STELLENT INC
Form 10-Q
November 09, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q
(MARK ONE)

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2005**

OR

o **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 0-19817.
STELLENT, INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

MINNESOTA	**41-1652566**
(STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION)	**(I.R.S. EMPLOYER IDENTIFICATION NO.)**
7500 FLYING CLOUD DRIVE	**55344-3748**
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)	**(ZIP CODE)**

(952) 903-2000
(REGISTRANT S TELEPHONE NUMBER, INCLUDING AREA CODE)
7777 GOLDEN TRIANGLE DRIVE
EDEN PRAIRIE, MINNESOTA 55344
(FORMER NAME, FORMER ADDRESS AND FORMER FISCAL YEAR, IF CHANGED SINCE LAST REPORT)

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 þ No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Securities Exchange Act of 1934)
Yes þ No o

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date. Common Stock, $.01 par value 28,281,610 shares as of October 24, 2005.

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Certification by President & CEO Pursuant to Rule 13a-14(a)/15d-15(a) Section 302 of the Sarbanes-Oxley Act of 2002
Certification by Executive Vice President, CFO, Secretary & Treasurer Pursuant to Rule 13a-14(a)/15d-15(a) Section 302 of the Sarbanes-Oxley Act of 2002
Certification by President & CEO Pursuant to 18 U.S.C. Section 1350 Section 906 of the Sarbanes-Oxley Act of 2002
Certification by Executive Vice President, CFO, Secretary & Treasurer Pursuant to 18 U.S.C. Section 1350 Section 906 of the Sarbanes-Oxley Act of 2002

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

STELLENT, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS)
(UNAUDITED)

	September 30, 2005	March 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 45,752	$ 49,113
Short-term marketable securities	15,390	17,523
Trade accounts receivable, net	29,757	30,063
Prepaid royalties, current portion	706	965
Prepaid expenses and other current assets	4,556	3,884
Total current assets	96,161	101,548
Long-term marketable securities	8,767	6,114
Property and equipment, net	7,155	4,333
Prepaid royalties, net of current portion	793	1,044
Goodwill	74,395	67,640
Other acquired intangible assets, net	5,116	5,615
Other	936	1,358
Total assets	$ 193,323	$ 187,652
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 1,374	$ 3,867
Deferred revenues, current portion	18,931	19,854
Commissions payable	2,571	2,419
Accrued expenses and other	10,751	7,867
Current installments of obligation under capital leases	176	170
Total current liabilities	33,803	34,177
Obligation under capital leases, net of current installments	373	
Deferred revenues, net of current portion	975	946
Total liabilities	35,151	35,123

Shareholders equity:				
Common stock		283		275
Additional paid-in capital		247,395		243,013
Unearned compensation		(232)		(469)
Accumulated other comprehensive income		343		966
Accumulated deficit		(89,617)		(91,256)
Total shareholders equity		158,172		152,529
Total liabilities and shareholders equity	$	193,323	$	187,652

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

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STELLENT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)
(UNAUDITED)

	Three Months Ended September 30,		Six Months Ended September 30,	
	2005	**2004**	**2005**	**2004**
Revenues:				
Product licenses	$ 13,321	$ 14,775	$ 27,049	$ 26,454
Services	6,938	5,042	12,098	9,400
Post-contract support	9,888	8,139	19,561	14,762
Total revenues	30,147	27,956	58,708	50,616
Cost of revenues:				
Product licenses	815	1,068	1,975	2,360
Services	6,484	5,431	11,509	9,610
Post-contract support	1,956	1,179	3,806	2,297
Amortization of capitalized software from acquisitions	443	643	859	1,106
Total cost of revenues	9,698	8,321	18,149	15,373
Gross profit	20,449	19,635	40,559	35,243
Operating expenses:				
Sales and marketing	11,712	10,931	23,148	20,720
General and administrative	2,812	3,057	5,982	5,581
Research and development	4,895	4,867	9,551	8,665
Acquisition-related sales, marketing and other costs				886
Amortization of acquired intangible assets and unearned compensation	210	175	374	354
Restructuring charges	648		665	2,461
Total operating expenses	20,277	19,030	39,720	38,667
Income (loss) from operations	172	605	839	(3,424)
Other:				
Interest income, net	478	149	893	343
Net income (loss) before income taxes	650	754	1,732	(3,081)

Provision for income taxes	93		93	
Net income (loss)	$ 557	$ 754	$ 1,639	$ (3,081)
Net Income (loss) per common share				
Basic	$ 0.02	$ 0.03	$ 0.06	$ (0.12)
Diluted	$ 0.02	$ 0.03	$ 0.06	$ (0.12)
Weighted average common shares outstanding				
Basic	28,101	26,720	27,815	25,300
Diluted	29,264	27,776	28,848	25,300

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

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STELLENT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	SIX MONTHS ENDED SEPTEMBER 30, 2005	SIX MONTHS ENDED SEPTEMBER 30, 2004
OPERATING ACTIVITIES		
Net income (loss)	$ 1,639	$ (3,081)
Adjustments to reconcile net income (loss) to cash used in operating activities:		
Depreciation and amortization	1,206	1,719
Amortization of intangible assets, acquisition expense and unearned compensation	1,256	1,459
Lease incentives	1,043	
Changes in operating assets and liabilities, net of amounts acquired:		
Accounts receivable	857	(5,262)
Prepaid expenses and other current assets	85	750
Accounts payable and other liabilities	(2,493)	(1,067)
Accrued liabilities	1,814	(48)
Deferred revenue	(1,044)	811
Accrued commissions	152	618
Net cash flows provided by (used in) operating activities	4,515	(4,101)
INVESTING ACTIVITIES:		
Maturities of marketable securities, net	(520)	7,541
Purchases of property and equipment	(3,488)	(930)
Business acquisition costs, net of cash acquired	(5,439)	(10,657)
Net cash flows used in investing activities	(9,447)	(4,046)
FINANCING ACTIVITIES:		
Proceeds from exercise of stock options and warrants	1,902	950
Proceeds from issuance of stock under Employee Stock Purchase Plan and other	480	432
Payments under capital leases	(188)	(241)
Net cash flows provided by financing activities	2,194	1,141
Cumulative effect of foreign currency translation adjustment	(623)	(29)
Net decrease in cash	(3,361)	(7,035)
Cash and equivalents, beginning of period	49,113	44,165

Cash and equivalents, end of period	$ 45,752	$ 37,130
Supplemental disclosure of non-cash investing and financing activities:		
Non-cash financing activity issuance of common stock for business combination	$ 2,008	$ 41,416
Non-cash financing activity assumption of stock option plan related to business combination	$	$ 7,964
Non-cash investing and financing activity purchase of equipment through capital leases	$ 567	$ 819

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

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STELLENT, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

NOTE 1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions for Quarterly Reports on Form 10-Q and instructions for Article 10 of Regulation S-X. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, have been recorded as necessary to present fairly Stellent, Inc s (the Company) consolidated financial position, results of operations and cash flow for the periods presented. These financial statements should be read in conjunction with the Company s audited consolidated financial statements included in the Company s Fiscal Year 2005 Annual Report on Form 10-K. The consolidated results of operations for the three and six month periods ended September 30, 2005 and 2004 are not necessarily indicative of the results that may be expected for any future period. References to fiscal years 2006 and 2005 represent the twelve months ended March 31, 2006 and 2005, respectively.

The condensed consolidated balance sheet at March 31, 2005 has been derived from audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. Such disclosures are contained in the Company s Annual Report on Form 10-K.

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

Revenue Recognition

Revenue consists principally of software license, support, consulting and training fees. The Company recognizes revenue in accordance with Statement of Position (SOP) 97-2, Software Revenue Recognition, as amended by SOP 98-9*, Modification of SOP 97-2, Software Revenue Recognition with Respect to Certain Transactions*, and Securities and Exchange Commission Staff Accounting Bulletin 104, *Revenue Recognition.*

Product license revenue is recognized under SOP 97-2 when (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred, (iii) the fee is fixed or determinable, and (iv) collectibility is probable and supported and the arrangement does not require services that are essential to the functionality of the software.

Persuasive Evidence of an Arrangement Exists - The Company determines that persuasive evidence of an arrangement exists with respect to a customer under, (i) a signature license agreement, which is signed by both the customer and the Company or, (ii) a purchase order, quote or binding letter-of-intent received from and signed by the customer, in which case the customer has either previously executed a signature license agreement with the Company or will receive a shrink-wrap license agreement with the software. The Company does not offer product return rights to end users or resellers.

Delivery has Occurred - The Company s software may be either physically or electronically delivered to the customer. The Company determines that delivery has occurred upon shipment of the software pursuant to the billing terms of the arrangement or when the software is made available to the customer through electronic delivery. Customer acceptance generally occurs at delivery.

The Fee is Fixed or Determinable - If at the outset of the customer arrangement, the Company determines that the arrangement fee is not fixed or determinable, revenue is typically recognized when the arrangement fee becomes due and payable. Fees due under an arrangement are generally deemed fixed and determinable if they are payable within twelve months.

Collectibility is Probable and Supported - The Company determines whether collectibility is probable and supported on a case-by-case basis. The Company may generate a high percentage of our license revenue from our current customer base, for whom there is a history of successful collection. The Company assesses the probability of collection from new customers based upon the number of years the customer has been in business and a credit review process, which evaluates the customer s financial position and ultimately its ability to pay. If the Company is unable to determine from the outset of an arrangement that collectibility is probable based upon the Company s review process, revenue is recognized as payments are received.

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STELLENT, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

With regard to software arrangements involving multiple elements, the Company allocates revenue to each element based on the relative fair value of each element. The Company s determination of fair value of each element in multiple-element arrangements is based on vendor-specific objective evidence (VSOE). The Company limits its assessment of VSOE for each element to the price charged when the same element is sold separately. The Company has analyzed all of the elements included in its multiple-element arrangements and has determined that it has sufficient VSOE to allocate revenue to consulting services and post-contract customer support (PCS) components of its license arrangements. The Company sells its consulting services separately, and has established VSOE on this basis. VSOE for PCS is determined based upon the customer s annual renewal rates for these elements. Accordingly, assuming all other revenue recognition criteria are met, revenue from perpetual licenses is recognized upon delivery using the residual method in accordance with SOP 98-9, and revenue from PCS is recognized ratably over their respective terms, typically one year.

The Company s direct customers typically enter into perpetual license arrangements. The Company s OEM group generally enters into term-based license arrangements with its customers, the term of which generally exceeds one year in length. The Company recognizes revenue from time-based licenses at the time the license arrangement is signed, assuming all other revenue recognition criteria are met, if the term of the time-based license arrangement is greater than twelve months. If the term of the time-based license arrangement is twelve months or less, the Company recognizes revenue ratably over the term of the license arrangement.

Services revenue consists of fees from consulting services, PCS and out-of-pocket expenses reimbursed by the Company. Consulting services include needs assessment, software integration, security analysis, application development and training. The Company bills consulting services fees either on a time and materials basis or on a fixed-price schedule. In general, the Company s consulting services are not essential to the functionality of the software. The Company s software products are fully functional upon delivery and implementation and generally do not require any significant modification or alteration for customer use. Customers purchase the Company s consulting services to facilitate the adoption of its technology and may dedicate personnel to participate in the services being performed, but they may also decide to use their own resources or appoint other professional service organizations to provide these services. Software products are billed separately from professional services. The Company recognizes revenue from consulting services as services are performed. The Company s customers typically purchase PCS annually, and the Company prices PCS based on either a percentage of the product license fee or product list price, as applicable. Customers purchasing PCS receive product upgrades, Web-based technical support and telephone hot-line support. Unspecified product upgrades are not provided without the purchase of PCS. The Company typically has not granted upgrade rights in its license agreements. Specified undelivered elements are allocated a relative fair value amount within a license agreement and the revenue allocated for these elements are deferred until delivery occurs.

Customer advances and billed amounts due from customers in excess of revenue recognized are recorded as deferred revenue.

Cost of Revenue

The Company expenses all manufacturing, packaging and distribution costs associated with product license revenue as cost of revenues. The Company expenses all technical support service costs associated with service revenue as a cost of revenues. The Company also expenses amortization of capitalized software from acquisition as cost of revenues. The Company reports out-of-pocket expenses reimbursed by customers as revenue and the corresponding expenses incurred as costs of revenue.

Cash, Cash Equivalents, Marketable Securities and Investments in Other Companies

Cash and Cash Equivalents: The Company considers all short-term, highly liquid investments that are readily convertible into known amounts of cash and have original maturities of three months or less to be cash equivalents.

Marketable Securities: Investments in debt securities with a remaining maturity of one year or less at the date of purchase are classified as short-term marketable securities. Investments are held in debt securities of the United States government and with corporations that have the highest possible credit rating. Investments in debt securities with a remaining maturity of greater than one year are classified as long-term marketable securities. These investments are classified as held to maturity and recorded at amortized cost as the Company has the ability and positive intent to hold to maturity.

Investments in Other Companies: Investments in other companies include investments in two non-public, start-up technology companies for which the Company uses the cost method of accounting. These investments are classified as long-term as the Company anticipates holding them for more than one year. The Company holds less than 20% interest in, and does not directly or indirectly exert significant influence over, any of the respective investees. During fiscal year 2005, the Company determined, based on its review of the financial statements of these companies, incremental financing that they received and discussions of business plans and forecasts with management of these companies, that a permanent decline in value had occurred. The Company recorded a remaining write-down of $1,136 on the investments in and advances to the companies during the fourth quarter of fiscal year 2005. At September 30, 2005, the recorded value of these investments was $0.

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STELLENT, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

Warranties

The Company generally warrants its software products for a period of 30 to 90 days from the date of delivery and estimates probable product warranty costs at the time revenue is recognized. The Company exercises judgment in determining its accrued warranty liability. Factors that may affect the warranty liability include historical and anticipated rates of warranty claims, material usage, and service delivery costs. Warranty costs incurred have not been material.

Indemnification Obligations

The Company generally undertakes intellectual property indemnification obligations in its software products or services agreements with customers. Typically these obligations provide that the Company will indemnify, defend and hold the customers harmless against claims by third parties that its software products or services infringe upon the copyrights, trademarks, patents or trade secret rights of such third parties. No such material claim has been made by any third party with regard to the Company s software products or services.

Comprehensive Income (Loss)

Other comprehensive income (loss) consist of gains or losses that under the accounting principles generally accepted in the United States of America are recorded as an element of shareholders equity and are excluded from operations. The following table represents comprehensive income (loss) for the six months ended September 30, 2005 and 2004:

	Six Months Ended September 30, 2005	Six Months Ended September 30, 2004
Net income (loss)	$ 1,639	$ (3,081)
Other comprehensive income:		
Foreign currency translation adjustments	(623)	(29)
Comprehensive income (loss)	$ 1,016	$ (3,110)

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 and assumptions 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 results could differ from those estimates.

Goodwill and Other Acquired Intangible Asset

The Company adopted Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets,* effective April 1, 2002 and, as a result, ceased to amortize goodwill at that time. The changes in the carrying amount of goodwill for the six months ended September 30, 2005 was as follows:

Balance as of April 1, 2005	$ 67,640
Acquisition of Optika	131
Earn-out related to the acquisition of Stellent, S.A. De C.V.	100
Earn-out related to the acquisition of Ancept	133
Acquisition of e-Onehundred Group	6,405
Foreign currency translation	(14)
Balance as of September 30, 2005	$ 74,395

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Other acquired intangible assets by major intangible asset class at September 30, 2005 were as follows:

	Acquired Value	Amortization Period in Years
Core technology	$ 5,282	3
Customer base	2,955	3 to 10
	$ 8,237	5.30 weighted average years

The other intangibles have no significant residual values. There are no other intangible assets which are not subject to amortization. Gross carrying amounts and accumulated amortization of the other acquired intangibles were as follows for each major intangible asset class:

	As of September 30, 2005		
	Gross Carrying Amount	Accumulated Amortization	Net Balances
Core technology capitalized software from acquisitions	$ 5,282	$ (2,730)	$ 2,552
Customer base intangible assets	2,955	(391)	2,564
	$ 8,237	$ (3,121)	$ 5,116

Amortization expense for other acquired intangible assets for the six months ended September 30, 2005 and 2004 was $1,020 and $1,316, respectively.

Estimated amortization expense for other acquired intangible assets is as follows for the years ending March 31:

2006 (remaining six months)	$ 1,053
2007	1,720
2008	635
2009	313
2010	270
Thereafter	1,125
	$ 5,116

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Stock-based Compensation

The Company s shareholders approved a new stock option plan for employees and directors in August 2005. The intrinsic value method is used to value the stock options issued to employees and directors, and the Company accounts for those plans under the recognition and measurement principles of Financial Accounting Standards Board, Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations. In the periods presented, no stock-based employee compensation cost is reflected in net income (loss), excluding the amortization of unearned compensation expense related to the Optika transaction, as all of the options granted under these plans had an exercise price equal to the market value of the underlying common stock on the date of grant. Had the fair value method been applied, the compensation expense would have been different in the periods presented. The following table illustrates the effect on net income (loss) and net income (loss) per share if the Company had applied the fair value method for the following periods:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2005	**2004**	**2005**	**2004**
Net income (loss) as reported	$ 557	$ 754	$ 1,639	$ (3,081)
Add: Stock-based compensation included in net income (loss) as reported	119	108	213	144
Less: Total stock based employee compensation expense determined under fair value based method for all awards	(1,658)	(3,497)	(3,686)	(6,519)
Net loss pro-forma	$ (982)	$ (2,635)	$ (1,834)	$ (9,456)
Weighted average shares outstanding				
Basic	28,101	26,720	27,815	25,300
Diluted	29,264	27,776	28,848	25,300
Net income (loss) per share as reported				
Basic and diluted	$ 0.02	$ 0.03	$ 0.06	$ (0.12)
Net loss per share pro-forma				
Basic and diluted	$ (0.03)	$ (0.10)	$ (0.07)	$ (0.37)

Employee based stock option plans assumptions:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2005	**2004**	**2005**	**2004**
Risk free interest yields	4.0%	2.9%	3.8%	2.5%
Dividend yield				
Volatility factor of expected market price of Company s stock	58%	95%	58%	95%
Weighted average expected life of options (years)	3.0	3.25	3.0	3.25

Employee stock purchase plan assumptions:

	Three Months Ended September 30,	Six Months Ended September 30,

	2005	2004	2005	2004
Risk free interest yields	3.1%	1.3%	3.1%	1.3%
Dividend yield				
Volatility factor of expected market price of Company s stock	44%	45%	44%	45%
Weighted average expected life of options (years)	0.5	0.5	0.5	0.5

New Accounting Pronouncements

In November 2005, the FASB issued FASB Staff Position (FSP) FAS 115-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*. The guidance in this FSP addresses the determination of when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. The FSP also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. The guidance in this FSP amends FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. The guidance in this FSP nullifies certain requirements of EITF Issue No. 03-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*, and supersedes *EITF Abstracts*, Topic D-44, *Recognition of Other-Than-Temporary Impairment upon the Planned Sale of a Security Whose Cost Exceeds Fair Value*. The guidance in this FSP is required to be applied to reporting periods beginning after December 15, 2005. The Company plans on adopting this statement during its third quarter of fiscal year 2006 and does not believe that the adoption of the provisions of FAS 115-1 will have a material impact on its consolidated financial statements.

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections.* This new standard replaces APB Opinion No. 20, Accounting Changes, and FASB Statement No. 3, Reporting Accounting Changes in Interim Financial Statements. Among other changes, SFAS No. 154 requires that a voluntary change in accounting principle be applied retrospectively with all prior period financial statements presented on the new accounting principle, unless it is impracticable to do so. SFAS No. 154 also provides that (1) a change in method of depreciating or amortizing a long-lived nonfinancial asset be accounted for as a change in estimate (prospectively) that was effected by a change in accounting principle, and (2) correction of errors in previously issued financial statements should be termed a restatement. The new standard is effective for accounting changes and correction of errors made in fiscal years beginning after December 15, 2005. The Company does not believe that the adoption of the provisions of SFAS No. 154 will have a material impact on the Company s consolidated financial statements.

In December 2004, FASB issued SFAS No. 123 (revised 2004), *Share-Based Payment,* known as Statement 123(R). Statement 123(R) will, with certain exceptions, require entities that grant stock options and shares to employees to recognize the fair value of those options and shares as compensation cost over the service (vesting) period in their financial statements. The measurement of that cost will be based on the fair value of the equity or liability instruments issued. The Company is required to adopt Statement 123(R) in the first interim period beginning after its fiscal year 2006. As part of this adoption, the Company will begin expensing options effective April 1, 2006 and has also elected not to restate the prior period results. Based on the current amount of outstanding stock options that will vest on or after April 1, 2006, the Company anticipates recognizing approximately $3.2 million of compensation expense during fiscal year 2007. This amount will fluctuate depending on future stock options granted to or forfeited by employees and directors.

Note 2. Basic and Diluted Net Income (Loss) Per Common Share

Basic net income (loss) per share is computed using the weighted average number of shares outstanding of common stock. Diluted net income (loss) per share is computed using the weighted average number of shares of common stock and common equivalent shares outstanding during the period. Common equivalent shares consist of stock options and were excluded from the computation if their effect was anti-dilutive. The components of basic and diluted net income (loss) per share were as follows:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2005	2004	2005	2004
Net income (loss)	$ 557	$ 754	$ 1,639	$ (3,081)
Weighted average common shares:				
Basic	28,101	26,720	27,815	25,300
Effect of dilutive stock options	1,163	1,056	1,033	

Diluted	29,264	27,776	28,848	25,300
Net income (loss) per share as reported				
Basic	$ 0.02	$ 0.03	$ 0.06	$ (0.12)
Diluted	$ 0.02	$ 0.03	$ 0.06	$ (0.12)

Note 3. Mergers and Acquisitions

During the second quarter of fiscal year 2005 the Company acquired a Korean entity for a total of $205 in cash. $180 was recorded as goodwill and $25 was allocated to other intangible assets. Additional pro forma disclosures required under SFAS No. 141, related to this acquisition were not considered material.

On June 20, 2005, the Company acquired certain assets of privately held e-Onehundred Group, a financial compliance solutions provider, for $5,000 in cash, 274 shares of the Company s stock valued at $2,000 and a potential $2,000 cash earn-out over a one-year period based upon revenue performance. The Company also incurred approximately $300 in professional fees and other costs directly associated with this acquisition. Approximately $6,400 of the purchase price was allocated to goodwill, $520 was allocated to capitalized software and customer base, (which both will be amortized over a three year period), $551 was allocated to assets acquired and $177 was allocated to liabilities assumed in the acquisition. Additional pro forma disclosures required under SFAS No. 141 related to this acquisition were not considered material.

On May 13, 2004, the Company acquired the outstanding shares of Stellent, S.A. De C.V. for approximately $750 in cash and assumed liabilities of $274, creating a business presence in Mexico. The Company is required to make contingent consideration payments (earn-out) for two years from the date of acquisition. Earn out amounts, which will be recorded as goodwill, cannot exceed $300 in the first year and $450 in the second year after the acquisition. As of September 30, 2005, the Company had accrued and recorded to goodwill approximately $234 related to this earn-out. Additional proforma disclosure required under SFAS No. 141, *Business Combinations*, related to this acquisition were not considered material.

On May 28, 2004, the Company acquired all outstanding shares of Optika Inc. for $10,000 in cash, approximately 4,200 shares of the Company s common stock valued at $41,416, the assumption of Optika s outstanding common stock options, and direct acquisition costs of approximately $1,594. The Company acquired Optika in order to add to, or strengthen and expand, its Universal Content Management software in the areas of document imaging, business process management and compliance capabilities. The valuation of the Company s stock was set at an average price at the time the merger agreement was signed, which was January 11, 2004. The fair value of Optika s option plan of $7,964 was estimated as of January 11, 2004 using the Black-Scholes option-pricing model with the following assumptions: no estimated dividends, expected volatility of 95%, risk free interest rate of 2.5% and expected option terms of 3 years for all options.

STELLENT, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

The total estimated purchase price is allocated to Optika s net tangible and identifiable intangible assets based upon their estimated fair values as of the date of completion of the acquisition. The excess of the purchase price over the net tangible and identifiable intangible assets has been recorded as goodwill. A restructuring plan was adopted as a result of the acquisition. The acquisition restructuring charge relates to severance costs for terminated employees of $596 and facility closing costs of $263 primarily related to lease obligations. All amounts have been paid out as of September 30, 2005. Based upon the purchase price and valuation, the following represents the allocation of the aggregate purchase price to the acquired net assets of Optika:

Purchase price:	
Cash	$ 10,000
Transaction costs	1,594
Value of common stock issued	41,416
Value of stock option grants	7,964
Total purchase consideration paid	$ 60,974
Fair value of assets acquired and liabilities assumed:	
Cash	$ 7,460
Accounts receivable	2,901
Fixed assets	471
Other assets	660
Accounts payable	(313)
Accrued expenses	(1,433)
Deferred revenue	(6,194)
Acquisition restructuring charge	(859)
Goodwill	51,286
Identifiable intangible assets	6,100
Unearned compensation	895
Total purchase price	$ 60,974

The estimate of unearned compensation was based on the fair market value of the unvested options as of May 28, 2004. Compensation expense will be recognized over the remaining vesting period of the options, which ranges from one month to 48 months, as each option grant vests.

The fair value of the deferred revenue was determined in accordance with EITF 01-3, *Accounting in a Business Combination for Deferred Revenue of an Acquiree*. The Company considers PCS contracts to be legal obligations, and has estimated fair value of the PCS contracts based on prices in recent exchange transactions.

The Company valued the identified intangible assets acquired using an appraisal. Identified intangible assets consist of:

	Estimated Useful	Estimated Annual

	Fair Value	Life	Amortization
Core technology	$ 3,400	3 years	$ 1,133
Customer base	2,700	10 years	270
	$ 6,100		$ 1,403

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STELLENT, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

As part of the acquisition of Optika the Company also acquired net deferred tax assets of approximately $13,390. These deferred tax assets relate to net operating loss (NOL) carryforwards and the tax effects of temporary differences primarily related to deferred revenue, depreciation and amortization and other accrued expenses. The $51,286 allocated to goodwill is not deductible for tax purposes.

Realization of the NOL carryforwards and the deferred tax temporary differences, which were acquired, are contingent on future taxable earnings. The deferred tax assets were reviewed for expected utilization using a more likely than not approach by assessing the available positive and negative evidence surrounding their recoverability.

The Company has recorded a full valuation allowance against the net deferred tax assets, acquired or otherwise, due to the uncertainty of future taxable income, which is necessary to realize the benefits of the deferred tax assets. NOL carryforwards were approximately $34,803. These NOLs begin to expire in 2010 and are subject to annual utilization limits due to prior ownership changes.

The Company will continue to assess and evaluate strategies that will enable the deferred tax asset, or portion thereof, to be utilized, and will reduce the valuation allowance appropriately at such time when it is determined that the more likely than not criteria is satisfied. Reversal of the valuation allowance will be applied first to reduce to zero any goodwill related to the acquisition, then to reduce to zero other noncurrent intangible assets related to the acquisition, and then to reduce income tax expense.

The following unaudited pro forma condensed consolidated results of operations have been prepared as if the acquisition of Optika had occurred as of April 1, 2003:

	Six months ended September 30,	
	2005	**2004**
Net revenues	$ 58,708	$ 53,166
Net income (loss)	$ 1,639	$ (6,644)
Net income (loss) per share		
Basic	$ 0.06	$ (0.26)
Diluted	$ 0.06	$ (0.26)
Weighted average shares outstanding		
Basic	27,815	25,300
Diluted	28,848	25,300

The unaudited pro forma condensed consolidated results of operations are not necessarily indicative of results that would have occurred had the acquisition occurred as of April 1, 2003, nor are they necessarily indicative of the results that may occur in the future.

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STELLENT, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

Note 4. Contingencies

The Company is a defendant, along with certain current and former officers and directors of the Company, in a putative class action lawsuit entitled *In re Stellent Securities Litigation.* The lawsuit is a consolidation of several related lawsuits (the first of which was commenced on July 31, 2003). The plaintiff alleges that the defendants made false and misleading statements relating to the Company and its future financial prospects in violation of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934. In fiscal year 2005 a settlement was reached, subject to final documentation and preliminary and final court approval. No further expenses of any significance are anticipated with this lawsuit.

Additionally, the Company is subject to various claims and litigation in the ordinary course of its business, including employment matters and intellectual property claims. Management does not believe the outcome of any current legal matters will have a material adverse effect on its consolidated financial position, results of operations or cash flows.

Note 5. Restructuring Charges

In connection with the integration of Optika and in connection with the Company s plans to reduce costs and improve operating efficiencies, the Company adopted two restructuring plans during fiscal 2005. The initial restructuring took place during the first quarter which included the termination of 30 employees and the closure of the Company s New York facility. Restructuring charges included in the Company s net loss during the first quarter of fiscal year 2005 related to this plan were approximately $1,866 for terminated employee benefits and approximately $595 for excess facilities. A change of estimate and impairment charge related to this restructuring plan resulted in $32 and $35 additional expense being recognized in the fourth quarter of fiscal year 2005. The Company recognized an additional change in estimate related to the New York facility of $140 during the second quarter of fiscal year 2006. At September 30, 2005, approximately $588 remained to be paid in connection with these charges. The final restructuring plan was completed during the fourth quarter of fiscal year 2005, which included the termination of 25 employees and the closure of the Company s Boise, Idaho and Mexican facilities. The expense recognized and included in the Company s net loss during the fourth quarter of fiscal year 2005 related to these restructuring plans totaled $1,129, with approximately $990 related to terminated employee benefits and approximately $139 related to excess facilities which includes an impairment on fixed assets of $25. During the first quarter of fiscal year 2006, the Company recorded a change in estimate resulting in additional expense totaling $74 related to the closure of our Mexican operations. At September 30, 2005, approximately $188 remained to be paid in connection with this charge.

During the second quarter of fiscal year 2006 the Company adopted a restructuring plan to reorganize its international sales operations and also consolidate certain general and administrative activities. This restructuring included the termination of 8 employees and the closure of the Company s Brazilian facility. The expense recognized and included in the Company s net income during the second quarter of fiscal year 2006 related to this restructuring totaled $508, of which approximately $321 related to terminated employee benefits and approximately $187 related to excess facilities and other exit costs. As of September 30, 2005 approximately $305 remained to be paid in connection with this charge.

In total, overall employee termination benefit costs of $629 will be paid out through June 2006 and the other exit costs totaling $510 will be paid out through January 2007.

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STELLENT, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

Selected information regarding the restructuring charges and related accrued liabilities by restructuring plan is as follows:

	Second Quarter 03	First Quarter 04	First Quarter 05		Fourth Quarter 05		Second Quarter 06		
	Other Exit Costs	**Employee Termination Benefits**	**Employee Termination Benefits**	**Other Exit Costs**	**Employee Termination Benefits**	**Other Exit Costs**	**Employee Termination Benefits**	**Other Exit Costs**	**Total**
Balance at April 1, 2003	$ 304	$	$	$	$	$	$	$	$ 304
Expense		396							396
Payments	(65)	(245)							(310)
Change in estimate	360								360
Balance at June 30, 2003	599	151							750
Payments	(43)	(38)							(81)
Balance at September 30, 2003	556	113							669
Payments	(43)	(38)							(81)
Balance at December 31, 2003	513	75							588
Payments	(49)								(49)
Change in estimate		(69)							(69)
Balance at March 31, 2004	464	6							470
Expense			1,866	595					2,461
Payments	(48)		(306)						(354)
Balance at June 30, 2004	416	6	1,560	595					2,577
Payments	(33)		(794)	(81)					(908)
Balance at September 30, 2004	383	6	766	514					1,669
Payments	(51)		(391)	(81)					(523)

Balance at December 31, 2004	332	6	375	433					1,146
Expense					990	114			1,104
Payments	(51)	(6)	(36)	(87)	(348)	(7)			(535)
Change in estimate			32						32
Balance at March 31, 2005	281		371	346	642	107			1,747
Payments	(87)		(91)	(87)	(265)	(142)			(672)
Change in estimate	(57)				27	47			17
Balance at June 30, 2005	137		280	259	404	12			1,092
Expense							321	187	508
Payments	(79)			(91)	(216)	(12)	(160)	(43)	(601)
Change in estimate				140					140
Balance at September 30, 2005	$ 58	$	$ 280	$ 308	$ 188	$	$ 161	$ 144	$ 1,139

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

FORWARD-LOOKING STATEMENTS

This Form 10-Q for the period ended September 30, 2005 contains certain forward-looking statements within the meaning of the safe harbor provisions of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). Such forward-looking statements are based on the beliefs of our management as well as on assumptions made by, and information currently available to, us at the time such statements were made. When used in this Form 10-Q, the words approximate, anticipate, believe, estimate, expect, intend and similar expressions, as they relate us, are intended to identify such forward-looking statements. Although we believe these statements are reasonable, readers of this Form 10-Q should be aware that actual results could differ materially from those projected by such forward-looking statements as a result of the risk factors listed below. Readers of this Form 10-Q should consider carefully the factors listed below, as well as the other information and data contained in this Form 10-Q. We caution the reader, however, that such list of factors may not be exhaustive and that those or other factors, many of which are outside of our control, could have a material adverse effect on us and our results of operations. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements set forth hereunder. We undertake no obligation to update publicly any forward-looking statements for any reason, even if new information becomes available or other events occur in the future.

OVERVIEW

In 1997, we launched one of the first software product suites on the market that was fully developed and created expressly for Web-based content and document management. At the time, content management today considered a critical component of an organization s communication and information technology (IT) infrastructure was an emerging technology used to help companies easily and quickly share information with employees, partners, customers and prospects using the World Wide Web.

Currently, our solutions which are comprised of Universal Content Management software and Content Components software help customers worldwide solve business problems related to efficiently creating, managing, sharing and archiving critical information.

Universal Content Management Software

Universal Content Management is our primary software product, consisting of a unified architecture and product which power multiple applications. These applications help organizations manage their business information over the web such as records, legal documents (e.g. contracts, and other business documents), presentations, Web content and graphics from the time it s created to the time it s archived or disposed of, so that employees, customers, partners and investors can more easily find, access and re-use that information. With our software, customers can increase employee productivity, reduce expenses and improve company-wide collaboration and communication.

Stellent Content Server is a fully functional system providing secure, personalized delivery of business information. This repository provides a core set of content services such as check-in/check-out, revision control, security, workflow, personalization and subscription that help ensure users can access only the most current information as appropriate to their role or permissions. Stellent Content Server also provides a variety of repository services, including file storage, metadata and search.

On top of Stellent Content Servers, users can add the five key elements of content management in our application modules document management and imaging, Web content management, digital asset management, collaboration and records management from a unified architecture, enabling customers to fully utilize their content management investment across the organization. We believe our tightly integrated products allow companies to implement content management applications using fewer products and consulting services than other content management offerings, which can lead to a lower total cost of ownership.

Content Component Software

Our Content Components software makes information created in more than 370 common office software applications more accessible to the business users who need it. Other technology companies embed this software to enable their own solutions to extract text and metadata, provide a high-fidelity view of file contents, and convert files into any one of 10 output formats. Since business information is often difficult to access without the native software application in which it was created, our Content Components software empowers users to locate and view information without need of the software application that created the file installed on their desktop or handheld device. These technologies are also integrated into our Universal Content Management software.

The Content Components software supports multiple operating systems and international environments, and enables access to documents in applications for diverse markets such as content management, search and retrieval, security and policy management, mobile and wireless, messaging, collaboration and publishing.

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RESULTS OF OPERATIONS
THREE MONTHS AND SIX MONTHS ENDED SEPTEMBER 30, 2005 AND 2004
REVENUES

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	**2004**	**Change**	**2005**	**2004**	**Change**
	(in thousands, except for percentages)					
Product licenses	$ 13,321	$ 14,775	(10%)	$ 27,049	$ 26,454	2%
Services	6,938	5,042	38%	12,098	9,400	29%
Post-contract support	9,888	8,139	21%	19,561	14,762	33%
Total	$ 30,147	$ 27,956	8%	$ 58,708	$ 50,616	16%
As a percentage of total revenue:						
Product licenses	44%	53%		46%	52%	
Services	23%	18%		21%	19%	
Post-contract support	33%	29%		33%	29%	

Revenues totaled $30.1 million and $58.7 million for the second quarter and first half of fiscal year 2006, respectively, compared to $28.0 million and $50.6 million for the second quarter and first half of fiscal year 2005. Total revenues for the second quarter and first half of fiscal year 2006 were up $2.2 million and $8.1 million, or 8% and 16%, respectively, from the second quarter and first half of fiscal year 2005. The increase in revenue was due to an overall increase in our Universal Content Management software orders, an overall increase in our services and an increase in our post-contract support revenue as a result of supporting a larger installed base. We also added additional services revenue during fiscal year 2006 with our recent acquisition of the e-Onehundred group in June 2005. These increases in our Universal Content Management software were more than offset by a decrease in our Content Component software for the September 2005 quarter.

As we license our products, whether on a perpetual basis for our Universal Content Management software or on a term basis for our Content Components software, our installed base of products increases. Since the rate of annual renewals of post contract customer support services on our Universal Content Management and Content Component software has remained high, our post contract customer support revenues have grown as our installed base of products has grown. Also, Universal Content Management revenues related to consulting services work can increase as a result of a larger installed base of products. We expect our installed base of products to continue to increase and our services and post-contract support revenue to grow.

Product Licenses

Revenues generated from product licenses totaled $13.3 million and $27.0 million for the second quarter and first half of fiscal year 2006, respectively, a decrease of $1.5 million and an increase of $0.6 million, or (10%) and 2%, respectively, from $14.8 million and $26.5 million in the second quarter and first half of fiscal year 2005 respectively. The decrease in revenues for the second quarter of fiscal year 2006 compared to the second quarter of fiscal year 2005 relates to a reduction in our Content Component software orders in particular from a transaction approximately $5.5 million in license revenue in the September 2004 quarter. The increase in license revenue when comparing the first half of fiscal year 2006 to the first half of fiscal year 2005 was due to an overall increase in our Universal Content Management software sales, which included one transaction of approximately $2.8 million during the first quarter of fiscal year 2006. Although we continue to anticipate expenditures for information technology to remain soft for the rest of fiscal year 2006, we do expect our overall license revenue to increase in absolute dollars and should represent approximately 47% to 49% of our total revenue for the remainder of fiscal year 2006.

Services

Revenues for services, consisting of consulting services, training and billable expenses, totaled $6.9 million and $12.1 million for the second quarter and first half of fiscal year 2006, respectively, increases of $1.9 million and $2.7 million, or 38% and 29%, respectively, from $5.0 million and $9.4 million in the second quarter and first half of fiscal year 2005 respectively. The increase in revenues for services was due to an increased number of consulting engagements associated with the increased number of new transactions sold during the first half of fiscal year 2006, as well as the e-Onehundred Group acquisition in June 2005. We anticipate that the percentage of service revenue to total revenue will continue to be approximately 18% to 20% during the remainder of fiscal year 2006.

Generally, customers prefer to have us perform consulting services or supplement their internal information technology staff, a trend we believe will continue. Our consulting service revenue relates almost exclusively to our Universal Content Management software as our Content Components software is embedded in another company s software and that company would typically perform the consulting services. Universal Content Management revenues related to consulting services work can increase as a result of a larger installed base of products. Because we expect the trend toward companies increasingly using the Web for communicating and publishing business information and the trend toward viewing information electronically to continue, we expect revenues attributable to consulting services to continue to increase. A decline in license revenues may result in fewer consulting services engagements.

Post-Contract Support

Revenues for post-contract support for the second quarter and first half of fiscal year 2006 totaled $9.9 million and $19.6 million, respectively, increases of $1.8 million and $4.8 million, or 21% and 33%, respectively, from $8.1 million and $14.8 million in the second quarter and first half of fiscal year 2005 respectively. The increase in revenues for our post-contract support was due to supporting a larger customer installed base of Universal Content Management and Content Component products. We anticipate that the percentage of post-contract support revenue to total revenue will be approximately 32% to 34% for the remainder of fiscal year 2006 and that post-contract support revenue in absolute dollars will increase.

As we license our products, whether on a perpetual basis for our Universal Content Management software or on a term basis for our Content Components software, our installed base of products increases. Since the rate of annual renewals of post-contract customer support services for our Universal Content Management and Content Component software has remained high, our post-contract customer support revenues grow because we have a larger installed base of products. Since post-contract customer support contracts are generally sold with each license transaction, a decline in license revenues may also result in a decline in customer support revenues. However, since post-contract customer support revenues are recognized over the duration of the support contract, the impact would lag behind a decline in license revenues.

COST OF REVENUES AND GROSS PROFIT

Cost of Revenues General

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	**2004**	**Change**	**2005**	**2004**	**Change**
	(in thousands, except for percentages)					
Cost of product licenses	$ 815	$ 1,068	(24%)	$ 1,975	$ 2,360	(16%)
Cost of amortization of capitalized software from acquisitions	443	643	(31%)	859	1,106	(22%)
Cost of services	6,484	5,431	19%	11,509	9,610	20%
Cost of post-contract support	1,956	1,179	66%	3,806	2,297	66%
Total cost of revenues	$ 9,698	$ 8,321	17%	$ 18,149	$ 15,373	18%
Gross profit	$ 20,449	$ 19,635	4%	$ 40,559	$ 35,243	15%
As a percentage of total revenue:						
Cost of product licenses	3%	4%		3%	4%	
	1%	2%		2%	2%	

Cost of amortization of capitalized software from acquisitions				
Cost of services	22%	19%	20%	19%
Cost of post-contract support	6%	5%	6%	5%
Total cost of revenues	32%	30%	31%	30%
Gross margin	68%	70%	69%	70%

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Total cost of revenues increased by $1.4 million and $2.8 million, or 17% and 18%, respectively, to $9.7 million and $18.1 million for the second quarter and first half of fiscal 2006 when compared to the same periods in fiscal year 2005. Total cost of revenues as a percentage of total revenues was 32% and 31% for the second quarter and first half of fiscal year 2006, compared to 30% for the same periods in fiscal year 2005. Overall gross profit increased by $0.8 million and $5.3 million, or 4% and 15%, to $20.4 million and $40.6 million for the second quarter and first half of fiscal year 2006 when compared to the second quarter and first half of fiscal year 2005. Total gross profit as a percentage of total revenues was 68% and 69% for the second quarter and first half of fiscal year 2006 compared to 70% for the same periods in fiscal year 2005. Although we were able to increase our overall gross profit dollars from generating higher levels of services and post-contract support revenue, our overall gross profit percentage was lower when comparing fiscal year 2006 to fiscal year 2005 due to a larger percentage of our revenue coming from services and post-contract support. Revenues generated from our services and post-contract support carry a lower gross margin percentage than our product license revenue.

Cost of Revenues Product Licenses

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	**2004**	**Change**	**2005**	**2004**	**Change**
	(in thousands, except for percentages)					
Cost of product licenses	$ 815	$ 1,068	(24%)	$ 1,975	$ 2,360	(16%)
Cost of amortization of capitalized software from acquisitions	443	643	(31%)	859	1,106	(22%)
Total cost of product licenses	$ 1,258	$ 1,711	(26%)	$ 2,834	$ 3,466	(18%)
Gross profit product licenses	$ 12,063	$ 13,064	(8%)	$ 24,215	$ 22,988	5%
As a percentage of product license revenue:						
Cost of product licenses	6%	7%		7%	9%	
Cost of amortization of capitalized software from acquisitions	3%	4%		3%	4%	
Total cost of product license revenues	9%	12%		10%	13%	
Product license gross margin	91%	88%		90%	87%	

Cost of revenues for product licenses. Cost of product licenses includes expenses incurred to manufacture, package and distribute our software products and related documentation, as well as costs of licensing third-party software embedded in or sold in conjunction with our software products. Cost of revenues for product licenses in the second quarter and first half of fiscal year 2006 totaled $1.3 million and $2.8 million, respectively, a decrease of $0.5 million and $0.6 million, from $1.7 million and $3.5 million in the second quarter and first half of fiscal year 2005. Gross profit as a percentage of revenues for product licenses was up to 91% and 90% for the second quarter and first half of fiscal year 2006 compared to 88% and 87% for the same periods in fiscal year 2005. The slight decrease in cost of revenues for product licenses was attributable to lower third-party software royalty costs associated with technology incorporated into certain Universal Content Management products and therefore was due to our product mix. During the first quarter of fiscal year 2006, we acquired the source code for our Sarbanes-Oxley Solution product from the e-Onehundred Group, which contributed to lower third-party royalty costs during the second quarter of fiscal year 2006. These reductions were partially offset by lower Content Component software product license revenue during the first quarter and first half of fiscal year 2006 when compared to the same period in the prior year, which carry a higher gross margin than our Universal Content Management software revenue.

Amortization of Capitalized Software from Acquisitions. Cost of product license revenues related to amortization of capitalized software from acquisitions was approximately $0.4 million and $0.9 million for the second quarter and first half of fiscal year 2006 compared to $0.6 million and $1.1 million for the second quarter and first half of fiscal year 2005. The cost of revenues for amortization of capitalized software from acquisitions was attributable to the amortization of capitalized software obtained in the acquisition of certain assets of RESoft, Kinecta, Active IQ, Ancept, Optika and the e-Onehundred Group, in July 2001, April 2002, March 2003, August 2003, May 2004 and June 2005, respectively. The slight decrease in cost of revenues related to amortization of capitalized software from fiscal 2005 compared to fiscal 2006 was attributable to the completion of amortization of capitalized software related to our acquisition of Kinecta during our fiscal year 2005. This was partially offset by amortization expense recognized in connection with our acquisition of Optika starting in June of 2004 and the e-Onehundred Group in July of 2005. We acquired technology from the companies listed above for incorporation into our Universal Content Management products in order to maintain competitive functionality. We expect to continue to evaluate selective potential acquisitions. To the extent we consummate additional acquisitions, and depending on the structure of such acquisitions, the assets acquired and the consideration paid, our costs of revenues related to amortization of capitalized software from acquisitions may increase.

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Cost of Revenues Services

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	2004	Change	2005	2004	Change
	(in thousands, except for percentages)					
Services cost of revenue	$ 6,484	$ 5,431	19%	$ 11,509	$ 9,610	20%
Gross profit services	$ 454	$ (389)	217%	$ 589	$ (210)	380%
As a percentage of respective revenue:						
Cost of services	93%	108%		95%	102%	
Gross profit	7%	(8%)		5%	(2%)	

Cost of services revenues, consisting of personnel, billable and unbilled travel expenses and other operating expense, increased by $1.1 million and $1.9 million, or 19% and 20%, to $6.5 million and $11.5 million for the second quarter and first half of fiscal year 2006 when compared to the same period in the prior year. Gross profit as a percentage of revenues for services improved to 7% and 5% for the second quarter and first half of fiscal year 2006 compared to negative gross margin percentages of 8% and 2% for the same periods in fiscal year 2005. The increase in consulting service costs when comparing the second quarter of fiscal year 2006 to the second quarter of fiscal year 2005 is due to our acquisition of the e-Onehundred Group in June 2005. We have made significant changes in the first six months of fiscal year 2006, including the appointment of a new head of services in Europe, increasing our hourly billing rates, improving our utilization and implementing a web based time management system. We anticipate that our cost of consulting and training services as a percentage of total consulting and training revenue will decrease for the remainder of fiscal year 2006, as we believe that we will continue to improve the utilization of the combined service departments of Stellent, Optika and the e-Onehundred Group and from the changes described above.

Since our support and service revenues have lower gross margins than our license revenues, our overall gross margins will typically decline if our support and service revenues increase as a percent of total revenues. Our cost of support and service revenues as a percentage of support and service revenues may vary from period to period, depending in part on whether the services are performed by our in-house staff, subcontractors or third-party system integrators. If our customers perform more services activities in-house or increase the use of third-party systems integrators, our support and service revenues and cost of support and service revenues realized on a per-customer basis may decline and result in lower gross margins.

Cost of Revenues Post-Contract Support

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	2004	Change	2005	2004	Change
	(in thousands, except for percentages)					
Post-contract support cost of revenue	$ 1,956	$ 1,179	66%	$ 3,806	$ 2,297	66%
Gross profit post-contract support	$ 7,932	$ 6,960	14%	$ 15,755	$ 12,465	26%
As a percentage of respective revenue:						
Post-contract support	20%	14%		19%	16%	
Gross profit	80%	86%		81%	84%	

Cost of post-contract support services, consisting of personnel and other operating expenses, increased by $0.8 million and $1.5 million, or 66%, to $2.0 million and $3.8 million for the second quarter and first half of fiscal year 2006 when compared to the same periods in fiscal year 2005. Gross profit as a percentage of post-contract support decreased to 80% and 81% for the second quarter and first half of fiscal year 2006 from 86% and 84% for the second quarter and first half of fiscal year 2005. The increase in the gross profit dollars was due to the increase in post-contract support revenue generated by a growing installed base of Universal Content Management and Content Component customers. The decrease in gross profit as a percentage for post-contract support was due to the additional personnel costs associated with our 24/7 support staff our international operations and other technical support groups. We anticipate our gross profit as a percentage for post-contract support revenue to be 80% to 82% for the remainder of fiscal year 2006.

Since our post-contract support revenues have lower gross margins than our license revenues, our overall gross margins will typically decline if our post-contract support revenues increase as a percent of license revenues. Our cost of post-contract support as a percentage of post-contract support revenues may vary from period to period, depending in part on whether we are able to sell support on new product license revenue and also if our annual renewal rates with our existing customers continues to remain high. Any significant change in our annual renewal rates could result in a decline in our gross profit margins.

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OPERATING EXPENSES

Sales and Marketing

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	2004	Change	2005	2004	Change
	(in thousands, except for percentages)					
Sales and marketing	$ 11,712	$ 10,931	7%	$ 23,148	$ 20,720	12%
Percentage of total revenues	39%	39%		39%	41%	

Sales and marketing expenses consist of salaries, commissions, benefits and related costs for sales and marketing personnel, travel and marketing programs, including customer conferences, promotional materials, trade shows and advertising. Sales and marketing expenses were $11.7 million and $23.1 million for the second quarter and first half of fiscal year 2006, an increase of $0.8 million and $2.4 million, or 7% and 12%, when compared to the same periods in fiscal year 2005. As a percentage of total revenues, sales and marketing expenses were 39% for the second quarter and first half of fiscal year 2006 compared to 39% and 41% for the second quarter and first half of fiscal year 2005. The increase in dollars is a direct result of the incremental compensation costs associated with the higher levels of revenue recognized during the second quarter and first half of fiscal year 2006 when compared to the same period in the prior year, severance costs associated with the departure of our executive vice-president of sales operations and higher levels of costs associated with sales conferences. The overall decrease in sales and marketing as a percentage of revenue is primarily due to a larger revenue base, achieving improved productivity from our sales personnel and the restructurings undertaken by us during the first and fourth quarter of fiscal year 2005. We believe we will see a future benefit from the sales reorganization actions taken during the second quarter of fiscal year 2006. We anticipate our sales and marketing expenses as a percentage of total revenue will be in the 37% to 39% range during the remainder of fiscal year 2006 as we will continue to achieve additional costs savings from the restructuring actions mentioned above. Ultimately, the overall sales and marketing expenses as a percentage of total revenue will be dependent on the timing of hiring of new sales and marketing personnel, our spending on marketing programs and the level of revenues, in particular license revenues, in each period, which may offset anticipated cost savings related to the restructuring actions described above.

General and Administrative

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	2004	Change	2005	2004	Change
	(in thousands, except for percentages)					
General and administrative	$ 2,812	$ 3,057	(8%)	$ 5,982	$ 5,581	7%
Percentage of total revenues	9%	11%		10%	11%	

General and administrative expenses consist of salaries and related costs for general corporate functions, including finance, accounting, human resources, legal and information technology, as well as insurance, professional fees and bad debt expense. For the second quarter and first half of fiscal year 2006, general and administrative expenses were $2.8 million and $6.0 million, a decrease of $0.2 million and an increase of $0.4 million, or (8%) and 7%, from $3.0 million and $5.6 million for the second quarter and first half of fiscal year 2005. The decrease in general and administrative expenses in the second quarter of fiscal year 2006 when compared to the same period in fiscal year 2005 was due to lower levels of professional fees from our shareholder litigation. We anticipate general and administrative costs will increase in the second half of fiscal year 2006 as our external auditors start their Sarbanes-Oxley procedures for fiscal year 2006. The increase in general and administrative costs when comparing the first half of fiscal year 2006 to the first half of fiscal year 2005 was due to an increase in accounting and other professional fees associated with our annual audit and related services and an increase in our bad debt expense. We expect general and administrative expenses will continue to be approximately 10% to 12% of total revenue during the remainder of fiscal year 2006. If new regulations are enacted by Congress, the Securities and Exchange Commission or the national stock exchanges, it could result in an increase to our general and administrative expenses.

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Research and Development

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	2004	Change	2005	2004	Change
	(in thousands, except for percentages)					
Research and development	$ 4,895	$ 4,867	1%	$ 9,551	$ 8,665	10%
Percentage of total revenues	16%	17%		16%	17%	

Research and development expenses consist of salaries and benefits, third-party contractors, facilities and related overhead costs associated with our product development and quality assurance activities. For the second quarter and first half of fiscal year 2006, research and development expenses totaled $4.9 million and $9.6 million, compared to $4.9 million and $8.7 million for the second quarter and first half of fiscal year 2005. Our research and development efforts continue to be focused on enhancing our many products, which also increases customer value through the interoperability of those products. These products include Universal Content Management, Content Component and our recent acquisition of e-Onehundred s Sarbanes-Oxley Solution. During the first half of fiscal year 2006, we announced the release of version 7.5 of our Multi-Site Web Content Management application, which provides a more robust management foundation for deploying and maintaining multiple Web sites. The increase in research and development expense for the first half of fiscal year 2006 when compared to the first half of fiscal year 2005 was due to the our continued effort to support the many product enhancement initiatives currently underway for those products mentioned above. We believe that our research and development expense as a percentage of total revenue will be approximately 16% to 18% during the remainder of fiscal year 2006.

Acquisition-Related Sales, Marketing and Other Costs

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	2004	Change	2005	2004	Change
	(in thousands, except for percentages)					
Acquisition-related sales, marketing and other costs	$	$	%	$	$ 886	(100%)
Percentage of total revenues	%	%		%	2%	

Acquisition-related sales, marketing and other costs of $0.9 million in the three months ended June 30, 2004 related to the Optika acquisition. Approximately $0.6 million of these costs related to advertising done in various periodicals announcing the completion of the Optika acquisition. We have generally not done this type of advertising in the past. Because we believe market trends may result from consolidation of the content management software market, from time to time we may seek to acquire businesses, products or technologies that are complementary to our business. Depending on the size, nature and structure of any future business acquisitions, our acquisition-related expenses may increase substantially.

Amortization of Acquired Intangible Assets and Other

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	2004	Change	2005	2004	Change
	(in thousands, except for percentages)					
Amortization of acquired intangible assets and other	$ 210	$ 175	20%	$ 374	$ 354	6%
Percentage of total revenues	1%	1%		1%	1%	

During the second quarter and first half of fiscal year 2006, amortization of acquired intangible assets consisted of amortization expense associated with the amount of the purchase price allocated to Optika s and e-Onehundred Group s customer base and stock compensation expense related to unvested stock options acquired in the acquisition of Optika. During the second quarter and first half of fiscal year 2005, additional amortization expense was recognized in connection with our acquisition of CCD in July 2000, RESoft in July 2001 and Kinecta in April 2002, which were fully amortized as of March 31, 2005.

Restructuring Charges

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	2004	Change	2005	2004	Change
	(in thousands, except for percentages)					
Restructuring charges	$ 648	$	100%	$ 665	$ 2,461	(73%)
Percentage of total revenues	2%	%		1%	5%	

We assessed many factors in determining whether and when to restructure our operations, with a significant consideration being the performance of the economy and the information technology markets in the United States and in Europe. During the second quarter of fiscal year 2006, we recognized $140 additional expense of related to a change in estimate for our New York leased facility. We also recognized a restructuring charge of $508 related to the closing of our Brazilian sales operation and to the reorganization of certain other international sales operations and also the consolidation of certain general and administrative activities. During the first half of fiscal year 2006, we recognized $74 of additional costs associated with the restructuring actions taken during the fourth quarter of fiscal year 2005 related to the closure of our Mexican operations. These additional costs were partially offset by a change in estimate resulting in a $57 reduction of expense related to our Massachusetts facility as a result of reaching a buyout arrangement on the remaining lease obligation. During the second quarter of fiscal year 2005, in connection with the Optika acquisition and management s plan to reduce costs and improve operating efficiencies, we recorded a restructuring charge of approximately $2.5 million. The restructuring charge was comprised of severance pay and benefits related to the involuntary termination of employees of approximately $1.9 million, with the remaining $0.6 million related to the closing of excess facilities and other exit costs. These cost reduction measures were taken to take advantage of the cost synergies from the Optika acquisition. However, we may be required to re-invest in certain areas to expand our customer base, grow our revenues and invest in product development, which may eliminate or exceed these cost savings.

Other Income (Expense)

	Three Months Ended September 30,			Six Months Ended September 30,		
	2005	2004	Change	2005	2004	Change
	(in thousands, except for percentages)					
Interest income	$ 478	$ 149	221%	$ 893	$ 343	160%
Percentage of total revenues	2%	1%		2%	1%	

Interest income, net increased by $0.3 million and $0.6 million or 221% and 160%, for the second quarter and first half of fiscal year 2006 when compared to the same period in the prior year. The increase was due to an increase in market interest rates during the past twelve months.

Net Operating Loss Carryforwards

As of March 31, 2005, we had net operating loss carryforwards of approximately $152.4 million. The net operating loss carryforwards will expire at various dates beginning in 2010, if not utilized. The Tax Reform Act of 1986 imposes substantial restrictions on the utilization of net operating losses and tax credits in the event of an ownership change of a corporation. In the past quarter, we have completed an NOL carryforward study with an outside professional firm. Of the total $152 million we had in NOL carryforwards at March 31, 2005, $85 million is U.S. based and not subject to limitations, and $35 million is U.S. based is subject to limitations. We acquired this $35 million NOL from our acquisition of Optika in May 2004. Approximately $26 million is foreign based and not subject to limitations and $6 million is foreign based and is subject to limitations. Even though we have substantial NOLs without limitations, we are still subject to U.S. Alternative Minimum Tax and tax expense required to be recognized pursuant to FAS109 related to prior asset based acquisitions, which were reflected in our second quarter fiscal year

2006. We have provided a valuation allowance against the entire amount of the deferred tax asset as of September 30, 2005 and March 31, 2005 because of uncertainty regarding its full realization. Our accounting for deferred taxes involves the evaluation of a number of factors concerning the realizability of our deferred tax assets. In concluding that a valuation allowance was required, management considered such factors as our history of operating losses, potential future losses and the nature of our deferred tax assets.

Liquidity and Capital Resources

We have funded our operations and satisfied our capital expenditure requirements primarily through public offerings of securities and cash flow from operations.

To date, we have invested our capital expenditures in property and equipment, consisting largely of computer hardware and software. Capital expenditures for the first half of fiscal year 2006 were $3.5 million, which was due primarily to our move into our new corporate headquarters. We have also entered into capital and operating leases for facilities and equipment. We expect that our capital expenditures will increase as our employee base grows.

As of September 30, 2005, we had $69.9 million in cash and marketable securities and $62.4 million in working capital. We currently believe that our cash and cash equivalents and marketable securities on hand will be sufficient to meet our working capital requirements for the foreseeable future, particularly through March 31, 2006. On a longer term basis, we may require additional funds to support our working capital requirements or for other purposes and may seek to raise such additional funds through public or private equity financings or from other sources. We cannot be certain that additional financing will be available on terms favorable to us, or on any terms, or that any additional financing will not be dilutive.

We continue to evaluate potential strategic acquisitions that could utilize equity and/or cash resources. Such opportunities could develop quickly due to market and competitive factors.

Cash, cash equivalents and marketable securities decreased $2.8 million, or 4%, to $69.9 million as of September 30, 2005 from $72.8 million at March 31, 2005. The decrease was primarily due to the $5.0 million of cash used in the acquisition of e-Onehundred Group in June 2005.

Cash provided by (used in) was as follows (in thousands):

	Six Months Ended September 30,	
	2005	**2004**
Cash provided by (used in) operating activities	$ 4,515	$ (4,101)
Cash used in investing activities	(9,447)	(4,046)
Cash provided by financing activities	2,194	1,141

Operating Activities. Net cash provided by operating activities of $4.5 million in the six months ended September 30, 2005 resulted from net income of $1.6 million. After excluding the effects of non-cash expenses including depreciation and amortization of $1.2 million, amortization of intangible assets of $1.3 million and lease incentives of $1.0 million, the adjusted cash provided before the effect of changes in working capital components was $5.1 million. Additional cash provided was the result of a $2.0 million increase in accrued liabilities, a decrease in accounts receivable of $0.9 million, and a decrease in prepaid expense of $0.1 million. Cash used in operating activities included a decrease in accounts payable of $2.5 million and a decrease in deferred revenue of $1.0 million.

A number of non-cash items were charged to expense and reduced our net income or increased our net loss for the six months ended September 30, 2005 and 2004, respectively. These items include depreciation and amortization of property and equipment and intangible assets. The extent to which these non-cash items increase or decrease in amount and increase or decrease our future operating results will have no net impact on our operating cash flows because the change in net income (loss) will be offset by a corresponding but opposite change in the non-cash adjustment.

Our primary source of operating cash flow is the collection of accounts receivable from our customers offset by payments to our employees, vendors and service providers. We measure the effectiveness of our collection efforts by an analysis of average accounts receivable days outstanding (days outstanding). Days outstanding were 91 days and 107 days for the six months ended September 30, 2005 and 2004, respectively. Collections of accounts receivable and related days outstanding will fluctuate in future periods due to the timing and amount of our future revenues, payment terms on customer contracts and the effectiveness of our collection efforts.

Our operating cash flows will also be impacted in the future based on the timing of payments to our vendors. We endeavor to pay our vendors and service providers in accordance with invoice terms and conditions. The timing of cash payments in future periods will be impacted by the nature of vendor arrangements and management s assessment of our cash inflows.

Investing Activities. Net cash used in investing activities was $9.4 million for the six months ended September 30, 2005. This resulted from $5.1 million used in the e-Onehundred acquisition, approximately $3.5 million to purchase property and equipment, net purchases from investment activity of approximately $0.5 million and $0.3 million related to other prior acquisition activities. During the second quarter of fiscal year 2006, we completed the move into our new corporate headquarters. In connection with this move, we were provided with $1.0 million of tenant improvements, which was included in our $3.5 million of property and equipment purchases.

Generally, our investment portfolio is classified as held to maturity. Our investments objectives are to preserve principal and provide liquidity, while at the same time maximizing yields without significantly increasing risk. We generally hold investments in commercial paper, corporate bonds and United States government agency securities to maturity.

We anticipate that we will continue to purchase property and equipment necessary in the normal course of our business. The amount and timing of these purchases and the related cash outflows in future periods is difficult to predict and is dependent on a number of factors including the hiring of employees, the rate of change of computer hardware and software used in our business and our business outlook. However, since we have completed the move into our new corporate headquarters, we expect our capital expenditures to return to a more normalized level for the remainder of fiscal year 2006.

Financing Activities. Net cash provided by financing activities of $2.2 million in the six months ended September 30, 2005 included approximately $2.4 million in net proceeds from the issuance of common stock related to the exercise of employee stock options and employee stock purchase plan. We also made $0.2 million of payments under capital leases during the first half of fiscal year 2006.

Our cash flows from financing activities are the result of cash receipts from the issuance of common stock. We receive cash from the exercise of common stock options and the sale of common stock under our Employee Stock Purchase Plan. While we expect to continue to receive these proceeds in future periods, the timing and amount of such proceeds is difficult to predict and is contingent on a number of factors including the price of our common stock, the number of employees participating in our stock option plans and our Employee Stock Purchase Plan and general market conditions. Upon all the available shares being issued under the Employee Stock Purchase Plan, it is our current intention not to authorize additional shares under this plan. Based on historical levels of employee participation and contributions, the last six-month plan period would end January 31, 2006.

Financial Risk Management

As a global concern, we face exposure to adverse movements in foreign currency exchange rates. These exposures may change over time as business practices evolve and could have a material adverse impact on our consolidated financial results. Our primary exposures relate to non-United States dollar-denominated revenues and operating expenses in Europe, Asia Pacific, Australia and Canada. At the present time, the exposure is not significant. We do not anticipate significant currency gains or losses in the near term.

Recent Accounting Pronouncements

In November 2005, the FASB issued FASB Staff Position (FSP) FAS 115-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments.* The guidance in this FSP addresses the determination of when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. The FSP also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. The guidance in this FSP amends FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities.* The guidance in this FSP nullifies certain requirements of EITF Issue No. 03-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*, and supersedes *EITF Abstracts*, Topic D-44, *Recognition of Other-Than-Temporary Impairment upon the Planned Sale of a Security Whose Cost Exceeds Fair Value.* The guidance in this FSP is required to be applied to reporting periods beginning after December 15, 2005. We plan on adopting this statement during our third quarter of fiscal year 2006 and do not believe that the adoption of the provisions of FAS 115-1 will have a material impact on our consolidated financial statements.

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections*. This new standard replaces APB Opinion No. 20, Accounting Changes, and FASB Statement No. 3, Reporting Accounting Changes in Interim Financial Statements. Among other changes, SFAS No. 154 requires that a voluntary change in accounting principle be applied retrospectively with all prior period financial statements presented on the new accounting principle, unless it is impracticable to do so. SFAS No. 154 also provides that (1) a change in method of depreciating or amortizing a long-lived nonfinancial asset be accounted for as a change in estimate (prospectively) that was effected by a change in accounting principle, and (2) correction of errors in previously issued financial statements should be termed a restatement. The new standard is effective for accounting changes and correction of errors made in fiscal years beginning after December 15, 2005. We do not believe that the adoption of the provisions of SFAS No. 154 will have a material impact on our consolidated financial statements.

In December 2004, the FASB issued SFAS No. 123 (revised 2004), *Share-Based Payment,* known as Statement 123(R). Statement 123(R) will, with certain exceptions, require entities that grant stock options and shares to employees to recognize the fair value of those options and shares as compensation cost over the service (vesting) period in their financial statements. The measurement of that cost will be based on the fair value of the equity or liability instruments issued. We are required to adopt Statement 123(R) in the first interim period beginning after our fiscal year 2006. As part of this adoption, we will begin expensing options effective April 1, 2006 and have also elected not to restate the prior period results. Based on the current amount of outstanding stock options that will vest on or after April 1, 2006, we anticipate recognizing approximately $3.2 million of compensation expense during our fiscal year 2007. This amount will fluctuate depending on future stock options granted to or forfeited by employees and directors.

Critical Accounting Policies and Estimates

In preparing our condensed consolidated financial statements, we make estimates, assumptions and judgments that can have a significant impact on our revenues, income or loss from operations and net income or loss, as well as on the value of certain assets and liabilities on our consolidated balance sheet. We believe that there are several accounting policies that are critical to an understanding of our historical and future performance, as these policies affect the reported amounts of revenues, expenses and significant estimates and judgments applied by management. While there are a number of accounting policies, methods and estimates affecting our consolidated financial statements, areas that are particularly significant include:

- revenue recognition;
- allowance for doubtful accounts;
- accrual for restructuring and excess facilities costs;
- accounting for income taxes; and
- valuation and evaluating impairment of long-lived assets, intangible assets and goodwill.

Revenue Recognition

We currently derive all of our revenues from licenses of software products and related services. We recognize revenue in accordance with SOP 97-2, *Software Revenue Recognition*, as amended by SOP 98-9, Modification of SOP 97-2, *Software Revenue Recognition with Respect to Certain Transactions*, and Securities and Exchange Commission Staff Accounting Bulletin 104, *Revenue Recognition*.

Product license revenue is recognized under SOP 97-2 when (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred, (iii) the fee is fixed or determinable, and (iv) collectibility is probable and supported and the arrangement does not require services that are essential to the functionality of the software.

Persuasive Evidence of an Arrangement Exists We determine that persuasive evidence of an arrangement exists with respect to a customer under, (i) a signature license agreement, which is signed by both the customer and us, or, (ii) a purchase order, quote or binding letter-of-intent received from and signed by the customer, in which case the customer has either previously executed a signature license agreement with us or will receive a shrink-wrap license agreement with the software. We do not offer product return rights to end users or resellers.

Delivery has Occurred Our software may be either physically or electronically delivered to the customer. We determine that delivery has occurred upon shipment of the software pursuant to the billing terms of the arrangement or when the software is made available to the customer through electronic delivery. Customer acceptance generally occurs at delivery.

The Fee is Fixed or Determinable If at the outset of the customer arrangement, we determine that the arrangement fee is not fixed or determinable, revenue is typically recognized when the arrangement fee becomes due and payable. Fees due under an arrangement are generally deemed fixed and determinable if they are payable within twelve months.

Collectibility is Probable and Supported We determine whether collectibility is probable and supported on a case-by-case basis. We may generate a high percentage of our license revenue from our current customer base, for whom there is a history of successful collection. We assess the probability of collection from new customers based upon the number of years the customer has been in business and a credit review process, which evaluates the customer s financial position and ultimately its ability to pay. If we are unable to determine from the outset of an arrangement that collectibility is probable based upon our review process, revenue is recognized as payments are received.

With regard to software arrangements involving multiple elements, we allocate revenue to each element based on the relative fair value of each element. Our determination of fair value of each element in multiple-element arrangements is based on vendor-specific objective evidence (VSOE). We limit our assessment of VSOE for each element to the price charged when the same element is sold separately. We have analyzed all of the elements included in our multiple-element arrangements and have determined that we have sufficient VSOE to allocate revenue to consulting services and post-contract customer support (PCS) components of our license arrangements. Generally, we sell our consulting services separately, and have established VSOE on this basis. VSOE for PCS is determined based upon the customer s annual renewal rates for these elements. Accordingly, assuming all other revenue recognition criteria are met, revenue from perpetual licenses is recognized upon delivery using the residual method in accordance with SOP 98-9, and revenue from PCS is recognized ratably over their respective terms, typically one year.

Our direct customers typically enter into perpetual license arrangements. Our Content Components Division generally enters into term-based license arrangements with its customers, the term of which generally exceeds one year in length. We recognize revenue from time-based licenses at the time the license arrangement is signed, assuming all other revenue recognition criteria are met, if the term of the time-based license arrangement is greater than twelve months. If the term of the time-based license arrangement is twelve months or less, we recognize revenue ratably over the term of the license arrangement.

Services revenue consists of fees from consulting services and PCS. Consulting services include needs assessment, software integration, security analysis, application development, training and billable expenses. We bill consulting services fees either on a time and materials basis or on a fixed-price schedule. In general, our consulting services are not essential to the functionality of the software. Our software products are fully functional upon delivery and implementation and generally do not require any significant modification or alteration for customer use. Customers purchase our consulting services to facilitate the adoption of our technology and may dedicate personnel to participate in the services being performed, but they may also decide to use their own resources or appoint other professional service organizations to provide these services. Software products are billed separately from professional services. We recognize revenue from consulting services as services are performed. Our customers typically purchase PCS annually, and we price PCS based on a percentage of the product license fee or a percentage of product list price. Customers purchasing PCS receive product upgrades, Web-based technical support and telephone hot-line support. Unspecified product upgrades are typically not provided without the purchase of PCS. We typically have not granted specific upgrade rights in our license agreements. Specified undelivered elements are allocated a relative fair value amount within a license agreement and the revenue allocated for these elements are deferred until delivery occurs.

Customer advances and billed amounts due from customers in excess of revenue recognized are recorded as deferred revenue.

We follow very specific and detailed guidelines, discussed above, in determining revenues; however, certain judgments and estimates are made and used to determine revenue recognized in any accounting period. Material differences may result in the amount and timing of revenue recognized for any period if different conditions were to prevail. For example, in determining whether collection is probable, we assess our customers ability and intent to pay. Our actual experience with respect to collections could differ from our initial assessment if, for instance, unforeseen declines in the overall economy occur and negatively impact our customers financial condition.

Accounts Receivable and Allowance for Doubtful Accounts

The preparation of our consolidated financial statements requires management to make estimates and assumptions that affect the reported amount of assets and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported period. Specifically, we make estimates as to the overall collectibility of accounts receivable and provide an allowance for amounts deemed to be uncollectible. Management specifically analyzes its accounts receivable and establishes a reserve based on factors that include historical bad debt experience, customer credit-worthiness, and current economic trends.

Restructuring and Excess Facilities Accrual

Due to the recent economic slowdown and associated reduction in information technology spending, we implemented a series of restructuring and facility consolidation plans to improve our operating performance. We also implemented restructuring plans during fiscal year 2005 related to the integration of our acquisition of Optika. Restructuring and facilities consolidation costs consist of expenses associated with workforce reductions and consolidation of excess facilities.

Workforce Reductions

In connection with our restructuring plans, we accrue for severance payments and other related termination benefits provided to employees in connection with involuntary staff reductions. We accrue for these benefits in the period when benefits are communicated to the terminated employees. Typically, terminated employees are not required to provide continued service to receive termination benefits. If continued service is required, then the severance liability is accrued over the required service period. In general, we use a formula based on a combination of the number of years of service and the employee s position within our company to calculate the termination benefits to be provided to affected employees. At September 30, 2005, approximately $0.6 million was accrued for future severance and termination benefits payments that is payable through June 2006.

Excess Facilities

In connection with our restructuring and facility consolidation plans, we perform evaluations of our then-current facilities requirements and identify facilities that are in excess of our current and estimated future needs. When a facility is identified as excess and we have ceased use of the facility, we accrue the fair value of the lease obligations.

In determining fair value, we consider expected sublease income over the remainder of the lease term and related exit costs if any. To determine the estimated sublease income, we receive appraisals from real estate brokers to aid in our estimate. In addition, during our evaluation of our facilities requirements, we also identify operating equipment and leasehold improvements that may have suffered a reduction in their economic useful lives. Most of our excess facilities are being marketed for sublease and are currently unoccupied. Accordingly, our estimate of excess facilities could differ from actual results and such differences could result in additional charges that could materially affect our consolidated financial position and results of operations. At September 30, 2005, we had approximately $0.4 million accrued for excess facilities, which is payable through January 2007. We reassess our excess facilities liability each period based on current real estate market conditions.

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Accounting for Income Taxes

As part of the process of preparing our consolidated financial statements, we are required to estimate our income tax liability in each of the jurisdictions in which we do business. This process involves estimating our actual current tax expense together with assessing temporary differences resulting from differing treatment of items, such as deferred revenues, for tax and accounting purposes. These differences result in deferred tax assets and liabilities. We must then assess the likelihood that these deferred tax assets will be recovered from future taxable income and, to the extent we believe that recovery is not more likely than not or unknown, we must establish a valuation allowance.

Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our deferred tax assets. At September 30, 2005, we have recorded a full valuation allowance of $71.1 million against our deferred tax assets, due to uncertainties related to our ability to utilize our deferred tax assets, consisting principally of certain net operating losses carried forward. The valuation allowance is based on our estimates of taxable income by jurisdiction and the period over which our deferred tax assets will be recoverable. The Company had U.S. net operating loss (NOL) carryforwards of approximately $120 million and foreign net operating losses of approximately $32.0 million at March 31, 2005, which begin to expire in 2010. In the past quarter, we have completed our NOL carryforward study with an outside professional firm. Of the total $152 million we had in NOL carryforwards at March 31, 2005, $85 million is U.S. based and not subject to limitations and $35 million is U.S. based and subject to limitations. We acquired this $35 million NOL from our acquisition of Optika in May 2004. Approximately $26 million is foreign based and not subject to limitations and $6 million is foreign based and subject to limitations. Even though we have substantial NOLs without limitations, we are still subject to U.S. Alternative Minimum Tax and tax expense required to be recognized pursuant to FAS109 related to prior asset based acquisitions, which were reflected in our second quarter fiscal year 2006.

Realization of the NOL carryforwards and other deferred tax temporary differences are contingent on future taxable earnings. The deferred tax asset was reviewed for expected utilization using a more likely than not approach as required by SFAS No. 109, *Accounting for Income Taxes*, by assessing the available positive and negative evidence surrounding its recoverability.

We will continue to assess and evaluate strategies that will enable the deferred tax asset, or portion thereof, to be utilized, and will reduce the valuation allowance appropriately at such time when it is determined that the more likely than not approach is satisfied.

Valuation and Evaluation of Impairment of Long-lived Assets

We account for long-lived assets in accordance with the provisions of SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets.* This Statement requires that long-lived and intangible assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net undiscounted cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. Based on our review no impairment of long-lived assets has occurred through September 30, 2005.

Valuation and Evaluation of Goodwill and Other Acquired Intangible Assets

On April 1, 2002, we adopted SFAS No. 142, *Goodwill and Other Intangible Assets.* SFAS No. 142 requires that goodwill no longer be amortized and that goodwill be tested annually for impairment or more frequently if events and circumstances warrant. We are required to perform an impairment review of goodwill on at least an annual basis. This impairment review involves a two-step process as follows:

> Step 1 We compare the fair value of our reporting unit to its carrying value, including goodwill. If the reporting unit s carrying value, including goodwill, exceeds the unit s fair value, we move on to Step 2. If the unit s fair value exceeds the carrying value, no further work is performed and no impairment charge is necessary.

Step 2 We perform an allocation of the fair value of the reporting unit to its identifiable tangible and non-goodwill intangible assets and liabilities. This derives an implied fair value for the reporting unit s goodwill. We then compare the implied fair value of the reporting unit s goodwill with the carrying amount of the reporting unit s goodwill. If the carrying amount of the reporting unit s goodwill is greater than the implied fair value of its goodwill, an impairment charge would be recognized for the excess.

We have determined that we have two reporting units. We performed and completed our required annual impairment testing on January 1, 2005. As part of this review, we engaged a independent third-party valuation of the two reporting units. Upon completing our review, we determined that the carrying value of our recorded goodwill as of this date had not been impaired and no impairment charge was recorded.

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We are also required to assess goodwill for impairment on an interim basis when indicators exist that goodwill may be impaired based on the factors mentioned above. For example, if our market capitalization declines below our net book value or we suffer a sustained decline in our stock price, we will assess whether our goodwill has been impaired. A significant impairment could result in additional charges and have a material adverse impact on our consolidated financial condition and operating results. No circumstances occurred during the first nine months of calendar year 2005 that would have created an impairment loss at September 30, 2005.

RISK FACTORS

DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

The risks and uncertainties described below are not the only risks we face. These risks include those that we consider to be significant at this time to investment decisions regarding our common stock. There may be risks that you, in particular, view differently than we do, and there are other risks and uncertainties that we do not presently know of or that we currently deem immaterial, but that may, in fact, harm our business in the future. If any of these events occur, our business, results of operations and financial condition could be seriously harmed, and the trading price of our common stock could decline.

You should consider carefully the following factors, in addition to other information in this Quarterly Report on Form 10-Q, in evaluating our company and business.

BECAUSE OUR INFRASTRUCTURE COSTS ARE GENERALLY FIXED AND THE TIMING OF OUR REVENUES FROM QUARTER TO QUARTER IS HIGHLY VARIABLE, OUR FUTURE PERFORMANCE IS DIFFICULT TO PREDICT, MAKING AN INVESTMENT IN OUR COMMON STOCK SUBJECT TO HIGH VOLATILITY.

While our products and services are not seasonal, our revenues and operating results are difficult to predict and may fluctuate significantly from quarter to quarter. If our quarterly revenues or operating results fall below the expectations of investors or securities analysts, the price of our common stock could fall substantially. A large part of our sales typically occurs in the last month of a quarter, frequently in the last week or even the last days of the quarter. If these sales were delayed from one quarter to the next for any reason, our operating results could fluctuate dramatically. In addition, our sales cycles may vary, making the timing of sales difficult to predict. Furthermore, our infrastructure costs are generally fixed. As a result, modest fluctuations in revenues between quarters may cause large fluctuations in operating results. These factors all tend to make the timing of revenues unpredictable and may lead to high period-to-period fluctuations in operating results.

Our quarterly revenues and operating results may fluctuate for several additional reasons, many of which are outside of our control, including the following:

- demand for our products and services;
- the timing of new product introductions and sales of our products and services;
- unexpected delays in introducing new products and services;
- increased expenses, whether related to sales and marketing, research and development, administration or services;
- changes in the rapidly evolving market for Web content management solutions;
- the mix of revenues from product licenses and services, as well as the mix of products licensed;
- the mix of services provided and whether services are provided by our staff or third-party contractors;
- the mix of domestic and international sales;
- costs related to possible acquisitions of technology or businesses;

general economic conditions; and

public announcements by our competitors.

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WE HAVE A HISTORY OF MAKING ACQUISITIONS, INCLUDING LARGE STRATEGIC ACQUISITIONS, AND FUTURE POTENTIAL ACQUISITIONS MAY BE DIFFICULT TO COMPLETE OR TO INTEGRATE AND MAY DIVERT MANAGEMENT S ATTENTION AND CAUSE OUR OPERATING RESULTS TO SUFFER.

We may seek to acquire or invest in businesses, products or technologies that are complementary to our business. If we identify an appropriate acquisition opportunity, we may be unable to negotiate favorable terms for that acquisition, successfully finance the acquisition or integrate the new business or products into our existing business and operations. In addition, the negotiation of potential acquisitions and the integration of acquired businesses or products may divert management time and resources from our existing business and operations. To finance acquisitions, we may use a substantial portion of our available cash or we may issue additional securities, which would cause dilution to our shareholders.

WE MAY NOT BE PROFITABLE IN THE FUTURE, WHICH WOULD CAUSE OUR FINANCIAL POSITION TO SUFFER AND MAY CAUSE THE MARKET PRICE OF OUR STOCK TO FALL.

Our revenues may not grow in future periods and we may not sustain profitability. If we do not sustain profitability, our financial position will suffer and the market price of our stock may fall. Our ability to sustain profitable operations depends upon many factors beyond our direct control. These factors include, but are not limited to:

- the demand for our products;
- our ability to quickly introduce new products;
- the level of product and price competition;
- our ability to control costs; and
- general economic conditions.

THE INTENSE COMPETITION IN OUR INDUSTRY FROM RECENT AND EXPECTED INDUSTRY CONSOLIDATION MAY REDUCE OUR FUTURE SALES AND PROFITS.

The market for our products is highly competitive and is likely to become more competitive from recent and expected industry consolidation. We may not be able to compete successfully in our chosen marketplace, which may have a material adverse effect on our business, operating results and financial condition. Additional competition may cause pricing pressure, reduced sales and margins, or prevent our products from gaining and sustaining market acceptance. Many of our current and potential competitors have greater name recognition, access to larger customer bases, and substantially more resources than we have. Competitors with greater resources than ours may be able to respond more quickly than we can to new opportunities, changing technology, product standards or customer requirements.

WE DEPEND ON THE CONTINUED SERVICE OF OUR KEY PERSONNEL; IF WE LOSE THE SERVICES OF OUR KEY PERSONNEL OUR ABILITY TO EXECUTE OUR OPERATING PLAN, AND OUR OPERATING RESULTS, MAY SUFFER.

We are a small company and depend greatly on the knowledge and experience of our senior management team and other key personnel. If we lose any of these key personnel, our business, operating results and financial condition could be materially adversely affected. Our success will depend in part on our ability to attract and retain additional personnel with the highly specialized expertise necessary to generate revenue and to engineer, design and support our products and services. Like other software companies, we face intense competition for qualified personnel. We may not be able to attract or retain such personnel.

WE HAVE RELIED AND EXPECT TO CONTINUE TO RELY ON SALES OF OUR UNIVERSAL CONTENT MANAGEMENT SOFTWARE AND CONTENT COMPONENT SOFTWARE PRODUCTS FOR OUR REVENUES; IF OUR UNIVERSAL CONTENT MANAGEMENT SOFTWARE AND IMAGING AND BUSINESS PROCESS MANAGEMENT SOFTWARE DOES NOT GAIN AND MAINTAIN CUSTOMER ACCEPTANCE, OUR REVENUES AND OPERATING RESULTS MAY SUFFER.

We currently derive all of our revenues from product licenses and services associated with our Universal Management, business process management and Content Component software products. The market for content management and viewing software products is new and rapidly evolving. We cannot be certain that a viable market for our products will continue or that it will be sustainable. If we do not increase employee productivity and revenues related to our existing products or generate revenues from new products and services, our business, operating results and financial condition may be materially adversely affected. We will continue to depend on revenues related to new and enhanced versions of our software products for the foreseeable future. Our success will largely depend on our ability to increase sales from existing products and generate sales from product enhancements and new products. We cannot be certain that we will be successful in upgrading and marketing our existing products or that we will be successful in developing and marketing new products and services. The market for our products is highly competitive and is subject to rapid technological change. Technological advances could make our products less attractive to customers and adversely affect our business. In addition, complex software product development involves certain inherent risks, including risks that errors may be found in a product enhancement or new product after its release, even after extensive testing, and the risk that discovered errors may not be corrected in a timely manner.

IF WE CANNOT PROTECT OUR INTELLECTUAL PROPERTY, WHICH CONSISTS PRIMARILY OF OUR PROPRIETARY SOFTWARE PRODUCTS, AND DO SO COST-EFFECTIVELY, OUR BUSINESS, OPERATING RESULTS AND FINANCIAL CONDITION MAY SUFFER.

If we are unable to protect our intellectual property, or incur significant expense in doing so, our business, operating results and financial condition may be materially adversely affected. Any steps we take to protect our intellectual property may be inadequate, time consuming and expensive. We currently have one pending patent application; but no patent has yet been issued. Without significant patent or copyright protection, we may be vulnerable to competitors who develop functionally equivalent products. We may also be subject to claims that our current products infringe on the intellectual property rights of others. Any such claim may have a material adverse effect on our business, operating results and financial condition.

We anticipate that software product developers will be increasingly subject to infringement claims due to growth in the number of products and competitors in our industry, and the overlap in functionality of products in different industries. Any infringement claim, regardless of its merit, could be time-consuming, expensive to defend, or require us to enter into royalty or licensing agreements. Such royalty or licensing agreements may not be available on commercially favorable terms, or at all.

We rely on trade secret protection, confidentiality procedures and contractual provisions to protect our proprietary information. Despite our attempts to protect our confidential and proprietary information, others may gain access to this information. Alternatively, other companies may independently develop substantially equivalent information.

WE COULD BE SUBJECT TO PRODUCT LIABILITY CLAIMS IF OUR SOFTWARE PRODUCTS DAMAGE CUSTOMERS DATA, FAIL TO MAINTAIN ACCESS SECURITY OR OTHERWISE FAIL TO PERFORM TO SPECIFICATIONS, WHICH COULD HARM OUR OPERATING RESULTS AND FINANCIAL POSITION AND REDUCE THE VALUE OF AN INVESTMENT IN OUR COMMON STOCK.

If software errors or design defects in our products cause damage to customers data and our agreements do not protect us from related product liability claims, our business, operating results and financial condition may be materially adversely affected. In addition, we could be subject to product liability claims if our security features fail to prevent unauthorized third parties from entering our customers intranet, extranet or Internet Websites. Our software products are complex and sophisticated and may contain design defects or software errors that are difficult to detect and correct. Errors, bugs or viruses spread by third parties may result in the loss of market acceptance or the loss of customer data. Our agreements with customers that attempt to limit our exposure to product liability claims may not be enforceable in certain jurisdictions where we operate.

FUTURE REGULATION OF THE INTERNET OR AFFECTING WEB-BASED COMMUNICATIONS COULD BE ADOPTED THAT RESTRICT OUR BUSINESS, WHICH MAY LIMIT OUR ABILITY TO GENERATE REVENUES FROM OUR PRODUCTS.

Federal, state or foreign agencies may adopt new legislation or regulations governing the use and quality of Web content. We cannot predict if or how any future laws or regulations would impact our business and operations. Even though these laws and regulations may not apply to our business directly, they could indirectly harm us to the extent that they impact our customers and potential customers.

WE HAVE BEEN NAMED A DEFENDANT IN SECURITIES CLASS-ACTION LAWSUITS AND WE MAY IN THE FUTURE BE NAMED IN ADDITIONAL LITIGATION, WHICH MAY RESULT IN SUBSTANTIAL COSTS AND DIVERT MANAGEMENT S ATTENTION AND RESOURCES.

Shareholder class-action suits have been filed naming Stellent and certain of our current and former officers and directors as co-defendants. We have reached a settlement, subject to final documentation and preliminary and final court approval.

Securities class-action litigation has often been brought against companies following periods of volatility in the price of their securities. This risk is greater for technology companies, which have experienced greater-than-average stock price volatility in recent years and, as a result, have been subject to, on average, a greater number of securities class-action claims than companies in other industries. We may in the future again be the target of this kind of litigation, and such litigation could also result in substantial costs and divert management s attention and resources.

THE MARKET PRICE OF OUR COMMON STOCK COULD FLUCTUATE SIGNIFICANTLY DUE TO VARIATIONS IN OUR OPERATING RESULTS, CHANGES IN THE SOFTWARE INDUSTRY AND OTHER FACTORS, RESULTING IN SUDDEN CHANGES IN THE MARKET VALUE OF AN INVESTMENT IN OUR COMMON STOCK.

The market price of our common stock has fluctuated significantly in the past and may do so in the future. The market price of our common stock may be affected by each of the following factors, many of which are outside of our control:

- variations in quarterly operating results;
- changes in estimates by securities analysts;
- changes in market valuations of companies in our industry;
- announcements of significant events, such as major sales;
- acquisitions of businesses or losses of major customers; and
- sales of our equity securities.

WE CAN ISSUE SHARES OF PREFERRED STOCK WITHOUT SHAREHOLDER APPROVAL, WHICH COULD ADVERSELY AFFECT THE RIGHTS OF COMMON SHAREHOLDERS.

Our articles of incorporation permit us to establish the rights, privileges, preferences and restrictions, including voting rights, of unissued shares of our capital stock and to issue such shares without approval from our shareholders. The rights of holders of our common stock may suffer as a result of the rights granted to holders of preferred stock that may be issued in the future. In addition, we could issue preferred stock to prevent a change in control of our company, depriving shareholders of an opportunity to sell their stock at a price in excess of the prevailing market price.

OUR SHAREHOLDER RIGHTS PLAN AND CERTAIN PROVISIONS OF MINNESOTA LAW MAY MAKE A TAKEOVER OF STELLENT DIFFICULT, DEPRIVING SHAREHOLDERS OF OPPORTUNITIES TO SELL SHARES AT ABOVE-MARKET PRICES.

Our shareholder rights plan and certain provisions of Minnesota law may have the effect of discouraging attempts to acquire Stellent without the approval of our board of directors. Consequently, our shareholders may lose opportunities to sell their stock for a price in excess of the prevailing market price.

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NEW LEGISLATION AND POTENTIAL NEW ACCOUNTING PRONOUNCEMENTS ARE LIKELY TO IMPACT OUR FUTURE CONSOLIDATED FINANCIAL POSITION AND RESULTS OF OPERATIONS.

Recently, there have been significant regulatory changes, including the Sarbanes-Oxley Act of 2002, and there are new accounting pronouncements or regulatory rulings that will have an impact on our future consolidated financial position and results of operations. The Sarbanes-Oxley Act of 2002 and other rule changes and proposed legislative initiatives following several highly publicized corporate accounting and corporate governance failures are likely to increase general and administrative costs. Further, in December 2004, the Financial Accounting Standards Board issued a revision to Statement No. 123, *Share-Based Payment*, that will, with certain exceptions, require entities that grant stock options and shares to employees to recognize the fair value of those options and shares as compensation expense over the service (vesting) period in their financial statements. These and other potential changes could materially increase the expenses we report under accounting principles generally accepted in the United States of America and adversely affect our consolidated operating results. Additionally, the impact of these changes may increase costs incurred by our customers and prospects, which could result in delays or cancellations in spending on enterprise content management software and services like those that we provide. Such delays and cancellations could have a material adverse impact on our consolidated statement of operations and financial condition.

REALIZING THE BENEFITS FROM OUR ACQUISITION OF OPTIKA REQUIRES US TO OVERCOME INTEGRATION AND OTHER CHALLENGES WHICH MAY BE DIFFICULT BECAUSE OPTIKA IS ACCUSTOMED TO OPERATING AS AN AUTONOMOUS BUSINESS.

Any failure to meet the challenges involved in successfully integrating our preexisting operations with those of Optika or to realize any of the anticipated benefits or synergies of the acquisition could seriously harm our operating results. Realizing the benefits of the acquisition will depend in part on our ability to overcome significant challenges, including:

- combining Optika s Colorado-based operations with our Minnesota headquartered preexisting operations;
- integrating and managing the combined company with a small management team;
- retaining and assimilating the key personnel of Optika accustomed to working without the oversight of a parent company;
- integrating the sales organization of Optika, which historically relied extensively on indirect sales channels and generated a high proportion of maintenance and other revenues, with our preexisting sales organization, which relies extensively on direct sales and generates a high proportion of product license revenues;
- retaining preexisting customers of each company in light of changes that may occur as a result of the acquisition and attracting new customers while overcoming integration challenges;
- retaining strategic partners in light of changes that have occurred and may occur in each company s operations as a result of the acquisition and attracting new strategic partners while overcoming integration challenges; and
- creating and maintaining uniform standards, controls, procedures, policies and information for two companies accustomed to operating under autonomous management.

The risks of failure to overcome these integration challenges include:

- the potential disruption of our on-going business and distraction of our management;
- lost sales or decreased revenues as a result of difficulties inherent in combining product offerings, coordinating sales and marketing efforts to communicate effectively our capabilities;
- the potential need to demonstrate to customers that the acquisition will not result in adverse changes in customer service standards or business; and

impairment of relationships with employees, suppliers and customers as a result of any integration of new management personnel.

CHARGES TO EARNINGS RESULTING FROM THE APPLICATION OF THE PURCHASE METHOD OF ACCOUNTING MAY ADVERSELY AFFECT OUR MARKET VALUE.

In accordance with accounting principles generally accepted in the United States of America, we have accounted for the recent acquisitions using the purchase method of accounting, which will result in charges to earnings that could have a material adverse effect on the market value of our common stock. Under the purchase method of accounting, we allocated the total purchase price in an acquisition to the acquired company s net tangible assets, amortizable intangible assets and intangible assets with indefinite lives based on their fair values as of the date of the closing of the acquisition, and recorded the excess of the purchase price over those fair values as goodwill. We will incur additional depreciation and amortization expense over the useful lives of certain of the net tangible and intangible assets acquired in connection with acquisitions. In addition, to the extent the value of goodwill or intangible assets with indefinite lives becomes impaired, we may be required to incur material charges relating to the impairment of those assets. These depreciation, amortization and potential impairment charges could have a material impact on our results of operations.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Our interest income on cash, cash equivalents and marketable securities is affected by changes in interest rates in the United States. Changes in these rates have a significant effect on our interest income. Interest rates earned on invested funds have increased by approximately 3% since June 2004. We believe that there may be future exposure to interest rate market risk.

Our investments are held primarily in commercial paper which is affected by equity price market risk and other factors. We do not anticipate that exposure to these risks will have a material impact on us, due to the nature of our investments.

We have no history of, and do not anticipate in the future, investing in derivative financial instruments. Many transactions with international customers are entered into in U.S. dollars, precluding the need for foreign currency hedges. Any transactions that are currently entered into in foreign currency are not deemed material to the financial statements. Thus, the exposure to market risk is not material.

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, our management conducted an evaluation, under the supervision and with the participation of our chief executive officer and chief financial officer, of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934). Based on this evaluation, the officers concluded that our company s disclosure controls and procedures were effective to ensure that information required to be disclosed by our company in reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms.

(b) Changes in Internal Control Over Financial Reporting

Our management, with the participation of our chief executive officer and chief financial officer, performed an evaluation as to whether any change in the internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) occurred during the period covered by this report. Based on that evaluation, the chief executive officer and chief financial officer concluded that no change occurred in the internal control over financial reporting during the period covered by this report that materially affected or were reasonably likely to materially affect, the internal control over financial reporting.

Management, including our chief executive officer and chief financial officer, does not expect that our disclosure controls and procedures or internal control over financial reporting will prevent all errors or fraud. An internal control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all internal control systems, no evaluation of controls can provide absolute assurance that all control issues, errors and instances of fraud, if any, within our company have been detected.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In the normal course of business, we are subject to various claims and litigation, including employment matters and intellectual property claims. Management does not believe the outcome of any current legal matters will have a material adverse effect on our consolidated financial position, results of operations or cash flows.

The Company is a defendant, along with our certain current and former officers and directors of the Company, in a putative class action lawsuit entitled *In re Stellent Securities Litigation.* The lawsuit is a consolidation in Federal District Court for the District of Minnesota of several related lawsuits (the first of which was commenced on July 31, 2003). The plaintiff alleges that the defendants made false and misleading statements relating to the Company and its future financial prospects in violation of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934. In fiscal year 2005 a settlement was reached, subject to final documentation and preliminary and final court approval. No further expenses of any significance are anticipated with this lawsuit.

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

On June 20, 2005, we completed our purchase of certain assets of e-Onehundred Group, LLC. In accordance with the asset purchase agreement, we acquired these assets for consideration that included 273,560 shares of our unregistered common stock. The issuance of these securities was exempt from registration under the Securities Act of 1933 pursuant to Rule 506 promulgated under Regulation D.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

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

On August 10, 2005 the Company held its Annual Meeting of the Shareholders to consider a vote upon the following proposals. The tabulation of the votes, in favor, against, and abstaining with regard to the proposals is set forth below.

	PROPOSAL	AFFIRMATIVE VOTES	NEGATIVE VOTES	ABSTAIN VOTES	BROKER NON-VOTES
1.	Election of Directors:				
	Robert F. Olson	21,224,650	5,070,123		
	Philip E. Soran	22,079,114	4,215,659		
	Kenneth H. Holec	22,080,340	4,214,433		
	Raymond A. Tucker	22,054,809	4,239,964		
	Steven C. Waldron	21,790,773	4,504,000		
	Alan B. Menkes	22,080,031	4,214,742		
2.	To approve the Company s 2005 Equity Incentive Plan, which combines 878,855 shares currently available for awards pursuant to existing equity incentive plans with 2,321,145 additional shares, to provide a maximum of 3,200,000 shares available for equity incentives under this plan	12,365,340	6,980,976	124,386	6,824,071
3.	Ratification of the appointment of Grant Thornton LLP as independent auditors for the Company for fiscal year ended	24,314,771	293,734	1,686,268	

March 31, 2006.

ITEM 5. OTHER INFORMATION

Not applicable.

ITEM 6. EXHIBITS

FILE	DESCRIPTION	REFERENCE
3.1	Amended and Restated Articles of Incorporation	Incorporated by reference to Exhibit 3.1 of the Registrant s Form 8-K dated August 29, 2001
3.2	Bylaws	Incorporated by reference to Exhibit 4.2 of the Registrant s Registration Statement on Form S-8, File No. 333-75828
10.1	Form of Non-Statutory Stock Option Agreement Employee under the Stellent, Inc. 2005 Equity Incentive Plan	Incorporated by reference to the same numbered Exhibit to the Registrant s Form 8-K dated October 14, 2005
10.2	Form of Non-Statutory Stock Option Agreement Executive Employee under the Stellent, Inc. 2005 Equity Incentive Plan	Incorporated by reference to the same numbered Exhibit to the Registrant s Form 8-K dated October 14, 2005
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31.1	Certification by Robert F. Olson, Chairman of the Board, President and Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	Electronic Transmission
31.2	Certification by Gregg A. Waldon, Executive Vice President, Chief Financial Officer, Secretary and Treasurer, pursuant to Section 302 of	Electronic Transmission

	the Sarbanes-Oxley Act of 2002.	
32.1	Certification by Robert F. Olson, Chairman of the Board, President and Chief Executive Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.	Electronic Transmission
32.2	Certification by Gregg A. Waldon, Executive Vice President, Chief Financial Officer, Secretary and Treasurer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Electronic Transmission

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SIGNATURES

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

	STELLENT, INC. (Registrant)
Date: November 9, 2005	By: /s/ Robert F. Olson Robert F. Olson, Chairman of the Board, President and Chief Executive Officer (Principal Executive Officer)
Date: November 9, 2005	By: /s/ Gregg A. Waldon Gregg A. Waldon Executive Vice President, Chief Financial Officer, Secretary and Treasurer (Principal Financial and Accounting Officer)

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