

ELEVON INC  
Form 10-K  
March 28, 2003

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

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**Form 10-K**

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(Mark One)

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

**For the fiscal year ended December 31, 2002**

or

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

**For the transition period from            to**

**Commission file number 0-19872**

**Elevon, Inc.**

*(Exact name of Registrant as specified in its Charter)*

**Delaware**

*(State or Other Jurisdiction of  
Incorporation or Organization)*

**95-2862954**

*(IRS Employer  
Identification Number)*

**303 Second Street, 3 North**

**San Francisco, California 94107**

*(Address of Principal Executive Offices including Zip Code)*

**(415) 495-8811**

*(Registrant's Telephone Number, Including Area Code)*

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

**None**

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

**Common Stock, \$.001 Par Value Per Share**

*(Title of 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 ☐

## Edgar Filing: ELEVEN INC - Form 10-K

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 the 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 ☒

Based on the average bid and ask prices of the Registrant's common stock on the Over the Counter Bulletin Board on March 14, 2003, the aggregate market value of the voting stock held by non-affiliates of the Registrant was \$12,610,962. Shares of the Registrant's common stock held by each officer and director and by each person who owns 5% or more of the Registrant's outstanding common stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

The number of shares of the Registrant's common stock outstanding as of March 14, 2003 was 15,576,952.

### DOCUMENTS INCORPORATED BY REFERENCE

Part III of this Report on Form 10-K incorporates information by reference from the Registrant's definitive Proxy Statement to be used in conjunction with its 2002 Annual Meeting of Stockholders, to be held on May 22, 2003.

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**PART I**

**Item 1. Business Overview**

***Introduction***

The Company (hereinafter "Eleven", "Walker", "we", "our", "us", or the "Company") was incorporated in California in 1973 as Walker Interactive Systems, Inc. and reincorporated in Delaware in March 1992. In February 2002, Walker announced that it would do business as Eleven, Inc., and our name was formally changed in May 2002. We design, develop, market and support, on a worldwide basis, a family of enterprise financial, operational and analytical software products that enable large and medium-sized organizations, higher education institutions, and federal, state and government agencies to optimize their business processes, reduce business costs, and improve management information needed to run their business. We derive our revenue from software licenses, software maintenance and professional consulting services. Our collaborative commerce solutions and analytical applications are licensed to large and mid-size companies and similarly sized governmental organizations worldwide.

***Recent Update***

On September 6, 2002, we sold our United Kingdom operations and our Eleven 5 intellectual property to Novele Limited ("Novele", now doing business as "Arelon") located in London, United Kingdom. Under the terms of a share purchase agreement, we sold the stock of our wholly owned subsidiary, Eleven International Limited, to Novele for consideration of \$16.5 million. Approximately \$15.7 million cash was received at closing. The remaining balance of approximately \$800,000 was due on or before December 31, 2002 subject to certain conditions under the terms of the agreement. We deferred \$200,000 of the gain and subsequently recognized it during the fourth quarter of fiscal 2002 following the completion of certain customer requirements. We have informally agreed with Arelon to extend, on a month-to-month basis, the remaining \$600,000, plus interest. In addition to acquiring the Eleven operations headquartered in the United Kingdom, Novele acquired the QSP ("Eleven 5") intellectual property, which we had previously acquired from the administrative receiver for the QSP Group PLC in November 2001 for \$2.0 million in cash. Novele also became an exclusive distributor of Eleven 2 and Active Financial Planning ("AFP") software in the United Kingdom and certain other territories, pursuant to a software distribution agreement.

We recognized an after-tax gain in respect of the sale of our United Kingdom operations and Eleven 5 intellectual property of \$19.0 million, or \$1.20 per diluted share, in the consolidated statement of operations for the year ended December 31, 2002.

During the quarters ended June 30 and December 31, 2002, the Board of Directors approved restructuring plans to reduce operating costs and strengthen the Company's position to successfully execute its strategy. The Company recorded a pre-tax restructuring charge totaling \$1.1 million, mainly for severance costs related to the involuntary termination of employees in the Company's United States and United Kingdom operations.

During the second quarter of 2002, our evaluation of capitalized software carrying amounts against the related estimated net realizable values of the assets indicated that the estimated net realizable values of certain assets were not sufficient to recover the associated carrying values and resulted in an impairment charge of \$365,000. In addition, we recorded a benefit of \$1.7 million during the quarter ended June 30, 2002 related to a reduction in estimated liabilities associated with divested product lines.

On February 4, 2002, we announced we would start doing business as Eleven, Inc. On May 23, 2002, the stockholders approved an amendment to our Restated Certificate of Incorporation to formally change the Company's name to Eleven, Inc. The certificate was filed with the Secretary of State of the State of Delaware on May 31, 2002. On July 15, 2002, our ticker symbol on the Over the Counter Bulletin Board was changed to "ELVN".

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In the second quarter of 2000, we formed a wholly owned subsidiary, RareVision, Inc., to further the development and market testing of a business-to-business internet model for a web-based, knowledge management analytical application for smaller businesses. During fiscal 2000 and 2001, product development and marketing expenses totaling \$6.6 million were incurred and charged to operations. During 2001, further development of the RareVision product line on a standalone basis was ceased and the remaining components of the development effort were integrated into our analytics product line.

### ***Strategic Direction***

During 1999, we changed our strategic direction to emphasize e-business solutions and analytical applications, and began to refocus ourselves as a provider of e-business and collaborative commerce solutions. As part of our strategic redirection, we redesigned our software products specifically for Internet architecture and collaborative e-business models. We believe that our architecture is among the most scalable and adaptable for enterprise-level business software, and our strategy is to offer enterprise financial, operational and analytical solutions to a variety of industries. Our collaborative commerce solutions integrate processes within and across enterprise boundaries for the benefit of the enterprise, its suppliers and its customers. These processes include procurement, revenue management, financial management and insight, business planning, budgeting, forecasting and financial consolidation.

Our software products utilize the Microsoft Windows operating systems on the desktop, NT, UNIX and S/390 operating systems on the server and industry-leading On Line Analytical Processing ( OLAP ), Relational Database Management Systems ( RDBMS ) including IBM s DB2 and DB2 OLAP server, Hyperion Solutions Essbase and Microsoft SQL/Server. Our collaborative commerce solutions utilize the latest-generation IBM z-series Web Application Server. Eleven Collaborative Synergies™ solutions represent our core suite of business and financial solutions, utilizing the power of the enterprise server for highly scalable transaction processing and reliability/ availability, with the thin client architecture of the browser based interface. This Internet-based architecture provides an optimized platform for delivery of collaborative commerce solutions. Historically, we also developed and marketed, and continue to market analytical applications, which provide financial reporting, budgeting and financial consolidation solutions for large and mid-sized organizations. These analytical applications integrate with Eleven Collaborative Synergies solutions and also work on a standalone basis with leading Enterprise Resource Planning applications. Our software products include productivity tools that allow applications to be extensively customized to fit the customer s particular requirements. We complement our software products by providing specialized consulting services to assist customers with customization and implementation.

We derive our revenue from software licenses, software maintenance and professional consulting services. Our solutions are licensed primarily to Global 2000 companies and similarly sized business and governmental organizations worldwide. Our solutions and services are marketed in the United States primarily through a direct sales force, and in Europe our Eleven 2 and AFP solutions are marketed through a distribution agreement with Novele Limited.

### **Industry Background**

Large, geographically diverse organizations generate enormous amounts of financial, operational, sales, marketing and other data. We believe that the transaction-oriented information systems used by these organizations are typically critical to their efficiency, productivity and competitiveness, providing the availability of continuous and simultaneous information to employees, customers and suppliers. In the day-to-day operations of large organizations, transactional data needs to be promptly and easily retrieved from a variety of financial and operational systems, summarized and organized into meaningful business information that has a consistent business context. The process of integrating the data is complex when large organizations employ multiple accounting systems, operational systems and transactional databases, spread their business across many different geographies and have different information requirements by function and across the organization. Furthermore, we believe that the current business climate of deregulation and merger/ acquisition activities in many industries has added additional complications as well as the need for scalable and adaptable business processes.

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Organizations attempt to collect, summarize, organize and present information from heterogeneous computer systems and transactional data sources in various ways. Reports can be assembled through entry of data into spreadsheets and by using data from accounting systems and other operational systems. Many organizations have tried to automate information systems through the use of software developed internally or through assistance from outside consultants. We believe that these custom-built systems are becoming increasingly obsolete because they are rigid in structure, expensive and time consuming to create and maintain, and difficult to update when business processes and requirements change. Moreover, we believe growing competition has increased the demand for more timely business information specific to each function within the organization.

### **Market Opportunities**

The following market dynamics are important factors shaping our strategy moving forward:

#### ***e-Business and Collaborative Commerce***

The term e-business means many things to many people, but we believe it is well defined as the transformation of key business processes through the use of Internet technologies. The core processes that are the foundation of business are merged with the standards, simplicity and connectivity of the Internet. This melding of Internet technologies with key business processes creates opportunities for powerful interactive, transaction-intensive solutions that let companies do business in ever more efficient and effective ways. Innovative companies of all sizes are using the Web to communicate with their suppliers, their customers and their partners, to connect with their back-end data-systems, and to transact commerce. We expect the opportunities presented by this new business model to enable organizations to collaborate more fully with their suppliers, customers and partners in a seamless manner. This opportunity has now defined itself as collaborative commerce. The market potential for collaborative commerce solutions is significant, according to leading analysts such as IDC, Meta Group and Gartner Group. We believe that Eleven Collaborative Synergies solutions, which extend beyond the four walls of the enterprise, will allow current business processes to be streamlined and integrated, by removing valueless processes, creating valuable new processes, and moving misplaced processes.

#### ***Analytical Applications and Business Intelligence***

The need for better business information has created a growing need for analytical application software to help organizations gain business knowledge from the large volumes of transactional data available from daily operations. These software solutions work on a stand-alone basis, or in conjunction with core financial systems to translate data into business insight, and thus maximize the value of financial information.

#### ***Internet Architectures***

In recent years, the market has seen the rapid adoption of thin client/centralized server architecture models, a significant contrast to the client/server architectures that have been prevalent since the mid-1990s. Internet based computing can enable companies to protect their existing information technology investments while taking advantage of new technologies by dynamically linking Internet, client/server and legacy systems. We believe that our Internet architecture model has created opportunities for competitive advantage in our market, and for our customers, through a combination of business processes optimized for the Internet model, improved collaboration, browser based interfaces, enhanced services, shared services and lower transaction costs. Eleven Collaborative Synergies solutions are designed to support this integrated Internet architecture and the collaborative enterprise process model.

#### ***Shared Services***

Large organizations should be able to reduce the costs and complexity of information systems by centralizing many administrative functions. These centralized functions are now being combined with distributed operational procedures. We believe our high-volume, collaborative synergies solutions support both



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models for distributing information when and where it is needed within the extended organization, significantly enhancing the availability of timely information.

### ***High Volume Transactions***

Large, geographically diverse organizations generate large volumes of transactions and data. As organizations extend their business beyond traditional enterprise boundaries through collaborative commerce, their transaction-oriented systems will often require increasing scalability to handle the increased volume from additional users and ever-growing transaction volumes. We believe our solutions provide scalable, cost-effective, high transaction volume capabilities.

## **Our Strategy**

Our objective is to be a leading provider of collaborative solutions for the real-time enterprise. Our strategy for achieving this goal is as follows:

### ***Enable the Transformation of Key Business Processes Through the Use of Internet Technologies***

We believe that the collaborative commerce enablement of key business processes has created opportunities for competitive advantage in our market through Internet/intranet-enabled solutions. We expect that our collaborative synergies solutions will allow organizations to transform core business processes utilizing existing information technology investments while taking advantage of powerful interactive, transaction-intensive solutions that let companies do business in ever more efficient and effective ways. We believe that our customers will have the ability to extend the reach of their business applications directly to employees, customers and suppliers worldwide.

### ***Deliver Solutions which Provide Management Insight into Key, Complex Business Processes in Selected Vertical Markets***

We believe that large, complex businesses are best understood in a multidimensional context, by key performance indicators and across business units, time periods, geographies and product lines. Our solutions capture and warehouse key business processes and business information while retaining the business context of the information through our analytical solutions. These solutions analyze the transactional data within the applications to deliver information that we expect will allow managers to be more informed about their organization's performance. Empowered by management insight, managers at all levels of the organization should then have the opportunity to better run their area of the business, enhancing competitiveness and bottom-line profitability. Our solutions use OLAP and relational database technology, which was developed specifically for multidimensional business analysis.

### ***Extend New and Existing Long-Term Relationships with Strategic Partners***

We have existing strategic relationships with leading hardware and software suppliers such as IBM, Microsoft, Hyperion Solutions, Inc., and Information Builders, Inc. We believe that the development of our relationships with these partners, as well as expanding the scope of the relationships to include e-business and e-commerce solutions, will contribute to our future revenue growth.

### ***Deliver Lower Cost/ Higher Performance Solutions***

While many vendors of enterprise software solutions are focusing their technology efforts on supporting a distributed client/server model, we intend to continue to build and enhance our e-business solutions for the IBM z900 as an e-business server. We build collaborative applications using Java technologies with a process we call Shared Transformation Enterprise Processes ( STEPs ). We believe that this puts us in a position to support multiple high-volume Internet- based computing environments. We believe that this capability, together with the growth of collaborative commerce, Internet bandwidth and processes that reflect an e-business way of working, supporting both shared and distributed service models, is a far more cost effective model than other distributed architecture models available in the market today.

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### ***Retain and Extend Long-Term Customer Relationships***

We intend to continue our focus on generating additional revenues from existing customers through software licenses, the introduction of new Eleven Collaborative Synergies solutions and services, and warranty maintenance. In addition, providing consulting and support services to existing customers represents a significant portion of our total revenues. We expect that follow-on revenues will create efficiencies for deployment of sales and marketing resources and strengthen relationships with our customers.

### **Eleven Solutions and Services**

Eleven Collaborative Synergies solutions for the enterprise are designed to improve core business processes and to provide the functionality to create competitive advantage in an ever-changing global marketplace. We attempt to achieve this by offering solutions that combine flexible collaborative commerce solutions, analytical applications, deep industry knowledge and best practices expertise.

### **Solutions**

#### ***Collaborative Synergies Solutions***

Eleven Collaborative Synergies solutions are designed to support new processes as organizations redefine existing processes as a result of collaborating with their suppliers and customers beyond the four walls of the enterprise. These solutions are intended to align stakeholder incentives and transform unproductive processes into win/win workflows. The goal of Eleven Collaborative Synergies solutions is to streamline inefficiencies, eliminate redundancies, reengineer roadblocks and reassign misplaced processes – those where work is done on one side of a barrier while the best resources and incentives for the task wait on the other – to match mission with motivation. We expect these improvements to compress business cycles, increase process velocity, and enhance value chain visibility.

Eleven Collaborative Synergies solutions are organized into the following key operational areas:

*e-finance* delivers solutions that provide the organization with the transaction processing power, information access and real-time monitoring required to manage the business. Eleven 2 e-finance includes the general ledger, asset management and project cost management modules.

*e-procurement* automates and extends the purchasing process beyond the four walls of the enterprise, giving all parties a high degree of visibility and control. Eleven 2 e-procurement includes the accounts payable, inventory management and purchase order modules.

*e-revenue* extends the billing, credit, accounts receivable and collection processes beyond the organization to where they become collaborative relationships. Eleven 2 e-revenue includes the accounts receivable, billing and collection modules.

*STEPS* a suite of integrated, granular, collaborative software applications designed to seamlessly extend existing corporate systems outside the organization to solve specific, common business problems.

*Portals* business processes engineered to allow for any number of roles as dictated by business needs. Eleven Roles automate specific processes and offer the user great flexibility, while simplifying multiple tasks in the process. We currently cover the following key roles:

*e-finance portal:* e-analyst.

*e-procurement portal:* e-administration, e-approval, e-buyer, e-content management, e-employee expense, e-employee expense payables, and e-requisitioner.

*e-revenue portal:* e-administrator, e-collector, e-care, e-credit, e-data entry, and e-payment applier.

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### ***Analytical Applications***

We broadened the scope of our collaborative synergies offerings with the addition of analytical solutions that work with transactional data to provide in-depth insight into the enterprise. This combination of collaborative synergies solutions and analytical applications, which includes planning, forecasting and financial consolidation solutions, allows our customers the opportunity to better manage company-wide performance.

The analytical applications employ a flexible architecture that leverages a single OLAP engine for all its applications. This provides companies with a solution that should ensure data integrity and be easy to deploy and maintain. As a result, organizations can gain the ability to make fast, informed business decisions and continually monitor performance improvement at all levels of the organization.

The analytical applications are available for multiple operating systems and OLAP databases. They allow companies to track performance metrics that are specific to their organization. Any combination of these applications complements Eleven's Collaborative Synergies solutions as well as non-Eleven financial and operational solutions.

Our analytical applications include:

*Planning and Forecasting* Automates the planning, forecasting and budgeting processes to reduce planning cycles, facilitate continuous planning and enable the prediction of company performance.

*Financial Consolidation* Manages the collection, adjustment and reporting of consolidated results for enterprise-wide statutory, management and tax reporting.

*Active Financial Planning* web-based planning and decision support system that offers real-time collaboration focused on predictive and corrective planning.

### **Product Development**

We continually work to enhance our existing products and develop new products to meet our customers' ever-changing requirements. Our success will depend, in part on our ability to develop product enhancements and new products that keep pace with technological changes and changes in customers' business practices. Product development costs charged to operations, including amortization of capitalized software development costs, were 21% of total revenues in 2002, 24% in 2001, and 35% in 2000.

Due to the layered architecture of our collaborative synergies solutions, and our efforts to continually enhance our products in order to respond to evolving technologies, we believe that our core products have long life cycles. As operating systems, databases and presentation software technologies evolve, we expect to be able to modify our collaborative synergies solutions through an upgrade and by changing only the corresponding layer of software without having to change the other components of the system. Therefore, our customers are able to modify our collaborative synergies solutions through an upgrade and by changing only the corresponding layer of software without having to change the other components of the system. Therefore, our customers should not have to completely replace our products in response to technological change. We work closely with our customers and prospective customers to determine their requirements and to define the functionality of our new products and enhancements to our existing products.

### **Services**

#### ***Professional Services***

It is our experience that organizations are increasingly leveraging information technology to accomplish their business objectives. Large, global organizations often rely heavily on their software investments to remain competitive. We provide a full range of services to support these needs. We believe our professional services organization adds significant incremental value, offering implementation, customization, migration, training and related services to our customers. We have suites of reusable tools and utilities designed to enable customers to complete customizations efficiently and cost effectively.

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Some of the areas addressed by our services include:

*Integration* to integrate the customers' existing applications into the Eleven Collaborative Synergies solutions.

*Performance tuning* to increase computer throughput, reduce processing time and otherwise improve performance.

*Migration* to assist in making cost-effective migrations to a new release or from one platform to another.

*Conversion and integration* to integrate third-party applications into our framework or convert these products to our applications through our reusable components, methodologies and e-technology.

### ***Customer Support and Maintenance***

Our customer support and maintenance program includes 24-hour hotline telephone support for problem determination and resolution, account management, and ongoing functional and technical enhancements for installed products.

## **Reportable Segments**

Our product and service offerings are considered a single reportable segment. Information regarding domestic and international revenues and assets is contained in Note 11 to the Consolidated Financial Statements.

## **Sales and Marketing**

We sell our products primarily through our direct sales force. In support of our sales force, we conduct marketing programs, which include direct mail, public relations, advertising, seminars, trade shows and ongoing customer communication programs. The sales cycle begins with the generation of a sales lead, or often the receipt of a request for proposal ( RFP ) from a prospect, which is followed by qualification of the lead, an analysis of the customer's needs, response to the RFP (one or more presentations to the customer), customer internal approval activities and contract negotiation and finalization. While our sales cycle varies by product and by customer, our sales cycle has historically ranged from three to twelve or more months. The current slowdown in the United States economy has had the effect of further extending our sales cycle.

We market our products primarily to large or complex organizations with collaborative commerce and e-business requirements having intensive data processing and information management requirements. In each of the last three fiscal years, a substantial portion of our product revenue was derived from existing customers licensing either new products or products for additional sites.

We regard our professional services and product development organizations as integral parts of our marketing strategy because of the length and technical nature of the sales process. Professional services and product development employees participate directly in the sales cycle and educate prospective customers on the advantages of using Eleven solutions rather than those developed internally or by other third parties.

Historically, the Company has primarily operated in three geographic areas, North America, Europe/ Middle East/ Africa and Asia Pacific. Following the disposal of our United Kingdom and Eleven 5 operations in September 2002, the Company will have insignificant revenues and assets in the Europe/ Middle East/ Africa region. During the years ended December 31, 2002 and 2001, revenue generated from products and services provided to ADT Security Services, Inc., a unit of Tyco International Ltd., represented 18.2% and 17.4% of revenue, respectively. The same customer represented 18.2% and 17.6% of accounts receivable as of December 31, 2002 and 2001, respectively. No customer represented in excess of 10% of total revenues or accounts receivable for 2000.

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### **Competition**

The business and financial application software market for large, complex organizations is intensely competitive. The principal competitors with Eleven Collaborative Synergies solutions are SAP AG, Oracle Corporation and PeopleSoft, Inc. Our analytical applications compete primarily with Hyperion Solutions Corporation, Cognos, Inc. and Comshare, Inc.

We also compete to a lesser extent with other independent software application vendors. Some of our current and potential competitors have substantially greater financial, technical, marketing and sales resources than we do. Some of these competitors also offer business application products not offered by us, primarily in the areas of human resources and manufacturing. However, we remain one of the few companies committed to providing and enhancing applications for the IBM z900 e-business server. Most of our competitors offer only UNIX-based applications.

We encounter competition from a broad range of firms in the professional services market. These competitors include the current and former consulting divisions of the major accounting firms, which possess greater resources than we do and compete with us mainly on the basis of the scope of services offered, and small independent firms that compete primarily on the basis of price.

### **Proprietary Rights**

We regard our products as proprietary and attempt to protect them with a combination of trade secrets, copyright and trademark laws, our license agreements with customers, our internal security systems, confidentiality procedures and employment agreements. Although we take steps to protect our trade secrets, we cannot assure you that misappropriation will not occur. In addition, the laws of some foreign countries do not protect our proprietary rights to the same extent as the laws of the United States.

We typically provide our products to users under non-exclusive, non-transferable, perpetual licenses. Under the general terms and conditions of our standard product license agreement, the licensed software may be used only for internal operations. We make source code for some of our products available to our customers under agreements that restrict access to and use of the source code.

We seek to protect our software, documentation and other written materials under copyright laws, which afford only limited protection. We also assert trademark rights in our product names. We have not sought to protect our products under patent laws, as we believe that the rapid pace of technological change in the computer industry makes patent or copyright protection of less significance than such factors as the knowledge and experience of management and personnel, name recognition, maintenance and support of software products and our ability to develop, enhance, market and acquire software products and services.

Although we believe that our products do not infringe upon the proprietary rights of third parties, there can be no assurance that third parties will not assert infringement claims against us in the future with respect to current or future products, or that any such assertions will not require us to enter into royalty arrangements or result in costly litigation.

For a description of certain proprietary risk factors, see Management's Discussion and Analysis of Financial Condition and Results of Operations Additional Risk Factors.

### **Employees**

As of December 31, 2002, we had 103 employees, 96 of whom were based in the United States and 7 were based internationally. Of the total, 15 employees were engaged in sales and marketing, 12 were in customer support, 26 were in professional services, 21 were in product development and 29 were in data processing, administration and finance positions.

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We currently lease the properties described below:

<u>Location</u>	<u>Usage</u>	<u>Approximate Square Footage</u>	<u>Square Footage Sublet</u>	<u>Lease Expiration</u>
San Francisco, USA	Our headquarters	55,000		2007
Chicago, USA	Operations	11,000		2006
Atlanta, USA	Operations	1,800		2003
Toronto, Canada	Sublet	4,000	4,000	2003
Total Square Footage		71,800	4,000	

We believe that we have adequate facilities to accommodate our operations in the near term and that additional space will be available at commercially reasonable terms as needed. Our San Francisco office lease requires us to maintain significantly more space than we need for our current operations.

As of December 31, 2002, approximately 4,000 square feet of office space in Toronto, Canada, is not occupied by us and is sublet.

**Item 3. *Legal Proceedings***

As of December 31, 2002, there were no pending legal proceedings, other than ordinary routine litigation incidental to our business, to which we are a party or to which any of our property is subject, which we anticipate would have a material adverse effect on our financial condition or results of operations.

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

No matters were submitted to a vote of security holders during the quarter ended December 31, 2002.

**PART II****Item 5. *Market for Registrant's Common Stock and Related Security Holder Matters***

Our common stock has been traded on the Over the Counter Bulletin Board under the symbol `ELVN` since July 15, 2002. From March 6, 2001 to July 14, 2002, our common stock was traded on the Over the Counter Bulletin Board and before that it was traded on the Nasdaq National Stock Market, under the symbol `WALK`. As of March 14, 2003, there were approximately 1,800 stockholders of record of our common stock. We have not paid any cash dividends and do not anticipate paying any cash dividends in the foreseeable future. The high and low sale prices per share of our common stock, for the periods set forth below, are as reported by the Nasdaq National Stock Market System and the range of high and low bid information per share for our common stock for the periods set forth below are as quoted on the Over the Counter Bulletin Board.

<u>Quarter Ending</u>			
<u>March 31,</u>	<u>June 30,</u>	<u>September 30,</u>	<u>December 31,</u>

# Edgar Filing: ELEVON INC - Form 10-K

	2002	2002	2002	2002
<b>Over the Counter Bulletin Board</b>				
Bid range per common share				
High	\$2.35	1.97	1.24	1.39
Low	\$0.82	1.21	0.74	1.02
	10			

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	<b>January 1, 2001 through March 5, 2001</b>	<b>March 6, 2001 through March 31, 2001</b>	<b>June 30, 2001</b>	<b>September 30, 2001</b>	<b>December 31, 2001</b>
<b>Over the Counter Bulletin Board</b>					
Bid range per common share					
High	\$	0.84	1.00	0.84	0.96
Low	\$	0.69	0.51	0.45	0.44
<b>Nasdaq National Stock Market</b>					
Price range per common share					
High	\$2.47				
Low	\$0.78				

**Item 6. Selected Consolidated Financial Data**

The following table should be read in conjunction with our financial statements and the notes thereto, and Management's Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this Form 10-K.

	<b>Years Ended December 31,</b>				
	<b>2002(1)</b>	<b>2001</b>	<b>2000(2)</b>	<b>1999(3)</b>	<b>1998</b>
<b>(In thousands, except per share amounts)</b>					
<b>Statement of Operations Data:</b>					
Total revenues	\$41,913	\$49,065	\$ 51,422	\$ 87,978	\$101,413
Income (loss) before income taxes	20,663	1,586	(26,565)	(24,887)	7,266
Net income (loss)	20,563	1,486	(26,747)	(37,788)	4,525
<b>Per Share Data:</b>					
Basic net income (loss) per share	\$ 1.34	\$ 0.10	\$ (1.84)	\$ (2.67)	\$ 0.32
Diluted net income (loss) per share	\$ 1.30	\$ 0.10	\$ (1.84)	\$ (2.67)	\$ 0.31
<b>Shares:</b>					
Shares utilized to compute basic net income (loss) per share	15,332	14,917	14,535	14,154	14,012
Shares utilized to compute diluted net income (loss) per share	15,797	14,958	14,535	14,154	14,688
<b>Balance Sheet Data:</b>					
Cash, cash equivalents and investments	\$20,836	\$ 5,041	\$ 9,619	\$ 22,014	\$ 22,597
Total assets	30,463	25,012	27,560	57,950	95,097
Stockholders' equity (deficit)	16,983	(3,587)	(5,223)	19,119	57,051

- (1) Includes a gain on sale of our United Kingdom and Eleven 5 operations of \$19.0 million, a special credit of \$1.7 million relating to a reduction in estimated liabilities associated with divested product lines, a \$365,000 charge for the impairment of certain capitalized software, and a \$1.1 million restructuring charge mainly related to severance costs.
- (2) Includes a \$4.8 million charge for the impairment of certain capitalized software and a \$1.9 million restructuring charge mainly related to severance costs.
- (3) Includes a \$10.4 million charge for the impairment of certain capitalized software and goodwill, a \$4.5 million restructuring charge mainly related to severance costs in connection with the change in our strategic direction, and a \$12.5 million increase in the tax valuation allowance.





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

The following discussion of our results of operations and financial condition should be read in conjunction with our financial statements and notes thereto included elsewhere in this Annual Report on Form 10-K. This Annual Report on Form 10-K contains forward-looking statements, including statements related to industry trends, expected resolution of legal proceedings, cash commitments, liquidity, capital resources and working capital requirements. Discussions containing such forward-looking statements may be found in the material set forth under "Legal Proceedings" and "Management's Discussion and Analysis of Financial Condition and Results of Operations," generally and specifically therein under the captions "Management Overview," "Liquidity and Capital Resources" and "Additional Risk Factors," as well as elsewhere in this Annual Report on Form 10-K. Actual events or results may differ materially from those discussed herein. We disclaim any obligation to update these forward-looking statements as a result of subsequent events. The risk factors on pages 19 through 24, among others, should be considered in evaluating our prospects and future financial performance.

#### **MANAGEMENT OVERVIEW**

Approximately three years ago we announced our intention to focus the Company as a provider of e-business, analytical and collaborative commerce solutions with the goal of returning the Company to sustainable, profitable and cashflow positive operating results. Positioning the Company to achieve those goals required the divestiture of non-core operations, and in fiscal 2000 we divested the IMMPOWER and Aptos product lines. This refocusing of our product offerings in fiscal 2000 also resulted in an impairment charge of \$4.8 million related to capitalized development costs of certain legacy software. In addition, we incurred severance costs of \$1.9 million as we reduced our operating costs to align more closely with our expected revenue base.

To expand both our customer base and our platform offerings, in November 2001 we acquired the QSP Group PLC intellectual property (Eleven 5) from an administrative receiver for \$2.0 million. In September 2002 we sold our United Kingdom operations and the Eleven 5 intellectual property to Novele Limited (Novele, now doing business as Arelon) for \$16.5 million.

The events and aftermath of September 11, 2001 and the slowdown in the United States economy are factors that have led our customer base to reduce levels of corporate spending on information technology, which has negatively impacted our operating results for fiscal 2002. To address the decrease in revenue, we again reduced our operating costs through employee reductions and incurred severance costs of \$1.1 million. In fiscal 2002 we achieved operating income of \$1.6 million and generated cash from operating activities of \$2.3 million. We exited 2002 in a stronger, more liquid financial position as a result of selling our United Kingdom operations and the Eleven 5 intellectual property.

Looking forward, a continued sluggish United States economy could lead to reduced levels of corporate spending on information technology, which, in turn, would further extend our sales cycle and negatively impact our operating results. If these circumstances occur, our license revenues could continue to be below historical levels.

In addition, a significant portion of our consulting revenue for any given year is generally derived from several individually larger consulting engagements. Consulting revenue from a single North American customer represented 17.2% and 12.9% of total consolidated revenue in 2002 and 2001, respectively. This engagement was substantially completed in the fourth quarter of 2002. Completed consulting engagements must be replaced with new engagements, which historically have been associated with new license revenues or migrations to current releases of our software. Should corporate spending on information technology continue at reduced levels, it is likely that fewer new consulting engagements will be obtained in the near term and our consulting revenues will decline as compared to historical levels.

Further, our maintenance revenues could decline as a result of reduced new license sales, customers completing migrations to different platforms, and customers discontinuing maintenance in an effort to reduce their operating costs.

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We have reduced our operating costs primarily through reductions in both headcount and in discretionary sales and marketing spending, but a significant portion of our costs are fixed in the short term. Our San Francisco office lease, which expires in 2007, requires us to maintain significantly more space than we need for our current operations and there continues to be an excess of space in the sublease market.

### **CRITICAL ACCOUNTING POLICIES**

We believe the accounting policies described below to be the most critical in determining and understanding our results of operations. For a more detailed discussion of these policies and significant estimates inherent in the preparation of our consolidated financial statements, see Note 1 to the Consolidated Financial Statements.

#### ***Revenue Recognition***

Our revenues are derived from the sale of software licenses and from providing consulting and support services, generally to our licensees. The amount and timing of our revenues is critical in determining our results of operations, particularly on a quarterly basis. Our revenue also is key in the determination of certain costs that vary with revenue, such as commissions and royalties. Notwithstanding the detailed guidelines we have established in determining periodic revenue, judgments and estimates are required in the application of our revenue recognition policy.

#### ***Capitalization and Amortization of Product Development Costs***

Product development costs are a significant component of our operating costs. Our policy and its application in determining which costs are currently capitalized and amortized in future periods, or expensed as incurred, can impact our results of operations. Although our policy has definitive guidelines for the capitalization and amortization of software development costs, judgments are required in the estimation of future gross revenues from a product that are dependent upon factors such as market acceptance and the rate of technological change. Generally, we amortize capitalized software costs over a two-year period and review capitalized software costs on an on-going basis. If appropriate, we revise the amortization rate based on our then current assessment of future gross revenues. We cannot assure you that such future assessments will not differ from our initial estimates, which determine the capitalized amount and rate of amortization.

### **RESULTS OF OPERATIONS**

#### ***2002 compared to 2001***

As more fully described in Note 4 to the consolidated financial statements and in *Management Overview* in *Management's Discussion and Analysis of Financial Condition and Results of Operations*, in November 2001 we acquired the QSP intellectual property and in September 2002 we sold our United Kingdom operations and the previously acquired QSP intellectual property to Novele Limited.

To assist in understanding the effects of the divestiture of our United Kingdom operations and the previously acquired QSP intellectual property, the historical results for the operations remaining after the divestiture ( *North America* ) and the divested operations ( *United Kingdom* ), where relevant, have been shown separately.

Variations in the United Kingdom results for 2002 and 2001 relate primarily to the incremental revenues and costs associated with reestablishment of the former QSP operations, taking into account that fiscal 2001 includes two months of QSP operations together with a full year of our United Kingdom operations, and fiscal 2002 includes approximately eight months of our United Kingdom and QSP operations.

**Table of Contents****Revenues**

	<b>North America</b>	<b>United Kingdom</b>	<b>2002 Total</b>	<b>North America</b>	<b>United Kingdom</b>	<b>2001 Total</b>
Revenues:						
License and royalty	\$ 1,940	\$ 1,692	\$ 3,632	\$ 6,132	\$ 2,533	\$ 8,665
Maintenance	13,752	5,867	19,619	16,605	5,505	22,110
Consulting	13,305	5,357	18,662	14,230	4,060	18,290
Total revenues	\$28,997	\$12,916	\$41,913	\$36,967	\$12,098	\$49,065

Revenues for the years ended December 31, 2002 and 2001 from a single customer were 18.2% and 17.4% of our total revenue, respectively.

North America license and royalty revenues in 2002 were \$1.9 million, a decrease of \$4.2 million, or 68.4%, as compared to 2001. Our license revenues for 2002, in common with many other software companies, were negatively impacted by the general economic slowdown and reduction in corporate spending for technology. We also signed several individually larger license agreements during 2001, which contributed to the decrease in license revenues in 2002 when compared to 2001.

North America maintenance revenues in 2002 were \$13.8 million, a decrease of \$2.9 million, or 17.2%, as compared to 2001. North America maintenance revenues for 2001 included revenue from several maintenance agreements that were not renewed, due to customer acquisitions or the completion of migrations to alternative platforms. In 2001 we also provided short-term extended support to several customers who were migrating to current releases, and derived incremental revenue from the early termination of one customer agreement.

North America consulting revenues in 2002 were \$13.3 million, a decrease of \$925,000, or 6.5%, as compared to 2001. The decrease in consulting revenues is mainly attributable to a decline in service revenues from our legacy Analytics business, as we transitioned to the implementation of beta versions of our new AFP product.

**Costs of Licenses, Maintenance and Consulting**

	<b>North America</b>	<b>United Kingdom</b>	<b>2002 Total</b>	<b>North America</b>	<b>United Kingdom</b>	<b>2001 Total</b>
Cost of revenues	\$ 11,055	\$ 5,636	\$ 16,691	\$ 12,847	\$ 5,359	\$ 18,206

North America costs of licenses, maintenance and consulting in 2002 were \$11.1 million, a decrease of \$1.8 million, or 14.0%, as compared to 2001, and represented 38.1% and 34.8% of total revenues in 2002 and 2001, respectively. The total North America cost of revenues is lower for 2001 because proportionately more license revenue was recognized than in 2002. The cost of license revenue, which is mainly related to third-party license costs, was insignificant for both years.

The North America cost of maintenance, as a percentage of related revenue, decreased in 2002 compared to 2001, mainly due to lower employee-related and subcontractor costs.

The North America costs of consulting, as a percentage of related revenue, increased in 2002 as compared to 2001. Lower employee-related costs were offset by an increase in subcontractor costs.

**Sales and Marketing**

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	North America	United Kingdom	2002 Total	North America	United Kingdom	2001 Total
Sales and marketing	\$6,142	\$2,936	\$9,078	\$8,999	\$3,460	\$12,459

North America sales and marketing costs in 2002 were \$6.1 million, a decrease of \$2.9, or 31.8%, as compared to 2001. As a percentage of North America revenues, sales and marketing expenses were 21.2% and

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24.3% in 2002 and 2001, respectively. The decrease is mostly attributable to reductions in our discretionary spending and sales and marketing employee-related costs.

## Product Development

Product development related expense, excluding amortization of capitalized software, was as follows (in thousands):

	2002	2001
Product development expenditures	\$ 7,035	\$ 10,032
Less:		
Additions to capitalized software	(1,086)	(1,708)
Product development expense	\$ 5,949	\$ 8,324

Net product development expense decreased \$2.4 million, or 28.5%, in 2002 as compared to 2001 and was 14.2% and 17.0% of total revenues in 2002 and 2001, respectively. Total product development expenditures decreased \$3.0 million, mainly reflecting the cessation of RareVision development where costs of \$2.9 million were incurred during 2001. Product development expenses for 2002 include \$339,000 relating to the divested Eleven 5 product line.

Additions to capitalized software decreased \$622,000, or 36.4%, in 2002 as compared to 2001 and were 15.4% and 17.0% of product development expenditures in 2002 and 2001, respectively. The decrease in product development expenditures capitalized in 2001 is primarily attributable to product development resources being allocated to projects that did not meet the criteria for capitalization.

## Amortization of Capitalized Software

Capitalized software amortization in 2002 was \$2.8 million, a decrease of \$591,000, or 17.4%, as compared to 2001. Several development projects, primarily those relating to our legacy analytics products, became fully amortized during 2002. The decrease was partially offset by incremental amortization of the Eleven 5 intellectual property during 2002 of \$672,000.

## General and Administrative

	North America	United Kingdom	2002 Total	North America	United Kingdom	2001 Total
General and administrative	\$4,736	\$1,341	\$6,077	\$4,410	\$1,459	\$5,869

North America general and administrative expenses in 2002 were \$4.7 million, an increase of \$326,000, or 7.4%, as compared to 2001. As a percentage of North America revenues, general and administrative expenses were 16.3% and 11.9% in 2002 and 2001, respectively. The increase in general and administrative expenses in 2002 as compared to 2001 relates to the inclusion of a \$450,000 benefit from the termination of a lease and a \$300,000 reversal of an accrual resulting from a favorable sales tax determination in 2001, whereas no such benefits were recorded in 2002. This was partially offset by savings in employee-related costs during 2002.

## Restructuring Charge, Impairment of Capitalized Software and Special Credit

During 2002, we recorded pretax restructuring charges totaling \$1.1 million comprised of severance costs related to the involuntary termination of employees in our United States and United Kingdom operations, an impairment charge of \$365,000 for capitalized software, and a benefit of \$1.7 million related to a reduction in estimated liabilities associated with divested product lines. There were no impairment or restructuring charges in fiscal 2001.



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### **Interest and Other Income**

In 2002, we earned \$165,000 in interest income compared to \$335,000 in 2001, a decrease of \$170,000 or 50.7%. The decrease was due to lower interest rates and lower average cash balances available for investment. Other income for the year ended December 31, 2001 also includes a realized gain of \$442,000 from the disposal of the Aptos product line.

### **Income Tax Expense**

In both 2002 and 2001, we provided \$100,000 for state and foreign income taxes that could not be offset against net operating loss carryforwards.

### ***2001 compared to 2000***

### **Revenues**

Total revenues in 2001 were \$49.1 million, a decrease of \$ 2.4 million, or 4.6%, as compared to 2000. The decrease in total revenues relates primarily to the divested IMMPOWER and Aptos product lines.

License revenues in 2001 were \$8.7 million, an increase of \$3.5 million, or 68.9%, as compared to 2000. The increase in license revenue is due to the execution of several large license agreements during the year ended December 31, 2001, as customers migrated to our new generation of products. Our e-business enterprise solutions have a long sales cycle as collaborative commerce involves coordination with multiple vendors, which generally increases the value of each transaction and adds time and complexity to the process. A number of license agreements concluded in 2001 were the culmination of sales efforts that had started at least twelve months previously.

Maintenance revenues in 2001 were \$22.1 million, a decrease of \$4.6 million, or 17.2%, as compared to 2000. Approximately \$1.7 million of the decrease relates to divested product lines. The remainder of the decrease is attributable to lower license revenue from the legacy product lines during previous years resulting in the lapse of related maintenance contracts in excess of new contracts and renewals.

Consulting revenues in 2001 were \$18.3 million, a decrease of \$1.3 million, or 6.6%, as compared to 2000. The decrease in consulting revenues is attributable to the divested product lines, which generated revenues of \$2.1 million in the year ending December 31, 2000.

### **Costs of Licenses, Maintenance and Consulting**

Cost of licenses, maintenance and consulting in 2001 were \$18.2 million, a decrease of \$7.5 million, or 29.2%, as compared to 2000, and represented 37.1% and 50.0% of total revenues in 2001 and 2000, respectively.

The costs of licenses as a percentage of license revenues decreased in 2001 as compared to 2000. The decrease in 2001 results from a smaller proportion of license revenues being generated from our products that utilize technology licensed from third parties.

The cost of maintenance, as a percentage of related revenue, increased in 2001 compared to 2000. Although costs have remained substantially the same, maintenance revenues have decreased as discussed above.

The costs of consulting, as a percentage of related revenue, decreased in 2001 as compared to 2000. The decrease in 2001 is primarily attributable to higher utilization and realized rates associated with certain consulting engagements.

### **Sales and Marketing**

Sales and marketing costs in 2001 were \$12.5 million, a decrease of \$5.5 million, or 30.5%, as compared to 2000. As a percentage of total revenues, sales and marketing expenses were 25.4% and 34.9% in 2001 and



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2000, respectively. The decrease is mostly attributable to reductions in our discretionary spending and sales and marketing employee-related costs.

**Product Development**

Product development related expense, excluding amortization of capitalized software, was as follows (in thousands):

	<b>2001</b>	<b>2000</b>
Product development expenditures	\$ 10,032	\$ 16,671
Less:		
Additions to capitalized software	(1,708)	(3,441)
Product development expense	\$ 8,324	\$ 13,230

Product development expense decreased \$4.9 million, or 37.1%, in 2001 as compared to 2000 and was 17.0% and 25.7% of total revenues in 2001 and 2000, respectively. Additions to capitalized software decreased \$1.7 million, or 50.3%, in 2001 as compared to 2000 and were 17.0% and 20.6% of product development expenditures in 2001 and 2000, respectively. The decrease in product development expenditures capitalized in 2001 is primarily attributable to product development resources being allocated to projects that did not meet the criteria for capitalization.

In June 2000, we formed a wholly owned subsidiary, RareVision, Inc., to further the development and market testing of a business-to-business Internet model for a web-based, knowledge management analytical application for smaller businesses. Product development expenditures attributable to RareVision, Inc. amounted to \$2.9 million in fiscal 2001 and \$3.3 million in 2000.

We divested our IMMPOWER product line in April 2000 and our Aptos product line in October 2000. Product development expense attributable to the IMMPOWER and Aptos product lines was \$1.5 million in 2000.

**Amortization of Capitalized Software**

Capitalized software amortization in 2001 was \$3.4 million, a decrease of \$1.4 million, or 28.5%, as compared to 2000. The decrease in capitalized software amortization is primarily attributable to the impairment of \$4.8 million of capitalized software as part of our restructuring actions during 2000.

**General and Administrative**

General and administrative expenses in 2001 were \$5.9 million, a decrease of \$4.6 million, or 44.0%, as compared to 2000. As a percentage of total revenues, general and administrative expenses were 12.0% and 20.4% in 2001 and 2000, respectively. The decrease in 2001 is primarily due to lower employee and occupancy costs resulting from our restructuring actions in 2000.

**Impairment and Restructuring Charges**

There were no impairment or restructuring charges in fiscal 2001. Impairment and restructuring charges for fiscal 2000 were \$6.7 million, comprised of \$1.9 million for employee reductions and facilities consolidation and \$4.8 million for the impairment of capitalized software, primarily related to the legacy Tamaris product line (see Note 3: Impairment and Restructuring Charges).

**Interest and Other Income**

In 2001, we earned \$335,000 in interest income compared to \$809,000 in 2000, a decrease of \$474,000 or 58.6%. The decrease was due to lower interest rates and lower cash balances available for investment. Also, other income for the year ended December 31, 2001 includes a realized gain of \$442,000 from the disposal of the Aptos product line.



**Table of Contents****Income Tax Expense**

In 2001, we provided \$100,000 for state and foreign income taxes that could not be offset against net operating loss carryforwards, a decrease of \$82,000 or 45.1% compared to 2000. In 2000, we provided \$182,000 for state and foreign income taxes that could not be offset against net operating loss carryforwards.

**LIQUIDITY AND CAPITAL RESOURCES**

As of December 31, 2002, our principal sources of liquidity included cash, cash equivalents and short-term investments aggregating \$20.8 million, and funds from operations. In the first quarter of fiscal 2003 we cancelled our \$4.0 million line of credit. We never borrowed under this line of credit. We have future operating lease obligations of approximately \$9.5 million through 2007 (see Note 10: Commitments and Contingencies) and capital lease obligations of approximately \$79,000 through 2003.

	<b>Facilities</b>	<b>Equipment and Software</b>	<b>Capital Leases</b>	<b>Total</b>
2003	\$ 1,918	\$ 479	\$ 79	\$ 2,476
2004	1,923	4		1,927
2005	2,048	1		2,049
2006	1,849	1		1,850
2007	1,312			1,312
	<hr/>	<hr/>	<hr/>	<hr/>
Total	\$ 9,050	\$ 485	\$ 79	\$ 9,614
	<hr/>	<hr/>	<hr/>	<hr/>

In addition, we lease certain software on a month-to-month basis. On an annualized basis, the cost of this leased software would be approximately \$250,000.

Our operating activities, which included our United Kingdom operations through September 6, 2002, provided cash of \$2.3 million in 2002, used cash of \$205,000 in 2001, and used cash of \$10.3 million in 2000. The increase in cash generation was primarily driven by an improvement in operating income. Net income in 2002 of \$20.6 million, including a \$19.0 million gain relating to the sale of our United Kingdom operations, and the net loss in 2000 of \$26.7 million included \$365,000 and \$4.8 million respectively of non-cash charges related to impairment of certain capitalized software assets.

Financing activities comprise proceeds from employee stock purchase plan issuances, offset by capital lease payments. These activities provided cash of \$90,000, \$139,000 and \$1.9 million in 2002, 2001 and 2000, respectively. In 2002, 2001 and 2000, proceeds from the issuance of stock under our employee stock purchase plan and proceeds from stock options exercised provided \$231,000, \$293,000, and \$1.9 million in cash, respectively.

Excluding the movements between categories of cash and cash equivalents, investing activities include the proceeds from the divestiture of our United Kingdom operations, purchase of fixed assets, and additions to capitalized software. These activities provided \$13.4 million of cash in 2002, and used cash of \$4.5 million and \$4.0 million in cash during 2001 and 2000, respectively.

For the years ending December 31, 2002, 2001 and 2000, our capital expenditures were \$554,000, \$805,000 and \$614,000, respectively. Our capital expenditures are primarily computer equipment to support and maintain our infrastructure. The increase in additions for fiscal 2001 resulted from our implementation of a new internal financial reporting system; leasehold improvements and the infrastructure to support our relocated Chicago office; and the addition of infrastructure to support the personnel added following the reestablishment of the Eleven 5 business after our acquisition of the QSP intellectual property. With the divestiture of our United Kingdom operations in September 2002, we expect our future capital expenditures to be below historical levels.

For the years ending December 31, 2002, 2001 and 2000, cash used for software development costs was \$1.1 million, \$1.7 million and \$3.4 million, respectively. We released our e2 product in fiscal 2000 with further



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enhancements being released in 2001. The e2 product is now mature and we would not expect significant additional costs to be capitalized in the near term. No development costs were capitalized during the time we owned the Eleven 5 intellectual property. Our AFP product was in development from mid 2001 through fiscal 2002 and represents the majority of software development costs capitalized in fiscal 2002.

We believe that our principal sources of liquidity, which include cash, cash equivalents and short term investments of \$20.8 million as of December 31, 2002 and funds expected from operations will satisfy our currently anticipated working capital and capital expenditure requirements for at least the next twelve months. Variations in our working capital requirements are dependent primarily on the rate of growth in our revenues, the timing and mix of our revenues, and the timing of collections of accounts receivable associated with our revenues. However, the following factors could affect liquidity and capital resources:

Our performance is sensitive to general economic conditions. A sustained recession, in which customers delay or cancel discretionary software purchases, would be damaging to our operational results and cashflows.

Our ability to successfully transition our product offerings to collaborative commerce solutions and to gain market acceptance for our new products.

Our ability to align our operating costs with our revenue base, especially in relation to license and consulting revenues where the revenue streams are inconsistent.

Our operating results and cashflow would be significantly enhanced if we were to be successful in subletting our San Francisco office space.

We cannot assure you that we will not need to raise additional capital to fund operations within the next twelve months. We cannot assure you that additional financing can be obtained on acceptable terms, or at all. If additional funds are raised by issuing equity securities, dilution to stockholders may result. If adequate funds are not available, our financial condition, our results from operations and the market price of our stock could be adversely affected.

## **ADDITIONAL RISK FACTORS**

We operate in a rapidly changing environment that involves numerous risks and uncertainties that could have a material adverse effect on us. The following discussion details some, but not all, of these risks and uncertainties.

### **Our operating results may fluctuate, which may adversely affect the trading price of our stock.**

Our operating results fluctuate as a result of a variety of factors including:

the execution of new license agreements;

the shipment of software products;

customer acceptance criteria for services performed;

completion of milestone or other significant development requirements pursuant to our license agreements;

the financial terms of consulting agreements and the inclusion of fixed as opposed to variable pricing;

third-party royalty payments for licensed software;

the demand for our products and services;

changes in our product and services mix;

the development and launch of new products and services, and the life cycles of our existing products and services;



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product development expenditures required to update and expand our product portfolio and related third-party consulting costs;

sales and marketing expenses generally related to the entry into new markets with new or existing products and maintenance of market share in existing markets;

acquisitions and the integration and development of acquired entities or products;

competitive conditions in the industry; and

general economic conditions.

As a result, we believe that period-to-period comparisons of our operating results are not necessarily meaningful and should not be relied upon as indications of our future performance.

Our quarterly operating results are particularly dependent on the number of license agreement bookings we execute in each quarter. The amount of quarterly bookings has varied substantially from quarter to quarter due to a variety of reasons including:

a high proportion of license agreements are negotiated during the latter part of each quarter and these negotiations may not be completed before the quarter end;

the sales cycles for some of our products are relatively long due to our focus on enterprise solutions as opposed to individual products, which adds complexity to the customer's selection, negotiation and approval process;

our longer sales cycle resulting from our transition to e-business, as the transition to collaborative commerce involves coordination with multiple vendors that can delay the sales process;

the amount related to each booking may vary significantly due to the need for different solutions for different customers;

procurement procedures may vary from customer to customer, which may affect the timing of the bookings;

the period for a customer to complete product evaluations and to complete any subsequent purchase approval may be delayed due to resource limitations; and

economic, political and industrial conditions can adversely affect business opportunities without notice.

In addition, bookings that we execute during a particular quarter may not be recognized as revenue during such quarter because such bookings may not have met our revenue recognition criteria. We cannot assure you that we will be able to effect new bookings in accordance with historical results or management's expectations, and our inability to do so could have a material adverse effect on our operating results, financial condition and the market price of our stock.

While we typically sell our software under a standard license agreement, license agreements associated with large enterprise solutions often require the negotiation of terms and conditions that differ substantially from our standard license agreement terms. The negotiation of these agreements may extend the sales cycle. We may not always obtain terms and conditions that permit the recognition of revenue upon shipment of the licensed product. Accordingly, revenue may not be recognized after shipment of a product because specified milestones have not been met or because applicable services have not been completed.

We have and expect to enter into fixed-price consulting agreements, particularly in response to increased competition in the industry. We have recognized lower profit margins on certain fixed-price service agreements when compared to variable agreements. No assurance can be given that we will be able to conclude fixed-price agreements on terms that will allow us to achieve acceptable operating margins, and the failure to do so could have a material adverse effect on our operating results, financial condition and the market price of our stock.

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We historically have generated a majority of our consulting revenue from implementation and migration services. We have provided services that include, but are not limited to, Year 2000 readiness engagements, best practice solution engagements and other hardware and software solutions. We intend to continue to pursue consulting engagements for which we believe we are qualified. We cannot assure you that these engagements will result in profit margins equal to or greater than those engagements that are specific to a customer's product implementation. We cannot assure you that we will be able to obtain large consulting engagements to replace those that are concluded. Further, we cannot assure you that consulting revenue generated from non-implementation related projects will continue in the future. Our inability to obtain consulting engagements and derive adequate profit margins from such engagements could have a material adverse effect on our operating results, financial condition and the market price of our stock.

Our maintenance revenues are sensitive to a reduction in new license sales, customers completing migrations to different platforms, and customers discontinuing maintenance in an effort to reduce their operating costs.

Employee and facility related expenditures comprise a significant portion of our operating costs and expenses, and are therefore relatively fixed over the short term. In addition, our expense levels are based, in significant part, on our forecasted revenue. If revenue levels fall below our expectations, operating results are likely to be adversely affected. There can be no assurance that we will be able to achieve profitability on a quarterly or annual basis in the future. Any of the foregoing factors could cause our future operating results to fall below the expectations of public securities market analysts, which could have an adverse effect on the trading price of our common stock.

**We were delisted from the Nasdaq National Market, which may adversely affect the trading price of our stock.**

Since March 6, 2001 our stock has traded on the Over the Counter Bulletin Board. This is generally considered a less efficient market, and our stock price, as well as the liquidity of our common stock, may be adversely affected as a result. Further, it is unlikely that our stock will be relisted on the Nasdaq National Market, or any other exchange, in the future.

**The market price of our stock may experience volatility, which may cause the value of your investment in our common stock to decline.**

Technology companies, including ourselves, frequently experience volatility in their common stock prices. Factors such as quarterly fluctuations in results of operations, announcements of technological innovations by us or our competitors, the introduction of new products by us or our competitors, and macroeconomic conditions in the computer hardware and software industries generally may have a material adverse impact on the market price of our stock. If revenues or earnings in any quarter fail to meet the expectations of the investment community, our stock price could be impacted immediately. In addition, we have issued shares and stock options, which, if sold directly or exercised and sold on the open market in large concentrations, could cause our stock price to decline in the short term. Furthermore, the stock market has from time to time experienced extreme price and volume fluctuations that have particularly affected the market price for many technology companies, in some cases unrelated to the operating performance of those companies. These broad market fluctuations may materially adversely affect the market price of our stock.

**If we are unable to renew our existing third party license agreements or obtain new agreements, we may not be able to successfully develop our technology and our business, operating results and financial condition may be adversely affected.**

We generate revenue from internally developed software products, some of which utilize technology licensed from third parties. We expect to continue utilizing third party technology and may enter into agreements with additional business partners. If sales of software utilizing third party technology increase disproportionately, gross margins may be below historical levels due to third party royalty obligations. We cannot assure you that the third parties will renew existing agreements with us or will not require financial conditions that are unfavorable to us. Our maintenance fees are in part based on royalties that we have to pay to third parties. To the extent that we have third party royalty costs that we are unable to pass on to our



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customers, the profitability of our maintenance business will be adversely affected. In addition, we cannot assure you that existing third party agreements will not be terminated. If we are unable to continue utilizing third party technology, we may not be able to successfully develop certain of our current and new products and our business, operating results and financial condition could be adversely affected.

**If there is a downturn in the industry or in general economic conditions, our business, operating results and financial condition may be adversely affected.**

Certain software companies, including us, have experienced significant economic downturns as a result of technological shifts and competitive pressures. These downturns are characterized by decreased product demand, price erosion, work slowdowns and layoffs. Our operations have experienced and may continue to experience substantial fluctuations from period to period because of such industry patterns and general economic and political conditions which affect the timing of orders from customers. We have suffered from the postponement or cancellation of information technology spending at several customers or prospective customers, even when the spending in question has already been budgeted. We cannot assure you that such factors will not have a materially adverse effect on our business, operating results, financial condition, or market price of our stock.

**Our royalty revenue stream is dependent on the success of Novele in selling the Elevon 2 product.**

Following the disposal of our United Kingdom operations, Novele Limited has become the exclusive distributor for the Elevon 2 product in the United Kingdom and certain other territories. Our revenues, operating results and financial condition are likely to be adversely affected if Novele is unsuccessful in marketing and selling this product.

**If we are unable to compete successfully in our market it will harm our business.**

The business and financial applications software market for large, complex organizations is intensely competitive. Our principal competitors with e-business solutions are SAP AG, Oracle Corporation and PeopleSoft, Inc. With our analytical applications, we principally compete with Hyperion Solutions Corporation, Cognos, Inc. and Comshare, Inc.

We also compete to a lesser extent with other independent software application vendors. Some of our current and potential competitors have substantially greater financial, technical, marketing and sales resources than us. Some of these competitors also offer business application products not offered by us, primarily in the areas of human resources and manufacturing. However, we remain one of the few companies committed to providing and enhancing applications for the mainframe environment. Most of the competitors listed above compete with us by offering UNIX-based applications.

We encounter competition from a broad range of firms in the professional services market, including the current and former consulting divisions of the major accounting firms, which possess greater resources than we do, and small independent firms that compete primarily on the basis of price.

The principal competitive factors in the market for business and financial applications software and services include product functionality, flexibility, portability, integration, reliability, performance, product availability, speed of implementation, quality of customer support and user documentation, vendor reputation, experience, financial stability, cost effectiveness and price. We believe that we compete favorably with respect to these factors. There can be no assurance, however, that we will be able to compete successfully in the future, and the failure to do so could have a material adverse effect on our operating results, financial condition and the market price of our stock.

**If we are unable to stay current with the rapid technological change that characterizes the software industry, our products may not gain marketplace acceptance and our business, operating results and financial condition could suffer.**

The software industry is characterized by rapid technological change. The pace of change has accelerated due to advances in mainframe and client/ server technology and the growth in Internet, intranet and extranet utilization. We expect to evaluate potential opportunities and may invest in those that are compatible with our

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strategic direction. However, there can be no assurance that any such investments will be profitable. Our legacy products are also designed primarily for use with certain mainframe and client/server systems. The introduction of products embodying new technologies and the emergence of new industry standards can render existing products obsolete. Accordingly, our future success depends in part upon our ability to continue to enhance our current products and to develop and introduce new products that respond to evolving customer requirements and keep pace with technological development and emerging industry standards, such as new operating systems, hardware platforms, interfaces and third party applications software.

We cannot assure you that:

we will be successful in developing and marketing product enhancements or new products that respond to technological change, changes in customer requirements or emerging industry standards;

we will not experience difficulties that could delay or prevent the successful development, introduction and marketing of such products and enhancements; or

any new products or enhancements that we may introduce will achieve market acceptance.

The failure to do any of the above could have a material adverse effect on our operating results, financial condition and the market price of our stock.

**If we are unable to introduce, develop and market new and enhanced versions of our software products, we may be put at a competitive disadvantage.**

Our success depends on our continued ability to introduce, develop and market new and enhanced versions of our software products. However, we cannot assure you that this process can be maintained. We plan to continue our investment in product development in future periods. However, we cannot assure you that revenues will be sufficient to support the future product development that is required for us to be competitive. Although we may be able to release new products in addition to enhancements to existing products, we cannot assure you that our new or upgraded products will be accepted by the market, will not be delayed or canceled, or will not contain errors or bugs that could affect the performance of the product or cause damage to users' data.

**If we are unable to effectively protect our intellectual property, we may be put at a competitive disadvantage; and if we are involved in an intellectual property rights dispute, we may not prevail and may be subject to significant liabilities or required to license rights from a third party.**

We regard our products as proprietary. Through our license agreements with customers and our internal security systems, confidentiality procedures and employee agreements, we have taken steps to maintain the trade secrecy of our products. However, we cannot assure you that misappropriation will not occur. In addition, the laws of some countries do not protect our proprietary rights to the same extent as do the laws of the United States. We cannot assure you that the confidentiality of any proprietary information will provide any meaningful competitive advantage. We have no patents relating to our products. We believe that, because of the rapid pace of technological change in the computer software industry, that patents and copyrights are less significant than factors such as the knowledge, ability and experience of our employees, frequent product enhancements and the timeliness and quality of support services. We cannot assure you that our current efforts to retain our products as proprietary will be adequate. The failure to do so could have a material adverse effect on our operating results, financial condition and the market price of our stock.

Although we believe that our products do not infringe upon the proprietary rights of third parties, we cannot assure you that third parties will not assert infringement claims against us in the future with respect to current or future products, or that any such assertions will not require us to enter into royalty arrangements or result in costly litigation, or result in us being unable to use the intellectual property.

**We may be subject to product liability claims if our software fails in mission critical applications, and limitation of liability provided in our license agreements may not protect us.**

The license and support of our software for use in mission critical applications creates the risk of product liability claims against us. Our license agreements with our customers contain provisions designed to limit our

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exposure to potential product liability claims. It is possible, however, that the limitation of liability provisions contained in such license agreements may not be enforced as a result of international, federal, state and local laws or ordinances or unfavorable judicial decisions. Damage liability or injunctive relief resulting from such claims could have a materially adverse impact on our business, operating results and financial condition.

**Our business depends on certain key executives, the loss of whom could weaken our management team, and on attracting and retaining qualified personnel.**

We believe that our continued success depends in large part upon our ability to attract, train and retain highly skilled technical, sales, marketing and managerial personnel. Competition for such personnel is intense and we sometimes experience difficulty in locating candidates with appropriate qualifications or within desired geographic locations. The success of our business is dependent on our ability to attract, train, retain and productively manage such personnel.

**We have excess capacity in our San Francisco headquarters.**

Our headquarters are located in San Francisco under a lease that expires in 2007. Although historical commercial building vacancy rates have been low in San Francisco, recent changes in the economy have resulted in a significant increase in available office space. Our San Francisco headquarters office space exceeds our current needs, and while we are seeking to reduce this excess office space we cannot assure you that this can be achieved at economic terms acceptable to us.

**The difficulties inherent in integrating acquired businesses, products or technology could have an adverse effect on our results of operations, business and financial condition.**

We have acquired and may continue to acquire complimentary businesses, products or technology. The process of integrating an acquired company's business into our operations may result in unforeseen operating difficulties and expenditures and may require significant management attention that would otherwise be available for the ongoing development of our business. Acquisitions involve numerous risks, including difficulties in the assimilation of operations, technologies and products of the acquired company, risks associated with entering markets in which we have no or limited direct prior experience and the potential loss of key employees of the acquired company. We cannot assure you that we will successfully integrate any new acquisition or realize any anticipated benefits of an acquisition. Further, future acquisitions by us could result in potentially dilutive issuances of equity securities, the incurrence of debt and contingent liabilities and amortization related to goodwill and other intangible assets, which could materially affect our operating results and financial condition.

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

We have short-term U.S. dollar interest-bearing investments, aggregating \$7.8 million at December 31, 2002, that are subject to interest rate risk. We analyzed our investments at year-end to determine the sensitivity to interest rate changes. The fair values of these instruments were determined by net present values. Our sensitivity analysis used the same change in interest rates for all maturities. All other factors were held constant. If interest rates changed by 1%, the expected effect on net income related to our investments would be immaterial.

Following the divestiture of our United Kingdom operations, our exposure to exchange rate risk is minimal. We do not engage in interest rate swaps or enter into foreign currency forward contracts.

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

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Consolidated Statements of Stockholders' Equity (Deficit) for the years ended December 31, 2002, 2001 and 2000	29
Consolidated Statements of Cash Flows for the years ended December 31, 2002, 2001 and 2000	30
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**INDEPENDENT AUDITORS' REPORT**

To the Stockholders and Board of Directors of Eleven, Inc.:

We have audited the accompanying consolidated balance sheets of Eleven, Inc. and subsidiaries as of December 31, 2002 and 2001, and the related consolidated statements of operations, stockholders' equity (deficit) and cash flows for each of the three years in the period ended December 31, 2002. Our audits also included the consolidated financial statement schedule listed in Item 15(a)2. These financial statements and the financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and consolidated financial statement schedule based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 Eleven, Inc. and its subsidiaries at December 31, 2002 and 2001, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2002 in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such consolidated financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ DELOITTE & TOUCHE LLP

San Francisco, California

March 17, 2003

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## ELEVEN, INC.

## CONSOLIDATED BALANCE SHEETS

	December 31,	
	2002	2001
	(In thousands, except per share amounts)	
ASSETS		
Current Assets:		
Cash and equivalents	\$ 13,060	\$ 4,583
Short-term investments	7,776	458
Accounts receivable, net of allowance for doubtful accounts of \$146 in 2002 and \$476 in 2001	4,730	11,431
Prepaid expenses	683	904
Other receivables	705	50
Total current assets	26,954	17,426
Property and equipment, net	865	1,740
Capitalized software, net of accumulated amortization of \$53,270 in 2002 and \$52,865 in 2001	1,650	4,853
Long-term accounts receivable	624	562
Other assets	370	431
Total assets	\$ 30,463	\$ 25,012
LIABILITIES AND STOCKHOLDERS EQUITY (DEFICIT)		
Current Liabilities:		
Accounts payable	\$ 859	\$ 2,411
Accrued liabilities	3,171	8,660
Deferred revenue	6,851	11,809
Total current liabilities	10,881	22,880
Deferred revenue	1,286	2,901
Other long-term obligations	1,313	2,818
Total liabilities	13,480	28,599
Commitments and contingencies (see Note 10)		
Stockholders' equity (deficit):		
Common stock, \$.001 par value: 50,000 shares authorized; issued 15,517 shares December 31, 2002; 14,987 shares December 31, 2001	16	15
Additional paid-in capital	76,981	76,751
Accumulated other comprehensive income	134	358
Accumulated deficit	(60,148)	(80,711)
Total stockholders' equity/(deficit)	16,983	(3,587)
Total liabilities and stockholders' equity/(deficit)	\$ 30,463	\$ 25,012

See notes to consolidated financial statements



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## ELEVON, INC.

## CONSOLIDATED STATEMENTS OF OPERATIONS

	Year Ended December 31,		
	2002	2001	2000
(In thousands, except per share amounts)			
<b>REVENUES:</b>			
License and royalty	\$ 3,632	\$ 8,665	\$ 5,131
Maintenance	19,619	22,110	26,706
Consulting	18,662	18,290	19,585
Total revenues	41,913	49,065	51,422
<b>OPERATING EXPENSES:</b>			
Costs of revenues:			
Costs of licenses, maintenance and consulting	16,691	18,206	25,696
Amortization of capitalized software	2,807	3,398	4,755
Sales and marketing	9,078	12,459	17,929
Product development	5,949	8,324	13,230
General and administrative	6,077	5,869	10,482
Impairment of capitalized software	365		4,799
Restructuring charges	1,136		1,905
Special credit	(1,732)		
Total operating expenses	40,371	48,256	78,796
Operating income (loss)	1,542	809	(27,374)
Interest and other income , net	165	777	809
Gain on sale of United Kingdom operations and Elevon 5 intellectual property	18,956		
Income (loss) before income taxes	20,663	1,586	(26,565)
Provision for income taxes	100	100	182
<b>NET INCOME (LOSS)</b>	<b>\$ 20,563</b>	<b>\$ 1,486</b>	<b>\$ (26,747)</b>
<b>BASIC NET INCOME (LOSS) PER SHARE</b>	<b>\$ 1.34</b>	<b>\$ 0.10</b>	<b>\$ (1.84)</b>
Shares utilized to compute basic net income (loss) per share	15,332	14,917	14,535
<b>DILUTED NET INCOME (LOSS) PER SHARE</b>	<b>\$ 1.30</b>	<b>\$ 0.10</b>	<b>\$ (1.84)</b>
Shares utilized to compute diluted net income (loss) per share	15,797	14,958	14,535

See notes to consolidated financial statements



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## ELEVEN, INC.

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)

	Common Stock		Treasury Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total Stockholders Equity/(Deficit)
	Shares	Amount	Shares	Amount				
(In thousands, except share amounts)								
<b>Balance at December 31, 1999</b>	14,257,185	\$ 14	(26,091)	\$ (44)	\$74,566	\$ 33	\$ (55,450)	\$ 19,119
Common stock issued under stock option and employee stock purchase plans	403,394	1	26,091	44	1,892			1,937
Comprehensive loss:								
Currency translation adjustment						398		
Unrealized gain on investments						70		
Net loss for 2000							(26,747)	
Total comprehensive loss								(26,279)
<b>Balance at December 31, 2000</b>	14,660,579	15			76,458	501	(82,197)	(5,223)
Common stock issued under stock option and employee stock purchase plans	326,908				293			293
Comprehensive income (loss):								
Currency translation adjustment						(150)		
Unrealized gain on investments						7		
Net income for 2001							1,486	
Total comprehensive income								1,343
<b>Balance at December 31, 2001</b>	14,987,487	15			76,751	358	(80,711)	(3,587)
Common stock issued under stock option and employee stock purchase plans	529,778	1			230			231
Comprehensive income (loss):								
Currency translation adjustment						(217)		
Unrealized loss on investments						(7)		
Net income for 2002							20,563	
Total comprehensive income								20,339
<b>Balance at December 31, 2002</b>	15,517,265	\$ 16		\$	\$76,981	\$ 134	\$ (60,148)	\$ 16,983

See notes to consolidated financial statements



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## ELEVEN, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	2002	2001	2000
(In thousands)			
<b>Cash Flows From Operating Activities:</b>			
Net income (loss)	\$ 20,563	\$ 1,486	\$ (26,747)
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:			
Depreciation and amortization	3,741	4,631	6,806
Provision for doubtful accounts	99	(167)	24
Special Credit (Note 4)	(1,732)		
(Gain)/Loss on property retirements	27	(49)	
Impairment of capitalized software	365		4,799
Gain on sale of United Kingdom operations and e5 intellectual property	(18,956)		
Changes in operating assets and liabilities:			
Accounts receivable	2,119	(2,128)	7,826
Prepays and other assets	(622)	(50)	1,617
Accounts payable and accrued liabilities	(2,913)	(3,490)	(3,604)
Deferred revenue	(230)	(547)	(3,608)
Proceeds from divestitures			946
Disposals of fixed and other assets in divested activities			1,122
Other	(181)	109	493
Net cash provided (used) by operating activities	2,280	(205)	(10,326)
<b>Cash Flows From Financing Activities:</b>			
Proceeds from employee stock purchase plan issuances and stock options exercised	231	293	1,937
Capital lease payments	(141)	(154)	(21)
Net cash provided by financing activities	90	139	1,916
<b>Cash Flows From Investing Activities:</b>			
Purchases of short-term and long-term investments	(7,798)	(4,490)	(3,635)
Maturities of short-term investments	458	7,704	500
Sales of short-term investments		1,700	10,611
Proceeds from gain on sale of United Kingdom operations and e5 intellectual property, net of expenses of \$835	15,065		
Purchases of property and equipment	(554)	(805)	(614)
Purchase of QSP intellectual property		(2,000)	
Additions to capitalized software	(1,086)	(1,708)	(3,441)
Other	22	29	21
Net cash provided by investing activities	6,107	430	3,442
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	<b>8,477</b>	<b>364</b>	<b>(4,968)</b>
<b>Cash and Cash Equivalents Beginning of Period</b>	<b>4,583</b>	<b>4,219</b>	<b>9,187</b>
<b>Cash and Cash Equivalents End of Period</b>	<b>\$ 13,060</b>	<b>\$ 4,583</b>	<b>\$ 4,219</b>

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## Supplemental Disclosure:

Cash paid for income taxes	\$ 111	\$ 80	\$ 305
	<u>          </u>	<u>          </u>	<u>          </u>
Interest paid on capital leases	\$ 10	\$ 20	\$ 17
	<u>          </u>	<u>          </u>	<u>          </u>

See notes to consolidated financial statements

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Amounts in thousands, except per share data)

**1. Organization and Summary of Significant Accounting Policies**

*Description of the Company.* The Company (hereinafter "Elevon", "Walker" or the "Company") was incorporated in California in 1973 as Walker Interactive Systems, Inc. and reincorporated in Delaware in March 1992. In May 2002 we formally changed our name to Elevon, Inc. We design, develop, market and support, on a worldwide basis, a family of enterprise financial, operational and analytical software products that enable large and medium-sized organizations, higher education institutions, and federal, state and government agencies to optimize their business processes, reduce business costs, and improve management information needed to run their business. The Company derives its revenues from software licensing, software maintenance and professional consulting services. The Company's e-business solutions and analytic applications are licensed to large and mid-size companies and similarly sized governmental organizations worldwide.

During 1999, Walker changed its strategic direction to emphasize the e-business solutions and analytical product lines, concentrating on refocusing the Company as a provider of e-business solutions. In 1999 and during 2000, the Board of Directors approved restructuring plans designed to reduce costs and strengthen the Company's position to successfully execute its e-business strategy. In refocusing its resources and efforts on e-business solutions for the enterprise, the Company incurred impairment and restructuring charges and divested its IMMPOWER and Aptos product lines (see Note 3: Impairment and Restructuring Charges and Note 4: Acquisitions and Divestitures).

On September 6, 2002, we sold our United Kingdom operations and our Elevon 5 intellectual property to Novele Limited ("Novele"), located in London, United Kingdom. Under the terms of a share purchase agreement, we sold the stock of our wholly owned subsidiary, Elevon International Limited, to Novele for consideration of \$16.5 million. In addition to acquiring the Elevon operations headquartered in the United Kingdom, Novele acquired the QSP ("Elevon 5") intellectual property, which we had previously acquired from the administrative receiver for the QSP Group PLC in November 2001 for \$2.0 million in cash. Novele also became an exclusive distributor of the Elevon 2 software in the United Kingdom and certain other territories, pursuant to a software distribution agreement.

*Principles of Consolidation.* The consolidated financial statements include the accounts of Elevon, Inc. and its wholly owned subsidiaries. All inter-company balances and transactions have been eliminated.

*Use of Estimates.* The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual amounts could differ from those estimates.

Significant estimates used in the preparation of consolidated financial statements include:

(i) *Capitalization and amortization of product development costs.* Software development costs are capitalized when technological feasibility is established and are generally amortized over two years, upon release to customers. The decision to commence capitalization and the rate of amortization require estimates of future gross revenues from the product that are dependent upon factors such as market acceptance and the rate of technological change. We perform periodic reviews of such estimates and, if appropriate, revise the amortization rate.

(ii) *Accruals associated with restructurings and divestitures.* Commencing in 1999, the Company began to redefine its core business and implemented a significant change in its strategic direction. This has resulted in the divestiture of three product lines, the rationalization of international operations, the impairment of certain capitalized software, the consolidation of facilities and the severance of employees. All these actions required estimates, which are periodically reviewed and adjusted, if appropriate, based on the current circumstances.

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

The amounts that the Company will ultimately incur or recover could differ materially from the Company's current estimates. The underlying assumptions and facts supporting these estimates could change in 2003 and thereafter.

*Cash and Cash Equivalents.* Cash equivalents are stated at cost, which approximates fair value. All liquid investments with original maturities of three months or less are considered cash, cash equivalents and short-term investments.

*Short Term Investments.* The Company classifies investments that mature in less than one year as short-term investments, and investments that have contractual maturities of more than one year as long-term investments. The Company's short-and long-term investments are classified as available-for-sale and reported at fair value. Net unrealized gains and losses are excluded from earnings and reported net of income taxes as accumulated other comprehensive income in stockholders' equity/ (deficit). Realized gains and losses are computed based on the amortized cost of each security. There were no material gross realized gains or losses from the sale of investments during the three-year period ended December 31, 2002.

*Capitalized Software.* Capitalized software includes certain costs of purchased and internally developed software, and is stated at the lower of cost or net realizable value. Capitalization of internally developed software begins upon the establishment of technological feasibility. Amortization of capitalized development costs begins when the products are available for general release to customers, and is computed as the greater of (i) the ratio of current gross revenues for a product to the total of current and anticipated future gross revenues for the product, or (ii) the straight-line method over the remaining estimated economic life of the product. It is possible that these estimates of anticipated future gross revenues, the remaining estimated economic life of the products, or both, could be reduced significantly due to either competitive factors or the rate of technological change.

*Property and Equipment.* Property and equipment is stated at cost. Depreciation is computed primarily utilizing the straight-line method over the estimated useful lives that range from three to ten years. Leasehold improvements are amortized utilizing the straight-line method over the lesser of the estimated useful lives or remaining lease terms.

*Revenue Recognition.* The Company licenses software to end-users under non-cancelable license agreements and provides services such as installation, implementation, training, and software maintenance. Software license revenue for contracts not requiring significant customization services is recognized upon meeting each of the following criteria: an executed agreement has been signed; products have been shipped; the license fee is fixed and determinable; collection of the resulting receivable is probable; and vendor-specific objective evidence exists to allocate the total fee to any undelivered elements of the arrangement. Vendor-specific objective evidence is based on the price generally charged when an element is sold separately, or if not yet sold separately, is established by authorized management. Maintenance revenue is recognized ratably over the maintenance period, generally one year. Revenue from consulting and other services is recognized as the related services are provided.

*Concentration of Credit Risk and Credit Evaluation.* The Company's investment portfolio is diversified and consists of short-term investment grade securities. The Company's accounts receivable are derived from sales to customers located in the United States, Europe/ Middle East/ Africa and Asia Pacific. The Company performs ongoing credit evaluations of its customers' financial condition and maintains reserves for estimated losses.

During the years ended December 31, 2002 and 2001, revenue generated from products and services provided to ADT Security Services, Inc., a unit of Tyco International Ltd., represented 18.2% and 17.4% of revenue, respectively. The same customer represented 18.2% and 17.6% of accounts receivable as of December 31, 2002 and 2001, respectively. No customer represented in excess of 10% of total revenues or accounts receivable for 2000.

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

*Translation of Foreign Currencies.* The functional currency of the Company's foreign subsidiaries is the respective local currency. Accordingly, assets and liabilities of the foreign subsidiaries are translated to U.S. dollars at the exchange rates in effect as of the balance sheet date and results of operations for each subsidiary are translated using average rates in effect for the period presented. Gains and losses from translation of foreign subsidiaries' financial statements are reported as a separate component of stockholders' equity. Gains and losses from transactions denominated in currencies other than the functional currencies of the Company or its subsidiaries are included in general and administrative expense and have not been significant.

*Earnings Per Share.* Basic EPS is computed by dividing net income (loss) by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur from common shares issuable through stock options and other convertible securities.

*Certain Significant Risks and Uncertainties.* The Company operates in the software industry, and accordingly, can be affected by a variety of factors. For example, management believes that the Company's inability to appropriately manage any of the following areas could have a significant negative effect on the Company's future financial position, results of operations and cash flows: focusing the Company's strategy around the e-business market; market acceptance of the Company's products acquired, developed and under development for the e-business market; fundamental changes in the technology underlying software products; sustained weakness in the economy; development and management of strategic alliances; and the hiring and retention of key employees.

*Recently Issued Accounting Standards.* In June 1998 and June 1999, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 133, Accounting for Derivative Instruments and Hedging Activities, and SFAS No. 137, Accounting for Derivative Instruments and Hedging Activities - Deferral of the Effective Date of FASB Statement No. 133. These statements define derivatives, require that all derivatives be carried at fair value and provide for hedge accounting when certain conditions are met. Under SFAS No. 133, certain contracts that were not formerly considered derivatives may now meet the definition of a derivative. The Company evaluated the requirements of SFAS No. 133 and concluded that adoption of this statement, effective January 1, 2001, had no impact on the Company's financial position or results of operations.

In October 2001, the FASB issued SFAS No. 144, Accounting for the Impairment of Long-Lived Assets, which addresses financial accounting and reporting for the impairment or disposal of long-lived assets. SFAS No. 144 supersedes SFAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of, but retains the fundamental provisions for recognizing and measuring impairment of long-lived assets to be held and used or disposed of by sale. The Statement also supersedes the accounting and reporting provisions for the disposal of a segment of a business, and eliminates the exception to consolidation for a subsidiary for which control is likely to be temporary. SFAS No. 144 eliminates the conflict between accounting models for treating the dispositions of long-lived assets that existed between SFAS No. 121 and the guidance for a segment of a business accounted for as a discontinued operation by adopting the methodology established in SFAS No. 121, and also resolves implementation issues to SFAS No. 121. The Company evaluated the requirements of SFAS No. 144 and concluded that adoption of this statement, effective January 1, 2002, had no impact on the Company's financial position or results of operations.

In June 2002, the FASB issued SFAS No. 146, Accounting for Costs Associated with Exit or Disposal Activities, which addresses accounting for restructuring and similar costs. SFAS No. 146 supersedes previous accounting guidance, principally Emerging Issues Task Force Issue No. 94-3, Liability Recognition for Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring). The Company will adopt the provisions of SFAS No. 146 for restructuring activities initiated after December 31, 2002. SFAS No. 146 requires that the liability for costs associated with an exit or disposal activity be recognized when the liability is incurred. Under EITF 94-3, a liability for an exit cost was recognized at the date of the Company's

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

commitment to an exit plan. SFAS No. 146 also establishes that the liability should initially be measured and recorded at fair value. Accordingly, SFAS No. 146 may affect the timing of recognizing future restructuring costs as well as the amounts recognized.

In December 2002, the FASB issued SFAS No. 148, Accounting for Stock-Based Compensation-Transition and Disclosure. SFAS No. 148 amends SFAS No. 123, Accounting for Stock-Based Compensation, to provide alternative methods of transition for a voluntary change to the fair value-based method of accounting for stock-based employee compensation ( transition provisions ). In addition, SFAS No. 148 amends the disclosure requirements of Accounting Principles Board ( APB ) Opinion No. 28, Interim Financial Reporting, to require proforma disclosure in interim financial statements by companies that elect to account for stock-based compensation using the intrinsic value method prescribed in APB No. 25, Disclosure Provisions. The transition methods of SFAS No. 148 are effective for financial statements for fiscal years ending after December 15, 2002. The company continues to use the intrinsic value method of accounting for stock-based compensation. As a result, the transition provisions do not have an effect on the Company's consolidated financial statements. The Company has adopted the disclosure requirements of SFAS No. 148.

*Stock-Based Compensation.* At December 31, 2002 the Company has three stock-based employee compensation plans, which are described more fully in Note 9. The Company accounts for those plans under the recognition and measurement principles of APB Opinion No. 25, Accounting for Stock Issued to Employees, 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 FASB Statement No. 123, Accounting for Stock Based Compensation, to stock-based employee compensation. Refer to Note 9 for the assumptions used in calculating the estimated fair value of the stock options.

	Year Ended December 31,		
	2002	2001	2000
Net income (loss):			
As reported	\$ 20,563	\$ 1,486	\$ (26,747)
Deduct: Total stock based employee compensation	(1,442)	(2,468)	(4,565)
Pro forma	\$ 19,121	\$ (982)	\$ (31,312)
Earnings (loss) per share:			
Basic as reported	\$ 1.34	\$ 0.10	\$ (1.84)
Basic Pro forma	\$ 1.25	\$ (0.07)	\$ (2.15)
Diluted as reported	\$ 1.30	\$ 0.10	\$ (1.84)
Diluted Pro forma	\$ 1.21	\$ (0.07)	\$ (2.15)

**2. Comprehensive Income (Loss)**

The components of comprehensive income (loss) are as follows:

	Year Ended December 31,		
	2002	2001	2000
Net income (loss)	\$ 20,563	\$ 1,486	\$ (26,747)
Currency translation adjustment	(217)	(150)	398
Unrealized gain/(loss) on investments	(7)	7	70
Total comprehensive income (loss)	\$ 20,339	\$ 1,343	\$ (26,279)





**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****3. Impairment and Restructuring Charges**

During the quarters ended June 30 and December 31, 2002, the Board of Directors approved restructuring plans to reduce operating costs and strengthen the Company's position to successfully execute its strategy. The Company recorded a pre-tax restructuring charge totaling \$1.1 million, mainly for severance costs related to the involuntary termination of 68 employees in the Company's United States and United Kingdom operations, primarily in the sales, professional services, research and development and customer support departments.

In accordance with SFAS No. 86, Accounting for the Costs of Computer Software to Be Sold, Leased or Otherwise Marketed, the Company periodically evaluates capitalized software carrying amounts against the related estimated net realizable values of the assets. During the second quarter of 2002, this evaluation indicated that the estimated net realizable values of certain assets were not sufficient to recover the associated carrying values and resulted in an impairment charge of \$365. The following table summarizes the restructuring and impairment charges incurred in 2002:

	<b>Fiscal 2002 Charges</b>	<b>Asset Writedown</b>	<b>Cash Payments in 2002</b>	<b>Non-Cash Charges in 2002</b>	<b>Balance at December 31, 2002</b>
Employee severance	\$ 1,048	\$	\$(773)	\$(47)	\$ 228
Legal, outplacement services and other restructuring costs	88		(37)	(1)	50
Impairment of capitalized software	365	(365)			
	<u>1,501</u>	<u>\$(365)</u>	<u>\$(810)</u>	<u>\$(48)</u>	<u>\$ 278</u>

The remaining cash obligations are expected to be paid during the first three quarters of 2003. The remaining liability of \$278 is recorded in Accrued Liabilities on the balance sheet as of December 31, 2002.

During the quarter ended September 30, 2000, the Board of Directors approved a strategic restructuring plan designed to reduce costs and strengthen the Company's position to successfully execute its e-business strategy. The Company recorded a pretax restructuring charge totaling \$1.9 million comprised mainly of severance costs related to the involuntary termination of employees in the Company's United States and United Kingdom operations, and costs arising from the consolidation of facilities in San Francisco and Aylesbury, United Kingdom. These severance costs were paid during fiscal 2000 and 2001.

In accordance with SFAS No. 86, Accounting for the Costs of Computer Software to Be Sold, Leased or Otherwise Marketed, the Company periodically evaluates capitalized software carrying amounts against the related estimated net realizable values of the assets. During the third quarter of 2000, this evaluation indicated that the estimated future undiscounted cashflows were not sufficient to recover the carrying values of certain assets and resulted in an impairment charge of \$4.8 million, primarily related to the legacy Tamaris product.

**4. Acquisition and Divestitures*****Fiscal 2001 and 2002 Acquisition and Divestiture***

On November 1, 2001, the Company acquired from the administrative receiver of QSP Group PLC (QSP), QSP's intellectual property and a consulting contract. QSP, headquartered in Newcastle, United Kingdom, was a global provider of financial systems on mainframe and UNIX platforms to Global 2000 companies and was placed in administrative receivership on October 17, 2001. The acquisition cost of \$2.0 million was allocated to the intellectual property and was amortized on a straight line-basis over a two-year period from the date of acquisition. Subsequent to November 1, 2001, the Company hired certain former QSP employees, provided consulting services under the acquired contract, and engaged with the former QSP



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

customer base to establish new relationships. Revenues and costs related to these activities have been included in the Company's consolidated financial statements from November 1, 2001 through September 6, 2002.

On September 6, 2002, the Company sold its United Kingdom operations and its Eleven 5 intellectual property to Novele Limited ( Novele, now doing business as Arelon ), located in London, United Kingdom. Under the terms of a share purchase agreement, Eleven sold the stock of its wholly owned subsidiary, Eleven International Limited, to Novele for consideration of \$16.5 million. Approximately \$15.7 million cash was received at closing. The remaining balance of approximately \$800 was due on or before December 31, 2002 subject to certain conditions under the terms of the agreement. We deferred \$200 of the gain and subsequently recognized it during the fourth quarter of fiscal 2002 following the completion of certain customer requirements. We have informally agreed with Arelon to extend, on a month-to-month basis, the remaining \$600,000, plus interest. In addition to acquiring the Eleven operations headquartered in the United Kingdom, Novele acquired the Eleven 5 intellectual property, which Eleven had acquired from the administrative receiver for QSP in November 2001. Novele also became an exclusive distributor of Eleven 2 and Active Financial Planning ( AFP ) software in the United Kingdom and certain other territories, pursuant to a software distribution agreement. Under the terms of the distribution agreement, for the specified territories the Company will receive a royalty based on a percentage applied to actual maintenance revenues and new license sales of the Eleven 2 and AFP products.

The Company recognized an after-tax gain in respect of the above transaction of \$19.0 million, or \$1.20 per diluted share, in the consolidated statement of operations for the year ended December 31, 2002. The gain was calculated as follows:

Proceeds received	\$ 15,900
Proceeds receivable	600
Transaction costs	(835)
Net book value of Eleven 5 intellectual property	(1,167)
Elimination of deficit	4,458
	<u>\$ 18,956</u>

The operations and related intellectual property sold had revenues, operating expenses (including amortization) and net income (loss) as follows:

	<b>Twelve Months Ended December 31,</b>		
	<b>2002</b>	<b>2001</b>	<b>2000</b>
Total revenue	\$ 12,916	\$ 12,098	\$ 12,758
Total expenses	\$ 11,206	\$ 10,532	\$ 15,978
Net income/(loss) before interest and taxes	\$ 1,710	\$ 1,566	\$ (3,220)
Diluted net income/(loss) per share	\$ 0.11	\$ 0.10	\$ (0.21)

***Fiscal 2000 Divestitures***

In October 2000, the Company sold the net assets of its Aptos product line to B-Plan Information Systems Limited ( B-Plan ). The Aptos product line was an integrated suite of client/server financial applications for medium-sized companies and was marketed primarily in the United Kingdom. The divestiture agreement provided for total consideration of approximately \$2.3 million. The Company received an initial payment of approximately \$425 in December 2000, and, in October 2001, the Company and B-Plan executed a mutual release from any and all claims associated with the divestiture agreement. Under the terms of the mutual release agreement, B-Plan paid the Company approximately \$442, including interest, in November 2001 and is obligated to pay the Company an aggregate of £400 in quarterly installments from April 2002 through January 2006. The first quarterly payment from B-Plan was received in April 2002 and total payments of £75 have been recognized in the financial statements for fiscal 2002 as received.



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

In April 2000, the Company sold its stock ownership in Revere Inc. ( Revere ) to Gores Technology Group ( GTG ). Revere's main product comprised the IMMPOWER asset management application. The divestiture agreement provided that GTG pay the Company \$500 at closing, and, dependent upon the parties reaching mutual agreement on a final determination of Revere's net assets as defined in the divestiture agreement, an additional amount may be due to or from GTG. Management believes no additional amounts are due to or from GTG.

During the period that the Company owned and operated the divested product lines, reserves were established in the normal course of business to provide for contractual and other obligations. The Company retained certain of those reserves when the product lines were divested to cover certain existing obligations and those that were expected to arise from the change in ownership. During the approximately two-year period since the divestitures, the Company believes that it has discharged substantially all obligations associated with the divestitures through cash payments and negotiation. The residual amount of \$1.7 million has been included as a special credit in the consolidated statement of operations during the year ended December 31, 2002.

**5. Short-Term Investments**

Short term investments available-for-sale are summarized as follows:

<b>December 31, 2002</b>	<b>Amortized Costs</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>
Short-term investments	\$7,780	\$	\$(4)	\$7,776
<b>December 31, 2001</b>	<b>Amortized Costs</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>
Short-term investments	\$455	\$ 3	\$	\$458

**6. Property and Equipment**

Property and equipment at December 31, 2002 and 2001 are comprised of the following:

	<b>December 31,</b>	
	<b>2002</b>	<b>2001</b>
Equipment	\$ 4,280	\$ 16,612
Furniture and fixtures	905	1,594
Leasehold improvements	378	884
Property under capital leases	2,698	3,549
	8,261	22,639
Less:		
Accumulated depreciation and amortization	(7,396)	(20,899)

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Property and equipment, net	\$ 865	\$ 1,740
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Depreciation and amortization expense totaled \$934, \$1.2 million and \$2.1 million for 2002, 2001, and 2000, respectively. Amortization expense for capital leases during the years ending December 31, 2002, 2001 and 2000 totaled \$143, \$128, and \$161, respectively, and additions to equipment under capital leases totaled zero, \$136 and \$240, respectively. The net book value of property under capital leases as of December 31, 2002, 2001 and 2000 was \$62, \$205 and \$351, respectively. During 2002 assets with a historical cost of \$9.7 million and net book value \$16 were written off.

**Table of Contents****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****7. Liabilities**

Accrued liabilities are comprised of the following:

	<b>December 31,</b>	
	<b>2002</b>	<b>2001</b>
Salaries, commissions, and other compensation	\$ 965	\$2,588
State, foreign and taxes other than on income	486	1,259
Accrued facilities expenses	81	452
Royalties	507	614
Current portion of capital leases	79	71
Restructuring expenses	278	
Other accrued expenses	775	3,676
	<b>\$3,171</b>	<b>\$8,660</b>

Deferred revenue (current) includes deferred software maintenance of \$6.6 million and \$10.6 million at December 31, 2002 and 2001, respectively.

Other long-term obligations are comprised of the following:

	<b>December 31,</b>	
	<b>2002</b>	<b>2001</b>
Accrued facilities expenses	\$ 1,076	\$2,070
Long term portion of capital leases		149
Taxes other than on income	237	265
Other		334
	<b>\$ 1,313</b>	<b>\$2,818</b>



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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**8. Income Taxes**

The Company's deferred tax balances at December 31, 2002 and 2001 are as follows:

	December 31,	
	2002	2001
<b>Deferred Tax Assets:</b>		
Deferred revenue recognized for tax	\$ 96	\$ 204
Excess book depreciation over tax depreciation	594	514
Accrued liabilities and reserves	607	1,635
Software development costs capitalized for tax	2,734	3,160
Research and development credits	3,688	3,632
Alternative minimum tax credit carryforwards	488	486
Net operating loss carryforwards	8,110	10,499
Foreign tax credits carryforwards	1,312	1,647
Foreign losses	374	3,855
Capital loss carryover	9,745	4,608
Other	279	295
	<u>28,027</u>	<u>30,535</u>
Valuation allowance	(28,027)	(30,535)
Deferred Tax Assets - net	<u>\$</u>	<u>\$</u>

The Company established a 100% valuation allowance at December 31, 2002 and 2001 due to the uncertainty of realizing future tax benefits from its net operating loss carryforwards and other deferred tax assets.

At December 31, 2002, the Company has federal net operating loss carryforwards of approximately \$23.0 million which expire in varying amounts from 2008 through 2020, federal research tax credits of \$1.5 million which expire in varying amounts from 2005 through 2022 and capital loss carryovers of \$24.5 million which expire in varying amounts from 2005 through 2007. Foreign tax credits of \$335 expired in 2002, with the remaining credits of \$1.3 million expiring in varying amounts between 2003 and 2004. Additionally the Company has California state research tax credits of \$3.5 million and alternative minimum tax credits of \$488 that have no expiration date. In the event of a future change in corporate ownership, the use of certain carryforwards may be limited or prohibited. Approximately \$4.5 million of the net operating loss carryforwards with an associated tax benefit of approximately \$1.5 million relates to the benefits of stock option deductions which when recognized will be allocated directly to equity.

The provision for income taxes (all current) is comprised of:

	2002	2001	2000
State	\$ 39	\$ 24	\$ 52
Foreign	61	76	130
Total	<u>\$ 100</u>	<u>\$ 100</u>	<u>\$ 182</u>



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The effective income tax rate differs from the amount computed by applying the federal statutory income tax rate as follows:

		Year ended December 31,					
		2002	%	2001	%	2000	%
Provision (benefit) at statutory rate	Federal	\$ 7,016	34%	\$ 505	34%	\$ (8,964)	(34)%
State income and capital taxes		301	1%	(24)	(2)%	(1,474)	(5)%
Provision at statutory rates of controlled foreign subsidiaries		(32)	0%	(34)	(2)%	247	1%
Federal research and development credit, net of expired credits		(100)	(1)%	(150)	(10)%	(150)	(1)%
Decrease in tax credits resulting from the expiration and true-up of assessments, changes in tax accounting methods and sale of subsidiary		426	2%	845	57%	1,658	6%
Valuation allowance		(2,508)	(12)%	2,265	42%	6,374	24%
Decrease in net operating losses resulting from the sale of subsidiaries		3,225	16%			1,513	6%
Decrease in net operating losses resulting from true-up		218	1%	622	152%	1,306	5%
Increase in capital loss carryover resulting from sale of subsidiary		(5,137)	(25)%	(4,573)	(307)%		
Permanent difference on divestiture		(3,777)	(18)%				
Other, net		468	2%	644	43%	(328)	(1)%
Provision for income taxes		\$ 100	1%	\$ 100	7%	\$ 182	1%

**9. Stock Option and Other Employee Benefit Plans*****401(k) Plan***

The Company has a 401(k) tax-deferred savings plan covering all of its eligible domestic employees. For eligible international employees, the Company contributes to the employees' personal pension plans. Company matching contributions, which are not required by either the domestic or international plans, totaled \$615, \$636 and \$995 in 2002, 2001 and 2000, respectively. Matching contributions are based upon the amount of the employee contribution.

***Stock Option Plans***

Under the Company's employee stock option plans that currently have shares available for grant, 6,350 shares of common stock have been reserved for grant to employees, consultants and directors. For incentive stock options, the exercise price of each option granted is 100% of fair market value on the date of the grant. Non-statutory options may be granted at prices not less than 85% of fair market value at the date of grant. All options have been granted with the exercise price equal to market value of the common stock at the date of grant. Options granted under the plans generally vest over a period of two to four years and expire ten years from the date of grant. Options vest in full upon a change of control, as defined in the 2002 Equity Incentive Plan and the 1995 Nonstatutory Stock Option Plan for Non-Officer Employees.

At December 31, 2002, 1,801 shares of common stock were available for future option grants.

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

A summary of the Company's stock option activity follows:

		Year Ended December 31,					
		2002		2001		2000	
		Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding	beginning of period	4,641	\$ 3.63	4,752	\$ 5.30	4,592	\$ 5.71
Granted		299	1.15	1,423	0.89	1,772	4.35
Exercised		(78)	0.85	(2)	0.35	(298)	4.66
Cancelled or expired		(1,070)	3.20	(1,532)	6.28	(1,314)	5.53
Outstanding	end of period	3,792	\$ 3.61	4,641	\$ 3.63	4,752	\$ 5.30
Exercisable	end of period	2,767		2,226		2,151	

The following table summarizes information about stock options outstanding at December 31, 2002:

Range of Exercise Price	Options Outstanding			Options Exercisable	
	Outstanding at December 31, 2002	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Exercisable at December 31, 2002	Weighted Average Exercise Price
\$0.69 to \$3.19	2,108	7.9	\$ 1.81	1,431	\$ 1.99
3.31 to 4.94	891	6.9	3.34	663	3.33
5.81 to 7.00	314	4.2	6.60	311	6.60
7.13 to 12.88	401	5.8	9.43	284	9.61
13.13 to 13.75	78	4.0	13.59	78	13.59
	3,792	7.1	\$ 3.61	2,767	\$ 3.94

***Stock Purchase Plan***

The Company has an Employee Stock Purchase Plan, which provides for the sale of up to 2,250 shares to eligible employees by means of payroll deductions. Employees may designate up to 10% of their earnings, as defined, to purchase shares at prices not less than 85% of fair market value, with a limit of 10,000 shares per employee per calendar year. From inception through December 31, 2002, 1,931 shares had been purchased at prices ranging from \$0.57 to \$11.53 per share.

The fair value of the employees' purchase rights was estimated using the Black-Scholes option pricing model. The weighted average fair value per share for shares purchased through the Company's Employee Stock Purchase Plan during 2002, 2001 and 2000 was \$0.46, \$0.44 and \$2.30, respectively.

***Additional Stock Plan Information and Pro forma Results***

SFAS No. 123 requires the disclosure of pro forma net income and earnings per share had the Company adopted the fair value method in 1995. Under SFAS No. 123, the fair value of the stock-based awards to employees is calculated through the use of option pricing models, even though such models were developed to estimate the fair value of freely tradable, fully transferable options without vesting restrictions, which significantly differ from the Company's stock option awards. These models also require subjective assumptions, including future stock price volatility and expected time to exercise, which greatly affect the calculated

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

values. The Company's calculations were made using the Black-Scholes Multiple Option Model with the following weighted average assumptions for the three years ended December 31, 2002, 2001 and 2000:

	Year Ended December 31,		
	2002	2001	2000
Dividend yield	0.0%	0.0%	0.0%
Volatility	100.4%	122.7%	309.9%
Risk free interest rate	3.0%	3.5%	5.6%
Expected term, in years	3.8	3.3	3.9

The weighted average fair values per share at date of grant for options granted during 2002, 2001 and 2000 were \$0.90, \$0.75 and \$4.35, respectively.

The Company's calculations are based on a multiple option valuation approach and forfeitures are recognized as they occur. Refer to the table in Note 1 that illustrates the effect on net income (loss) and earnings (loss) per share if the Company had applied the fair value recognition provisions of FASB Statement No. 123, "Accounting for Stock Based Compensation", to stock-based employee compensation.

**10. Commitments and Contingencies**

The Company has operating leases for office space with varying expiration dates through 2007, and for computer equipment and software with varying expiration dates through 2003. The leases generally provide for minimum annual rentals and payment of taxes, insurance and maintenance costs. Rental expense for operating leases was \$3.3 million, \$2.9 million and \$4.2 million in 2002, 2001 and 2000, respectively.

Future minimum lease payments under non-cancelable operating leases, net of expected sublease payments, are as follows:

	Facilities	Equipment and Software	Total
2003	\$ 1,918	\$ 479	\$ 2,397
2004	1,923	4	1,927
2005	2,048	1	2,049
2006	1,849	1	1,850
2007	1,312		1,312
	<hr/>	<hr/>	<hr/>
Total minimum payments	\$9,050	\$485	\$9,535
	<hr/>	<hr/>	<hr/>

In addition, we lease certain software on a month-to-month basis. On an annualized basis, the cost of this leased software would be approximately \$250.

On September 6, 2002 in connection with the sale of our United Kingdom operations, we transferred a lease in The Gate House, Aylesbury, United Kingdom to Novele and contracted to assign a lease in Walker House, Aylesbury, United Kingdom. The assignment of the Walker House lease was based on oral confirmation of consent from the landlord. The share purchase agreement required Novele to provide us with the necessary co-operation and support to enable us to negotiate with the landlord of The Gate House and obtain the release of a guaranty covering this property. However, as of the date of this report, the landlord of The Gate House has not released us from the guaranty, and the landlord of Walker House has not executed a consent to the assignment of the lease to Walker House. We therefore remain contingently liable for the full rent in the event that a third party defaults on The Gate House lease and directly liable for any default on the Walker House lease. The maximum potential liability for the remainder of The Gate House lease, which expires in 2016, would be approximately \$5.5 million. The maximum

potential liability for the remainder of the Walker House lease, which expires in 2009, would be approximately \$1.4 million. No amounts have been

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

accrued in the financial statements as we do not consider it likely that we will be liable for any future payments on these properties.

The Company is not party to any legal proceedings other than ordinary routine litigation incidental to the Company's business. The Company believes that the ultimate resolution of these matters will not have a material adverse effect on the Company's consolidated financial statements taken as a whole.

**11. Geographic Operations**

The Company's products and services are considered a single reportable segment. Historically, the Company has primarily operated in three geographic areas, North America, Europe/ Middle East/ Africa and Asia Pacific. Following the disposal of our United Kingdom and Eleven5 operations in September 2002, the Company will have insignificant revenues and assets in the Europe/ Middle East/ Africa region. Corporate assets consist of cash and cash equivalents, short- and long-term investments and capitalized software. Geographic data are as follows:

	Year Ended December 31,		
	2002	2001	2000
<b>Revenues:</b>			
North America	\$28,611	\$35,329	\$36,909
Europe, Middle East and Africa	12,475	12,113	12,909
Asia Pacific	827	1,623	1,604
	<u>          </u>	<u>          </u>	<u>          </u>
Total revenues	\$41,913	\$49,065	\$51,422
	<u>          </u>	<u>          </u>	<u>          </u>

	Year Ended December 31,		
	2002	2001	2000
<b>Identifiable assets:</b>			
North America	\$ 7,867	\$10,115	\$ 9,696
Europe, Middle East and Africa	63	4,755	3,475
Asia Pacific	47	248	229
Corporate	22,486	9,894	14,160
	<u>          </u>	<u>          </u>	<u>          </u>
Total assets	\$30,463	\$25,012	\$27,560
	<u>          </u>	<u>          </u>	<u>          </u>

**12. Treasury Stock Acquisitions**

In 1995, the Board of Directors authorized the Company to spend up to \$17.5 million for the repurchase of the Company's outstanding common stock. As of December 31, 2002, the Company had acquired 1,060 shares of its common stock at a cost of \$11.1 million. As of December 31, 2002 the Company had reissued 1,060 repurchased shares in connection with the Company's employee stock purchase plan, one of its employee stock option plans, and the purchase acquisition of Revere, Inc. No treasury stock acquisitions were made in 2002, 2001 or 2000.

**13. Earnings Per Share**

The Company calculates basic earnings per share (EPS) and diluted EPS in accordance with SFAS No. 128, Earnings per Share. Basic EPS is computed by dividing net income (loss) by the weighted average number of common shares outstanding for that period. Diluted EPS takes into account the effect of dilutive instruments, such as stock options, and uses the average share price for the period in determining the number



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of incremental shares that are to be added to the weighted average number of shares outstanding. Diluted EPS for 2000 excludes any effect of such instruments because their inclusion would be antidilutive.

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

The following is a summary of the calculation of the number of shares used in calculating basic and diluted EPS:

	Year Ended December 31,		
	2002	2001	2000
Shares used to compute basic EPS	15,332	14,917	14,535
Add: effect of dilutive securities	465	41	
Shares used to compute diluted EPS	15,797	14,958	14,535

For the purposes of computing diluted earnings per share, weighted average common share equivalents do not include stock options with an exercise price that exceeded the average fair market value of the Company's common stock for the period as the effect would be anti-dilutive. Options to purchase shares of common stock that were excluded from the computation were as follows:

	Year Ended December 31,		
	2002	2001	2000
Number of anti-dilutive shares excluded	3,223	4,417	4,661

**14. Selected Quarterly Financial Data (Unaudited)**

Quarterly financial data for the periods indicated are as follows:

	Quarters ended			
	March 31,	June 30,(1)	Sept. 30,(2)	Dec. 31,(3)
<b>2002</b>				
Revenues	\$ 13,132	\$ 12,085	\$ 10,551	\$ 6,145
Income/(loss) from operations	257	215	1,203	(133)
Income before provision for income taxes	278	237	20,003	145
Net income	253	212	19,778	320
Basic net income per share	\$ 0.02	\$ 0.01	\$ 1.28	\$ 0.02
Diluted net income per share	\$ 0.02	\$ 0.01	\$ 1.27	\$ 0.02
<b>2001</b>				
Revenues	\$ 12,634	\$ 12,497	\$ 10,691	\$ 13,243
Income/(loss) from operations	29	244	(28)	564
Income before provision for income taxes	160	340	44	1,042
Net income	135	315	19	1,017
Basic net income per share	\$ 0.01	\$ 0.02	\$ 0.00	\$ 0.07
Diluted net income per share	\$ 0.01	\$ 0.02	\$ 0.00	\$ 0.07

- (1) During the quarter ended June 30, 2002, we recorded a special credit of \$1.7 million relating to a reduction in estimated liabilities associated with divested product lines, a \$365 charge for the impairment of certain capitalized software, and a restructuring charge of \$892 mainly related to employee severance costs.

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- (2) During the quarter ended September 30, 2002, we recorded a gain on sale of our United Kingdom and Elevon 5 operations of \$18.8 million.
- (3) During the quarter ended December 31, 2002, we recorded a gain on sale of our United Kingdom and Elevon 5 operations of \$200 and a restructuring charge of \$244, mainly related to employee severance costs.

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

Not applicable.

**PART III**

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

The information required by this Item is incorporated herein by reference to the Company's Proxy Statement in connection with its 2002 Annual Meeting of Stockholders under the captions Proposal 1 Election of Directors, Additional Information Management and Additional Information Section 16(a) Beneficial Ownership Reporting Compliance.

**Item 11. *Executive Compensation***

The information required by this Item is incorporated herein by reference to the Company's Proxy Statement in connection with its 2002 Annual Meeting of Stockholders under the caption Executive Compensation.

**Item 12. *Security Ownership of Certain Beneficial Owners and Management***

The information required by this Item is incorporated herein by reference to the Company's Proxy Statement in connection with its 2002 Annual Meeting of Stockholders under the captions Security Ownership of Certain Beneficial Owners and Management and Securities Authorized for Issuance Under Equity Compensation Plans.

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

The information required by this Item is incorporated herein by reference to the Company's Proxy Statement in connection with its 2002 Annual Meeting of Stockholders under the caption Certain Transactions.

**Item 14. *Controls and Procedures***

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Within 90 days prior to the date of this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and the Company's Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on the foregoing, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective.

**Table of Contents****PART IV****Item 15. Exhibits and Reports on Form 8-K**

- (a) Documents filed as part of this report.

**1. Consolidated Financial Statements**

	<b>Page</b>
Independent Auditors' Report	26
Consolidated Balance Sheets as of December 31, 2002 and 2001	27
Consolidated Statements of Operations for the years ended December 31, 2002, 2001, and 2000	28
Consolidated Statements of Stockholders' Equity (Deficit) for the years ended December 31, 2002, 2001, and 2000	29
Consolidated Statements of Cash Flows for the years ended December 31, 2002, 2001, and 2000	30
Notes to Consolidated Financial Statements	31

**2. Consolidated Financial Statement Schedule**

Schedule II Valuation and Qualifying Accounts	53
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All other financial statement schedules not listed above are omitted as the required information is not applicable or the information is presented in the consolidated financial statements or related notes.

**3. Exhibits**

The following exhibits are filed herewith or incorporated by reference:

<b>Exhibit Number</b>	<b>Exhibit Title</b>
2.1	Agreement and Plan of Reorganization dated as of October 29, 1997, among the Registrant, Copper Acquisition Sub, and Revere, Inc.(6)
3.1	The Company's Amended and Restated Certificate of Incorporation.(2)
3.2	Bylaws of Registrant.(9)
10.1	Form of Indemnity Agreement entered into between the Registrant and its directors and officers.(3)
10.2*	1992 Employee Stock Purchase Plan, as amended to date.(11)
10.3*	1989 Employee Stock Option Plan and related forms of Incentive Stock Option Grant and Supplemental Stock Option Grant.(3),(9)
10.4*	1986 Employee Stock Purchase Plan and related form of Employee Stock Purchase Agreement.(3)
10.5	Purchase and Sale Agreement between Registrant and Global Software, Inc., dated as of August 31, 1990.(3)
10.6	Lease between Registrant and Marathon U.S. Realities, Inc., dated October 20, 1988 and Amendment No. 1, dated as of October 31, 1990.(3)
10.7	Lease between Registrant and Chicago Title and Trust Company, dated as of December 3, 1990.(3)
10.8	Agreement for Lease between Registrant, Walker Interactive Products International and Alton House Limited, dated as of March 18, 1991.(3)
10.9*	1993 Non-Employee Directors' Stock Option Plan, as amended to date.(12)

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- 10.10\* 1994 Equity Incentive Plan, as amended to date.(13)
- 10.11 Agreement for the Sale and Purchase of The Solutions Group Limited by and among Walker Interactive Products International, and Adrian J. Dixon and Nigel G. Heath, dated as of June 30, 1995.(1)

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<b>Exhibit Number</b>	<b>Exhibit Title</b>
10.12*	Form of Executive Employment Agreement entered into between Registrant and certain of its officers.(5)
10.13*	1995 Executive Employment Agreement between the Registrant and Leonard Y. Liu, as amended to date.(4),(7)
10.14*	1995 Non-Statutory Stock Option Plan for Non-Officer Employees, as amended to date.(18)
10.15	Lease between Registrant and Equitable Assurance Society of the United States, dated November 25, 1997.(10)
10.15A	Lease between Registrant and Equitable Assurance Society of the United States as amended October 1,1999.(18)
10.16*	1998 Executive Employment Agreement between the Registrant and Thomas W. Hubbs.(8)
10.17*	Form of Executive Severance Benefits Agreement entered into between the Registrant and certain of its employees.(7)
10.18*	Separation agreement with Barbara M. Hubbard and the Registrant.(13)
10.19*	Agreement with Leonard Y. Liu and the Registrant.(14)
10.20*	Form of Executive Severance Benefits Agreement entered into between the Registrant and certain of its employees.(15)
10.21*	Executive Employment Agreement entered into between the Registrant and Frank M. Richardson.(18)
10.22*	Executive Severance Benefits Agreement entered into between the Registrant and Bruce Dawson.(18)
10.23*	Executive Severance Benefits Agreement entered into between the Registrant and Paul Lord.(18)
10.24*	Agreement with Leonard Y. Liu and the Registrant.(18)
10.25*	Consulting Services Agreement with Yeun H. Lee and the Registrant.(18)
10.26*	Separation Agreement with Mike Shabbazian and the Registrant.(18)
10.27*	Executive Employment Agreement entered into between the Registrant and Stanley V. Vogler(16)
10.28	Shareholders Rights Agreement dated June 1, 2000(17)
10.29	Aptos Sale Agreement dated October 13, 2000(19)
10.30	Agreement for the sale of Intellectual Property Rights and a consulting contract between QSP Group PLC, QSP Solutions Limited, Walker Financial Solutions Limited and Peter George Mills, dated October 2001(20)
10.31	Share Purchase Agreement, dated as of September 6, 2002, by and between Eleven, Inc., a Delaware corporation, and Novele Limited, a United Kingdom company(21)
10.32	Software Distribution Agreement for AFP, dated as of September 6, 2002, by and between Eleven, Inc., a Delaware corporation, and Novele Limited, a United Kingdom company(22)
10.33	Software Distribution Agreement for e-2, dated as of September 6, 2002, by and between Eleven, Inc., a Delaware corporation, and Novele Limited, a United Kingdom company(23)
10.34 *	Executive Employment Agreement entered into between the Registrant and Frank M. Richardson.(24)
10.35 *	Executive Employment Agreement entered into between the Registrant and Stanley V. Vogler(25)
21.1	Subsidiaries.
23.1	Independent Auditors Consent.
24.1	Power of Attorney. Reference is made to the signature page.

(1) Incorporated by reference to the corresponding exhibit to the Current Report on Form 8-K, filed July 13, 1995.

(2) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 1992.

## Edgar Filing: ELEVEN INC - Form 10-K

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- (3) Incorporated by reference to the corresponding exhibit to the Registration Statement on Form S-1, as amended (Registration No. 33-45737).
  - (4) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending September 30, 1995.
  - (5) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 1995.
  - (6) Incorporated by reference to the corresponding exhibit to the Current Report on Form 8-K, filed December 11, 1997.
  - (7) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending September 30, 1998.
  - (8) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending June 30, 1998.
  - (9) Incorporated by reference to the attachment of the Company's 1998 Proxy Statement.
  - (10) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 1997.
  - (11) Incorporated by reference to the attachment of the Company's 1999 Proxy Statement.
  - (12) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 1998.
  - (13) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending March 31, 1999.
  - (14) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending June 30, 1999.
  - (15) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending September 30, 1999.
  - (16) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending March 31, 2000.
  - (17) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending June 30, 2000.
  - (18) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 1999.
  - (19) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 2000.
  - (20) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 2001.
  - (21) Incorporated by reference to Exhibit 2.1 to the Current Report on Form 8-K, filed September 20, 2002.
  - (22) Incorporated by reference to Exhibit 2.2 to the Current Report on Form 8-K, filed September 20, 2002.
  - (23) Incorporated by reference to Exhibit 2.3 to the Current Report on Form 8-K, filed September 20, 2002.
  - (24) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 2002.
  - (25) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 2002.
- \* Indicates a management contract or compensatory plan.
- (b) Reports on Form 8-K

During the quarter ended December 31, 2002, the Company did not file any reports on Form 8-K.





**Table of Contents****ELEVON, INC.****FORM 10-K****SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant, Elevon,, Inc., a Delaware corporation, has duly caused this Report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of San Francisco, State of California, on March 27, 2003.

ELEVON, INC.  
(Registrant)

By: /s/ FRANK RICHARDSON

Frank Richardson  
*Chief Executive Officer*

Date: March 27, 2003

**POWER OF ATTORNEY**

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Frank Richardson and Stanley V. Vogler, and each or any one of them, his or her true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him or her and in his or her name, place and stead, in any and all capacities, to sign any and all amendments to this Report, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully to all intents and purposes as he or she might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them, or his or her substitutes or substitute, may lawfully do or cause to be done by virtue hereof.

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

<b>Signature</b>	<b>Title</b>	<b>Date</b>
<u>/s/ DAVID C. WETMORE</u>	Chairman of the Board of Directors	March 27, 2003
David C. Wetmore		
<u>/s/ FRANK RICHARDSON</u>	Chief Executive Officer, Director	March 27, 2003
Frank Richardson		
<u>/s/ STANLEY V. VOGLER</u>	Chief Financial Officer (Principal Financial and Accounting Officer)	March 27, 2003
Stanley V. Vogler		
<u>/s/ RICHARD C. ALBERDING</u>	Director	March 27, 2003
Richard C. Alberding		



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<b>Signature</b>	<b>Title</b>	<b>Date</b>
<hr/>		
/s/ TANIA AMOCHAEV	Director	March 27, 2003
<hr/>		
Tania Amochaev		
/s/ WILLIAM A. HASLER	Director	March 27, 2003
<hr/>		
William A. Hasler		

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**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER**

I, Frank M. Richardson, certify that:

1. I have reviewed this annual report on Form 10-K of Eleven, Inc.;
2. Based on my knowledge, this annual 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 annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual 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 annual report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) designed such disclosure controls and procedures 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 annual report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and
  - c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

/s/ FRANK M. RICHARDSON

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Frank M. Richardson

March 27, 2003

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**CERTIFICATION OF THE CHIEF FINANCIAL OFFICER**

I, Stanley V. Vogler, certify that:

1. I have reviewed this annual report on Form 10-K of Eleven, Inc.;
2. Based on my knowledge, this annual 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 annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual 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 annual report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) designed such disclosure controls and procedures 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 annual report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and
  - c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
  - a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

/s/ STANLEY V. VOGLER

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Stanley V. Vogler

March 27, 2003

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**ELEVON, INC.**

**FORM 10-K**

**SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS**

<b>Allowance for Doubtful Accounts:</b>	<b>Balance at Beginning of Period</b>	<b>Additions Charged to Costs and Expenses</b>	<b>Amounts Written Off &amp; Other(1)</b>	<b>Balance at End of Period</b>
	<b>(In thousands)</b>			
Year Ended December 31, 2002	\$ 476	99	429	146
Year Ended December 31, 2001	\$ 1,528	(167)	885	476
Year Ended December 31, 2000	\$4,554	24	3,050	1,528

- (1) Includes the divestiture of the United Kingdom Operations and Elevon 5 intellectual property in September 2002, the IMMPOWER product line in April 2000 and the Aptos product line in October 2000.

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**ELEVEN, INC.**

**EXHIBIT INDEX**

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3.1	The Company's Amended and Restated Certificate of Incorporation.(2)
3.2	Bylaws of Registrant.(9)
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10.5	Purchase and Sale Agreement between Registrant and Global Software, Inc., dated as of August 31, 1990.(3)
10.6	Lease between Registrant and Marathon U.S. Realities, Inc., dated October 20, 1988 and Amendment No. 1, dated as of October 31, 1990.(3)
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10.8	Agreement for Lease between Registrant, Walker Interactive Products International and Alton House Limited, dated as of March 18, 1991.(3)
10.9*	1993 Non-Employee Directors' Stock Option Plan, as amended to date.(12)
10.10*	1994 Equity Incentive Plan, as amended to date.(13)
10.11	Agreement for the Sale and Purchase of The Solutions Group Limited by and among Walker Interactive Products International, and Adrian J. Dixon and Nigel G. Heath, dated as of June 30, 1995.(1)
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10.15A	Lease between Registrant and Equitable Assurance Society of the United States as amended October 1, 1999.(18)
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10.22*	Executive Severance Benefits Agreement entered into between the Registrant and Bruce Dawson.(18)
10.23*	Executive Severance Benefits Agreement entered into between the Registrant and Paul Lord.(18)
10.24*	Agreement with Leonard Y. Liu and the Registrant.(18)
10.25*	Consulting Services Agreement with Yeun H. Lee and the Registrant.(18)



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<b>Exhibit Number</b>	<b>Exhibit Title</b>
10.26*	Separation Agreement with Mike Shahbazian and the Registrant.(18)
10.27*	Executive Employment Agreement entered into between the Registrant and Stanley V. Vogler(16)
10.28	Shareholders Rights Agreement dated June 1, 2000(17)
10.29	Aptos Sale Agreement dated October 13, 2000(19)
10.30	Agreement for the sale of Intellectual Property Rights and a consulting contract between QSP Group PLC, QSP Solutions Limited, Walker Financial Solutions Limited and Peter George Mills, dated October 2001
10.31	Share Purchase Agreement, dated as of September 6, 2002, by and between Eleven, Inc., a Delaware corporation, and Novele Limited, a United Kingdom company(21)
10.32	Software Distribution Agreement for AFP, dated as of September 6, 2002, by and between Eleven, Inc., a Delaware corporation, and Novele Limited, a United Kingdom company(22)
10.33	Software Distribution Agreement for e-2, dated as of September 6, 2002, by and between Eleven, Inc., a Delaware corporation, and Novele Limited, a United Kingdom company(23)
10.34	Executive Employment Agreement entered into between the Registrant and Frank M. Richardson.(24)
10.35	Executive Employment Agreement entered into between the Registrant and Stanley V. Vogler(25)
21.1	Subsidiaries.
23.1	Independent Auditors Consent.
24.1	Power of Attorney. Reference is made to the signature page.

- (1) Incorporated by reference to the corresponding exhibit to the Current Report on Form 8-K, filed July 13, 1995.
- (2) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 1992.
- (3) Incorporated by reference to the corresponding exhibit to the Registration Statement on Form S-1, as amended (Registration No. 33-45737).
- (4) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending September 30, 1995.
- (5) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 1995.
- (6) Incorporated by reference to the corresponding exhibit to the Current Report on Form 8-K, filed December 11, 1997.
- (7) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending September 30, 1998.
- (8) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending June 30, 1998.
- (9) Incorporated by reference to the attachment of the Company's 1998 Proxy Statement.
- (10) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 1997.
- (11) Incorporated by reference to the attachment of the Company's 1999 Proxy Statement.
- (12) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 1998.
- (13) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending March 31, 1999.
- (14) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending June 30, 1999.
- (15) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending September 30, 1999.

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- (16) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending March 31, 2000.
- (17) Incorporated by reference to the corresponding exhibit to the Quarterly Report on Form 10-Q for the quarter ending June 30, 2000.
- (18) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 1999.
- (19) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 2000.
- (20) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 2001.
- (21) Incorporated by reference to Exhibit 2.1 to the Current Report on Form 8-K, filed September 20, 2002.
- (22) Incorporated by reference to Exhibit 2.2 to the Current Report on Form 8-K, filed September 20, 2002.
- (23) Incorporated by reference to Exhibit 2.3 to the Current Report on Form 8-K, filed September 20, 2002.
- (24) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 2002.
- (25) Incorporated by reference to the corresponding exhibit to the Annual Report on Form 10-K for the year ending December 31, 2002.
- \* Indicates a management contract or compensatory plan.