The amount of any compensation deemed to be received by an employee as a result of the issuance of shares of Restricted Stock or the grant or exercise of an Option or the sale of shares received upon such award or exercise will not constitute compensation with respect to which any other employee benefits of such employee are determined, including, without limitation, benefits under any bonus, pension, profit-sharing, life insurance or salary continuation plan, except as otherwise specifically determined by the Board of Directors.

18. AMENDMENT OF THE PLAN.

18.1 The Board of Directors may at any time, and from time to time, modify or amend the Plan in any respect, except that if at any time the approval of the shareholders of the Company is required under Section 422 of the Code or any successor provision with respect to Incentive Stock Options, the Board of Directors may not effect such modification or amendment without such approval.

18.2 The termination or any modification or amendment of the Plan shall not, without the consent of an optionee or the recipient of Restricted Stock, affect his or her rights under an Option or Restricted Stock award previously granted to him or her. With the consent of the recipient of Restricted Stock or optionee affected, the Board of Directors may amend outstanding Restricted Stock Agreements or Option Agreements in a manner not inconsistent with the Plan. The Board of Directors shall have the right to amend or modify the terms and provisions of the Plan and of any outstanding Incentive Stock Options to the extent necessary to qualify any or all such Options for such favorable federal income tax treatment (including deferral of taxation upon exercise) as may be afforded incentive stock options under Section 422 of the Code.

19. WITHHOLDING. The Company shall have the right to deduct from payments of any kind otherwise due to the optionee or recipient of Restricted Stock, any federal, state or local taxes of any kind required by law to be withheld with respect to issuance of any shares of Restricted Stock or shares issued upon exercise of Options. Subject to the prior approval of the Company, which may be withheld by the Company in its sole discretion, the obligor may elect to satisfy such minimum withholding obligations, in whole or in part, (i) by causing the Company to withhold shares of Common Stock otherwise issuable or (ii) by delivering to the Company shares of Common Stock already owned by the obligor. The shares so delivered or withheld shall have a fair market value equal to such withholding obligation. The fair market value of the shares used to satisfy such withholding obligation shall be determined by the Company as of the date that the amount of tax to be withheld is to be determined. A person who has made an election pursuant to this Section 19 may only satisfy his or her withholding obligation with shares of Common Stock which are not subject to any repurchase, forfeiture, unfulfilled vesting or other similar requirements.

20. EFFECTIVE DATE AND DURATION OF THE PLAN.

20.1 EFFECTIVE DATE. The Plan shall become effective when adopted by the Board of Directors, but no Incentive Stock Option shall become exercisable unless and until the Plan shall have been approved by the Company's shareholders. If such shareholder approval is not obtained within twelve months after the date of the Board's adoption of the Plan, no Options previously granted under the Plan shall be deemed to be Incentive Stock Options and no Incentive Stock Options shall be granted thereafter. Amendments to the Plan not requiring shareholder approval shall become effective when adopted by the Board of Directors; amendments requiring shareholder approval (as provided in Section 18.1) shall become effective when adopted by the Board of Directors, but no Incentive Stock Option granted after the date of such amendment shall become exercisable (to the extent that such amendment to the Plan was required to enable the Company to grant such Incentive Stock Option to a particular optionee) unless and until such amendment shall have been approved by the Company's shareholders. If such shareholder approval is not obtained within twelve months of the Board's adoption of such amendment, any Incentive Stock Options granted on or after the date of such amendment shall terminate to the extent that such amendment to the Plan was required to enable the Company to grant such Option to a particular optionee. Subject to this limitation, Options may be granted under the Plan at any time after the effective date and before the date fixed for termination of the Plan.

20.2 TERMINATION. Unless sooner terminated by action of the Board of Directors, the Plan shall terminate upon the close of business on the day next preceding the tenth anniversary of the date of its adoption by the Board of Directors.

21. PROVISION FOR FOREIGN PARTICIPANTS. The Board of Directors may, without amending the Plan, modify the terms of Option or Restricted Stock Agreements to differ from those specified in the Plan with respect to participants who are foreign nationals or employed outside the United States to recognize differences in laws, rules, regulations or customs of such foreign jurisdictions with respect to tax, securities, currency, employee benefit or other matters.

22. REQUIREMENTS OF LAW. The Company shall not be required to sell or issue any shares under any Option or Restricted Stock Agreement if the issuance of such shares shall constitute a violation by the optionee or by the Company of any provisions of any law or regulation of any governmental authority. In addition, in connection with the Securities Act of 1933, as now in effect or hereafter amended (the "Act"), the Company shall not be required to issue any shares upon exercise of any Option unless the Company has received evidence satisfactory to it to the effect that the holder of such Option will not transfer such shares except pursuant to a registration statement in effect under the Act or unless an opinion of counsel satisfactory to the Company has been received by the Company to the effect that such registration is not required in connection with any such transfer. Any determination in this connection by the Board shall be final, binding and conclusive. In the event the shares issuable on exercise of an Option are not registered under the Act or under the securities laws of each relevant state or other jurisdiction, the Company may imprint on the certificate(s) appropriate legends that counsel for the Company considers necessary or advisable to comply with the Act or any such state or other securities law and in the instance of shares that are deposited in an electronic account, the Company may restrict transactions associated with such shares as the Company considers necessary or advisable to comply with the Act or any such state or other securities law. The Company may register, but in no event shall be obligated to register, any securities covered by the Plan pursuant to the Act; and in the event any shares are so registered the Company may remove any legend on certificates representing such shares and remove any restrictions on transactions associated with such shares. The Company shall not be obligated to take any affirmative action in order to cause the exercise of an Option or the issuance of shares pursuant thereto to comply with any law or regulation of any governmental authority.

23. GOVERNING LAW. This Plan and each Option or Restricted Stock Agreement shall be governed by the laws of the Commonwealth of Massachusetts, without regard to its principles of conflicts of law.

APPENDIX A  
TO SONIC SOFTWARE CORPORATION 2001 STOCK INCENTIVE PLAN  
FOR CALIFORNIA RESIDENTS ONLY

This Appendix to the Sonic Software Corporation 2001 Stock Incentive Plan (the "Plan") shall have application only to participants in the Plan who are residents of the State of California. Capitalized terms contained herein shall have the same meanings given to them in the Plan, unless otherwise provided in this Appendix. NOTWITHSTANDING ANY PROVISION CONTAINED IN THE PLAN TO THE CONTRARY AND TO THE EXTENT REQUIRED BY APPLICABLE LAW, THE FOLLOWING TERMS AND CONDITIONS SHALL APPLY TO ALL OPTIONS AND RESTRICTED STOCK AWARDS (COLLECTIVELY "AWARDS") GRANTED TO RESIDENTS OF THE STATE OF CALIFORNIA, UNTIL SUCH TIME AS THE COMMON STOCK BECOMES SUBJECT TO REGISTRATION UNDER THE SECURITIES ACT OF 1933:

1. Nonqualified Stock Options shall have an exercise price that is not less than 85% of the Fair Market Value of the stock at the time the Option is granted, as determined by the Board, except that the exercise price shall be 110% of the Fair Market Value in the case of any person who owns stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or its parent or subsidiary corporations.

2. The purchase price for any Stock Awards that may be purchased under the Plan ("Stock Purchase Rights") shall be at least 85% of the Fair Market Value of the Common Stock at the time the Participant is granted the Stock Purchase Right or at the time the purchase is consummated. Notwithstanding the foregoing, the purchase price shall be 100% of the Fair Market Value of the Common Stock at the time the Participant is granted the Stock Purchase Right or at the time the purchase is consummated in the case of any person who owns stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or its parent or subsidiary corporations.

3. Options shall have a term of not more than ten years from the date the Option is granted.

4. Awards shall be nontransferable other than by will or the laws of descent and distribution. Notwithstanding the foregoing, and to the extent permitted by Section 422 of the Code, the Plan Administrator, in its discretion, may permit distribution of an Option to an inter vivos or testamentary trust in which the Option is to be passed to beneficiaries upon the death of the trustor (settlor), or by gift to "immediate family" as that term is defined in Rule 16a-1(e) of the Exchange Act.

5. Options shall become exercisable at the rate of at least 20% per year over five years from the date the Option is granted, subject to reasonable conditions such as continued employment. However, in the case of an Option granted to officers, directors or consultants of the Company or any of its affiliates, the Option may become fully exercisable, subject to reasonable conditions such as continued employment, at any time or during any period established by the Company or any of its affiliates.

6. Unless employment is terminated for Cause, the right to exercise an Option in the event of termination of employment, to the extent that the Participant is otherwise entitled to exercise an Option on the date employment terminates, shall be

(a) at least six months from the date of termination of employment if termination was caused by death or Disability; and

(b) at least 30 days from the date of termination if termination of employment was caused by other than death or Disability;

(c) but in no event later than the remaining term of the Option.

7. No Award may be granted to a resident of California more than ten years after the earlier of the date of adoption of the Plan and the date the Plan is approved by the shareholders.

8. Any Award exercised before shareholder approval is obtained shall be rescinded if shareholder approval is not obtained within 12 months before or after the Plan is adopted. Such shares shall not be counted in determining whether such approval is obtained.

9. The Company shall provide annual financial statements of the Company to each California resident holding an outstanding Award under the Plan. Such financial statements need not be audited and need not be issued to key employees whose duties at the Company assure them access to equivalent information.

10. Any right of repurchase on behalf of the Company in the event of a Participant's termination of employment shall be at a purchase price that is (a) not less than the Fair Market Value of the securities upon termination of employment, and the right to repurchase shall be exercised for cash or cancellation of purchase money indebtedness for the shares within 90 days of termination of employment (or in the case of securities issued upon exercise of Options after the date of termination, within 90 days after the date of the exercise), and the right shall terminate when the stock at issue becomes publicly traded; or (b) at the original purchase price, provided that the right to repurchase at the original purchase price lapses at the rate of at least 20% of the shares per year over five years from the date the Option or Stock Purchase Right is granted (without respect to the date the Option or Stock Purchase Right was exercised or became exercisable) and the right to repurchase shall be exercised for cash or cancellation of purchase money indebtedness for the shares within 90 days of termination of employment (or in the case of securities issued upon exercise of Options after the date of termination, within 90 days after the date of the exercise). In addition to the restrictions set forth in clauses (a) and (b), the securities held by an officer, direct or consultant of the Company or an affiliate of the Company may be subject to additional or greater restrictions.

PEERDIRECT CORPORATION

2003 STOCK INCENTIVE PLAN

1. PURPOSE.

The purpose of this plan (the "Plan") is to secure for PeerDirect Corporation, a Delaware corporation (the "Company"), and its shareholders the benefits arising from capital stock ownership by employees, officers and directors of, and consultants or advisors to, the Company and its parent and subsidiary corporations who are expected to contribute to the Company's future growth and success. Under the Plan recipients may be awarded both (i) Options (as defined in Section 2.1) to purchase the Company's common stock, par value \$.01 ("Common Stock"), and (ii) shares of the Company's Common Stock ("Restricted Stock Awards"). Except where the context otherwise requires, the term "Company" shall include the parent and all present and future subsidiaries of the Company as defined in Sections 424(e) and 424(f) of the Internal Revenue Code of 1986, as amended or replaced from time to time (the "Code"). Those provisions of the Plan which make express reference to Section 422 of the Code shall apply only to Incentive Stock Options (as that term is defined in the Plan). Appendix A to this Plan shall apply only to participants in the Plan who are residents of the State of California.

2. TYPES OF AWARDS AND ADMINISTRATION.

2.1 OPTIONS. Options granted pursuant to the Plan ("Options") shall be authorized by action of the Board of Directors of the Company and may be either incentive stock options ("Incentive Stock Options") meeting the requirements of Section 422 of the Code or non-statutory Options which are not intended to meet the requirements of Section 422. The vesting of Options may be conditioned upon the completion of a specified period of employment with the Company and/or such other conditions or events as the Board may determine. The Board may also provide that Options are immediately exercisable subject to certain repurchase rights in the Company dependent upon the continued employment of the optionee and/or such other conditions or event as the Board may determine.

2.1.1 INCENTIVE STOCK OPTIONS. All Options when granted are intended to be non-statutory Options, unless the applicable Option Agreement (as defined in Section 5.1) explicitly states that the Option is intended to be an Incentive Stock Option. Incentive Stock Options may only be granted to employees of the Company. For so long as the Code shall so provide, Options granted to any employee under the Plan (and any other incentive stock option plans of the Company) which are intended to constitute Incentive Stock Options shall not constitute Incentive Stock Options to the extent that such Options, in the aggregate, become exercisable for the first time in any one calendar year for shares of Common Stock with an aggregate fair market value (determined as of the respective date or dates of grant) of more than \$100,000. If an Option is intended to be an Incentive Stock Option, and if for any reason such Option (or any portion thereof) shall not qualify as an Incentive Stock Option, then, to the extent of such nonqualification, such Option (or portion thereof) shall be regarded as a non-statutory



Option appropriately granted under the Plan provided that such Option (or portion thereof) otherwise meets the Plan's requirements relating to non-statutory Options.

2.2 RESTRICTED STOCK AWARDS. The Board in its discretion may grant Restricted Stock Awards, entitling the recipient to acquire, for a purchase price determined by the Board, shares of Common Stock subject to such restrictions and conditions as the Board may determine at the time of grant ("Restricted Stock"), including continued employment and/or achievement of pre-established performance goals and objectives.

2.3 ADMINISTRATION. The Plan shall be administered by the Board of Directors of the Company, whose construction and interpretation of the terms and provisions of the Plan shall be final and conclusive. The Board of Directors may in its sole discretion issue Restricted Stock and grant Options to purchase shares of Common Stock, and issue shares upon exercise of such Options as provided in the Plan. The Board shall have authority, subject to the express provisions of the Plan, to construe Restricted Stock Agreements (as defined in Section 5.2), Option Agreements and the Plan, to prescribe, amend and rescind rules and regulations relating to the Plan, to determine the terms and provisions of Restricted Stock Agreements and Option Agreements, and to make all other determinations in the judgment of the Board of Directors necessary or desirable for the administration of the Plan. The Board of Directors may correct any defect or supply any omission or reconcile any inconsistency in the Plan or in any Restricted Stock Agreement or Option Agreement in the manner and to the extent it shall deem expedient to carry the Plan into effect and it shall be the sole and final judge of such expediency. No director or person acting pursuant to authority delegated by the Board of Directors shall be liable for any action or determination under the Plan made in good faith. The Board of Directors may, to the full extent permitted by or consistent with applicable laws or regulations (including, without limitation, applicable state law), delegate any or all of its powers under the Plan to a committee (the "Committee") appointed by the Board of Directors, and if the Committee is so appointed all references to the Board of Directors in the Plan shall mean and relate to such Committee.

### 3. ELIGIBILITY.

Options may be granted, and Restricted Stock may be issued, to persons who are, at the time of such grant or issuance, employees, officers or directors of, or consultants or advisors to, the Company; provided, that the class of persons to whom Incentive Stock Options may be granted shall be limited to employees of the Company.

3.1 10% SHAREHOLDER. If any employee to whom an Incentive Stock Option is to be granted is, at the time of the grant of such Option, the owner of stock possessing more than 10% of the total combined voting power of all classes of stock of the Company (after taking into account the attribution of stock ownership rules of Section 424(d) of the Code) ("10% Shareholder"), any Incentive Stock Option granted to such individual must: (i) have an exercise price per share of not less than 110% of the fair market value of one share of Common Stock at the time of grant; and (ii) expire by its terms not more than five years from the date of grant.

#### 4. STOCK SUBJECT TO PLAN.

Subject to adjustment as provided in Section 14.2 below, the maximum number of shares of Common Stock which may be issued under the Plan is 5,000,000 shares. If an Option shall expire or terminate for any reason without having been exercised in full, the unpurchased shares subject to such Option shall again be available for subsequent Option grants or Restricted Stock awards under the Plan. If shares of Restricted Stock shall be forfeited to, or otherwise repurchased by, the Company pursuant to a Restricted Stock Agreement, such purchased shares shall again be available for subsequent Option grants or Restricted Stock awards under the Plan. If shares issued upon exercise of an Option are tendered to the Company in payment of the exercise price of an Option, such tendered shares shall again be available for subsequent Option grants or Restricted stock awards under the Plan.

#### 5. FORMS OF RESTRICTED STOCK AGREEMENTS AND OPTION AGREEMENTS.

5.1 OPTION AGREEMENT. As a condition to the grant of an Option, each recipient of an Option shall execute an option agreement ("Option Agreement") in such form not inconsistent with the Plan as may be approved by the Board of Directors. Such Option Agreements may differ among recipients.

5.2 RESTRICTED STOCK AGREEMENT. As a condition to the issuance of Restricted Stock, each recipient thereof shall execute an agreement ("Restricted Stock Agreement") in such form not inconsistent with the Plan as may be approved by the Board of Directors. Such Restricted Stock Agreements may differ among recipients and need not be entitled "Restricted Stock Agreements."

5.3 "STAND-OFF" AGREEMENT. Unless the Board of Directors specifies otherwise, each Restricted Stock Agreement and Option Agreement shall provide that upon the request of the Company or the managing underwriter(s), the holder of any Option or the purchaser of any Restricted Stock shall, in connection with any registrations of securities of the Company, agree in writing that for a period of time (not to exceed 180 days) from the effective date of the Securities and Exchange Commission registration statement for such offering, the holder or purchaser will not sell, make any short sale of, loan, grant any option for the purchase of, or otherwise dispose of any shares of the common stock of the Company owned or controlled by him.

#### 6. PURCHASE PRICE.

6.1 GENERAL. The purchase price per share of Restricted Stock and per share of stock deliverable upon the exercise of an Option shall be determined by the Board of Directors, provided, however, that in the case of an Incentive Stock Option, the exercise price shall not be less than 100% of the fair market value of such stock, as determined by the Board of Directors, at the time of grant of such Option, or less than 110% of such fair market value in the case of any Incentive Stock Option granted to a 10% Shareholder.

6.2 PAYMENT OF PURCHASE PRICE. Option Agreements may provide for the payment of the exercise price by (i) delivery of a personal, certified or bank check or postal money order payable to the order of the Company in an amount equal to the exercise price of

such Option, (ii) delivery to the Company of shares of Common Stock of the Company already owned by the optionee for a period of six months and having a fair market value equal in amount to the exercise price of the Option being exercised, (iii) a personal recourse note issued by the optionee to the Company in a principal amount equal to such aggregate exercise price and with such other terms, including interest rate and maturity, as the Company may determine in its discretion; provided, however, that the interest rate borne by such note shall not be less than the lowest applicable federal rate, as defined in Section 1274(d) of the Code, (iv) any other means which the Board of Directors determines are consistent with the purpose of the Plan and with applicable laws and regulations or (v) any combination of such methods of payment. The fair market value of any shares of Common Stock or other non-cash consideration which may be delivered upon exercise of an Option shall be determined by the Board of Directors. Restricted Stock Agreements may provide for the payment of any purchase price in any manner approved by the Board of Directors at the time of authorizing the issuance thereof.

#### 7. OPTION PERIOD.

Notwithstanding any other provision of the Plan or any Option Agreement, each Option and all rights thereunder shall expire on the date specified in the applicable Option Agreement, provided that such date shall not be later than 10 years after the date on which the Option is granted (or five years in the case of an Incentive Stock Option granted to a 10% Shareholder), and in either case, shall be subject to earlier termination as provided in the Plan.

#### 8. EXERCISE OF OPTIONS.

8.1 GENERAL. Each Option shall be exercisable either in full or in installments at such time or times and during such period as shall be set forth in the agreement evidencing such Option, subject to the provisions of the Plan. To the extent not exercised, installments shall accumulate and be exercisable, in whole or in part, at any time after becoming exercisable, but not later than the date the Option expires.

8.2 NOTICE OF EXERCISE. Any option granted under the Plan may be exercised by the optionee by delivering to the Company on any business day a written notice specifying the number of Common Shares the optionee then desires to purchase (the "Notice"), accompanied by payment for such shares.

8.3 DELIVERY. As promptly as practicable after receipt of such written notification and payment, the Company shall deliver or cause to be delivered to the optionee certificates for the number of shares with respect to which such Option has been so exercised, issued in the optionee's name or, at the Company's election, the Company shall deposit such shares into an electronic share account maintained for the benefit of the optionee; provided, however, that such delivery of certificates shall be deemed effected for all purposes when the Company or a stock transfer agent shall have deposited such certificates in the United States mail, addressed to the optionee, at the address specified in the Notice; and that such deposit of shares shall be deemed effected for all purposes when the deposit is reflected in the optionee's account.

9. NONTRANSFERABILITY OF OPTIONS.

No Option shall be assignable or transferable by the person to whom it is granted, either voluntarily or by operation of law, except by will or the laws of descent and distribution. During the life of an optionee, an Option shall be exercisable only by the optionee.

10. TERMINATION OF EMPLOYMENT; DISABILITY; DEATH. Except as may be otherwise expressly provided in the terms and conditions of the Option Agreement, Options shall terminate on the earliest to occur of:

- (i) the date of expiration thereof;
- (ii) immediately upon termination of the optionee's employment with or services to the Company by the Company for Cause (as hereinafter defined), or upon voluntary termination of employment by the optionee (other than for death or permanent disability as defined below); or
- (iii) 90 days after the date of termination of the optionee's employment with or services to the Company by the Company without Cause (other than for death or permanent and total disability as defined below).

Until the date on which the Option so expires, the optionee may exercise that portion of his Option which is exercisable at the time of termination of the employment or service relationship.

An employment relationship between the Company and the optionee shall be deemed to exist during any period during which the optionee is employed by the Company or by a parent or any Subsidiary of the Company. Whether an authorized leave of absence or an absence due to military or government service shall constitute termination of the employment relationship between the Company and the optionee shall be determined by the Board at the time thereof.

For purposes of this Section 10, the term "Cause" shall mean (a) any material breach by the optionee of any agreement to which the optionee and the Company are both parties, (b) any act (other than retirement) or omission to act by the optionee which may have a material and adverse effect on the Company's business or on the optionee's ability to perform services for the Company, including, without limitation, the commission of any crime (other than minor traffic violations), or (c) any material misconduct or material neglect of duties by the optionee in connection with the business or affairs of the Company, its parent or any Subsidiary or affiliate of the Company.

In the event of the permanent and total disability or death of an optionee while in an employment or other relationship with the Company and before the date of expiration of such option, such option shall terminate on the earlier of such date of expiration or one year following the date of such disability or death. After disability or death, the optionee (or in the case of death, his executor, administrator or any person or persons to whom his option may be transferred by will or by laws of descent and distribution) shall have the right, at any time prior to such termination, to exercise the option to the extent the optionee was entitled to exercise such

option as of the date of his disability or death. An optionee is permanently and totally disabled if he is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to last for a continuous period of not less than 12 months; permanent and total disability shall be determined in accordance with Section 22(e)(3) of the Code and the regulations issued thereunder.

11. RIGHTS AS A SHAREHOLDER. The holder of an Option shall have no rights as a shareholder with respect to any shares covered by the Option (including, without limitation, any rights to receive dividends or non-cash distributions with respect to such shares) until the date of issue of a stock certificate to him or her for such shares or the date of deposit of such shares in an electronic deposit account for the benefit of him or her. No adjustment shall be made for dividends or other rights for which the record date is prior to the date such stock certificate is issued or such shares deposited.

12. ADDITIONAL PROVISIONS. The Board of Directors may, in its sole discretion, include additional provisions in Restricted Stock Agreements and Option Agreements, including, without limitation, restrictions on transfer, rights of the Company to repurchase shares of Restricted Stock or shares of Common Stock acquired upon exercise of Options, commitments to pay cash bonuses, to make, arrange for or guaranty loans or to transfer other property to optionees upon exercise of Options, or such other provisions as shall be determined by the Board of Directors; provided that such additional provisions shall not be inconsistent with any other term or condition of the Plan and such additional provisions shall not be such as to cause any Incentive Stock Option to fail to qualify as an Incentive Stock Option within the meaning of Section 422 of the Code.

13. ACCELERATION, EXTENSION, ETC. The Board of Directors may, in its sole discretion, (i) accelerate the date or dates on which all or any particular Option or Options may be exercised or (ii) extend the dates during which all, or any particular, Option or Options may be exercised.

#### 14. ADJUSTMENT UPON CHANGES IN CAPITALIZATION

14.1 NO EFFECT OF OPTIONS UPON CERTAIN CORPORATE TRANSACTIONS. The existence of outstanding Options shall not affect in any way the right or power of the Company to make or authorize any or all adjustments, recapitalizations, reorganizations or other changes in the Company's capital structure or its business, or any merger or consolidation, or any issue of Common Shares, or any issue of bonds, debentures, preferred or prior preference stock ahead of or affecting the Common Shares or the rights thereof, or the dissolution or liquidation of the Company, or any sale or transfer of all or any part of its assets or business, or any other corporate act or proceeding, whether of a similar character or otherwise.

14.2 ADJUSTMENT PROVISIONS. If, through or as a result of any merger, consolidation, sale of all or substantially all of the assets of the Company, reorganization, recapitalization, reclassification, stock dividend, stock split, reverse stock split or other similar transaction, (i) the outstanding shares of Common Stock are increased, decreased or exchanged for a different number or kind of shares or other securities of the Company, or (ii) additional shares or new or different shares or other securities of the Company or other non-cash assets are distributed with respect to such shares of Common Stock or other securities, an appropriate and

proportionate adjustment may be made in (x) the maximum number and kind of shares reserved for issuance under the Plan, (y) the number and kind of shares or other securities subject to any then outstanding Options, and (z) the price for each share subject to any then outstanding Options, without changing the aggregate purchase price as to which such Options remain exercisable. Notwithstanding the foregoing, no adjustment shall be made pursuant to this Section 14 if such adjustment would cause the Plan to fail to comply with Section 422 of the Code.

14.3 NO ADJUSTMENT IN CERTAIN CASES. Except as hereinbefore expressly provided, the issue by the Company of shares of stock of any class, or securities convertible into shares of stock of any class, for cash or property or for labor or services, either upon direct sale or upon the exercise of rights or warrants to subscribe therefore, or upon conversion of shares or obligations of the Company convertible into such shares or other securities, shall not affect, and no adjustment by reason thereof shall be made with respect to, the number or price of shares of Common Stock then subject to outstanding options.

14.4 BOARD AUTHORITY TO MAKE ADJUSTMENTS. Any adjustments under this Section 14 will be made by the Board of Directors, whose determination as to what adjustments, if any, will be made and the extent thereof will be final, binding and conclusive. No fractional shares will be issued under the Plan on account of any such adjustments.

#### 15. EFFECT OF CERTAIN TRANSACTIONS

15.1 GENERAL. In the event of a consolidation or merger or sale of all or substantially all of the assets of the Company in which outstanding shares of Common Stock are exchanged for securities, cash or other property of any other corporation or business entity, or in the event of a liquidation of the Company, the Board of Directors of the Company, or the board of directors of any corporation assuming the obligations of the Company, may, in its discretion, take any one or more of the following actions, as to some or all outstanding Options (and need not take the same action as to each such Option): (i) provide that such Options shall be assumed, or equivalent Options shall be substituted, by the acquiring or succeeding corporation (or an affiliate thereof), provided that any such Options substituted for Incentive Stock Options shall meet the requirements of Section 424(a) of the Code, (ii) upon written notice to the optionees, provide that all unexercised Options will terminate immediately prior to the consummation of such transaction unless exercised by the optionee (to the extent otherwise then exercisable) within a specified period following the date of such notice, (iii) in the event of a merger under the terms of which holders of the Common Stock of the Company will receive upon consummation thereof a cash payment for each share surrendered in the merger (the "Merger Price"), make or provide for a cash payment to the optionees equal to the difference between (A) the Merger Price times the number of shares of Common Stock subject to such outstanding Options (to the extent then exercisable at prices not in excess of the Merger Price) and (B) the aggregate exercise price of all such outstanding Options, in exchange for the termination of such Options, and (iv) provide that all or any outstanding Options shall become exercisable in full immediately prior to such event.

15.2 SUBSTITUTE OPTIONS. The Company may grant Options in substitution for Options held by employees of another corporation who become employees of the Company, or a

subsidiary of the Company, as the result of a merger or consolidation of the employing corporation with the Company or a subsidiary of the Company, or as a result of the acquisition by the Company, or one of its subsidiaries, of property or stock of the employing corporation. The Company may direct that substitute Options be granted on such terms and conditions as the Board of Directors considers appropriate in the circumstances.

15.3 RESTRICTED STOCK. In the event of a business combination or other transaction of the type detailed in Section 15.1, any securities, cash or other property received in exchange for shares of Restricted Stock shall continue to be governed by the provisions of any Restricted Stock Agreement pursuant to which they were issued, including any provision regarding vesting, and such securities, cash, or other property may be held in escrow on such terms as the Board of Directors may direct, to insure compliance with the terms of any such Restricted Stock Agreement.

16. NO SPECIAL EMPLOYMENT RIGHTS. Nothing contained in the Plan or in any Option or Restricted Stock Agreement shall confer upon any optionee any right with respect to the continuation of his or her employment by the Company or interfere in any way with the right of the Company at any time to terminate such employment or to increase or decrease the compensation of the optionee.

17. OTHER EMPLOYEE BENEFITS. The amount of any compensation deemed to be received by an employee as a result of the issuance of shares of Restricted Stock or the grant or exercise of an Option or the sale of shares received upon such award or exercise will not constitute compensation with respect to which any other employee benefits of such employee are determined, including, without limitation, benefits under any bonus, pension, profit-sharing, life insurance or salary continuation plan, except as otherwise specifically determined by the Board of Directors.

#### 18. AMENDMENT OF THE PLAN.

18.1 The Board of Directors may at any time, and from time to time, modify or amend the Plan in any respect, except that if at any time the approval of the shareholders of the Company is required under Section 422 of the Code or any successor provision with respect to Incentive Stock Options, the Board of Directors may not effect such modification or amendment without such approval.

18.2 The termination or any modification or amendment of the Plan shall not, without the consent of an optionee or the recipient of Restricted Stock, affect his or her rights under an Option or Restricted Stock award previously granted to him or her. With the consent of the recipient of Restricted Stock or optionee affected, the Board of Directors may amend outstanding Restricted Stock Agreements or Option Agreements in a manner not inconsistent with the Plan. The Board of Directors shall have the right to amend or modify the terms and provisions of the Plan and of any outstanding Incentive Stock Options to the extent necessary to qualify any or all such Options for such favorable federal income tax treatment (including deferral of taxation upon exercise) as may be afforded incentive stock options under Section 422 of the Code.

19. WITHHOLDING. The Company shall have the right to deduct from payments of any kind otherwise due to the optionee or recipient of Restricted Stock, any federal, state or local taxes of any kind required by law to be withheld with respect to issuance of any shares of Restricted Stock or shares issued upon exercise of Options. Subject to the prior approval of the Company, which may be withheld by the Company in its sole discretion, the obligor may elect to satisfy such minimum withholding obligations, in whole or in part, (i) by causing the Company to withhold shares of Common Stock otherwise issuable or (ii) by delivering to the Company shares of Common Stock already owned by the obligor. The shares so delivered or withheld shall have a fair market value equal to such withholding obligation. The fair market value of the shares used to satisfy such withholding obligation shall be determined by the Company as of the date that the amount of tax to be withheld is to be determined. A person who has made an election pursuant to this Section 19 may only satisfy his or her withholding obligation with shares of Common Stock which are not subject to any repurchase, forfeiture, unfulfilled vesting or other similar requirements.

20. EFFECTIVE DATE AND DURATION OF THE PLAN.

20.1 EFFECTIVE DATE. The Plan shall become effective when adopted by the Board of Directors, but no Incentive Stock Option shall become exercisable unless and until the Plan shall have been approved by the Company's shareholders. If such shareholder approval is not obtained within twelve months after the date of the Board's adoption of the Plan, no Options previously granted under the Plan shall be deemed to be Incentive Stock Options and no Incentive Stock Options shall be granted thereafter. Amendments to the Plan not requiring shareholder approval shall become effective when adopted by the Board of Directors; amendments requiring shareholder approval (as provided in Section 18.1) shall become effective when adopted by the Board of Directors, but no Incentive Stock Option granted after the date of such amendment shall become exercisable (to the extent that such amendment to the Plan was required to enable the Company to grant such Incentive Stock Option to a particular optionee) unless and until such amendment shall have been approved by the Company's shareholders. If such shareholder approval is not obtained within twelve months of the Board's adoption of such amendment, any Incentive Stock Options granted on or after the date of such amendment shall terminate to the extent that such amendment to the Plan was required to enable the Company to grant such Option to a particular optionee. Subject to this limitation, Options may be granted under the Plan at any time after the effective date and before the date fixed for termination of the Plan.

20.2 TERMINATION. Unless sooner terminated by action of the Board of Directors, the Plan shall terminate upon the close of business on the day next preceding the tenth anniversary of the date of its adoption by the Board of Directors.

21. PROVISION FOR FOREIGN PARTICIPANTS. The Board of Directors may, without amending the Plan, modify the terms of Option or Restricted Stock Agreements to differ from those specified in the Plan with respect to participants who are foreign nationals or employed outside the United States to recognize differences in laws, rules, regulations or customs of such foreign jurisdictions with respect to tax, securities, currency, employee benefit or other matters.



22. REQUIREMENTS OF LAW. The Company shall not be required to sell or issue any shares under any Option or Restricted Stock Agreement if the issuance of such shares shall constitute a violation by the optionee or by the Company of any provisions of any law or regulation of any governmental authority. In addition, in connection with the Securities Act of 1933, as now in effect or hereafter amended (the "Act"), the Company shall not be required to issue any shares upon exercise of any Option unless the Company has received evidence satisfactory to it to the effect that the holder of such Option will not transfer such shares except pursuant to a registration statement in effect under the Act or unless an opinion of counsel satisfactory to the Company has been received by the Company to the effect that such registration is not required in connection with any such transfer. Any determination in this connection by the Board shall be final, binding and conclusive. In the event the shares issuable on exercise of an Option are not registered under the Act or under the securities laws of each relevant state or other jurisdiction, the Company may imprint on the certificate(s) appropriate legends that counsel for the Company considers necessary or advisable to comply with the Act or any such state or other securities law and in the instance of shares that are deposited in an electronic account, the Company may restrict transactions associated with such shares as the Company considers necessary or advisable to comply with the Act or any such state or other securities law. The Company may register, but in no event shall be obligated to register, any securities covered by the Plan pursuant to the Act; and in the event any shares are so registered the Company may remove any legend on certificates representing such shares and remove any restrictions on transactions associated with such shares. The Company shall not be obligated to take any affirmative action in order to cause the exercise of an Option or the issuance of shares pursuant thereto to comply with any law or regulation of any governmental authority.

23. GOVERNING LAW. This Plan and each Option or Restricted Stock Agreement shall be governed by the laws of the Commonwealth of Massachusetts, without regard to its principles of conflicts of law.

APPENDIX A  
TO PEERDIRECT CORPORATION 2003 STOCK INCENTIVE PLAN  
FOR CALIFORNIA RESIDENTS ONLY

This Appendix to the PeerDirect Corporation 2003 Stock Incentive Plan (the "Plan") shall have application only to participants in the Plan who are residents of the State of California. Capitalized terms contained herein shall have the same meanings given to them in the Plan, unless otherwise provided in this Appendix. NOTWITHSTANDING ANY PROVISION CONTAINED IN THE PLAN TO THE CONTRARY AND TO THE EXTENT REQUIRED BY APPLICABLE LAW, THE FOLLOWING TERMS AND CONDITIONS SHALL APPLY TO ALL OPTIONS AND RESTRICTED STOCK AWARDS (COLLECTIVELY "AWARDS") GRANTED TO RESIDENTS OF THE STATE OF CALIFORNIA, UNTIL SUCH TIME AS THE COMMON STOCK BECOMES SUBJECT TO REGISTRATION UNDER THE SECURITIES ACT OF 1933:

1. Nonqualified Stock Options shall have an exercise price that is not less than 85% of the Fair Market Value of the stock at the time the Option is granted, as determined by the Board, except that the exercise price shall be 110% of the Fair Market Value in the case of any person who owns stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or its parent or subsidiary corporations.

2. The purchase price for any Stock Awards that may be purchased under the Plan ("Stock Purchase Rights") shall be at least 85% of the Fair Market Value of the Common Stock at the time the Participant is granted the Stock Purchase Right or at the time the purchase is consummated. Notwithstanding the foregoing, the purchase price shall be 100% of the Fair Market Value of the Common Stock at the time the Participant is granted the Stock Purchase Right or at the time the purchase is consummated in the case of any person who owns stock possessing more than 10% of the total combined voting power of all classes of stock of the Company or its parent or subsidiary corporations.

3. Options shall have a term of not more than ten years from the date the Option is granted.

4. Awards shall be nontransferable other than by will or the laws of descent and distribution. Notwithstanding the foregoing, and to the extent permitted by Section 422 of the Code, the Plan Administrator, in its discretion, may permit distribution of an Option to an inter vivos or testamentary trust in which the Option is to be passed to beneficiaries upon the death of the trustor (settlor), or by gift to "immediate family" as that term is defined in Rule 16a-1(e) of the Exchange Act.

5. Options shall become exercisable at the rate of at least 20% per year over five years from the date the Option is granted, subject to reasonable conditions such as continued employment. However, in the case of an Option granted to officers, directors or consultants of the Company or any of its affiliates, the Option may become fully exercisable, subject to reasonable conditions such as continued employment, at any time or during any period established by the Company or any of its affiliates.

6. Unless employment is terminated for Cause, the right to exercise an Option in the event of termination of employment, to the extent that the Participant is otherwise entitled to exercise an Option on the date employment terminates, shall be

(a) at least six months from the date of termination of employment if termination was caused by death or Disability; and

(b) at least 30 days from the date of termination if termination of employment was caused by other than death or Disability;

(c) but in no event later than the remaining term of the Option.

7. No Award may be granted to a resident of California more than ten years after the earlier of the date of adoption of the Plan and the date the Plan is approved by the shareholders.

8. Any Award exercised before shareholder approval is obtained shall be rescinded if shareholder approval is not obtained within 12 months before or after the Plan is adopted. Such shares shall not be counted in determining whether such approval is obtained.

9. The Company shall provide annual financial statements of the Company to each California resident holding an outstanding Award under the Plan. Such financial statements need not be audited and need not be issued to key employees whose duties at the Company assure them access to equivalent information.

10. Any right of repurchase on behalf of the Company in the event of a Participant's termination of employment shall be at a purchase price that is (a) not less than the Fair Market Value of the securities upon termination of employment, and the right to repurchase shall be exercised for cash or cancellation of purchase money indebtedness for the shares within 90 days of termination of employment (or in the case of securities issued upon exercise of Options after the date of termination, within 90 days after the date of the exercise), and the right shall terminate when the stock at issue becomes publicly traded; or (b) at the original purchase price, provided that the right to repurchase at the original purchase price lapses at the rate of at least 20% of the shares per year over five years from the date the Option or Stock Purchase Right is granted (without respect to the date the Option or Stock Purchase Right was exercised or became exercisable) and the right to repurchase shall be exercised for cash or cancellation of purchase money indebtedness for the shares within 90 days of termination of employment (or in the case of securities issued upon exercise of Options after the date of termination, within 90 days after the date of the exercise). In addition to the restrictions set forth in clauses (a) and (b), the securities held by an officer, direct or consultant of the Company or an affiliate of the Company may be subject to additional or greater restrictions.

## PROGRESS SOFTWARE CORPORATION

## 2004 INDUCEMENT STOCK PLAN

SECTION 1. General Purpose of the Plan; Definitions. The name of the plan is the Progress Software Corporation 2004 Inducement Stock Plan (the "Plan"). The purpose of the Plan is to encourage and enable employees of Progress Software Corporation, a Massachusetts corporation (the "Company"), and its Subsidiaries to acquire a proprietary interest in the Company. It is anticipated that providing employees with a direct stake in the Company's welfare will assure a closer identification of their interests with those of the Company and its stockholders, thereby stimulating their efforts on the Company's behalf and strengthening their desire to remain with the Company. The Company intends that the Plan be reserved for persons to whom the Company may issue securities without stockholder approval as an inducement pursuant to Rule 4350(i)(1)(A)(iv) of the Marketplace Rules of the Nasdaq Stock Market, Inc. The Company intends that this purpose will be effected by the granting of Awards (as defined below) under the Plan.

The following terms shall be defined as set forth below:

"Affiliate" means any company in an "affiliated group," as such term is defined in Section 1504(a) of the Code, which includes the Company.

"Award" or "Awards," except where referring to a particular category of grant under the Plan, shall include Non-Statutory Stock Options, Restricted Stock Awards, Unrestricted Stock Awards and Performance Share Awards.

"Board" means the Board of Directors of the Company.

"Cause" means (i) any material breach by the participant of any agreement to which the participant and the Company are both parties, (ii) any act or omission to act by the participant which may have a material and adverse effect on the Company's business or on the participant's ability to perform services for the Company, including, without limitation, the commission of any crime (other than ordinary traffic violations), or (iii) any material misconduct or material neglect of duties by the participant in connection with the business or affairs of the Company or any affiliate of the Company.

"Change of Control" shall have the meaning set forth in Section 15.

"Code" means the Internal Revenue Code of 1986, as amended, and any successor code, and related rules, regulations and interpretations.

"Committee" shall mean the Board or, if appointed by the Board, a committee of not less than two (2) directors. It is the intention of the Company that the Plan shall be administered by "non-employee directors" within the meaning of Rule 16b-3 under the Securities Exchange Act of 1934, as amended, but the authority and validity of any act taken or not taken by the

Committee shall not be affected if any director administering the Plan is not a non-employee director.

"Disability" means disability as set forth in Section 22(e)(3) of the Code.

"Effective Date" means the date on which the Plan is adopted by the Board as set forth in Section 17.

"Eligible Persons" shall have the meaning set forth in Section 4.

"Fair Market Value" on any given date means the closing price per share of the Stock on such date as reported by a nationally recognized stock exchange, or, if the Stock is not listed on such an exchange, as reported by the Nasdaq Stock Market, or, if the Stock is not quoted by the Nasdaq Stock Market, the fair market value of the Stock as determined by the Committee.

"Non-Statutory Stock Option" means any stock option that is not an incentive stock option as defined in Section 422 of the Code.

"Normal Retirement" means retirement from active employment with the Company and its Subsidiaries in accordance with the retirement policies of the Company and its Subsidiaries then in effect.

"Officer" means an officer as defined in Rule 16a-1(f) of the Securities Exchange Act of 1934, as amended.

"Performance Share Award" means an Award granted pursuant to Section 8.

"Restricted Stock" shall have the meaning set forth in Section 6.

"Restricted Stock Award" means an Award granted pursuant to Section 6.

"Stock" means the common stock, \$0.01 par value per share, of the Company, subject to adjustments pursuant to Section 3.

"Stock Option" means any option to purchase shares of Stock granted pursuant to Section 5.

"Subsidiary" means a subsidiary as defined in Section 424 of the Code.

"Unrestricted Stock Award" means an award granted pursuant to Section 7.

SECTION 2. Administration of Plan; Committee Authority to Select Participants and Determine Awards.

(a) Committee. The Plan shall be administered by the Committee. The Committee shall select one of its members as its chairman and shall hold its meetings at such times and places as it shall deem advisable. A majority of its members shall constitute a quorum, and all actions of the Committee shall require the affirmative vote of a majority of its members. Any action may be taken by a written instrument signed by all of the members, and any action so

taken shall be as fully effective as if it had been taken by a vote of a majority of the members at a meeting duly called and held. Except as specifically reserved to the Board under the terms of the Plan, the Committee shall have full and final authority to operate, manage and administer the Plan on behalf of the Company. Action by the Committee shall require the affirmative vote of a majority of all members thereof.

(b) Powers of Committee. The Committee shall have the power and authority to grant and modify Awards consistent with the terms of the Plan, including the power and authority:

(i) to select the persons to whom Awards may from time to time be granted;

(ii) to determine the time or times of grant, and the extent, if any, of Non-Statutory Stock Options, Restricted Stock Awards, Unrestricted Stock Awards and Performance Share Awards, or any combination of the foregoing, granted to any one or more participants;

(iii) to determine the number of shares to be covered by any Award;

(iv) to determine and modify the terms and conditions, including restrictions, not inconsistent with the terms of the Plan, of any Award, which terms and conditions may differ among individual Awards and participants, and to approve the form of written instruments evidencing the Awards; provided, however, that no such action shall adversely affect rights under any outstanding Award without the participant's consent;

(v) to accelerate the exercisability or vesting of all or any portion of any Award;

(vi) subject to the provisions of Section 5(b), to extend the period in which any outstanding Stock Option may be exercised;

(vii) to determine whether, to what extent, and under what circumstances Stock and other amounts payable with respect to an Award shall be deferred either automatically or at the election of the participant and whether and to what extent the Company shall pay or credit amounts equal to interest (at rates determined by the Committee) or dividends or deemed dividends on such deferrals;

(viii) to delegate to other persons the responsibility for performing ministerial actions in furtherance of the Plan's purpose; and

(ix) to adopt, alter and repeal such rules, guidelines and practices for administration of the Plan and for its own acts and proceedings as it shall deem advisable; to interpret the terms and provisions of the Plan and any Award (including related written instruments); to make all determinations it deems advisable for the administration of the Plan; to decide all disputes arising in connection with the Plan; and to otherwise supervise the administration of the Plan.

All decisions and interpretations of the Committee shall be binding on all persons, including the Company and Plan participants.

SECTION 3. Shares Issuable under the Plan; Mergers; Substitution.

(a) Shares Issuable. The maximum number of shares of Stock with respect to which Awards may be granted under the Plan, subject to adjustment upon changes in capitalization of the Company as provided in this Section 3, shall be 200,000 shares of Stock. For purposes of this limitation, if any shares of Stock covered by an Award granted under the Plan, or to which such an Award relates, are repurchased or forfeited, or if an Award has expired, terminated or been canceled for any reason whatsoever (other than by reason of exercise or vesting), then such shares of Stock or the shares of Stock covered by such Award, as the case may be, shall be added back to the shares of Stock with respect to which Awards may be granted under the Plan. Subject to such overall limitation, any type or types of Award may be granted with respect to shares of Stock. Shares of Stock issued under the Plan may be authorized but unissued shares or shares reacquired by the Company.

(b) Stock Dividends, Mergers, etc. In the event that the Company effects a stock dividend, stock split or similar change in capitalization affecting the Stock, the Committee shall make appropriate adjustments in (i) the number and kind of shares of stock or securities with respect to which Awards may thereafter be granted (including without limitation the limitations set forth in Section 3(a) above), (ii) the number and kind of shares remaining subject to outstanding Awards, and (iii) the option or purchase price in respect of such shares. In the event of the merger, consolidation, dissolution or liquidation of the Company, the Committee in its sole discretion may, as to any outstanding Awards, make such substitution or adjustment in the aggregate number of shares reserved for issuance under the Plan and in the number and purchase price (if any) of shares subject to such Awards as it may determine and as may be permitted by the terms of such transaction, or accelerate, amend or terminate such Awards upon such terms and conditions as it shall provide (which, in the case of the termination of the vested portion of any Award, shall require payment or other consideration which the Committee deems equitable in the circumstances).

(c) Substitute Awards. The Committee may grant Awards under the Plan by assumption of or in substitution for stock and stock-based awards granted or issued by another company to its directors, officers, employees, consultants and other service providers if such persons become Eligible Persons in connection with an acquisition of that company or any division thereof by the Company, whether by merger, consolidation, purchase of stock, purchase of assets or otherwise. The Committee may direct that the substitute awards be granted on such terms and conditions as the Committee considers appropriate in the circumstances. Shares which may be delivered under such substitute awards may be in addition to the maximum number of shares provided for in Section 3(a).

SECTION 4. Eligibility. Awards may be granted only to persons to whom the Company may issue securities without stockholder approval in accordance with Rule 4350(i)(1)(A)(iv) of the Marketplace Rules of the Nasdaq Stock Market, Inc. ("Eligible Persons"), provided, however, that members of the Board and Officers are not eligible to receive Awards under the Plan.

SECTION 5. Stock Options. The Committee may grant Stock Options to Eligible Persons pursuant to the Plan. Any Stock Option granted under the Plan shall be in writing and in such form as the Committee may from time to time approve. Stock Options granted under the Plan shall be Non-Statutory Stock Options.

The Committee in its discretion may determine the effective date of Stock Options. Stock Options granted pursuant to this Section 5 shall be subject to the following terms and conditions and the terms and conditions of Section 9 and shall contain such additional terms and conditions, not inconsistent with the terms of the Plan, as the Committee shall deem desirable:

(a) Exercise Price. The exercise price per share for the Stock covered by a Stock Option granted pursuant to this Section 5 shall be determined by the Committee at the time of grant; provided, however, that the exercise price shall not be less than Fair Market Value on the date of grant.

(b) Option Term. The term of each Stock Option shall be fixed by the Committee, but no Stock Option shall be exercisable more than ten (10) years after the date the Stock Option is granted.

(c) Exercisability; Rights of a Stockholder. Stock Options shall become vested and exercisable at such time or times, whether or not in installments, and upon such conditions, as shall be determined by the Committee at or after the grant date. The Committee may at any time accelerate the exercisability of all or any portion of any Stock Option. An optionee shall have the rights of a stockholder only as to shares acquired upon the exercise of a Stock Option and not as to unexercised Stock Options.

(d) Method of Exercise. Stock Options may be exercised in whole or in part, by delivering written notice of exercise to the Company, specifying the number of shares to be purchased. Payment of the purchase price may be made by one or more of the following methods:

(i) in cash, by certified or bank check or other instrument acceptable to the Committee;

(ii) with the consent of the Committee, in the form of shares of Stock owned by the optionee for a period of at least six (6) months and not then subject to restrictions. Such surrendered shares shall be valued at Fair Market Value on the exercise date;

(iii) with the consent of the Committee, by the optionee delivering to the Company a properly executed exercise notice together with irrevocable instructions to a broker to promptly deliver to the Company cash or a check payable and acceptable to the Company to pay the purchase price; provided that in the event the optionee chooses to pay the purchase price as so provided, the optionee and the broker shall comply with such procedures and enter into such agreements of indemnity and other agreements as the Committee shall prescribe as a condition of such payment procedure. The Company need not act upon such exercise notice until the Company receives full payment of the exercise price; or



(iv) by any other means (including, without limitation, by delivery of a promissory note of the optionee payable on such terms as are specified by the Committee; provided, however, that the interest rate borne by such note shall not be less than the lowest applicable federal rate, as defined in Section 1247(d) of the Code) which the Committee determines are consistent with the purpose of the Plan and with applicable laws and regulations.

The delivery of certificates representing shares of Stock to be purchased pursuant to the exercise of a Stock Option will be contingent upon receipt from the optionee (or a purchaser acting in his stead in accordance with the provisions of the Stock Option) by the Company of the full purchase price for such shares and the fulfillment of any other requirements contained in the Stock Option or imposed by applicable laws and regulations, as determined by the Committee in its sole discretion.

(e) Transferability of Options. No Stock Option shall be transferable by the optionee otherwise than by will or by the laws of descent and distribution, and all Stock Options shall be exercisable, during the optionee's lifetime, only by the optionee or his or her legal representative; provided, however, that the Committee may, in the manner established by the Committee, permit the transfer, without payment of consideration, of a Non-Statutory Stock Option by an optionee to a member of the optionee's immediate family or to a trust or partnership whose beneficiaries are members of the optionee's immediate family; and such transferee shall remain subject to all the terms and conditions applicable to the option prior to the transfer. For purposes of this provision, an optionee's "immediate family" shall mean the holder's spouse, children and grandchildren.

(f) Form of Settlement. Shares of Stock issued upon exercise of a Stock Option shall be free of all restrictions under the Plan, except as otherwise provided in this Plan or in the terms of such Stock Option.

#### SECTION 6. Restricted Stock Awards.

(a) Nature of Restricted Stock Award. The Committee in its discretion may grant Restricted Stock Awards to any Eligible Person, entitling the recipient to acquire, for a purchase price determined by the Committee (but not less than Fair Market Value on the date of grant), shares of Stock subject to such restrictions and conditions as the Committee may determine at the time of grant ("Restricted Stock"), including continued employment and/or achievement of pre-established performance goals and objectives.

(b) Acceptance of Award. A participant who is granted a Restricted Stock Award shall have no rights with respect to such Award unless the participant shall have accepted the Award within ten (10) days (or such shorter date as the Committee may specify) following the delivery of written notice to the participant of the Award by making payment to the Company of the specified purchase price of the shares covered by the Award and by executing and delivering to the Company a written instrument that sets forth the terms and conditions applicable to the Restricted Stock in such form as the Committee shall determine.

(c) Rights as a Stockholder. Upon complying with Section 6(b) above, a participant shall have all the rights of a stockholder with respect to the Restricted Stock, including voting and dividend rights, subject to non-transferability restrictions and Company repurchase rights described in this Section 6 and subject to such other conditions contained in the written instrument evidencing the Restricted Stock Award. Unless the Committee shall otherwise determine, certificates evidencing shares of Restricted Stock shall remain in the possession of the Company until such shares are vested as provided in Section 6(e) below.

(d) Restrictions. Shares of Restricted Stock may not be sold, assigned, transferred, pledged or otherwise encumbered or disposed of except as specifically provided herein. In the event of termination of employment with or services to the Company and its Subsidiaries for any reason (including death, Disability, Normal Retirement, and voluntary termination by the participant), the Company shall have the right, at the discretion of the Committee, to repurchase shares of Restricted Stock with respect to which conditions have not lapsed at their purchase price from the participant or the participant's legal representative. The Company must exercise such right of repurchase within sixty (60) days following such termination of employment (unless otherwise specified in the written instrument evidencing the Restricted Stock Award).

(e) Vesting of Restricted Stock. The Committee at the time of grant shall specify the date or dates and/or the attainment of pre-established performance goals, objectives and other conditions on which the non-transferability of the Restricted Stock and the Company's right of repurchase shall lapse. Subsequent to such date or dates and/or the attainment of such pre-established performance goals, objectives and other conditions, the shares on which all restrictions have lapsed shall no longer be Restricted Stock and shall be deemed "vested." Subject to Section 12, the Committee at any time may accelerate such date or dates and otherwise waive or amend any conditions of the Award.

(f) Waiver, Deferral and Reinvestment of Dividends. The written instrument evidencing the Restricted Stock Award may require or permit the immediate payment, waiver, deferral or investment of dividends paid on the Restricted Stock.

#### SECTION 7. Unrestricted Stock Awards.

(a) Grant or Sale of Unrestricted Stock. The Committee in its discretion may grant or sell to any Eligible Person shares of Stock free of any restrictions under the Plan ("Unrestricted Stock") at a purchase price determined by the Committee. Shares of Unrestricted Stock may be granted or sold as described in the preceding sentence in respect of past services or other valid consideration.

(b) Restrictions on Transfers. The right to receive Unrestricted Stock may not be sold, assigned, transferred, pledged or otherwise encumbered, other than by will or the laws of descent and distribution.

SECTION 8. Performance Share Awards. A Performance Share Award is an award entitling the recipient to acquire shares of Stock upon the attainment of specified performance goals. The Committee may make Performance Share Awards independent of or in connection with the granting of any other Award under the Plan. Performance Share Awards may be

granted under the Plan to any Eligible Person. The Committee in its discretion shall determine whether and to whom Performance Share Awards shall be made, the performance goals applicable under each such Award, the periods during which performance is to be measured, the conditions under which such Award shall terminate, and all other limitations and conditions applicable to the awarded Performance Shares.

#### SECTION 9. Termination of Stock Options.

##### (a) Standard Termination Provisions.

(i) Termination by Death. If any participant's employment by or services to the Company and its Subsidiaries terminates by reason of death, any Stock Option owned by such participant may thereafter be exercised to the extent exercisable at the date of death, by the legal representative or legatee of the participant, for a period of one (1) year (or such longer period as the Committee shall specify at any time) from the date of death, or until the expiration of the stated term of the Stock Option, if earlier.

##### (ii) Termination by Reason of Disability or Normal Retirement.

(A) Any Stock Option held by a participant whose employment by or service to the Company and its Subsidiaries has terminated by reason of Disability may thereafter be exercised, to the extent it was exercisable at the time of such termination, for a period of one (1) year (or such longer period as the Committee shall specify at any time) from the date of such termination, or until the expiration of the stated term of the Stock Option, if earlier.

(B) Any Stock Option held by a participant whose employment by or service to the Company and its Subsidiaries has terminated by reason of Normal Retirement may thereafter be exercised, to the extent it was exercisable at the time of such termination, for a period of ninety (90) days from the date of such termination, or until the expiration of the stated term of the Stock Option, if earlier.

(C) The Committee shall have sole authority and discretion to determine whether a participant's employment or services have been terminated by reason of Disability or Normal Retirement.

(iii) Termination for Cause. If any participant's employment by or services to the Company and its Subsidiaries has been terminated for Cause, any Stock Option held by such participant shall immediately terminate and be of no further force and effect; provided, however, that the Committee may, in its sole discretion, provide that such Stock Option can be exercised for a period of up to thirty (30) days from the date of termination of employment or services or until the expiration of the stated term of the Stock Option, if earlier.

(iv) Voluntary Termination. If any participant's employment by or services to the Company and its Subsidiaries is voluntarily terminated, any Stock Option held by such participant shall immediately terminate and be of no further force and effect; provided, however, that the Committee may, in its sole discretion, provide that such Stock Option can be exercised for a period of up to ninety (90) days from the date of termination of employment or services or until the expiration of the stated term of the Stock Option, if earlier.

(v) Other Termination. Unless otherwise determined by the Committee, if a participant's employment by or services to the Company and its Subsidiaries terminates for any reason other than death, Disability, Normal Retirement, for Cause or voluntary termination, any Stock Option held by such participant may thereafter be exercised, to the extent it was exercisable on the date of such termination, for ninety (90) days (or such longer period as the Committee shall specify at any time) from the date of termination or until the expiration of the stated term of the Stock Option, if earlier.

(b) Committee Discretion. Notwithstanding the foregoing, the Committee may grant Stock Options under the Plan which contain such terms and conditions with respect to termination as the Committee, in its discretion, may from time to time determine.

#### SECTION 10. Tax Withholding.

(a) Payment by Participant. Each participant shall, no later than the date as of which the value of an Award or of any Stock or other amounts received thereunder first becomes includable in the gross income of the participant for Federal income tax purposes, pay to the Company, or make arrangements satisfactory to the Committee regarding the payment of, any Federal, state, local or other taxes of any kind required by law to be withheld with respect to such income. The Company and its Subsidiaries shall, to the extent permitted by law, have the right to deduct any such taxes from any payment of any kind otherwise due to the participant.

(b) Payment in Shares. A participant may elect, with the consent of the Committee, to have such tax withholding obligation satisfied, in whole or in part, by (i) authorizing the Company to withhold from shares of Stock to be issued pursuant to an Award a number of shares with an aggregate Fair Market Value (as of the date the withholding is effected) that would satisfy the minimum withholding amount due with respect to such Award, or (ii) transferring to the Company shares of Stock owned by the participant for a period of at least six (6) months and with an aggregate Fair Market Value (as of the date the withholding is effected) that would satisfy the minimum withholding amount due with respect to such Award.

SECTION 11. Transfer, Leave of Absence, Etc. For purposes of the Plan, a transfer to the employment of the Company from a Subsidiary or from the Company to a Subsidiary, or from one Subsidiary to another, shall not be deemed a termination of employment. Whether authorized leave of absence, or absence on military or government service, shall constitute termination of the employment relationship between the Company and the participant shall be determined by the Committee at the time thereof.

SECTION 12. Amendments and Termination. The Board may at any time amend or discontinue the Plan in any manner allowed by law and the Committee may at any time, subject to Section 2, amend or cancel any outstanding Award (or provide substitute Awards) for the purpose of satisfying changes in law or for any other lawful purpose, but no such action shall adversely affect rights under any outstanding Award without the holder's consent.

SECTION 13. Status of Plan. With respect to the portion of any Award that has not been exercised, a participant shall have no rights greater than those of a general creditor of the Company unless the Committee shall otherwise expressly determine in connection with any Award or Awards. In its sole discretion, the Committee may authorize the creation of trusts or other arrangements to meet the Company's obligations to deliver Stock or make payments with respect to Awards hereunder, provided that the existence of such trusts or other arrangements is consistent with the provision of the foregoing sentence.

SECTION 14. Lockup Agreement. The acceptance of any Award under this Plan by the participant or any subsequent holder shall constitute the agreement of such person that, upon the request of the Company or the underwriters managing any underwritten offering of the Company's securities, such person will not, for a period of time (not to exceed one hundred eighty (180) days) following the effective date of any registration statement filed by the Company under the Securities Act of 1933, as amended, sell, make any short sale of, loan, grant any option for the purchase of, or otherwise dispose of any shares of Stock received pursuant to such Award, without the prior written consent of the Company or such underwriters, as the case may be, and that such person will execute and deliver to the Company or such underwriters a written agreement to that effect, in such form as the Company or such underwriters shall designate.

SECTION 15. Change in Control.

(a) Upon the occurrence of a Change of Control as defined in this Section 15:

(i) subject to the provisions of clause (iii) below, after the effective date of such Change of Control, each holder of an outstanding Stock Option or Performance Share Award shall be entitled, upon exercise of such Award, to receive, in lieu of shares of Stock (or consideration based upon the Fair Market Value of Stock), shares of such stock or other securities, cash or property (or consideration based upon shares of such stock or other securities, cash or property) as the holders of shares of Stock received in connection with the Change of Control;

(ii) the Committee may accelerate the time for exercise of, and waive all conditions and restrictions on, each unexercised and unexpired Stock Option and Performance Share Award, effective upon a date prior or subsequent to the effective date of such Change of Control, specified by the Committee;

(iii) the Committee may waive all conditions and restrictions on, each Restricted Stock Award and Unrestricted Stock Award, effective upon a date prior or subsequent to the effective date of such Change of Control, specified by the Committee; or

(iv) each outstanding Stock Option and Performance Share Award may be cancelled by the Committee as of the effective date of any such Change of Control provided that (x) notice of such cancellation shall be given to each holder of such an Award and (y) each holder of such an Award shall have the right to exercise such Award to the extent that the same is then exercisable or, if the Committee shall have accelerated the time for exercise of all such unexercised and unexpired Awards, in full during the 30-day period preceding the effective date of such Change of Control.

(b) "Change of Control" shall mean the occurrence of any one of the following events:

(i) any "person" (as such term is used in Sections 13(d) and 14(d)(2) of the Act) becomes a "beneficial owner" (as such term is defined in Rule 13d-3 promulgated under the Act) (other than the Company, any trustee or other fiduciary holding securities under an employee benefit plan of the Company, or any corporation owned, directly or indirectly, by the shareholders of the Company in substantially the same proportions as their ownership of stock of the Company), directly or indirectly, of securities of the Company representing thirty-five percent (35%) or more of the combined voting power of the Company's then outstanding securities; or

(ii) persons who, as of January 1, 1997, constituted the Company's Board (the "Incumbent Board") cease for any reason, including without limitation as a result of a tender offer, proxy contest, merger or similar transaction, to constitute at least a majority of the Board, provided that any person becoming a director of the Company subsequent to January 1, 1997 whose election was approved by, or who was nominated with the approval of, at least a majority of the directors then comprising the Incumbent Board shall, for purposes of this Plan, be considered a member of the Incumbent Board; or

(iii) the shareholders of the Company approve a merger or consolidation of the Company with any other corporation or other entity, other than (a) a merger or consolidation which would result in the voting securities of the Company outstanding immediately prior thereto continuing to represent (either by remaining outstanding or by being converted into voting securities of the surviving entity) more than 65% of the combined voting power of the voting securities of the Company or such surviving entity outstanding immediately after such merger or consolidation or (b) a merger or consolidation effected to implement a recapitalization of the Company (or similar transaction) in which no "person" (as hereinabove defined) acquires more than 50% of the combined voting power of the Company's then outstanding securities; or

(iv) the shareholders of the Company approve a plan of complete liquidation of the Company or an agreement for the sale or disposition by the Company of all or substantially all of the Company's assets.

#### SECTION 16. General Provisions.

(a) No Distribution; Compliance with Legal Requirements. The Committee may require each person acquiring shares pursuant to an Award to represent to and agree with the

Company in writing that such person is acquiring the shares without a view to distribution thereof, in such form as the Committee shall in its sole discretion deem advisable.

No shares of Stock shall be issued pursuant to an Award until, in the opinion of the Committee, all applicable securities laws and other legal and stock exchange requirements have been satisfied. The Committee may require the placing of such stop orders and restrictive legends on certificates for Stock and Awards as it deems appropriate.

(b) Delivery of Stock Certificates. Delivery of stock certificates to participants under this Plan shall be deemed effected for all purposes when the Company or a stock transfer agent of the Company shall have delivered such certificates in the United States mail, addressed to the participant, at the participant's last known address on file with the Company.

(c) Other Compensation Arrangements; No Employment Rights. Nothing contained in this Plan shall prevent the Board from adopting other or additional compensation arrangements, including trusts, subject to stockholder approval if such approval is required; and such arrangements may be either generally applicable or applicable only in specific cases. The adoption of the Plan or any Award under the Plan does not confer upon any employee any right to continued employment with the Company or any Subsidiary.

SECTION 17. Effective Date of Plan. The Plan shall become effective upon its adoption by the Board.

SECTION 18. Governing Law. This Plan and each Award under the Plan shall be governed by, and construed and enforced in accordance with, the substantive laws of The Commonwealth of Massachusetts without regard to its principles of conflicts of laws.

## SUBSIDIARIES OF PROGRESS SOFTWARE CORPORATION

## North America

Barbados	Progress Software International Sales Corporation
Canada	Progress Software Corporation of Canada Ltd.
Canada	PeerDirect Company
Delaware	eXcelon Corporation
Delaware	Falcon Asset Acquisition Corporation
Delaware	NuSphere Corporation
Delaware	PeerDirect Corporation
Delaware	Persistence Software Inc.
Delaware	Progress Software International Corporation
Delaware	Progress Software Corporation
Delaware	Sonic Software Corporation
Massachusetts	DataDirect Technologies Corp.
Massachusetts	Progress Security Corporation

## Europe

Austria	Progress Software GesmbH
Belgium	DataDirect Technologies NV
Belgium	Progress Software NV
Czech Republic	Progress Software spol. s.r.o.
Denmark	Progress Software A/S
Finland	Progress Software Oy
France	Object Design S.a.r.l.
France	Progress Software S.A.
France	Sonic Software S.a.r.l.
Germany	DataDirect Technologies GmbH
Germany	Persistence Software GmbH
Germany	Progress Software GmbH
Germany	Sonic Software GmbH
Italy	Progress Software Italy S.r.l.
Italy	Sonic Software S.r.l.
Netherlands	Progress Software B.V.
Netherlands	Progress Software Europe B.V.
Netherlands	Sonic Software B.V.
Norway	Progress Software A/S
Poland	Progress Software sp. z.o.o.
Spain	Progress Software S.L.U.
Sweden	Progress Software Svenska AB
Switzerland	Progress Software AG
United Kingdom	DataDirect Technologies Ltd.
United Kingdom	Progress Software Limited
United Kingdom	Persistence Software Ltd.
United Kingdom	Sonic Software (UK) Limited

## Latin America

Argentina	Progress Software de Argentina S.A.
-----------	-------------------------------------



Brazil	Progress Software do Brasil Ltda.
Chile	Progress Software de Chile S.A.
Colombia	Progress Software de Colombia S.A.
Mexico	Progress Software, S.A. de C.V.
Venezuela	Progress Software de Venezuela C.A.

Other	
Australia	eXcelon (Pty) Ltd.
Australia	Progress Software Pty. Ltd.
Hong Kong	Persistence Software Asia/Pacific Ltd.
Hong Kong	Progress Software Corporation Limited
Japan	DataDirect Technologies KK
Japan	Sonic Software KK
Malaysia	Progress Software (M) Sdn Bhd
Singapore	Progress Software Corporation (S) Pte. Ltd.
South Africa	Progress Software (Pty) Ltd.

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in Registration Statement Nos. 33-41752, 33-43045, 33-50654, 33-58892, 33-96320, 333-41393, 333-41401, 333-41403, 333-80571, 333-80559, 333-98035 and 333-101239 on Form S-8, of our reports dated February 11, 2005, relating to the consolidated financial statements of Progress Software Corporation and management's report of the effectiveness of internal control over financial reporting, appearing in this Annual Report on Form 10-K of Progress Software Corporation for the year ended November 30, 2004.

/s/ DELOITTE & TOUCHE LLP  
-----

Boston, Massachusetts  
February 11, 2005

## CERTIFICATION

I, Joseph W. Alsop, certify that:

1. I have reviewed this annual report on Form 10-K of Progress Software Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure control and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 11, 2005

/s/ JOSEPH W. ALSOP

-----  
Joseph W. Alsop  
Chief Executive Officer  
(Principal Executive Officer)

## CERTIFICATION

I, Norman R. Robertson, certify that:

1. I have reviewed this annual report on Form 10-K of Progress Software Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure control and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 11, 2005

/s/ NORMAN R. ROBERTSON

-----  
Norman R. Robertson  
Senior Vice President, Finance and  
Administration and Chief Financial Officer  
(Principal Financial Officer)

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report on Form 10-K of Progress Software Corporation (the Company) for the year ended November 30, 2004, as filed with the Securities and Exchange Commission on the date hereof (the Report), each of the undersigned, Joseph W. Alsop, Chief Executive Officer, and Norman R. Robertson, Senior Vice President, Finance and Administration and Chief Financial Officer, of the Company, certifies, to the best knowledge and belief of the signatory, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ JOSEPH W. ALSOP

/s/ NORMAN R. ROBERTSON

-----  
Chief Executive Officer

-----  
Senior Vice President, Finance and  
Administration and Chief Financial  
Officer

Date: February 11, 2005

Date: February 11, 2005