

VERINT SYSTEMS INC
Form 10-K
April 18, 2005

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d)

of the Securities Exchange Act of 1934

for the Year ended January 31, 2005

Commission File Number 000-49790

VERINT SYSTEMS INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

11-3200514
(I.R.S. Employer
Identification No.)

330 South Service Road

Melville, New York 11747

(Address of principal executive offices)

Registrant's telephone number, including area code: 631-962-9600

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

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<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Not applicable	Not applicable

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

Common Stock, \$.001 par value per share

(Title of Class)

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

Yes: No:

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

x

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

Yes: x No: "

The aggregate market value of Common Stock held by non-affiliates of the registrant, based on the closing price for the Common Stock on the NASDAQ National Market on the last business day of the registrant's most recently completed fiscal second quarter (July 31, 2004) was approximately \$382,720,000.

There were 31,682,552 shares of the registrant's Common Stock outstanding on April 8, 2005.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement for the 2005 Annual Meeting of Stockholders are incorporated by reference into Part III of this Form 10-K Report, which Proxy Statement is to be filed within 120 days after the end of the registrant's fiscal year ended January 31, 2005.

Verint®, Powering Actionable Intelligence®, LORONIX®, Intelligent Recording®, OpenStorage Portal®, cctvware®, SmartSight®, vCRM® and Building the Customer Intelligent Enterprise® are registered trademarks, and Actionable Intelligence, NEXTIVA, RELIANT, STAR-GATE, ULTRA, VANTAGE, Universal Database, Verint Systems and Verint's logos are trademarks, of Verint Systems Inc.

FORWARD-LOOKING STATEMENTS

Certain statements discussed in Item 1 (Business), Item 3 (Legal Proceedings), Item 7 (Management's Discussion and Analysis of Financial Condition and Results of Operations), and elsewhere in this Form 10-K constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks, uncertainties and other important factors that could cause the actual results, performance or achievements of results to differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements. Important risks, uncertainties and other important factors that could cause actual results to differ materially include, among others: changes in the demand for Verint's products; lengthy and variable sales cycles create difficulty in forecasting the timing of revenue; aggressive competition in all of Verint's markets, which creates pricing pressure; dependence on government contracts; expected increase in Verint's effective tax rate; challenges in increasing gross margins; decline in information technology spending; introducing quality products on a timely basis that satisfy customer requirements and achieve market acceptance; risks associated with integrating the assets and business acquired from ECtel Ltd. (ECtel) and RP Sicherheissysteme GMBH (RP Security); risks that Verint's intellectual property rights may not be adequate to protect its business or that others may claim that Verint infringes upon their intellectual property rights; perception that Verint improperly handles sensitive or confidential information; inability to maintain relationships with value added resellers and systems integrators; difficulty of improving Verint's infrastructure in order to be able to continue to grow; risks associated with Verint's ability to retain existing personnel and recruit and retain qualified personnel in all geographies in which Verint operates; risks associated with changes in the competitive or regulatory environment in which Verint operates; risks associated with significant foreign operations, including fluctuations in foreign currency exchange rates; risks associated with Comverse Technology, Inc. controlling Verint's business and affairs; and other risks described in filings with the Securities and Exchange Commission. These risks and uncertainties, as well as other factors, are discussed in greater detail at the end of Item 7 (Management's Discussion and Analysis of Financial Condition and Results of Operations) of this Form 10-K. Verint makes no commitment to revise or update any forward-looking statements in order to reflect events or circumstances after the date any such statement is made.

ITEM 1. BUSINESS.

Overview

Verint Systems Inc. (including its subsidiaries, Verint or the Company) is a leading provider of analytic software-based solutions for the security and business intelligence markets. Verint's analytic solutions collect, retain and analyze voice, fax, video, email, Internet and data transmissions from voice, video and IP networks for the purpose of generating actionable intelligence for decision makers to take more effective action. Verint offers solutions for generating actionable intelligence for communications interception, networked video and contact centers.

Verint was incorporated in Delaware on February 23, 1994 as Interactive Information Systems Corporation. On January 30, 1996, the Company changed its name to Comverse Information Systems Corporation. Effective January 31, 1999, Comverse Infomedia Systems Corp. merged with and into Comverse Information Systems Corporation, and changed the name of the Company to Comverse Infosys, Inc. On February 1, 2002, the Company changed its name to Verint Systems Inc. Verint's initial public offering closed on May 16, 2002. Upon the initial public offering, Comverse Technology, Inc. (Comverse Technology) owned 79.5% of Verint's Common Stock. As of January 31, 2005, approximately 59% of Verint's common stock was owned by Comverse Technology. Verint's principal executive offices are located at 330 South Service Road, Melville, New York 11747 and its telephone number at that address is (631) 962-9600. Verint has over 1,000 customers in over 50 countries, and has operations in 15 countries.

The Company makes available through Verint's website at www.verint.com its Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, and will make available this Annual Report on Form 10-K and its Proxy Statement, as well as amendments to these and other reports filed or furnished by the Company pursuant to Section 13 (a) or Section 15 (d) of the Securities Exchange Act of 1934 free of charge, as soon as reasonably practicable after the Company files such materials with the Securities and Exchange Commission.

Industry Background: Actionable Intelligence Overview

Verint provides analytic software-based solutions to enable customers to generate actionable intelligence from voice, fax, video, email, Internet and data transmissions. The process of generating actionable intelligence is a result of the following five elements: collection, retention, analysis, decision and distribution.

Collection of raw multimedia information is achieved through an interface with wireline and wireless communications networks, business communications infrastructures, closed circuit television, or CCTV cameras, as well as cameras with direct connection to IP networks.

Retention consists of storage of the collected multimedia information. Collected information can be processed concurrently with its storage. Data can be stored on existing storage facilities including storage area networks (SANs).

Analysis of stored information is performed through various voice, video and data mining techniques, as well as correlation with structured data. These analytical tools convert raw multimedia information into organized, useful data.

Decision criteria are established by users to filter and prioritize processed data. By applying decision criteria, the processed data becomes actionable intelligence.

Distribution of actionable intelligence to the appropriate decision makers is the last component of the multimedia analytic solution. Through automatic alerts, the decision makers are notified of actionable intelligence in a timely manner.

The Security and Business Intelligence Markets

Overview

Verint's solutions for the security market consist primarily of communications interception solutions used by law enforcement agencies, government agencies and telecommunications carriers, and networked video solutions used by government agencies and public and private organizations for use in airports, public buildings, financial institutions, retail stores, correctional facilities and corporate sites.

Verint's solutions for the business intelligence market consist primarily of solutions for enterprises that rely on contact centers for voice, email and Internet interactions with their customers. Additionally, an emerging segment of business intelligence utilizes networked video information to allow enterprises and institutions to enhance their operations, processes and performance.

Communications Interception

Communications interception is the monitoring and recording of voice and data transmissions to and from a specified target over communications networks in order to obtain intelligence and gather evidence. Law enforcement agencies are typically granted the authority from national and regional government authorities to monitor, record, process and store intercepted transmissions to and from specified targets. In addition, certain government agencies worldwide require the ability to monitor and intercept communications for the purpose of ensuring security.

Telecommunications carriers in certain countries are mandated by government regulation to ensure that their telecommunications networks satisfy certain technical requirements for channeling intercepted communications to law enforcement and government authorities. For example, in the United States, standards have been established under the Communications Assistance for Law Enforcement Act, or CALEA, and in Europe, similar standards have been adopted by the European Telecommunications Standards Institute, or ETSI. The purpose of CALEA and ETSI standards is to ensure that telecommunications carriers are able to fulfill the technical requirements of channeling intercepted transmissions to law enforcement agencies. Telecommunications carriers seeking to comply with CALEA and ETSI standards and communications equipment vendors seeking to provide compliant products have driven the demand for CALEA and ETSI compliant solutions.

Verint provides governmental entities, law enforcement agencies and telecommunications carriers with turnkey solutions and subsystems for this security market that are intended to enable them to operate within the legal limits of information monitoring and collection as laws governing electronic surveillance vary significantly by country, and within many countries at the state or provincial levels.

Networked Video

Organizations are increasingly recognizing the need for surveillance of their facilities and operations to ensure the proper level of security. In addition, there is heightened awareness of the security needs of public facilities, including airports and government buildings, as well as other organizations and institutions. Networked video security solutions address some of these security needs by providing a proactive approach to surveillance and security.

Traditionally, video security consisted of connecting surveillance cameras to analog monitors and VCR recording equipment that archived video images on tape. Today, digital video technology offers many advantages over analog equipment while allowing for the continued use of the existing infrastructure of installed cameras. These advantages include more efficient storage of video for faster search and retrieval, either locally or remotely through wireless and wireline IP networks, and the capability to interface with other digital security systems, such as access control and security databases. Additionally, as video data is digitized and compressed, a variety of intelligent video analysis tools can be applied, including advanced motion detection technologies and analysis of the behavior of individuals and objects. The combination of digital recording and intelligent video analysis technologies provides users with a more effective integrated security and surveillance solution.

Networked video security systems are marketed primarily to government agencies and public and private organizations for use in airports, public buildings, financial institutions, retail stores, correctional facilities and corporate sites that require the capture, retention and analysis of video information for crime prevention and investigation, asset protection and other related purposes.

An emerging segment of business intelligence utilizes networked video information to allow enterprises and institutions to enhance their operations, processes and performance. Traditional video security and surveillance systems allow enterprises to view and record actions and behaviors associated with security-related or criminal activity; however, information on the actions, behaviors and interactions of personnel or customers of an enterprise is also valuable.

The existing infrastructure of closed circuit television cameras often already captures much of this valuable operational information, but utilizing information recorded by analog recording systems is impractical. The expansion of digital recording and the introduction of intelligent video analysis tools allow an enterprise to easily access and utilize this valuable operational information.

Implementing video business intelligence applications can offer valuable information and process improvements to businesses in many vertical markets. Some of the applications for video business intelligence include the counting, categorizing, point-of-sale reporting, monitoring and assessment of customer and personnel activities. For example, in the retail market, condensing and reviewing in-store activities, businesses can analyze and adjust staffing and product placement based on observed activities. Likewise, comparisons can also be made of similar activities among several stores. Utilizing these business intelligence applications can improve customer service, enhance customer and employee safety, increase product sales and improve the efficiency of business operations.

Contact Center Actionable Intelligence

Developing and maintaining long-term customer relationships is critical to the success of an enterprise operating in the competitive global marketplace. However, to understand and enhance customer relations, an enterprise must first improve its business processes that involve a high degree of direct customer interaction. Today, many organizations interact with their customers or clients primarily through contact centers. Increasingly, the contact center is the primary hub within an organization for inbound or outbound communications with customers. Contact centers generally consist of supervisor and agent workstations that are staffed with customer service representatives and are connected to a central telephone switch as well as database management systems that capture, store and report relevant customer information. The Company believes that solutions that automate and evaluate key sales, marketing and customer service processes, improve the effectiveness of customer interactions and aid in the retention of contact center agents will become increasingly important.

As customers continue to interact with customer service representatives through multiple communication channels including the Internet, the role and importance of recording and quality assurance for contact centers is increasing. Additionally, the rapid growth of the Internet and electronic commerce has also increased the importance companies place on their customer relationships, since the consumers can easily evaluate products and prices from a wide range of geographically dispersed vendors and quickly change vendors at a relatively low cost. Enterprises across industries are being driven to purchase quality assurance software primarily to improve customer care, as well as to comply with industry-specific regulations. In addition, due to the high cost of agent training and the high turnover of contact center agents, the retention of contact center agents has become a high priority for many enterprises.

Contact center actionable intelligence solutions target enterprises that rely on contact centers for voice, email and Internet interactions with their customers. Actionable intelligence generated from such interactions helps these enterprises to better service and retain customers, improve business processes and optimize contact center agent performance and retention.

Companies possessing a better understanding of the characteristics and preferences of their customers are better positioned to customize product and service offerings for increased sales and enhanced customer retention. In addition, these companies will also be able to better identify opportunities to sell complementary or higher-end products and to more accurately forecast customer demand.

Verint's Solutions: Overview

Verint's solutions generate actionable intelligence from the recording and analysis of voice, video and data transmissions for the security and business intelligence markets. Verint's products are utilized by government agencies, leading corporations, financial institutions and telecommunications service and equipment providers.

Verint's solutions provide its customers with the following key benefits:

Robust functionality with advanced features. Verint's solutions address the needs of its customers by providing a wide range of functions. In addition, the Company has developed a number of applications that enhance the functionality of its base product offerings. For example, Verint's communications interception products feature a cell-phone tracking program that can identify the location of a wireless caller.

End-to-end or component systems. Verint's products are designed to deliver complete solutions for collection, retention and analysis of voice, fax, video, email, Internet and data transmissions from voice, video and IP networks. Verint can also provide portions of its solutions for customers who do not require an end-to-end system.

Intuitive user interface. Verint's products utilize standard user interfaces, such as web-browser and email software, which allow customers to operate Verint's software in a familiar and easy to use framework.

Scalable networked solution with centralized control. Verint's solutions are network enabled, so that customers can access recorded information from any secure network connection. By allowing for centralized monitoring, the Company believes that its solutions enable customers to more efficiently manage their security and business information located at dispersed sites. Verint's products can also be scaled to support thousands of inputs, both locally and across a customer networked site.

Open, extendable platform. Verint's software runs on standard platforms and integrates with standard storage, compression and database technologies.

The Company's solutions integrate with communications switches and customer relationship management software, as applicable, from multiple vendors across both traditional and next-generation communications networks. In addition, the Company has developed application programming interfaces, which enable Verint's customers to easily incorporate their proprietary database information into its solutions.

Global support and service. The Company has global presence with systems installed in more than 50 countries around the world and a service infrastructure designed to quickly and efficiently meet customer needs.

Expertise in national and international standards and laws. Verint's products are designed to comply with intricate local, national and international standards regarding the lawful interception of communications.

Communications Interception Solutions

The following table summarizes Verint's communications interception solutions:

<u>Product Line</u>	<u>Market Served</u>	<u>Type of Customer</u>	<u>Purpose/Description</u>	<u>Location of Product</u>
STAR-GATE	Security	Communications service providers Internet service providers Switch manufacturers	Access, delivery and administrative functions of communications interception	Embedded in circuit or packet-based switch infrastructure
RELIANT and VANTAGE	Security	Law enforcement agencies Intelligence agencies	Collection, delivery, storage, and analysis of intercepted communications	Law enforcement or intelligence agency monitoring center

STAR-GATE

Verint's STAR-GATE product line enables communications service providers, Internet service providers, and communications equipment manufacturers to overcome the complexities posed by global digital communications and comply with governmental requirements. STAR-GATE enables communications service providers in receipt of proper legal authorization to intercept simultaneous communications over a variety of wireline, wireless and IP networks for delivery to law enforcement and other government agencies. STAR-GATE's flexibility supports multi-network, multi-vendor switch environments for a common interface across communications networks and supports switches from communications equipment manufacturers, such as Alcatel, Ericsson, Lucent, Nokia, Nortel and Siemens. STAR-GATE also supports interfaces to packet data networks, such as the Internet and Voice over Internet Protocol (VoIP), as well as general packet radio services.

Verint's STAR-GATE product line performs two primary functions:

Administration. STAR-GATE automates the implementation of proper legal authorization for communications interception. This process includes assigning surveillance targets, defining recipients of intercepted data and setting time and security parameters conforming with the court order.

Mediation. STAR-GATE routes the intercepted data from the communications switch, converts data into the required legal interception standard format, and delivers the intercepted communications to the appropriate law enforcement agency.

STAR-GATE is designed to be compliant with CALEA and ETSI standards for both circuit switched and IP networks.

RELIANT AND VANTAGE

Verint's RELIANT and VANTAGE product lines provide intelligent recording and analysis solutions for communications interception activities for law enforcement organizations and intelligence agencies.

The RELIANT and VANTAGE solutions are comprised of a system administration workstation, an operator workstation, and collection and storage databases and servers. RELIANT and VANTAGE each collect intercepted communications from multiple channels and store them for immediate access and further analysis. The system enables the review of intercepted voice, fax and data transmissions in their original forms through an easy to use interface and analytics to generate actionable intelligence from the large amounts of information that can be collected.

RELIANT is used by law enforcement agencies, ranging from local police agencies to national law enforcement agencies, because RELIANT is designed to comply with communications interception legal regulations and to generate evidence from intercepted communications that is admissible in a court of law. VANTAGE is designed for passive monitoring and is used by law enforcement and intelligence agencies to generate intelligence to detect and neutralize threats and strengthen national security.

Networked Video Solutions

The following table summarizes Verint's networked video solutions:

<u>Product Line</u>	<u>Market Served</u>	<u>Type of Customer</u>	<u>Purpose/Description</u>	<u>Location of Product</u>
Nextiva	Security	Government agencies	Intelligent recording and analysis of networked video to enhance enterprise security	Enterprise solution with video management and analytical components at the edge and core of customer's wide area networks
		Public agencies		
		Transportation agencies		
		Corporations		
	Business intelligence	Large retail organizations and enterprises	Analysis of networked video to improve business processes and performance	Enterprise solution with video management and analytical components at the edge and core of customer's wide area networks

Verint Networked Video Solutions enable government and commercial organizations to enhance the security of their facilities and infrastructure and improve the performance of their operations by networking video across multiple locations and applying advanced content analytics to extract actionable intelligence from live and stored video. By alerting security personnel to potential security threats, Verint Networked Video Solutions are designed to help organizations prevent security breaches, improve response time and enhance operational efficiency.

In addition, Verint Networked Video Solutions enable enterprise customers to monitor and improve their operations through the analysis of live and recorded digital video. Verint's networked business intelligence video solution also contains software focused on maximizing operational effectiveness through video analysis.

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The Company's Networked Video Solutions are now offered as Nextiva, the newest release of the Company's Networked Video Solutions. Nextiva is an integrated platform and suite of software applications built on a standards-based, open architecture for scalability, rapid deployment, and ease of use in IP network environments. Nextiva captures video, audio and data from a wide variety of devices transmitted over wireline and wireless networks. Nextiva's rules-based engine and analytics are designed to enable effective follow-up action by rapidly distributing video, data, alarms and events to the appropriate security and operational personnel.

The Nextiva solution includes five integrated software applications:

Nextiva IntelliFlow is a rules-based engine with analytics that provides automatic event notification, video distribution, and process activation in response to events and behaviors.

Nextiva IntelliStream automatically distributes live and recorded video to video walls, PDA and computers across dispersed user locations in a bandwidth efficient manner.

Nextiva Review enables flexible live and recorded video viewing from a thick client or Web browser interface, with priority icons that make alarms and associated video accessible with a single click.

Nextiva Case Management turns on demand video and audio into a searchable database to facilitate effective case management, enabling information to be securely shared among authorized personnel.

Nextiva HealthCheck provides automated health monitoring and diagnostics to enable a proactive maintenance approach for maximum system availability and reduced service costs.

The Company's Nextiva offering can be provided as a complete end-to-end solution, or can be provided as subsystems and components depending on the customer's requirements.

Contact Center Actionable Intelligence Solutions

The following table summarizes Verint's contact center business intelligence solutions:

<u>Product Line</u>	<u>Market Served</u>	<u>Type of Customer</u>	<u>Purpose/Description</u>	<u>Location of Product</u>
ULTRA	Business Intelligence	Internal contact centers of large organizations and enterprises, including utilities and financial institutions	Recording and analysis of customer interactions with contact centers agents	Collects and analyzes data from contact centers and delivers actionable intelligence to decision makers throughout an enterprise
		Outsourced contact centers		

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ULTRA records and analyzes customer interactions to provide enterprises with business intelligence about their customers and help monitor and improve the performance of their contact centers. ULTRA's intelligent recording platform uses an innovative architecture that leverages voice and data processing technologies to offer customers multiple methods of recording contact center interactions while providing a flexible framework for expansions and changes in technologies.

ULTRA and its Analytics suite drives total quality by enabling organizations of all sizes to cost effectively capture all customer interactions and extract actionable intelligence from telephone, VoIP, email, chat or agent assisted co-browsing contacts. Easy access to all customer data through ULTRA's web-based desktop portal enables enterprises to use what they learn from customer contacts to optimize their processes, increase productivity, comply with risk management requirements and improve service to their customers.

ULTRA offers two sophisticated analytical tools, IntelliMiner and IntelliFind, which transform customer interactions into actionable intelligence. These advanced analytical solutions power true enterprise quality by enabling decision makers to extract intelligence from large amounts of data collected from the universe of customer contacts and use it to optimize performance and enhance profitability.

Sales and Marketing

The Company sells its products primarily through a combination of its direct sales force and channels, including agents, distributors, value added resellers and systems integrators. As of January 31, 2005, the Company had several sales offices in the United States and offices in Australia, Canada, France, Germany, Hong Kong, India, Israel, Japan, the Netherlands, Singapore and the United Kingdom. Verint's direct sales force consists of account executives, solutions consultants, and regional sales directors who possess industry-specific experience.

Verint's sales force pursues potential sales leads identified internally or provided by channels. The Company develops strategic marketing alliances with leading companies in its industry to expand the coverage and support of its direct sales force. Nearly 50% of the Company's sales are made directly. Verint's business development personnel are responsible for the initiation, negotiation and completion of these marketing alliances.

Verint's direct sales cycle typically begins with its initiation of a sales lead or the receipt of a request for information from a prospective customer. The sales lead, or request for information, is followed by an assessment of the customer's requirements, a formal proposal, presentations and product demonstrations, site visits to an existing customer that utilizes Verint's products and contract negotiation and signing. The sales cycle can vary substantially from customer to customer but typically lasts six months to one year.

The Company uses a variety of marketing programs to build brand name awareness, as well as to attract potential customers. These programs include market research, product and strategy updates with industry analysts, direct marketing programs to current and prospective customers, advertising, participation in industry trade shows, conferences, seminars, and a public relations program that includes demonstrations of Verint's products. To support sales efforts, the Company also produces promotional materials that include brochures, video presentations, data sheets and other technical descriptions.

Customers

Verint's products are currently used by over 1,000 organizations and are deployed in over 50 countries, across many industries and markets. Many users of Verint's products are large corporations or government agencies that operate from multiple locations and facilities across large geographic areas and sometimes across several countries.

These organizations typically implement Verint's solutions in stages, with implementation in one or more sites and then gradually expanding to a full enterprise, networked-based solution. None of Verint's customers, including systems integrators and value added resellers, individually accounted for more than 10% of its revenues in the year ended January 31, 2005 (fiscal 2004). In fiscal 2004, Verint derived approximately 55%, 33% and 12% of its revenues from sales to end users in the Americas, Europe and the Middle East (EMEA) and the Asia Pacific Region (APAC), respectively.

The Company derived approximately 35%, 29% and 22% of its revenues in the years ended January 31, 2003, 2004 and 2005 (fiscal 2002, 2003 and 2004), respectively, from contracts with various local, regional and national governments (including transportation authorities) worldwide, either directly or through channels. Previously, the Company did not include revenue generated from transportation authorities in the calculation of government revenue. However, since transportation authorities are government agencies (though, sometimes self-funded, as in the case of certain port authorities), the Company has determined it is appropriate to include revenues generated from these transportation authorities in its government revenue information. These percentages exclude sales to certain entities buying the Company's products as a result of specific government mandates, such as telecommunications service providers complying with communications interception requirements. Verint's business generated from such government contracts may be adversely affected for various reasons including if levels of government expenditures and authorizations for law enforcement and security related programs decrease, remain constant or shift to programs in areas where it does not provide products and services or if changes in government procurement procedures preclude the Company from participating in such government procurement processes. See Certain Trends and Uncertainties.

Verint's customers include Charter One Bank, CIBC, The Home Depot, HSBC, Internal Revenue Service, London Underground, SBC, Target, the U.S. Capitol and U.S. Department of Defense. These are examples of the Company's customers, though not necessarily representative, because the Company is often restricted from disclosing the names of its customers for security reasons, particularly its communications interception customers.

Research and Development

The Company continues to enhance the features and performance of its existing products and introduce new solutions by extensive research and development activities primarily in its facilities in North America and in Israel. As of January 31, 2005, the Company had approximately 430 employees engaged in its research and development activities, of which approximately 24% were located in North America and 70% were located in Israel, with the balance in other of Verint's locations. The Company believes that its future success depends on a number of factors, which include its ability to:

identify and respond to emerging technological trends in its target markets;

develop and maintain competitive solutions that meet its customers' changing needs; and

enhance its existing products by adding features and functionality to meet specific customer's needs, or that differentiate its products from those of its competitors.

As a result, the Company has made significant investments in research and development. The Company allocates its research and development resources in response to market research and customer demands for additional features and solutions. Verint's development strategy involves rolling out initial releases of its products and adding features over time. The Company incorporates product feedback it receives from its customers into its product development process. While the Company expects that new products will continue to be developed internally, it may, based on timing and cost considerations, acquire or license technologies, products or applications from third parties.

Verint's research and development that occurs in Israel and Canada benefits from local governmental investment programs. The Government of Israel, through the Office of the Chief Scientist of the Ministry of Industry and Trade (OCS), encourages research and development projects which result in products for export. Verint's gross research and development expenses were approximately \$22.6 million for fiscal 2002, \$27.2 million for fiscal 2003 and \$36.0 million for fiscal 2004. In fiscal 2002, 2003 and 2004, the Company received from the Office of the Chief Scientist conditional grants totaling approximately \$5.2 million, \$3.8 million and \$3.2 million, respectively, representing 23.1%, 13.8% and 8.8% of its total research and development expenditures in these periods. As of January 31, 2005, the Company has received approximately \$55.9 million in cumulative grants and has recorded approximately \$26.5 million in cumulative royalties to the OCS. The terms of these conditional grants limit the Company's ability to manufacture products, or transfer technologies, outside of Israel if such products or technologies were developed using these grants. The Company also benefits from the Scientific Research and Experimental Development (SR&ED) program in Canada. The Company recorded approximately \$0.2 million as reimbursement of research and development expenses from the SR&ED for each of the years ended January 31, 2004 and 2005. In addition, in fiscal 2004, the Company recorded other reimbursement of R&D expenses amounting to approximately \$0.7 million.

Manufacturing and Suppliers

Verint's manufacturing and assembly operations, which are performed in its U.S., Israeli, Canadian and German facilities, consist primarily of installing its software on externally purchased hardware components and final assembly and testing, which involves the application of extensive quality control procedures to materials, components, subassemblies and systems. The Company relies on several unaffiliated subcontractors for the supply of specific proprietary components and assemblies that are incorporated in its products. Although the Company has experienced delays and shortages in the supply of proprietary components on occasion in the past, to date, it has been able to obtain adequate supplies of all components in a timely manner, when necessary, from alternative sources. See *Certain Trends and Uncertainties*.

The Company maintains organization-wide quality assurance procedures, coordinating the quality control activities of its research and development, manufacturing and service departments.

Intellectual Property Rights

The Company has accumulated a significant amount of proprietary know-how and expertise in developing analytic solutions for its security and surveillance and business intelligence products. The Company regularly reviews new areas of technology to determine whether they are patentable.

The Company licenses certain software, technology and related rights for use in the manufacture and marketing of its products, and pays royalties to third parties under such licenses and other agreements. The Company believes that its rights under such licenses and other agreements are sufficient for the manufacturing and marketing of its products and, in the case of licenses, extend for periods at least equal to the estimated useful lives of the related technology and know-how.

In January 2000, Comverse Technology and Lucent, acting through subsidiary patent holding companies on behalf of themselves and their various subsidiaries and affiliates, entered into a non-exclusive cross-licensing arrangement covering current and certain future patents issued to Comverse Technology and its affiliates and a portfolio of current and certain future patents in the area of communications technology issued to Lucent and its affiliates. Under that arrangement, and pursuant to a patent license agreement between Verint and Comverse Technology, Lucent is entitled to non-exclusive royalty-free licenses under any patents granted to Verint or which it obtains the right to license during the term of the agreement, while Verint is entitled to a non-exclusive royalty-free sublicense to all patents that are licensed by Lucent to Comverse Technology.

Competition

The Company faces strong competition in the markets for its products, both in the United States and internationally. The Company expects competition to persist and intensify in the actionable intelligence market, primarily due to increased awareness of the value of actionable intelligence solutions. Verint's primary competitors are suppliers of security and recording systems and software, and indirect competitors that supply certain components to systems integrators. In the business intelligence market, the Company faces competition from organizations emerging from the traditional call logging or video recording markets as well as software companies that develop and sell products that perform specific functions for these markets. Additionally, many of Verint's competitors specialize in a subset of its portfolio of products and services. Primary competitors include, among others, Bosch, etalk, ETI, General Electric, Honeywell, JSI Telecom, March Networks, NICE Systems, Pelco, Raytheon, Siemens, SS8 Networks, Tyco, and Witness Systems. The Company believes it competes principally on the basis of:

product performance and functionality;

knowledge and experience in Verint's industry;

product quality and reliability;

customer service and support; and

price.

The Company believes that its success depends primarily on its ability to provide technologically advanced and cost effective solutions. Verint's competitors that manufacture other security-related systems or other recording systems may derive a competitive advantage in selling to customers that are purchasing or have previously purchased other compatible equipment from such manufacturers. The Company expects that competition will increase as other established and emerging companies enter its market, and as new products, services and technologies are introduced.

Employees

As of January 31, 2005, the Company had approximately 1,200 employees. A majority of its employees are scientists, engineers or technicians engaged in research and development, sales and marketing, and operations. The Company considers its relationship with its employees to be good. Verint's employees in the United States are not covered by any collective bargaining agreement. Verint's employees outside the United States are entitled to severance and other benefits mandated under local laws. Approximately 41%, 40%, 16% and 3% of the Company's employees are located in North America, Israel, Europe and APAC, respectively.

Israeli law generally requires the payment by employers of severance pay upon the death of an employee, retirement or upon termination of employment, and the Company provides for such payment obligations through monthly contributions to an insurance fund. Additionally, Israeli employees and employers are required to pay pre-determined sums to the National Insurance Institute, which covers medical and other benefits similar to the benefits provided by the United States Social Security Administration.

Proxy Agreement with the Department of Defense

One of Verint's subsidiaries, Verint Technology Inc. (Verint Technology), is engaged in the development, marketing and sale of Verint's communications interception solutions to various U.S. government agencies and telecommunications carriers. In order to conduct its business, Verint Technology is required to maintain facility security clearances under the National Industrial Security Program, or the NISP. The NISP requires companies maintaining facility security clearances to be insulated from foreign ownership, control or influence. In January 1999, the Company, Comverse Technology and the Department of Defense entered into a proxy agreement with respect to the ownership and operations of Verint Technology, which agreement was superseded in May 2001 to comply with the Department of Defense's most recent requirements. The proxy agreement has been approved by the Defense Security Service, which has oversight responsibilities on behalf of the Department of Defense.

Under the proxy agreement, the Company appointed three U.S. citizens that have the requisite personal security clearance as directors of Verint Technology and as holders of proxies to vote the stock of Verint Technology.

These individuals are responsible for the oversight of Verint Technology's security arrangements, including the separation of Verint Technology from the Company and its affiliates. As proxy holders, these individuals have the power to exercise all prerogatives of ownership of Verint Technology, except that without obtaining Verint's express written approval they may not authorize any individual sale or disposal of capital assets constituting a material amount of Verint Technology's assets, the mortgaging of assets other than for working capital or capital improvement purposes, any merger, consolidation, reorganization or dissolution of Verint Technology and the filing of a petition under the federal bankruptcy laws.

Under the proxy agreement, Verint Technology has also established a government security committee, which consists of the three proxy holders, each of whom has personal security clearances. As the government security committee, the three proxy holders oversee that Verint Technology maintains appropriate policies and procedures to safeguard classified information and sensitive but unclassified information, and that Verint Technology complies with the proxy agreement, as well as applicable laws and regulations. The government security committee is also in charge of the development and implementation of a technology control plan, which prescribes measures and establishes procedures to prevent unauthorized disclosure or export of controlled information by Verint Technology to the Company, any of its affiliates or others. In addition, the proxy agreement establishes procedures regarding meetings, visits and communications between Verint Technology, the Company and its other affiliates.

The Department of Defense receives an annual report from the proxy holders and periodically inspects Verint Technology's operations and facilities to assess their compliance with the NISP and the proxy agreement.

Export Regulations

The Company is subject to export restrictions in Israel with respect to certain components of its RELIANT and VANTAGE products which are developed and manufactured in Israel. In order to export certain components of its RELIANT and VANTAGE products from Israel, the Company is required to obtain export licenses from the Israeli Ministry of Defense prior to marketing these products in foreign countries. The Company is also required to obtain an additional license prior to the completion of each sale. To date, the Company has been successful in obtaining necessary permits.

The Company is also subject to export restrictions in Germany with respect to components of its RELIANT products which are developed and manufactured in Germany. To date, the Company has been able to rely on the terms of a general export license in Germany to export these components to countries outside the European Union. Under the terms of this license, the Company is also required to report to German authorities each shipment of these components outside of the European Union.

The Company may also be subject to U.S. export restrictions with respect to its communications interception solutions.

ITEM 2. PROPERTIES.

The Company leases approximately 78,000 square feet of office space in the United States.

This includes approximately 32,000 square feet in Melville, New York, where the Company's headquarters and some of its support and sales facilities are located. The lease for Verint's Melville, New York facilities expires in June 2013. The Company leases additional office space for its facilities in Chantilly, Virginia; Denver, Colorado and Columbia, Maryland. The Company leases approximately 85,000 square feet of office and storage space for manufacturing, development, support and sales facilities in Tel Aviv, Israel. This lease expires in December 2005. On August 20, 2004, the Company entered into a lease agreement for the lease of approximately 125,000 square feet of office and storage space for manufacturing, development, support and sales facilities in Herzelia, Israel. Under the lease agreement, occupancy of the new building and rent payments are expected to commence in October 2005 for a period of ten years. Annual rent payments are expected to be approximately \$2.3 million with annual adjustments linked to the U.S. Consumer Price Index, as well as automatic increases of 1.5% per year beginning in the third year of the lease term. The new lease agreement will replace the lease agreement for the Company's existing building in Israel.

Additionally, the Company leases approximately 13,000 square feet of office space for sales, installation and support in the United Kingdom, approximately 11,000 square feet of office space for manufacturing, development, support and sales in Flensburg, Germany, and approximately 22,000 square feet of office space for manufacturing, development support and sales in Laval, Canada. The Company also leases small office facilities in Germany, France, Denmark, India and the Netherlands.

The Company owns approximately 25 acres of land, including 40,000 square feet of office space for the development, manufacturing, support and sales of its Verint Video Solutions product lines in Durango, Colorado. The Company also owns approximately 29,000 square feet of office and storage space for sales, manufacturing, support and development in Bexbach, Germany.

The Company believes that its owned and leased facilities are adequate for its current operations, and that additional facilities can be acquired or developed to provide for expansion of its operations in the foreseeable future.

ITEM 3. LEGAL PROCEEDINGS.

From time to time, the Company is subject to claims in legal proceedings arising in the normal course of its business. The Company does not believe that it is currently a party to any pending legal action that could reasonably be expected to have a material adverse effect on its business, financial condition and results of operations.

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

Not applicable.

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

The Common Stock of Verint trades on the NASDAQ National Market under the symbol VRNT. The following table sets forth the range of closing prices of the Common Stock as reported on NASDAQ for the past two fiscal years:

Year	Fiscal Quarter	Low	High
2003	2/1/03 - 4/30/03	\$ 14.39	\$ 20.95
	5/1/03 - 7/31/03	\$ 19.00	\$ 26.25
	8/1/03 - 10/31/03	\$ 19.14	\$ 26.49
	11/1/03 - 1/31/04	\$ 20.66	\$ 25.30
2004	2/1/04 - 4/30/04	\$ 24.60	\$ 33.49
	5/1/04 - 7/31/04	\$ 26.74	\$ 34.74
	8/1/04 - 10/31/04	\$ 28.60	\$ 39.00
	11/1/04 - 1/31/05	\$ 34.28	\$ 42.01

There were 86 holders of record of Common Stock at April 8, 2005. Such record holders include a number of holders who are nominees for an undetermined number of beneficial owners. The Company believes that the number of beneficial owners of the shares of Common Stock outstanding at such date was approximately 8,800.

The Company has not declared or paid any cash dividends on its equity securities and does not expect to pay any cash dividends in the foreseeable future, but rather intends to retain its earnings to finance the development of its business. Any future determination as to the declaration and payment of dividends will be made by the Board of Directors in its discretion, and will depend upon the Company's earnings, financial condition, capital requirements and other relevant factors. See "Certain Trends and Uncertainties" regarding Comverse Technology's control of the Board of Directors.

ITEM 6. SELECTED FINANCIAL DATA.

The following table presents selected consolidated financial data for the Company for the years ended January 31, 2001, 2002, 2003, 2004 and 2005. Such information has been derived from the Company's audited consolidated financial statements and should be read in conjunction with the Company's consolidated financial statements and related notes and the section of this Form 10-K entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations."

	Years Ended January 31,				
	2001	2002	2003	2004	2005
	(in thousands, except per share data)				
Statement of Operations Data:					
Sales	\$ 141,677	\$ 131,235	\$ 157,775	\$ 192,744	\$ 249,824
Cost of sales	81,793	69,907	78,053	89,302	112,774
Gross profit	59,884	61,328	79,722	103,442	137,050
Research and development, net	14,249	15,184	17,357	23,233	31,961
Selling, general and administrative	48,162	45,923	52,314	63,020	83,070
Acquisition related expenses	3,510				1,481
In-process research and development					3,154
Workforce reduction, restructuring and impairment charges	1,528	2,754			
Income (loss) from operations	(7,565)	(2,533)	10,051	17,189	17,384
Interest and other income (expense), net	(497)	(564)	2,266	2,670	3,618
Income (loss) before income taxes	(8,062)	(3,097)	12,317	19,859	21,002
Income tax provision	497	1,552	2,170	1,921	1,930
Net income (loss)	\$ (8,559)	\$ (4,649)	\$ 10,147	\$ 17,938	\$ 19,072
Net income (loss) per share - basic	\$ (0.46)	\$ (0.25)	\$ 0.46	\$ 0.65	\$ 0.62
Net income (loss) per share - diluted	\$ (0.46)	\$ (0.25)	\$ 0.43	\$ 0.61	\$ 0.58
Weighted average shares:					
Basic	18,704	18,767	22,165	27,690	30,894
Diluted	18,704	18,767	23,542	29,437	32,626
	As of January 31,				
	2001	2002	2003	2004	2005
Balance Sheet Data:					
Cash and cash equivalents	\$ 43,330	\$ 49,860	\$ 73,583	\$ 77,516	\$ 45,100
Short-term investments			60,350	151,197	195,314
Working capital	3,512	41,160	69,323	204,564	196,381
Total assets	117,554	116,726	207,050	328,706	398,978
Convertible note			2,200	2,200	
Long-term bank loans, including current maturities	2,806	43,623	43,877	2,330	2,475
Stockholders' equity	22,525	18,735	96,166	244,668	283,375

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following discussion of Verint's financial condition and results of operations should be read in conjunction with its consolidated financial statements and the related notes thereto which appear elsewhere in this document.

Overview

Verint operates in one business segment providing actionable intelligence solutions. The Company provides analytic software-based actionable intelligence solutions to the security and business intelligence markets. Verint's solutions collect, retain, and analyze voice, fax, video, email, Internet and data transmissions from voice, video and IP networks for the purposes of generating actionable intelligence for decision makers to take more effective action. The Company's initial public offering closed on May 16, 2002.

For the security market, Verint offers its communications interception solutions STAR-GATE, RELIANT and VANTAGE, as well as the Company's suite of networked video security solutions, NEXTIVA. STAR-GATE enables communications service providers in receipt of proper legal authorization to intercept simultaneous communications over a variety of wireline, wireless and IP networks, for delivery to law enforcement and other government agencies, and is sold to communications service providers, Internet service providers and communications equipment manufacturers. RELIANT provides intelligent recording and analysis solutions for communications interception activities and is sold to law enforcement organizations and intelligence agencies. RELIANT equips agencies with an end-to-end solution for live monitoring of intercepted target communications and evidence collection management, regardless of the type of communication or network used. VANTAGE enables government agencies such as national security and intelligence agencies to intercept and analyze large amounts of voice and data communications based on a broad range of filtering criteria. Verint's NEXTIVA networked video security solutions provide recording and analysis of video for security and surveillance applications to government agencies, public organizations and corporations. These solutions can provide live video streaming and camera control over local and wide area computer networks for use in airports, public buildings, financial institutions, retail stores, correctional facilities and corporate sites.

For the business intelligence market, Verint offers ULTRA as its contact center actionable intelligence solution, as well as its networked video business intelligence solutions. Verint's ULTRA products are sold to contact centers within a variety of enterprises, including financial institutions, communications service providers and utilities. These solutions record customer interactions with contact centers to provide enterprises with business intelligence about their customers and help monitor and improve the performance of their contact centers. Verint's NEXTIVA networked video business intelligence solutions enable enterprises to monitor and improve their operations through the analysis of live and recorded digital video. These solutions are sold primarily to commercial enterprises such as retail chains.

In fiscal 2004 and 2003, sales of the Company's security solutions contributed approximately two thirds of its revenue, with the remaining one third contributed by sales of its business intelligence solutions. Revenues generated by sales of the Company's security solutions increased approximately 35% in fiscal 2004 as compared to fiscal 2003 and approximately 31% in fiscal 2003 as compared to fiscal 2002. Revenues generated by sales of the Company's business intelligence solutions increased approximately 26% in fiscal 2004 as compared to fiscal 2003 and increased approximately 8% in fiscal 2003 as compared to fiscal 2002. The Company's actionable intelligence solutions are sometimes sold to customers who apply them for both security and business intelligence.

In these instances the Company uses its judgment to determine the portion of those revenues that should be allocated as sales in the security or business intelligence markets based on its understanding of the customer's intended use of its solutions.

In addition, the Company derived approximately 35%, 29% and 22% of its revenues in fiscal 2002, 2003 and 2004, respectively, from contracts with various local, regional and national governments (including transportation authorities) worldwide, either directly or through channels. Previously, the Company did not include revenue generated from transportation authorities in the calculation of government revenue. However, since transportation authorities are government agencies (though, sometimes self-funded, as in the case of certain port authorities), the Company has determined it is appropriate to include revenues generated from these transportation authorities in its government revenue information. These percentages related to government sales exclude sales to certain entities buying the Company's products as a result of specific government mandates, such as telecommunications service providers complying with communications interception requirements.

In fiscal years 2004 and 2003, approximately 49% of revenue was derived from direct sales by the Company. In fiscal year 2004, Verint derived approximately 55%, 33% and 12% of its revenues from sales to end users in the Americas, EMEA and APAC, respectively, compared with approximately 55%, 32% and 13% for fiscal year 2003. Further, in fiscal year 2004, approximately 79% of the Company's revenues were derived from sales of products, while the remaining 21% were derived from service and maintenance, as compared to approximately 80% and 20% in fiscal year 2003.

The Company believes that there are many elements to its strategy, including:

- Understanding customer requirements and anticipating customer needs as a basis to improve its existing technology and to introduce new analytic capabilities in its software solutions

- Utilizing and enhancing strategic alliances, such as with systems integrators and software resellers, to enhance its products and increase its customer base

- Using its existing technologies in new markets and new applications

- Pursuing strategic acquisitions to extend the analytic capabilities of its solutions, expand its geographic presence or expand its customer base

The Company believes that many factors affect its continued ability to maintain and to increase revenues and profitability, including:

- Recognition of the value of actionable intelligence solutions by customers in the security and business intelligence markets, and demand for those solutions

Verint's ability to continue to introduce new, high-quality products and technologies in a timely and cost-effective manner

Continued aggressive competition in the security and business intelligence markets could cause the Company to have to reduce the prices of its products and services to remain competitive

Continuing to increase software in its offerings to customers in order to increase gross margins

The Company's continued ability to sell its solutions to governments and large customers, and expand its relationships with system integrators and resellers

Take steps to mitigate the effect of having significantly utilized its net operating loss carry forwards in the U.S., which is expected to significantly increase the Company's effective tax rate

Improve its infrastructure, and continue to attract and retain qualified personnel

Other factors discussed in Certain Trends and Uncertainties

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make certain 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. The following accounting policies involve a critical accounting estimate because they are particularly dependent on estimates and assumptions made by management about matters that are highly uncertain at the time the accounting estimates are made, and often require the exercise of substantial judgment based on historical experience and other factors. In addition, while the Company has used its best estimates based on facts and circumstances available to it at the time, different estimates reasonably could have been used in the current period, and changes in the accounting estimates used by the Company are reasonably likely to occur from period to period, which may have a material impact on the presentation of Verint's financial condition and results of operations. The Company reviews these estimates and assumptions periodically and reflects the effects of revisions, if any, in the period that they are determined to be necessary. Actual results could differ from those estimates. The Company has reviewed its critical accounting policies and their application in the preparation of its financial statements and related disclosures with its Audit Committee.

Revenue Recognition. Revenue is generally recognized at the time of shipment for sales of systems which do not require significant customization and collection of the resulting receivable is deemed probable by the Company.

The Company's systems are generally bundled hardware and software that is shipped together. Amounts received from customers pursuant to the terms specified in contracts but for which revenue has not been recognized are recorded as advance payments from customers. The Company generally has no obligations to customers after the date products are shipped, except for product warranties. The Company generally warrants its products for one year after sale. A provision for estimated warranty costs is recorded at the time of sale.

Customers may also purchase separate maintenance contracts, which generally consist of bug-fixing and telephone access to Company technical personnel, but in certain circumstances may also include the right to receive certain product updates, upgrades and enhancements. Revenue from these maintenance contracts is recognized ratably over the contract period. Customers may also place a single order to purchase both the Company's products, as well as maintenance contracts for these products. In such instances, the Company uses vendor-specific objective evidence to determine the fair value of the maintenance portion of the purchase, which is recognized ratably over the maintenance period. Amounts received from customers in excess of revenues earned under maintenance contracts are recorded as advance payments from customers.

Revenue from certain long-term contracts is recognized under the percentage-of-completion method on the basis of physical completion or using actual costs incurred relative to total expected costs under the contract. Revisions in estimates of costs and profits are reflected in the accounting period in which the facts that require the revision become known. At the time a loss on a contract is known, the entire amount of the estimated loss is accrued. Amounts received from customers in excess of revenues earned under the percentage-of-completion method are recorded as advance payments from customers. Related contract costs include all direct material and labor costs and those indirect costs related to contract performance, and are included in cost of sales in the Consolidated Statements of Operations.

Expense Recognition. Verint's cost of sales includes costs of materials, subcontractor costs, royalties and license fees, salary and related benefits for the operations and service departments, depreciation and amortization of equipment used in the operations and service departments, amortization of capitalized software development costs, travel costs, and an overhead allocation. Research and development costs include salary and related benefits, subcontracting costs, travel, depreciation and amortization of research and development equipment, an overhead allocation, and other costs associated with research and development activities, and is stated net of amounts reimbursed primarily by government programs. Selling, general and administrative costs include salary and related benefits, travel, depreciation and amortization, sales commissions, marketing and promotional materials, recruiting expenses, professional fees, facility costs, and other costs associated with sales, marketing, finance, human resources and administrative departments.

Software Development Costs. Software development costs are capitalized upon the establishment of technological feasibility and are amortized on a straight-line basis over the estimated useful life of the software, which is generally four years or less. Amortization begins in the period in which the related product is available for general release to customers.

The Company reviews capitalized software development costs for impairment at the end of each fiscal year, or whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss would be recognized when the estimated net realizable value of the software is less than its carrying amount. The net realizable value is the estimated future gross revenue from the software reduced by the estimated future costs of completing and supporting the software.

Results of Operations

The following table sets forth, for the periods indicated, certain financial data expressed as a percentage of sales:

	Years Ended January 31,		
	2003	2004	2005
Sales:			
Product revenues	82.6%	79.5%	79.0%
Service revenues	17.4	20.5	21.0
Total sales	100.0	100.0	100.0
Cost of sales:			
Product costs	35.8	32.7	31.3
Service costs	13.7	13.6	13.8
Total cost of sales	49.5	46.3	45.1
Gross profit	50.5	53.7	54.9
Research and development, net	11.0	12.1	12.8
Selling, general and administrative	33.1	32.7	33.3
In-process research and development			1.3
Acquisition related write-downs			0.6
Income from operations	6.4	8.9	7.0
Interest and other income, net	1.4	1.4	1.4
Income before income taxes	7.8	10.3	8.4
Income tax provision	1.4	1.0	0.8
Net income	6.4%	9.3%	7.6%

Year Ended January 31, 2005 Compared to Year Ended January 31, 2004

Sales. Sales for the year ended January 31, 2005, or fiscal 2004, increased by approximately \$57.1 million, or 30%, compared to the year ended January 31, 2004, or fiscal 2003. This increase reflected an increase in both sales of products of approximately \$44.0 million and service revenue of approximately \$13.0 million. This increase was principally due to an increase in sales volume in the Americas of approximately \$33.1 million, and in EMEA of approximately \$19.8 million.

The Company sells its products in multiple configurations and the price of any particular product varies depending on the configuration of the product sold. Due to the variety of customized configurations for each product that the Company sells, it is unable to quantify the effects of a change in the price of any particular product and/or a change in the number of products sold on its revenues. Sales to international customers represented approximately 49% of sales for fiscal 2004 as compared to approximately 48% of sales for fiscal 2003.

Cost of Sales. Cost of sales consists primarily of material and overhead costs, operations and service personnel costs, amortization of capitalized software and royalties. Cost of sales for fiscal 2004 increased by approximately \$23.5 million, or 26%, compared to fiscal 2003. This increase was attributable to an increase in materials and overhead costs of approximately \$14.6 million, an increase in personnel related costs of approximately \$4.9 million, mainly due to increased service headcount and increased personnel compensation, and an increase in other service and operation costs of approximately \$4.0 million, mainly due to increased royalties, amortization and travel expenses. Gross margin increased to 54.9% in fiscal 2004 from 53.7% in fiscal 2003.

Research and Development Expenses, net. Research and development (R&D) expenses consist primarily of personnel and subcontracting expenses and allocated overhead, net of certain software development costs that are capitalized as well as reimbursement under government programs. Software development costs are capitalized upon the establishment of technological feasibility and until related products are available for general release to customers. Research and development expenses, net, for fiscal 2004 increased by approximately \$8.7 million, or 38%, compared to fiscal 2003. The net increase was attributable to an increase in personnel related costs and subcontractors' work amounting to approximately \$7.3 million, an increase in depreciation and amortization expenses of approximately \$0.8 million and an increase of approximately \$0.6 million in other expenses. Capitalization of software development costs amounted to approximately \$4.2 million and approximately \$4.6 million in fiscal 2004 and 2003, respectively. Reimbursement under government and other programs amounted to approximately \$4.1 million and approximately \$4.0 million in fiscal 2004 and 2003, respectively. Historically, the Company has received more reimbursement under government programs for R&D expenses in a given fiscal year than it has had to pay to the appropriate government agency in royalties during that fiscal year. In fiscal 2004 and in future fiscal years, the Company paid or may have to pay more in royalties to these government agencies than it receives in reimbursement from these government agencies for R&D expenses in a given fiscal year.

Selling, General and Administrative Expenses. Selling, general and administrative expenses consist primarily of personnel costs and related expenses, sales and marketing expenses, including travel and agent commission, and other administrative expenses. Selling, general and administrative expenses, for fiscal 2004 increased by approximately \$20.1 million, or 32%, compared to fiscal 2003.

This increase was attributable to an increase in compensation and benefits for existing personnel and increase in headcount to support the increased level of sales in fiscal 2004 totaling approximately \$11.7 million, an increase in agent commissions of approximately \$1.0 million, an increase in travel expenses of approximately \$1.3 million, an increase in depreciation and amortization expenses of approximately \$1.4 million, an increase in rent and utilities expenses of approximately \$0.9 million and an increase in other expenses of approximately \$3.8 million. Selling, general and administrative expenses as a percentage of sales increased to 33.3% for fiscal 2004 from 32.7% for fiscal 2003.

In-Process Research and Development. During fiscal 2004, purchased in-process research and development of approximately \$3.2 million, resulting from the purchase of ECTel's government surveillance business, was charged to expense in the first quarter of fiscal 2004.

Acquisition Related Write-Downs. As a result of the acquisition of ECTel's government surveillance business, the Company had certain capitalized software development costs that became impaired due to the existence of duplicative technology and, accordingly, were written-down to their net realizable value at the date of acquisition. Such impairment charge amounted to approximately \$1.5 million, and was recorded in the first quarter of fiscal 2004.

Interest and Other Income, net. Net interest and other income for fiscal 2004 increased by approximately \$0.9 million as compared to fiscal 2003. The increase was attributable to an increase in interest income of approximately \$1.6 million due to an increase in interest rates and an increase in interest bearing short-term investments, a decrease in interest expense of approximately \$0.3 million due to repayment of loans, and a decrease in other expenses of approximately \$0.1 million. These changes were partially offset by a decrease in the Company's share in the profit of an affiliate of approximately \$0.4 million and a decrease in currency exchange gains of approximately \$0.7 million resulting mainly from fluctuations in the exchange rates of the U.S. dollar against the European and Israeli currencies.

Income Tax Provision. Income tax provision of approximately \$1.9 million was recorded in each of fiscal 2004 and fiscal 2003. The effective tax rate for fiscal 2004 was 9.2% as compared to 9.7% in fiscal 2003, reflecting the use of net operating loss carry-forwards in certain tax jurisdictions as well as the tax benefits associated with qualified activities of the Company's Israeli subsidiary, which is entitled to favorable income tax rates under a program of the Israeli Government for Approved Enterprise investments in that country. To the extent that the Company continues to be profitable in certain tax jurisdictions, it will continue to use available net operating loss carry forwards in these jurisdictions. When the Company ceases to have net operating loss carry forwards available to it in a tax jurisdiction, the Company's effective tax rate would increase in that jurisdiction. The Company's effective tax rate is expected to increase substantially in 2005 which could have a material and adverse effect on the Company's results of operations.

Net Income. Net income increased by approximately \$1.1 million for fiscal 2004 compared to fiscal 2003. Net income as a percentage of sales decreased to 7.6% for fiscal 2004 compared to 9.3% in fiscal 2003. This decrease was attributable to the factors described above.

Year Ended January 31, 2004 Compared to Year Ended January 31, 2003

Sales. Sales for the year ended January 31, 2004, or fiscal 2003, increased by approximately \$35.0 million, or 22%, compared to the year ended January 31, 2003, or fiscal 2002. This increase reflected an increase in both sales of products of approximately \$22.9 million and service revenue of approximately \$12.1 million. This increase was principally due to an increase in sales volume in the United States of approximately \$21.3 million as a result of increased sales of Verint's digital security and surveillance solutions. Due to the variety of customized configurations for each product that the Company sells, it is unable to quantify the effects of a change in the price of any particular product and/or a change in the number of products sold on its revenues. Sales to international customers represented approximately 48% of sales for fiscal 2003 as compared to approximately 51% of sales for fiscal 2002.

Cost of Sales. Cost of sales for fiscal 2003 increased by approximately \$11.2 million, or 14%, compared to fiscal 2002. This increase was attributable to an increase in materials and overhead costs of approximately \$6.4 million, an increase in personnel related costs of approximately \$3.1 million, mainly due to increased service headcount and increased personnel compensation, and an increase in other service and operation costs of approximately \$1.7 million associated with the increase in revenues. Gross margin increased to 53.7% in fiscal 2003 from 50.5% in fiscal 2002.

Research and Development Expenses, net. Research and development expenses, net, for fiscal 2003 increased by approximately \$5.9 million, or 34%, compared to fiscal 2002. The net increase was attributable to an increase in personnel related costs and subcontractors' work amounting to approximately \$3.9 million, decrease in government reimbursement of approximately \$1.2 million, an increase in travel related expenses of approximately \$0.3 million and an increase of approximately \$0.5 million in other expenses. Capitalization of software development costs amounted to approximately \$4.6 million and approximately \$4.8 million in fiscal 2003 and 2002, respectively. Reimbursements under government programs amounted to approximately \$4.0 million and approximately \$5.2 million in fiscal 2003 and 2002, respectively.

Selling, General and Administrative Expenses. Selling, general and administrative expenses for fiscal 2003 increased by approximately \$10.7 million, or 20%, compared to fiscal 2002. This increase was attributable to an increase in compensation and benefits for existing personnel and increase in headcount to support the increased level of sales in fiscal 2003 totaling approximately \$5.3 million, an increase in agent commissions of approximately \$0.7 million, an increase in travel expenses of approximately \$0.6 million, an increase in marketing related expenses of approximately \$1.3 million, an increase in bad debt expenses of approximately \$0.7 million and an increase in other expenses of approximately \$2.1 million. Selling, general and administrative expenses as a percentage of sales decreased to 32.7% for fiscal 2003 from 33.1% for fiscal 2002.

Interest and Other Income, net. Net interest and other income for fiscal 2003 increased by approximately \$0.4 million as compared to fiscal 2002. The increase was attributable to an increase in interest income of approximately \$0.5 million due to the increase in interest bearing cash balances following the Company's secondary public offering, a decrease in interest expense of approximately \$0.3 million due to repayment of loans and an increase in the Company's share in the profit of an affiliate of approximately \$0.9 million.

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These changes were partially offset by a decrease in currency exchange gains of approximately \$1.8 million resulting mainly from fluctuations in the exchange rates of the U.S. dollars against European and Israeli currencies, and a decrease in other expenses of approximately \$0.5 million, mainly due to a write-down of a certain investment in fiscal 2002.

Income Tax Provision. During fiscal 2003, the income tax provision decreased by approximately \$0.3 million as compared to fiscal 2002. This decrease was mainly attributable to prior years' tax adjustment following receipt of final tax assessments. The effective tax rate for fiscal 2003 was 9.7% reflecting prior years' tax adjustment mentioned above, use of net operating loss carry-forwards in certain tax jurisdictions and preferential tax rates in Israel.

Net Income. Net income increased by approximately \$7.8 million for fiscal 2003 as compared to fiscal 2002. Net income as a percentage of sales improved to 9.3% for fiscal 2003 compared to a loss of 6.4% in fiscal 2002. This increase was attributable to the factors described above.

Geographic Information

Summarized financial information for Verint's reportable geographic segments is presented in the following table. Sales in each geographic segment represents sales originating from that segment. Significant non-cash items represent write-down and impairments of operating assets and a charge for in-process research and development. Reconciling items represent elimination of intercompany transactions between subsidiaries operating in different geographic regions.

	United States	Israel	United Kingdom	Canada	Germany	Other	Reconciling Items	Consolidated Totals
(In thousands)								
Year Ended January 31, 2003								
Sales	\$ 85,817	\$ 62,622	\$ 22,897	\$ 804	\$ 9,784	\$ 1,028	\$ (25,177)	\$ 157,775
Costs and expenses	(80,847)	(57,477)	(21,624)	(777)	(10,361)	(1,743)	25,105	(147,724)
Operating income (loss)	\$ 4,970	\$ 5,145	\$ 1,273	\$ 27	\$ (577)	\$ (715)	\$ (72)	\$ 10,051
Depreciation and amortization	\$ 3,631	\$ 4,973	\$ 354	\$	\$ 323	\$ 126	\$	\$ 9,407
Significant non-cash items	\$	\$	\$	\$	\$	\$	\$	\$
Year Ended January 31, 2004								
Sales	\$ 101,703	\$ 75,805	\$ 24,769	\$ 8,705	\$ 9,924	\$ 1,190	\$ (29,352)	\$ 192,744
Costs and expenses	(88,180)	(68,396)	(25,580)	(7,561)	(11,327)	(2,066)	27,555	(175,555)
Operating income (loss)	\$ 13,523	\$ 7,409	\$ (811)	\$ 1,144	\$ (1,403)	\$ (876)	\$ (1,797)	\$ 17,189
Depreciation and amortization	\$ 3,106	\$ 5,415	\$ 413	\$ 812	\$ 495	\$ 34	\$ (206)	\$ 10,069
Significant non-cash items	\$ 9	\$ 405	\$ 2	\$ 97	\$ 1	\$	\$	\$ 514
Year Ended January 31, 2005								

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Sales	\$ 125,482	\$ 94,156	\$ 31,576	\$ 21,886	\$ 14,010	\$ 2,015	\$ (39,301)	\$ 249,824
Costs and expenses	(111,473)	(92,765)	(31,057)	(18,532)	(15,818)	(2,727)	39,932	(232,440)
Operating income (loss)	\$ 14,009	\$ 1,391	\$ 519	\$ 3,354	\$ (1,808)	\$ (712)	\$ 631	\$ 17,384
Depreciation and amortization	\$ 3,595	\$ 7,012	\$ 434	\$ 831	\$ 947	\$ 84	\$	\$ 12,903
Significant non-cash items	\$ 1,371	\$ 4,789	\$	\$ 14	\$	\$	\$	\$ 6,174

Year Ended January 31, 2005 Compared to Year Ended January 31, 2004

Sales for fiscal 2004 increased in all geographic segments, as compared to fiscal 2003, due to an overall increase in sales volume of products and services. Sales originating from the United States and Israel increased by approximately \$23.8 million, or 23%, and by approximately \$18.4 million, or 24%, respectively, in fiscal 2004 as compared with fiscal 2003. Costs and expenses in the United States and Israel increased by approximately \$23.3 million, or 26%, and by approximately \$24.4 million, or 36%, respectively. In the United States, the increase in sales accompanied by a relatively lower dollar increase in costs and expenses increased the operating income for fiscal 2004 as compared to fiscal 2003. In Israel, the increase in costs and expenses at a rate relatively higher than the increase in sales, mainly due to the occurrence of significant non-cash charges of approximately \$4.8 million resulting primarily from the acquisition of ECtel, lowered operating income.

Year Ended January 31, 2004 Compared to Year Ended January 31, 2003

Sales for fiscal 2003 increased in all geographic segments, as compared to fiscal 2002 due to an overall increase in sales volume of products and services. Sales originating from the United States and Israel increased by approximately \$15.9 million, or 19%, and by approximately \$13.2 million, or 21%, respectively, in fiscal 2003 as compared with fiscal 2002. Costs and expenses in the United States and Israel increased by approximately \$7.3 million or 9% and by approximately \$10.9 million, or 19%, respectively. The increase in sales accompanied by a relatively lower increase in costs and expenses, mainly for United States, increased the operating income for fiscal 2003 as compared to fiscal 2002 in those geographies.

Selected Quarterly Results of Operations

The following table sets forth consolidated statements of operations data for each of the eight consecutive fiscal quarters ended January 31, 2005. This information has been derived from our unaudited consolidated financial statements, which have been prepared substantially on the same basis as the audited consolidated financial statements appearing elsewhere in this report and include all adjustments, consisting only of normal recurring adjustments, that we consider necessary for a fair presentation of such information. You should read this information in conjunction with our consolidated financial statements and the related notes thereto appearing elsewhere in this Form 10-K. The operating results for any quarter are not necessarily indicative of the operating results of any future period.

	Three Months Ended							
	April 30, 2003	July 31, 2003	Oct. 31, 2003	Jan. 31, 2004	April 30, 2004	July 31, 2004	Oct. 31, 2004	Jan. 31, 2005
	(In thousands, except percentage data)							
Sales	\$ 44,415	\$ 46,892	\$ 49,012	\$ 52,425	\$ 56,638	\$ 60,167	\$ 63,989	\$ 69,030
Costs of sales	20,912	21,766	22,560	24,064	25,757	27,106	29,235	30,676
Gross profit	23,503	25,126	26,452	28,361	30,881	33,061	34,754	38,354
Research and development, net	5,335	5,692	5,952	6,254	6,791	7,889	8,409	8,872
Selling, general and administrative	14,669	15,301	16,044	17,006	18,594	19,820	21,290	23,366
In-process research and development					3,154			
Acquisition related write-downs					1,481			
Income from operations	3,499	4,133	4,456	5,101	861	5,352	5,055	6,116
Interests and other income, net	515	420	878	857	582	865	932	1,239
Income before income tax provision	4,014	4,553	5,334	5,958	1,443	6,217	5,987	7,355
Income tax provision (benefit)	502	576	667	176	(71)	546	807	648
Net income	\$ 3,512	\$ 3,977	\$ 4,667	\$ 5,782	\$ 1,514	\$ 5,671	\$ 5,180	\$ 6,707
As a percentage of sales								
Sales	100%	100%	100%	100%	100%	100%	100%	100%
Costs of sales	47.1	46.5	46.0	45.9	45.5	45.1	45.7	44.4
Gross profit	52.9	53.5	54.0	54.1	54.5	54.9	54.3	55.6
Research and development, net	12.0	12.1	12.1	11.9	12.0	13.1	13.1	12.9
Selling, general and administrative	33.0	32.6	32.8	32.5	32.8	32.9	33.3	33.8
In-process research and development					5.6			
Acquisition related write-downs					2.6			