SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2001

OR

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

For the transition period from _____________ to _______________

Commission File Number 0-16096

Borland Software Corporation

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**94-2895440**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

100 ENTERPRISE WAY
SCOTTS VALLEY, CALIFORNIA
95066-3249
(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code: **(831) 431-1000**

(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** ☒ **NO** ☐

The number of shares of common stock issued and outstanding as of October 31, 2001, the most recent practicable date prior to the filing of this report, was 65,559,233.

INDEX

		PAGE
PART I	**FINANCIAL INFORMATION**	
Item 1.	Financial Statements	1
	Condensed Consolidated Balance Sheets at September 30, 2001 and December 31, 2000	1
	Condensed Consolidated Statements of Operations for the three and nine months ended September 30, 2001 and 2000	2
	Condensed Consolidated Statements of Other Comprehensive Income for the three and nine months September 30, 2001 and 2000	3
	Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2001 and 2000	4
	Notes to the Condensed Consolidated Financial Statements	5
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	8
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	26
PART II	**OTHER INFORMATION**	
Item 1.	Legal Proceedings	28
Item 2.	Changes in Securities and Use of Proceeds	28
Item 6.	Exhibits and Reports on Form 8-K	28
	Signatures	30

PART I
FINANCIAL INFORMATION

Item 1. Financial Statements

BORLAND SOFTWARE CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(In Thousands, Except Par Value and Share Amounts)

	September 30, 2001 (Unaudited)	December 31, 2000 (Audited)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 269,703	$ 216,634
Short-term investments	10,907	45,925
Accounts receivable, net	33,083	33,495
Other current assets	12,499	12,935
Total current assets	326,192	308,989
Property and equipment, net	20,060	20,438
Other non-current assets	9,965	11,476
	$ 356,217	$ 340,903
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	$ 45,198	$ 45,753
Income taxes payable	6,786	5,337
Deferred revenue	20,358	18,765
Other	8,280	9,053
Total current liabilities	80,622	78,908
Long-term debt	—	8,674
Other long-term liabilities	10,458	10,641
	91,080	98,223
Stockholders' equity:		
Preferred stock: $.01 par value; 1,000,000 shares authorized; 455 and 625 shares issued and outstanding	—	—
Common stock: $.01 par value; 200,000,000 shares authorized; 65,403,473 and 61,966,879 shares issued and outstanding	654	620
Additional paid-in capital	482,131	472,902
Accumulated deficit	(193,170)	(209,721)
Deferred compensation	(1,229)	(1,527)
Cumulative other comprehensive income	4,942	5,611
	293,328	267,885
Less common stock in treasury, at cost – 4,836,300 and 4,473,800 shares	(28,191)	(25,205)
	265,137	242,680
	$ 356,217	$ 340,903

See Notes to the Condensed Consolidated Financial Statements.

BORLAND SOFTWARE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In Thousands, Except Per Share Amounts, Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	2000	2001	2000
Licenses and other revenues	$ 46,985	$ 40,926	$ 136,931	$ 120,700
Service revenues	8,048	6,631	25,810	20,073
Net revenues	55,033	47,557	162,741	140,773
Cost of licenses and other revenues	3,434	2,501	9,874	9,431
Cost of service revenues	5,576	4,944	16,627	14,760
Cost of revenues	9,010	7,445	26,501	24,191
Gross profit	46,023	40,112	136,240	116,582
Research and development	12,311	10,515	34,987	32,077
Sales, general and administrative	30,617	24,176	89,401	76,844
Restructuring and merger-related charges	—	—	—	3,556
Total operating expenses	42,928	34,691	124,388	112,477
Operating income	3,095	5,421	11,852	4,105
Interest income, net, and other	2,782	4,511	9,389	9,118
Non-recurring benefit	—	2,967	—	2,967
Income before income taxes	5,877	12,899	21,241	16,190
Income tax provision	1,204	1,455	4,302	3,890
Net income	$ 4,673	$ 11,444	$ 16,939	$ 12,300
Net income per share:				
Basic	$ 0.07	$ 0.18	$ 0.26	$ 0.19
Diluted	$ 0.06	$ 0.17	$ 0.23	$ 0.18
Weighted average number of common shares outstanding:				
Basic	65,233	61,506	64,563	61,308
Diluted	75,093	68,983	73,715	70,087

See Notes to the Condensed Consolidated Financial Statements.

BORLAND SOFTWARE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OTHER COMPREHENSIVE INCOME
(In Thousands, Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	**2000**	**2001**	**2000**
Net income	$ 4,673	$ 11,444	$ 16,939	$ 12,300
Other comprehensive income (loss):				
Foreign currency translation adjustments	707	(908)	(871)	(1,135)
Fair market value adjustment for available for sale securities	56	—	202	—
Other comprehensive income	$ 5,436	$ 10,536	$ 16,270	$ 11,165

See Notes to the Condensed Consolidated Financial Statements.

BORLAND SOFTWARE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Thousands, Unaudited)

	Nine Months Ended September 30, 2001	Nine Months Ended September 30, 2000
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 16,939	$ 12,300
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	5,752	7,109
Gain on sale of long-term investment	(383)	(723)
Loss on sale of fixed asset	15	1,540
CHANGE IN ASSETS AND LIABILITIES:		
Accounts receivable	(192)	(10,403)
Other assets	1,202	325
Accounts payable and accrued expenses	(269)	1,767
Income taxes payable	3,355	(2,371)
Other (primarily deferred revenue and restructuring)	(321)	3,254
Cash provided by operating activities	26,098	12,798
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(4,410)	(1,340)
Proceeds from sale of property	—	39,651
Net change in short-term investments	35,018	(30,592)
Long-term investment, net	383	(2,077)
Cash provided by investing activities	30,991	5,642
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of common stock, net	8,877	5,105
Repurchase of common stock	(2,986)	—
Repayment of long-term debt	(8,764)	(133)
Cash provided by (used in) financing activities	(2,873)	4,972
Effect of exchange rate changes on cash	(1,147)	(1,010)
Net change in cash and cash equivalents	53,069	22,402
Cash and cash equivalents at beginning of period	216,634	192,013
Cash and cash equivalents at end of period	$ 269,703	$ 214,415

See Notes to the Condensed Consolidated Financial Statements.

BORLAND SOFTWARE CORPORATION

Notes to Condensed Consolidated Financial Statements (unaudited)

NOTE 1—BASIS OF PRESENTATION

The accompanying Borland Software Corporation ("Borland") condensed consolidated financial statements at September 30, 2001 and for the three and nine months ended September 30, 2001 and September 30, 2000 are unaudited and have been prepared in accordance with generally accepted accounting principles for interim financial information and Rule 10-01 of Regulation S-X. Accordingly, they do not include all financial information and disclosures required by generally accepted accounting principles for complete financial statements and certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. The unaudited interim condensed consolidated financial statements have been prepared on the same basis as the annual consolidated financial statements and, in the opinion of management, reflect all adjustments, which include only normal recurring adjustments, necessary to present fairly Borland's financial position at September 30, 2001; its results of operations for the three and nine months ended September 30, 2001 and September 30, 2000; and its cash flows for the nine months ended September 30, 2001 and September 30, 2000. The preparation of condensed consolidated financial statements in conformity with generally accepted accounting principles 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 reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The results of operations for interim periods are not necessarily indicative of the results to be expected for our full fiscal year. The condensed consolidated financial statements and notes should be read in conjunction with our audited financial statements included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2000 as filed with the United States Securities and Exchange Commission (the "SEC") on March 29, 2001.

NOTE 2—NET INCOME PER SHARE

Basic net income per share is computed by dividing the net income available to common stockholders for the period by the weighted average number of common shares outstanding during the period. Diluted net income per share is computed by dividing the net income for the period by the weighted average number of common and common share equivalents outstanding during the period. Common share equivalents, which consist of incremental shares issuable upon exercise of stock options and warrants and upon conversion of the issued and outstanding shares of Series C convertible preferred stock, are included in diluted net income per share to the extent such shares are dilutive.

The following table sets forth the computation of basic and diluted net income per share for the periods indicated (in thousands, except per share amounts):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	2000	2001	2000
Numerator:				
Net income before accretion charges	$ 4,673	$ 11,444	$ 16,939	$ 12,300
Accretion charges to preferred stock	—	219	397	656
Income available to common stockholders for basic earnings per share	$ 4,673	$ 11,225	$ 16,542	$ 11,644
Denominator:				
Denominator for basic income per share - weighted average shares	65,233	61,506	64,563	61,308
Effect of dilutive securities	9,860	7,477	9,152	8,779
Denominator for dilutive income per share	75,093	68,983	73,715	70,087
Net income per share – basic	$ 0.07	$ 0.18	$ 0.26	$ 0.19
Net income per share – diluted	$ 0.06	$ 0.17	$ 0.23	$ 0.18

NOTE 3—RESTRUCTURING

The following table summarizes costs incurred during the nine months ended September 30, 2001 associated with prior period restructuring activities (in thousands):

	Severance and Benefits	Facilities	Other	Total
Accrual at December 31, 2000	$ 1,052	$ 620	$ 500	$ 2,172
Cash payments	606	298	213	1,117
Non-cash costs	(50)	—	151	101
Accrual at September 30, 2001	$ 496	$ 322	$ 136	$ 954

Subsequent to December 31, 2000, there have not been any significant changes to our estimate of the total costs of prior restructuring activities.

NOTE 4—REPAYMENT OF LONG-TERM DEBT

On July 13, 2001, we used approximately $9.0 million in cash to repay the outstanding portion of a mortgage note. The note related to a mortgage on an office building in Scotts Valley, California which previously served as our corporate headquarters and which is now fully leased to third party tenants through February 27, 2002. Such amounts included approximately $0.2 million in prepayment penalties to retire such note.

NOTE 5—REPURCHASE OF COMMON STOCK

During the quarter ended September 30, 2001, we repurchased 362,500 shares of our common stock on the open market at an average price of $8.24 a share for a total consideration of approximately $3.0 million.

NOTE 6—RECENT ACCOUNTING PRONOUNCEMENTS

In July 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141 ("SFAS 141"), "Business Combinations." SFAS 141 requires the purchase method of accounting for business combinations initiated after June 30, 2001 and eliminates the pooling-of-interests method of accounting for business conditions. We believe that the adoption of SFAS 141 will not have a significant impact on our financial statements.

In July 2001, the FASB issued SFAS 142, "Goodwill and Other Intangible Assets," which is effective for fiscal years beginning after March 15, 2001. SFAS 142 requires, among other things, the discontinuance of goodwill amortization. In addition, the standard includes provisions upon adoption for the reclassification of certain existing recognized intangibles as goodwill, reassessment of the useful lives of existing recognized intangibles, reclassification of certain intangibles out of previously reported goodwill and the testing for impairment of existing goodwill and other intangibles. We believe that the adoption of SFAS 142 will not have a significant impact on our financial statements.

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

A CAUTION ABOUT FORWARD-LOOKING STATEMENTS

The statements made throughout this Quarterly Report on Form 10-Q that are not historical facts are forward-looking statements and, accordingly, involve estimates, projections, goals, forecasts, assumptions and uncertainties that could cause actual results or outcomes to differ materially from those expressed or implied in the forward-looking statements.

These forward-looking statements may relate to, but are not limited to, future capital expenditures, acquisitions, future revenues, earnings, margins, costs, demand for our products, market and technological trends in the software industry, interest rates and inflation and various economic and business trends. You can identify forward-looking statements by the use of words such as "expect," "estimate," "project," "budget," "forecast," "anticipate," "intend," "plan," "may," "will," "could," "should," "believes," "predicts," "potential," "continue" and similar expressions or the negative or other variations thereof. Such factors are not exclusive and are in addition to other factors discussed elsewhere in this Form 10-Q, in our other filings with the SEC, or in materials incorporated therein by reference. You should consider the following factors with respect to any forward-looking statements made throughout this Form 10-Q:

- adverse general industry trends and the potential effects on us of competition in computer software product and services markets;
- unanticipated further deterioration of economic and financial conditions in the United States and around the world resulting from the terrorist attacks on September 11, 2001 and possible economic or other repercussions from possible future terrorist attacks;
- rapid technological changes that can adversely affect the demand for our products;
- changes in political, societal and economic conditions and local regulations of geographic areas where we do business;
- changes in our sales mix;
- customer business conditions;
- our ability to maintain or raise current pricing levels;
- financial or regulatory accounting principles or policies imposed by the Financial Accounting Standards Board, the SEC and similar agencies with regulatory oversight;
- the potential loss of key employees;
- our ability to attract and retain qualified personnel;
- general economic factors and capital market conditions;
- changes in tax compliance requirements, including tax rate changes, new tax laws and revised interpretation of tax laws;
- adverse changes, trends and conditions in the financial and capital markets;
- reduction in sales to, or loss of, any significant customers;
- growth rates in the software and professional services markets that we participate in;
- market acceptance of new or enhanced products or services developed, marketed or sold by us;
- the public's perception of Borland and its products;
- changes in laws and regulations, both domestically and overseas, which are applicable to the Internet and electronic commerce;
- our reliance on value-added resellers ("VARs") to market and sell many of our products;
- the lengthy sales cycles applicable to our enterprise software products;
- our dependence, with respect to certain of our business units, on licenses from third parties;

- product returns from retailers exceeding our reserves;
- our ability to successfully integrate acquisitions;
- delays in scheduled product availability dates (which could result from various occurrences including development or testing difficulties, software errors and project management problems);
- disruption of our products or services, or theft of proprietary information, by hackers;
- the increasing trend for software companies to consolidate and our ability to compete against these larger companies, and their substantially greater financial, technical, marketing and other resources;
- our ability to effectively safeguard our products from software piracy;
- changes in laws and regulations, domestically and overseas, with respect to the protection and enforcement of intellectual property rights, including but not limited to, those laws and regulations applicable to the patentability of computer software;
- the possibility that we may need to defend ourselves against intellectual property infringement lawsuits regardless of the merits of the underlying claims;
- the rate of adoption of Linux® as an operating system;
- catastrophic natural disasters;
- foreign currency exchange rate fluctuations;
- unanticipated changes in our operating expenses and capital expenditures; and
- other risks and uncertainties described under the caption "Factors That Could Affect Future Results and Market Price of Stock" in this Form 10-Q as well as in our other filings with the SEC and public announcements.

These factors are difficult to predict. They also involve uncertainties that may materially and adversely affect actual results, and may be beyond our control. New factors may emerge from time to time, and it is not possible for us to predict new factors, nor can we assess the potential effect of any new factors on us.

Forward-looking statements are found throughout this Form 10-Q. We caution you not to place undue reliance on these forward-looking statements, which unless otherwise indicated, speak only as of the date they were made. We do not undertake any obligation to release publicly any revisions to these forward-looking statements to reflect events or circumstances after the date of this Form 10-Q.

You are advised to read this Quarterly Report on Form 10-Q in conjunction with other reports and documents that we file from time to time with the SEC. In particular, please read our Annual Report on Form 10-K, our other Quarterly Reports on Form 10-Q and any Current Reports on Form 8-K that we may file from time to time. You may obtain copies of these reports directly from us or from the Securities and Exchange Commission at the SEC's Public Reference Room at 450 Fifth Street, N.W. Washington, D.C. 20549, and you may obtain information about obtaining access to the Reading Room by calling the SEC at 1-800-SEC-0330. In addition, the SEC maintains information for electronic filers (including us) at its web site www.sec.gov.

Overview

We are a leading provider of high performance e-business platform solutions designed to increase developer productivity and reduce time to market for enterprise software projects. E-business platform solutions consist of software products that allow businesses to develop, deploy and manage e-business applications. We offer products in all three phases of the process of implementing such solutions: development, deployment and management. For the development phase, Borland offers JBuilder,™ C++Builder,™ Delphi,™ and Kylix.™ Our deployment products include Borland® AppServer,™ InterBase® and VisiBroker.® To manage these systems, Borland offers Borland® AppCenter,™ a visual distributed application management solution. We also are in the process of developing Borland® TeamSource,™ a hosted collaborative development platform for distributed teams. We are committed to all major computing platforms as well as the open standards of the Internet. We also provide service and support for software developers worldwide through an online developer community and an e-commerce site, community.borland.com, which offers a range of technical information, value-added services and third-party products. We market and distribute products worldwide through our direct sales organization, e-commerce Internet site, independent distributors, dealers and value-added resellers ("VARs").

Product Offerings

The following are descriptions of our key product offerings:

E-Business Development

JBuilder: JBuilder is a comprehensive set of visual development tools that allow the creation of applets, servlets, JavaBeans®, Enterprise JavaBeans™ (EJB™) and distributed CORBA® (Common Object Request Broker Architecture) applications for the Java 2 platform. JBuilder enables programmers to rapidly create, edit, run and deploy applications that target a variety of Java enabled platforms such as Windows,® Solaris™ and Linux. In June 2001, we began shipping the latest version of this product, JBuilder 5.

Delphi: Delphi is a high-performance, rapid application development tool (RAD) used to create Windows, Internet and distributed software applications. The Delphi product combines visual productivity tools, a component library and a high-performance compiler so that software developers can build high-speed e-business systems more quickly than with conventional programming tools. Delphi and our Kylix product are compatible, allowing developers to build cross-platform workstation and server applications and deploy to either Windows or Linux. In June 2001, we began shipping Delphi 6, the latest version of the product containing Web Services and XML-based B2B integration support.

C++Builder: C++Builder is a software development tool and compiler for C and C++ computing languages used to create Internet, desktop, client/server and distributed applications. The C++Builder product combines visual productivity tools, a component library and a high performance compiler so that software developers can build high performance e-business applications more quickly than with conventional programming tools. In February 2000, we began shipping C++Builder 5, the latest version of this product.

Kylix: Kylix is our implementation of a RAD platform for the Linux operating environment. The implementation mirrors the Delphi and C++Builder development paradigms, but is implemented to generate native code and native look-and-feel applications for the Linux operating environment. Kylix and our Delphi product are compatible, allowing developers to build cross-platform workstation and server applications and deploy to either Windows or Linux. The product was announced in January 2001, and we began shipping Kylix in March 2001.

E-Business Deployment

InterBase: InterBase is a powerful, high-performance SQL database designed to be embedded into applications running on the Windows, Linux and Solaris platforms. InterBase provides superior relational database solutions to meet the business-critical embedded database needs for value-added resellers and application developers. In July 2000, we open-sourced InterBase software version 6.0. In March 2001, we released commercial versions of InterBase 6.0 for Linux, Windows and Solaris environments.

Borland AppServer: Borland AppServer was the industry's first application server product to combine the benefits of Java 2 Platform Enterprise Edition (J2EE™ platform), EJB and CORBA. The product, which is highly scalable, provides a foundation for deploying enterprise grade business applications. Borland AppServer simplifies and accelerates the integration, deployment and management of e-business applications. Borland AppServer integrates heterogeneous back-office systems comprised of ERP, supply chain, database management and legacy systems. In February 2001, we began shipping Borland AppServer 4.5, the latest version of this product.

VisiBroker: VisiBroker is an award-winning Object Request Broker™ (ORB™), based on CORBA, and designed to facilitate development and deployment of distributed enterprise applications that are scalable, flexible and easily maintained. Customers for this product have included Sun Microsystems, Inc., Hitachi Ltd., Oracle Corporation, Novell, Inc., Netscape Communications Corporation and Silicon Graphics, Inc.

These companies, among others, have played a key role in making VisiBroker a leading deployed and adopted ORB in the computer software industry. In the fourth quarter of 2000, we began shipping VisiBroker for Java 4.5, the latest version of this product.

E-Business System Management

Borland AppCenter: Borland AppCenter is the first management solution designed to enable customers to model, monitor and manage component-based application servers. Borland AppCenter provides robust management capabilities for CORBA- and EJB-based applications and is tightly integrated with VisiBroker and the Borland AppServer.

Services

In addition to our products, we offer a wide range of hosted development, consulting, training and support services to customers. Our service offerings include:

Borland TeamSource: We are in the process of developing Borland TeamSource, a collaborative development platform for distributed teams. Borland TeamSource speeds global e-business applications to market by reaching across the Internet to bridge functional, geographic and corporate boundaries among team members. The high-performance hosted infrastructure and business messaging of Borland TeamSource brings widely dispersed teams together and provides a secure environment that scales up or down with team members as they collaborate around digital assets.

Consulting services: We offer a variety of both packaged and custom consulting services that include architectural assessment, prototyping, legacy migration, application integration, performance evaluation, application deployment and data conversions. We work closely with third-party consulting firms and systems integrators who provide reengineering, technology assessments, customization, project management and implementation services.

Training services: We offer education and training services to assist customers in learning about our products and current technology trends. These programs range from introductory sessions to highly advanced seminars. Training services are offered at either customer sites or locations designated by us and are led by our employees or consultants.

Support services: We provide a wide range of support services, and offer such services on-site or through telephone or the Internet. A comprehensive range of support programs allow customers to choose the level of support for their business, from personalized support for corporate needs to minimum assistance levels for small businesses.

Results of Operations

Licenses and Other Revenues

Licenses and other revenues represent revenues from granting customers licenses to use our software products and revenues from subscription contracts. Licenses and other revenues totaled $47.0 million for the quarter ended September 30, 2001 compared to $40.9 million from the same quarter a year ago. Licenses and other revenues from our Java, RAD, Enterprise and other products group represented 40%, 34%, 19% and 7% of total licenses and other revenues for the quarter ended September 30, 2001, respectively. This is compared to 38%, 26%, 30% and 6% for the quarter ended September 30, 2000, respectively. Our Java product group consists of JBuilder. Our RAD product group consists of Delphi, Kylix and C++Builder. Our Enterprise product group consists of VisiBroker, Borland AppServer and Borland AppCenter. Our other products group consists primarily of InterBase.

Licenses and other revenues during the quarter ended September 30, 2001 were favorably affected by the continued success of JBuilder and Delphi, whose revenues grew 15% and 89%, respectively, over the same quarter a year ago. Licenses and other revenues from our Enterprise product group decreased by 30% over the same quarter a year ago principally due to softness in demand for Enterprise products by technology companies and the decline in business in the United States after the September 11 terrorist attacks. Licenses and other revenues from other products increased 40% from the same quarter a year ago principally due to a significant purchase of InterBase licenses by a single customer.

Licenses and other revenues totaled $136.9 million for the nine months ended September 30, 2001 compared to $120.7 million from the same period a year ago. License and other revenues from our Java, RAD, Enterprise and other products group represented 38%, 32%, 23% and 6%, respectively, of total licenses and other revenues for the nine months ended September 30, 2001. This is compared to 29%, 36%, 27% and 8%, respectively, for the nine months ended September 30, 2000.

Licenses and other revenues during the nine months ended September 30, 2001 were favorably affected by the continued success of our JBuilder and RAD products. For the nine months ended September 30, 2001, licenses and other revenues from JBuilder grew 45% over the same period a year ago. Licenses and other revenues from our RAD product group and the Enterprise product group for the nine month period ended September 30, 2001 remained consistent with revenues in the nine month period ended September 30, 2000.

Service Revenues

Service revenues represent amounts earned from technical support, training and consulting services related to our software products. Service revenues increased to $8.0 million for the quarter ended September 30, 2001, compared to $6.6 million for the quarter ended September 30, 2000. Technical support and consulting/training represented approximately 70% and 30% of total service revenues, respectively, for the quarter ended September 30, 2001 compared with 58% and 42% for the same quarter a year ago. For the nine months ended September 30, 2001, technical support and consulting/training represented approximately 64% and 36% of total service revenues, respectively, compared with 57% and 43% for the same nine months a year ago. The increase in service revenues is primarily due to growth in technical support revenues in the United States and Europe, Middle East and Africa ("EMEA"). The increase in service revenues represents our continued focus on direct sales and marketing of our support services to corporate customers. In the future, we expect service revenues to remain dependent upon our ability to grow the number of corporate customers.

International Revenues

International revenues represented 67% and 60% of our total net revenues for the three and nine months ended September 30, 2001, respectively, compared to 51% and 57% for the three and nine months ended September 30, 2000. The increase in the percentage of international revenue was due to expansion of our European and Asian-Pacific operations. Additionally, we experienced a reduction in demand in the United States during the last few weeks of the quarter due to the September 11 terrorist attacks. We expect that our international operations will continue to provide a significant portion of our total revenues.

The following table presents our total revenues by geographic area:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	**2000**	**2001**	**2000**
United States	$ 18,472	$ 23,160	$ 64,748	$ 58,755
EMEA	21,216	14,010	59,729	46,035
Japan	6,653	4,457	17,078	17,994
Other	8,692	5,930	21,186	17,989
Net revenues	$ 55,033	$ 47,557	$ 162,741	$ 140,773

Cost of Revenue

Cost of Licenses and Other Revenues

Cost of licenses and other revenues consist primarily of production costs such as purchase of compact discs, transferring software to electronic media, printing of user manuals, product packaging and distribution and royalties paid to third-party vendors. Cost of licenses and other revenues increased from $2.5 million for the quarter ended September 30, 2000 to $3.4 million for the quarter ended September 30, 2001. The cost of licenses and other revenues represented 7% and 6% of total licenses and other revenues in the quarters ended September 30, 2001 and 2000, respectively. The increase in cost of licenses and other revenues is due to increased sales of JBuilder and RAD products and higher external royalty costs associated with sales of our Borland Enterprise Studio for Java introduced earlier this year.

Cost of licenses and other revenues increased from $9.4 million for the nine months ended September 30, 2000 to $9.9 million for the nine months ended September 30, 2001. The cost of licenses and other revenues represented 7% and 8% of total licenses and other revenues for the nine month period ended September 30, 2001 and 2000, respectively. The dollar increase in cost of licenses and other revenues during the nine month period was principally due to increased sales of JBuilder and RAD products.

Cost of Service Revenues

Cost of service revenues consists primarily of salaries and benefits, third-party contractor costs, and related expenses incurred in providing technical support, consulting and training. Cost of service revenues were $5.6 million and $4.9 million for the quarters ended September 30, 2001 and 2000, respectively. Cost of service revenues as a percentage of service revenues decreased from 75% in the quarter ended September 30, 2000 to 69% for the quarter ended September 30, 2001. The cost of service revenues were $16.6 million and $14.8 million for the nine months ended September 30, 2001 and 2000, respectively. Cost of service revenue as a percentage of service revenues decreased from 74% for the nine months ended September 30, 2000 to 64% for the nine months ended September 30, 2001. The dollar increase in cost of service revenues was due to additional employee and third party costs in our professional service organization. The cost of service revenue decreased as a percentage of service revenue because a larger percentage of our service revenues were generated from more profitable service contracts. Due to the relative fixed nature of our cost of services, we expect the service revenue margins to remain a function of our ability to enter into enterprise level support contracts.

Operating Expenses

Research and Development

Research and development expenses consist primarily of salaries and other personnel-related expenses for those involved in research and development, costs of computer equipment used in software development, information technology and facilities costs and fees and expenses of third-party consultants. Research and development expenses were $12.3 million and $10.5 million, or, 22% of net revenues for the quarters ended September 30, 2001 and 2000. Research and development expenses were $35.0 million and $32.1 million, or, 21% and 23% of net revenues for the nine months ended September 30, 2001 and 2000, respectively. Research and development expenses increased in dollars primarily due to an increase in employee costs. Employee costs increased principally due to an increase in the number of research and development employees.

Sales, General and Administrative

Sales, general and administrative ("SG&A") expenses consist primarily of salaries, benefits, sales commissions, the cost of product marketing programs, and facility and information system costs. Sales, general and administrative expenses were $30.6 million and $24.2 million, or, 56% and 51% of net revenues for the quarters ended September 30, 2001 and 2000, respectively. Sales, general and administrative expenses were $89.4 million and $76.8 million, or, 55% of net revenues for the nine months ended September 30, 2001 and 2000, respectively. The dollar increase in sales, general and administrative expenses was principally due to an increase in the number of sales and marketing employees.

Interest Income, Net and Other

Interest income, net and other consists primarily of interest income, interest expense, foreign currency exchange and gains and losses on the sale of fixed assets. Interest income, net and other decreased from $4.5 million during the quarter ended September 30, 2000 to $2.8 million during the quarter ended September 30, 2001. Interest income, net and other increased from $9.1 million during the nine months ended September 30, 2000 to $9.4 million during the nine months ended September 30, 2001.

While cash, cash equivalents and short term investments have increased by $29.9 million, or 12%, from September 30, 2000 to September 30, 2001, interest income decreased by $1.5 million for the quarter ended September 30, 2001 compared to the quarter ended September 30, 2000 due to lower effective interest rates on investments. We anticipate that interest income will continue to be less than the corresponding prior year amounts for the remainder of the year as interest rates are expected to remain significantly lower.

Income Taxes

We recorded income tax expense of $1.2 million and $4.3 million for the three and nine months ended September 30, 2001, respectively. This compares to income tax expense of $1.4 million and $3.9 million for the three and nine months ended September 30, 2000, respectively. This is based on our expected effective tax rate of 20 percent for the year ending December 31, 2001, which is a combination of U.S. alternative minimum tax, non-U.S. income taxes and withholding taxes imposed in various jurisdictions regardless of the profitability of Borland in that jurisdiction. Our expected effective tax rate for the year ending December 31, 2001 is less than the effective tax rate for the year ended December 31, 2000 principally due to our utilization of tax loss and credit carryforwards.

Liquidity and Capital Resources

As of September 30, 2001, cash, cash equivalents and short-term investments totaled $280.6 million; up from $262.6 million at December 31, 2000. The major sources of cash during the nine months ended September 30, 2001 were $26.1 million in cash provided from operating activities and $8.9 million in cash received from the issuance of stock upon the exercise of warrants held by the former holders of our Series B preferred stock (the Board of Directors approved the retirement of the remaining 770 shares on October 26, 2001) and pursuant to employee stock options and our employee stock purchase plan. The major use of cash during this period was $9.0 million to repay the outstanding portion of a mortgage note, $4.4 million in cash used for the purchase of computer equipment and leasehold improvements, and $3.0 million in cash used for the repurchase of common stock.

We expect that our existing cash, cash equivalents, short-term investments and cash generated from operating activities will be sufficient to finance our business requirements at least through the next twelve months.

FACTORS THAT COULD AFFECT FUTURE RESULTS AND MARKET PRICE OF STOCK

We operate in a rapidly changing environment that involves many risks and uncertainties, some of which are beyond our control, which could affect our future results of operations as well as our stock price. The following discussion highlights some of these risks.

We Depend on the Overall Demand for Information Technology and Services

Our success depends on the growth of the overall demand for information technology and services, particularly in the market for our e-business platform solutions. Our business is affected by general economic and business conditions throughout the world. A softening of the demand for our e-business platform solutions specifically, and information technology and services generally, caused by a weakening of the economy, may result in decreased revenues or slower growth for us.

We Depend on Key Personnel

We believe that our future success will depend, in large part, on our ability to recruit and retain qualified employees, particularly highly skilled software engineers and management personnel. There can be no assurances that we will be successful in retaining or recruiting such personnel.

To retain key employees, we have instituted retention programs. We have increased compensation, bonuses, stock options and other fringe benefits in order to attract and retain management and other key personnel. We may be required to further increase such compensation and benefits. We are not certain that these efforts will succeed in retaining our key employees, and failure to attract and retain key personnel could significantly harm our business. These increased compensation costs may not be offset through either improved productivity or higher revenue.

Risks Related to New Product Introductions; Rapid Technological and Market Changes

The market for our products is highly competitive and is characterized by continuous technological advancement, evolving industry standards and changing customer requirements. Our success in generating revenues in the future will depend substantially on our ability to design and market new products and upgrades to our current products for existing and new computer platforms and operating environments.

We face a number of inherent risks in the current market environment, including, but not limited to, the following:

- we may introduce products later than we expect or later than competitors' introductions;
- the mere announcement by us of a new product or an upcoming upgrade to an existing product could cause potential customers to defer or cancel purchases of existing products and services;
- competitors may introduce competing products at lower prices;
- products may not meet customers' expectations regarding features and performance;
- competitors' products based on new technologies or new industry standards may quickly render an existing product obsolete and unmarketable;
- product upgrades, which enable users to upgrade from earlier versions of our products or our competitors' products, have lower prices and margins than new products; and/or
- the acceptance of some of our new products is highly dependent, in part, on the continued adoption of the Internet as a new computing paradigm and the continued adoption of the Linux operating system.

From time to time, we announce when we expect to begin shipping a new product. In the past, some of our products have shipped later, and sometimes substantially later, than when we originally expected. The loss of key employees may increase the risk of these delays. Some of our products are based on technology licensed from third parties. We have limited control over when and whether these technologies are upgraded. The failure or delay in enhancements of technology licensed from third parties could have a material adverse effect on our ability to develop and enhance our products. Due to these uncertainties inherent in software development, it is likely that these risks will materialize from time to time in the future. We could lose customers as a result of substantial delays in the shipment of new products or product upgrades.

Results of Our Research and Development Efforts are Uncertain

Our future success will depend upon our ability to enhance our current products and develop and introduce new products on a timely basis. We believe that we will need to incur significant research and development expenditures to remain competitive. The products we are currently developing or may develop in the future may not be technologically successful. In addition, the length of our product development cycle may be greater than we originally expected. We are likely to experience delays in future product development. If the resulting products are not technologically successful, they may not achieve market acceptance or compete effectively with products of our competitors.

Our competitors may respond more quickly to emerging technologies than we do. We may lose customers to competitors if we are not able to respond to requests for additional features and new products in a timely fashion. We may not be able to maintain or improve our competitive position against current or potential competitors, especially those with greater resources.

Risks of Entering a New Business Area

Our strategy is to focus on e-business system solutions at the enterprise, departmental and individual developer levels. Our sales are dependent on enterprise customers adopting distributed object technology for information processing and the Internet and corporate Intranets for commerce and communications.

Our distributed object software products, such as VisiBroker, Borland AppCenter and Borland AppServer, are based on several industry standards, including CORBA, Extended Markup Language or XML, EJB and the J2EE platform. These standards guide the development and management of applications created in object oriented programming languages such as C++ and Java. These industry standards have begun to gain widespread acceptance and they compete with proprietary solutions such as ActiveX® and DCOM and the emerging .Net™ initiative, all of which are marketed by Microsoft Corporation. CORBA-based implementations have been tried and tested in extremely demanding application environments, and are generally deemed suitable for enterprise class applications. EJB and J2EE platform implementations are earlier in the maturity cycle for use in enterprise class processing environments. The rate of adoption of these latter standards will affect our business results and success.

We are investing time and resources in developing products, such as Kylix, which was released and began shipping in the first quarter of 2001, for the Linux operating system. Linux is a new operating system that has yet to be adopted on a widespread basis. At this time, there are relatively few commercially viable products that operate on the Linux operating system. If Linux is not adopted, or is adopted more slowly than we anticipate, our investments in Linux compatible products may not generate the anticipated return, and as a result there could be a material and adverse effect on our business.

As a newcomer to these markets, we face a number of risks including:

- the new and evolving nature of the markets themselves;
- our need to make choices regarding the operating systems, database management systems, server software and hardware platforms on which to focus;
- the ongoing transition and investment of our resources for these markets;
- our limited experience in these markets; and
- the presence of several very large and well-established companies, as well as a number of smaller successful companies, that are already competing in some of these markets.

There can be no assurance that we will be successful in these new markets.

There is a further risk that a new hardware or software platform that we do not provide products for could rapidly grow in popularity. If we fail to introduce new products that address the needs of emerging market segments, if emerging segments are not adopted as anticipated, or if our new products do not achieve market acceptance, our future growth and profitability could suffer.

Risks Related to the Use of Java

A number of our most popular products are based on Java, an object-oriented software programming language and distributed computing platform developed by Sun Microsystems, Inc. Such products accounted for approximately 35% of our revenue during the quarter ended September 30, 2001. Java is a relatively new language and was developed primarily for the Internet and corporate Intranet applications. Alternatives to Java include the C# language and .Net computing platform offered by Microsoft Corporation. If Java does not continue to be widely adopted, or is adopted more slowly than anticipated, our business will suffer.

Additionally, some of our products require proprietary technology made available by Sun Microsystems, Inc. in order to operate. Pursuant to license agreements with Sun Microsystems, Inc., we license the Java 2 Platform, Standard Edition specification, the Java 2 Platform, Enterprise Edition specification, the Java 2 Platform, Micro Edition specification and the PersonalJava™ specification. If Sun Microsystems, Inc. stops making this proprietary technology available on commercially reasonable terms, due to the absence of effective alternatives to licensing this technology, our business will be harmed. Alternatively, if Sun Microsystems, Inc. makes significant changes to the Java language or its proprietary technology, or fails to correct defects and limitations in these products, our ability to continue improving and shipping our products could be impaired, perhaps materially. In the future, our customers also may require the ability to deploy our products on platforms for which technically acceptable Java implementations either do not exist or are not available on commercially reasonable terms.

Extremely Competitive Industry

The computer software industry is an intensely competitive industry. Rapid change, new and emerging technologies and fierce competition characterize the industry. The pace of change has accelerated due to the emergence of the Internet and corporate Intranets, programming languages such as Java, and operating systems such as Linux.

Our e-business platform solutions compete with products offered by a number of companies, including, but not limited to, BEA Systems, Inc., International Business Machines Corporation, Iona Technologies PLC, Microsoft Corporation, Oracle Corporation, Sun Microsystems, Inc. and Webgain, Inc. With respect to our Borland AppServer product, we compete primarily with BEA Systems, Inc. and International Business Machines Corporation. With respect to our VisiBroker product, we compete primarily with Iona Technologies PLC. With respect to our JBuilder product, we compete primarily with International Business Machines Company, Sun Microsystems, Inc. and Webgain, Inc. With respect to our Delphi and C++Builder products, we compete primarily with Microsoft Corporation. With respect to our TeamSource service, our potential competitors may include Merant, Microsoft Corporation, Oracle Corporation and Rational Software Corporation. At this time we have no significant competitors to our Borland AppCenter and Kylix products.

In addition, we compete with, and in some cases are dependent upon, operating systems vendors such as Apple Computer, Inc., Hewlett-Packard Company, International Business Machines Corporation, Microsoft Corporation, Red Hat, Inc. and Sun Microsystems, Inc. To the extent that we are unable to obtain information regarding existing and future operating systems from the developers of such systems, the release of our products for such systems may be delayed or may not be competitive. For example, Microsoft Corporation, the developer of the Windows operating environment, has introduced a product that includes certain basic application server functionality. The bundling of competing functionality in versions of Windows products requires us to compete with Microsoft Corporation in the Windows marketplace where Microsoft Corporation has certain inherent advantages due to its significantly greater financial, technical, marketing and other resources, greater name recognition, substantial installed base and the integration of its middleware functionality with Windows. We need to differentiate our products from those of Microsoft Corporation, based on scalability, functionality, interoperability with non-Microsoft Corporation platforms, performance and reliability as well as to establish that our products provide more effective solutions to customers' needs. There can be no assurance that we will be able to differentiate our products successfully from those offered by Microsoft Corporation, or that Microsoft Corporation's entry into the middleware market will not harm this portion of our business.

Some of our competitors have substantially greater financial, management, marketing and technical resources than we have. Many of our competitors have well-established relationships with our current and potential customers. They also have extensive knowledge of the market, and extensive development, sales and marketing resources, and they are capable of offering single vendor solutions. In particular, operating system vendors such as those mentioned above may offer similar products bundled with their own operating systems. For example, Microsoft Corporation has introduced DCOM for Microsoft Corporation operating systems. In addition, in the past, some of our competitors have utilized their greater resources to provide substantial signing bonuses and other inducements to lure key personnel away from us.

Some of our products are targeted at the market for standards-based distributed object software products. These markets are intensely competitive. We believe that our product quality, performance and price, vendor and product reputation, product architecture and quality of support make us competitive in these markets. Because there are relatively low barriers to entry to the markets for our AppServer and AppCenter products, we expect additional competition from other established and emerging companies. Increased competition could result in price reductions, fewer customer orders, reduced gross margins and loss of market share. Any one of these results could materially adversely affect our business, operating results and financial condition.

It is possible that current and new competitors may form alliances to gain significant market share. Some of our competitors have offered to license software for free to gain competitive advantage. For example, Sun Microsystems, Inc. offers NetBeans™ at no charge. This kind of competition could materially adversely affect our ability to sell additional licenses and maintenance and support renewals on profitable terms. Competitive pressures could require us to reduce the price of our products and related services. We are not certain that we will be able to compete successfully against current and future competition. The failure to compete successfully could have a material adverse effect on our business, operating results and financial condition.

We need to differentiate our products from our competitors' products based on functionality, interoperability, developer productivity, performance and reliability. There can be no assurance that we will be able to successfully differentiate our products from those of our competitors.

We also need to constantly expand our product lines to meet the needs of our customers. This includes not only the development, but also the acquisition, of new products and technologies. In addition, there is no guarantee that any newly acquired technologies or products will be successfully commercialized so as to realize revenue.

A Trend Toward Consolidation in our Industry May Impede Our Ability to Compete Effectively

Consolidation may occur among companies in the software industry as firms seek to offer more extensive suites of software products and broader arrays of software solutions. Changes resulting from consolidation may negatively impact our competitive condition. In addition, to the extent that we seek to expand our product lines, a trend toward consolidation may result in increased competition for attractive companies for acquisition, and higher prices for such companies.

Risks Associated with Potential Business Combinations

As a part of our business strategy, we may need to acquire businesses, products or technologies in the future. However, there may not be suitable businesses, products or technologies available for acquisition on terms acceptable to us. We will review potential acquisition prospects to determine if they:

- complement our existing product offerings;
- augment our market coverage;
- enhance our technological capabilities; or
- offer growth opportunities.

There may be substantial costs associated with acquisitions including the potential dilution to our earnings per share, the incurrence or assumption of debt, the assumption of contingent liabilities, the amortization of expenses related to goodwill and other intangible assets and the legal and other fees associated with the negotiation and consummation of the acquisition. Acquisitions entail numerous risks, including difficulty in the assimilation of operations, technologies, products and personnel, as well as difficulties and uncertainties in our ability to maintain key business relationships that the business entities have established. Acquisitions also divert the attention of management from other business concerns. An acquisition in a new area risks entering markets where we have limited or no prior experience as well as potential loss of key employees of the acquired organization. Further, there is no guarantee that the expected synergies will occur between ourselves and the new acquisition. There is also no assurance that we will be able to commercialize a new product or technology so as to realize revenue. Finally, despite due diligence reviews, acquired businesses may bring with them certain unanticipated or undisclosed liabilities and risks. Any one of these risks, if realized, could negatively affect our business, financial condition and operating results.

Dependence on Third-Party Licenses

We are dependent on licenses from third-party suppliers for some elements of our products. If any of these licenses were terminated or were not renewed, or these third parties failed to develop new or updated products in a timely manner, we might not be able to ship some of our products. We would then have to seek an alternative to the third party's product and, in some cases, it is possible that an alternative may not exist. This could result in delays in releasing and/or shipping the product, increased costs or reduced functionality of our products and could have a material and adverse effect on our business, operating results and financial condition.

Risks in Direct Sales, Lengthy Sales Cycles and Systems Implementation Selling

Selling enterprise software products directly to our customers entails sales cycles that are substantially more lengthy and more uncertain than those associated with our traditional business of selling desktop software through retail channels. Customers for enterprise products are predominately larger companies, institutions and government entities. These customers generally commit significant time and resources to evaluating enterprise software, and they require us to expend substantial time, effort and money educating them about our software products and solutions. As a result, sales to these types of customers generally require an extensive sales effort throughout the customer's organization, and they often require final approval by the customer's Chief Information Officer or other senior level employee. All of these factors substantially extend the sales cycle and increase the uncertainty of whether a sale will be made. We have experienced and expect to continue to experience delays and uncertainty in the sales cycle as well as increased expenses for these sales. The timing of sales could cause our results of operations to vary significantly from quarter to quarter and could have a material adverse impact on our results of operations.

We need to extensively train and effectively manage our sales personnel, invest additional resources in our sales efforts and educate our authorized resellers. Our failure to do so could have a material adverse impact on our business. We have made changes to our sales compensation programs in recent years in an effort to motivate our sales force and, accordingly, increase sales. There can be no assurance, however, that such programs will be successful in achieving this result in the long term, and such changes could significantly impact our sales-related expenses.

We have added trained technical support personnel to assist our customers in implementing our enterprise software products. Personnel with sufficient expertise and experience for these positions are in great demand, and we may not be able to attract or retain a sufficient number of qualified personnel. Our failure to do so could significantly harm our business.

Risks of Using Retail Distribution Channels

A significant portion of our sales are made through retail distribution channels. Demand in these channels fluctuate based on customer demand. Our retail distributors also carry the products of competitors. Some of our retail distributors have limited capital to invest in inventory. Their decision to purchase our products is based on a combination of demand for our products, our pricing and the terms and special promotions we offer.

Our net revenues and earnings may be affected by a practice called "channel fill." Channel fill occurs when a distributor purchases more products than it expects to sell in anticipation of price changes, sales promotions or incentives. After we announce a new version or new product and prior to the date of product availability, distributors, dealers and end users often delay purchases, cancel orders or return products in anticipation of the availability of the new version or product. We try to mitigate the negative effect of this pattern by deferring recognition of revenue associated with distributors' and resellers' inventories that are in excess of appropriate levels. However, channel fill may still affect our net revenues, particularly during periods where we announce several new products and/or new versions at the same time.

When we introduce new versions of our products, our distributors return their inventories of the older versions. Our return policy allows our distributors, with some limitations, to return products in exchange for credit toward new products. Similarly, end users may return products through dealers and distributors within a reasonable period from the date of purchase for a full refund. Retailers may then return the older versions to us. We estimate and maintain reserves for product returns. However, future product returns could exceed our reserves, and this could have a material adverse effect on our business.

Risks of Reliance on VARs

A part of our distribution strategy is to embed and bundle our technology in the products offered by value-added resellers, or VARs, such as AOL Time Warner, Inc., Cisco Systems, Inc., Hewlett-Packard Company, Hitachi Ltd., i2 Technologies, Inc. and Oracle Corporation. In the past, a small number of VAR customers accounted for a significant percentage of our enterprise product revenue.

For these sales, the pricing and discount terms and conditions of our license agreements are negotiated and vary among our customers. Most of our license agreements with these customers are non-exclusive and do not require them to recommend or offer our products exclusively. Many of our agreements do not require our customers to make a minimum number of purchases. We have virtually no control over the shipping dates or volumes of systems shipped by our customers. Many of the markets for VAR products are new and evolving. Therefore, we cannot predict that these customers will purchase our technology for their products in the future. If we are not successful in securing additional licenses with our current or new customers on profitable terms, our business, financial condition and results of operations could be materially and adversely affected.

Risks Associated with International Operations and Sales

A substantial portion of our revenue is from international sales. There are inherent risks in doing business internationally. Some of these risks include the following:

- general economic conditions in each country;
- seasonal reductions in business activity during the summer months in Europe and certain other parts of the world;
- the difficulty of staffing and managing an organization spread over various countries and continents;
- reduced or less certain protection for intellectual property rights than is available under the laws of the United States;
- fluctuations in foreign currency exchange rates;
- longer payment cycles in certain countries;
- export restrictions, tariffs and other trade barriers;
- changes in regulatory requirements;
- restrictions on the expatriation of currency from a particular country;
- compliance with various conflicting laws and regulations;
- overlap of different tax structures; and
- political instability.

One or more of these risk factors could have a material adverse effect on our future international operations and, consequently, on our business, operating results and financial condition. In addition, our subsidiaries generally operate in local currencies, and their results are translated monthly into U.S. dollars. If the value of the U.S. dollar increases significantly relative to foreign currencies, there could be a material adverse effect on our business, operating results and financial condition.

The Price of Our Common Stock May Fluctuate Significantly

Like the publicly-traded securities of other high technology companies, the market price of our common stock has experienced significant fluctuations and may continue to fluctuate significantly. During the 52-week period from September 30, 2000 to September 30, 2001, the price of our common stock has ranged from a low of $4.16 on October 13, 2000 to a high of $16.39 on July 17, 2001. On November 9, 2001, the most recent practicable date prior to the filing of this Form 10-Q, the closing price of a share of our common stock on The Nasdaq Stock Market® was $13.50. From time to time, the market price of our common stock may be significantly affected by a number of factors, including, but not limited to, the following:

- announcements of new products or product enhancements by us or our competitors;
- technological innovation by us or our competitors;
- quarterly variations in our results of operations or those of our competitors;
- changes in the prices of our products or those of our competitors;
- changes in actual or projected revenue and revenue growth rates for us as a whole or for specific geographic areas, business units, products or product categories;
- changes in the price-to-earnings and other multiples used to value companies in the software industry;
- changes in revenue, earnings or other estimates by the research analysts who cover Borland;
- actual or anticipated changes in information technology spending;
- speculation by the press, product analysts or research analysts with respect to Borland and its products, revenues and/or earnings, including the growth rate relating thereto;
- actual or anticipated changes in interest rates; and
- general market conditions or market conditions specific to the software industry.

The stock prices for many companies in the technology sector have experienced wide fluctuations which, at times, have been unrelated to the operating performance of such companies.

In the past, following periods of volatility in the market price of a company's securities, securities class action litigation has often been instituted against such companies. Were such litigation to be commenced against us, we would incur substantial costs and there would be diversion of our management's attention and resources, which could materially adversely affect our business, results of operations and financial condition.

Unpredictability of Future Revenues: Potential Fluctuations in Quarterly Operating Results and Seasonality

Our quarterly operating results have varied significantly in the past. We expect that our operating results will continue to vary significantly from time to time. We believe that these variations may result from many factors already described in this Form 10-Q and may include, but may not be limited to, any of the following factors:

- introduction of new products;
- the mix of channels through which we market, distribute and sell our products;
- the overall level of demand for our products and services;
- the size and timing of significant orders and their fulfillment;
- the number, timing and significance of product enhancements and new product announcements by us and our competitors;
- changes in pricing policies by us or our competitors;
- customer order deferrals in anticipation of enhancements or new products offered by us or our competitors;
- deferral of customer orders based on customers' uncertainty about our short-term and long-term prospects;
- product release cycles of existing products;
- product defects and other product quality problems;

- seasonal trends; and
- general domestic and international economic and political conditions.

An additional risk factor is the lengthening of our sales cycle. We expect that a significant percentage of our future revenues will be from large orders. These large sales typically contain multiple elements, including licenses for development and deployment products, technical support, maintenance, consulting and training services. A significant portion of the revenues from a large order is typically recognized over time. For example, when the contract is signed, the license and deployment fees may be recognized by us as revenue. However, revenues related to further services, such as technical support and consulting services, must be deferred until the services are rendered. The timing of recognition of revenues associated with larger sales may have a material adverse effect on our business, operating results and financial position.

Furthermore, many customers place orders toward the end of a given quarter. Revenues may also fluctuate based on our customers' fiscal year budgeting cycles. Therefore, revenues may be difficult to predict. Our costs are based on projected revenues and are relatively fixed in the short term. Therefore, if our revenue levels fall below projections, net income may be significantly reduced, and, accordingly, we may experience a loss.

As a result of all of these factors, we believe that quarterly revenues and operating results are difficult to forecast and period-to-period comparisons of our results of operations are not necessarily meaningful and should not be relied upon as indications of trends or our future performance.

Risks of Regulation of the Internet and Electronic Commerce

We intend to expand our business through, among other channels, electronic commerce on the Internet. The electronic commerce market on the Internet is new and rapidly evolving. While this is an evolving area of the law in the U.S. and overseas, currently there are relatively few laws or regulations that directly apply to commerce on the Internet. Changes in laws or regulations governing the Internet and electronic commerce, including, without limitation, those governing an individual's privacy rights, pricing, content, acceptable payment methods and quality of products or services could have a material adverse effect on our business, operating results and financial condition. Taxation of Internet commerce, or other charges imposed by government agencies or by private organizations may also be imposed. Laws and regulations applying to the solicitation, collection and processing of personal or consumer information could also be enacted. Any of these regulations could result in a decline in the use or popularity of the Internet as a medium for commerce, which could have an adverse effect on our future sales and revenue growth.

Our future sales and any future profits will be substantially dependent upon the widespread acceptance and use of the Internet by consumers and businesses as an effective medium for exchanging information and conducting business. To be successful, consumers and businesses that historically have used traditional means of commerce to transact business must continue to accept and utilize the Internet as a medium for conducting business and exchanging information. Consumers and businesses may eventually reject the Internet as a viable commercial medium for a number of reasons, including potentially inadequate network infrastructure, slow development of enabling technologies, insufficient commercial support and privacy concerns. In addition, delays in the development or adoption of new standards and protocols required to handle increased levels of Internet activity could cause the Internet to lose its viability as a commercial medium.

Risks Associated with Our Dependence on Encryption Technology

We use and will continue to use encryption technology in some of our products to provide security for the exchange of confidential information. Encryption technologies have been breached in the past. There can be no assurance that there will not be a compromise or breach of our security technology. If such a breach were to occur, it could have a material adverse effect on our business.

Protecting Our Intellectual Property Rights

As a software company, our intellectual property rights are among our most valuable assets. We rely on a combination of patent, copyright, trademark, trade secret laws, contractual arrangements, domain name registrations and other methods to protect our intellectual property rights. The protective steps we have taken may be inadequate to deter misappropriations of our intellectual property rights. In addition, it may be possible for an unauthorized third party to reverse-engineer or decompile our software products. We may be unable to detect the unauthorized use of, or take appropriate steps to enforce, our intellectual property rights. Litigation may be necessary to protect our intellectual property rights, particularly our patent portfolio which currently consists of 97 issued United States patents. Litigation can be time consuming and expensive. In addition, effective protection of intellectual property rights is unavailable or limited in certain foreign countries, making the possibility of misappropriation of our intellectual property more likely. Current U.S. laws that prohibit copying give us only limited practical protection from software “pirates,” and the laws of many other countries provide very little protection. Policing unauthorized use of our products is difficult, expensive and time consuming, and we expect that software piracy will be a persistent problem for our software products. In addition, the unique technology of the Internet has increased software piracy. Accordingly, we cannot be certain that we will be able to protect our intellectual property rights against unauthorized third-party copying or use. This could materially and adversely affect our revenues.

From time to time, we receive a notice claiming that we have infringed a third party’s patent or other intellectual property right. We expect that software products in general will increasingly be subject to such claims as the number of products and competitors increase and the functionality of products overlap. Further, the receipt of a notice alleging infringement may require, in certain situations, that we obtain an opinion of counsel to prevent an allegation of intentional infringement. Regardless of the merits of a claim, responding to any claim can be time consuming and costly and divert the efforts of our technical and management personnel from productive tasks. In the event of a successful claim against us, we may be required to pay significant monetary damages, including treble damages, if we are held to have willfully infringed, discontinue use and sale of the infringing products, expend significant resources to develop non-infringing technology and/or enter into royalty and licensing agreements that might not be offered or available on acceptable terms. If a successful claim were made against us and we failed to commercially develop or license a substitute technology, our business could be materially harmed. In addition, our insurance coverage for these types of claims may not be adequate.

Our Software Products and Web Site May Be Subject to Intentional Disruption

Our products or services may be the target of intentional disruptions, such as software viruses specifically designed to impede the performance of our products or services. Similarly, experienced computer programmers or hackers may attempt to penetrate our network security or the security of our web site and misappropriate proprietary information or cause interruptions to the delivery of our services or products. Our activities could be substantially disrupted, and our reputation and future sales could be harmed if these efforts were successful.

Risks of Software Defects and Liability Claims

Software products occasionally contain errors or defects, especially when they are first introduced or when new versions are released. We have not experienced any substantial problems to date from potential defects and errors. We routinely test our new products and new versions for defects and errors. We cannot be certain, however, that our products are completely free of defects and errors. Errors in our software may be caused by defects in third-party software incorporated into our software. If so, we may be unable to fix these defects without the cooperation of these software providers. Because these defects may not be as significant to our software providers as they are to us, we may not receive the full and timely cooperation that we may require. In addition, we may not have the contractual right to access the source code of third-party software and, even if we access the source code, we may be unable to detect and fix the defect. The discovery of a defect or error in a new version or product may result in the following consequences, among others:

- delayed shipping of the product;
- immediate loss of revenue;
- delay in market acceptance;

- diversion of development resources;
- damage to our reputation; and
- increased service and warranty costs.

These consequences could materially and adversely affect our business, operating results and financial condition.

Most of our license agreements contain provisions designed to limit our liability for potential product liability claims. It is possible, however, that these provisions may not protect us because of existing or future foreign, federal, state or local laws or ordinances or judicial decisions. A successful product liability claim for large damages brought against us could have a material adverse effect on our business, operating results and financial condition and we may not have adequate insurance coverage for such risks.

Our products interoperate with many parts of complicated computer systems, such as mainframes, servers, personal computers, application software, databases, operating systems and data transformation software. Failure of any one of these parts could cause all or large parts of computer systems to fail. In such circumstances, it may be difficult to determine which part failed, and it is likely that customers would bring a lawsuit against several companies, including us. Regardless of the merits of a claim, responding to any claim can be time consuming and costly and divert the efforts of our technical and management personnel from productive tasks. In addition, our insurance coverage for these types of claims may not be adequate.

Risks of Certain Anti-Takeover Provisions

In December 1991, we implemented a stockholder rights plan to protect our stockholders in the event of a proposed takeover that has not been recommended or approved by our Board of Directors. Under our stockholder rights plan, each share of our outstanding common stock has attached to it one preferred share purchase right. Each preferred share purchase right entitles the holder, under certain circumstances, to purchase shares of our common stock at a 50% discount from its then current market price. The preferred share purchase rights are redeemable at a nominal price and expire in December 2001. On October 26, 2001, our Board of Directors approved a successor stockholder rights plan, substantially similar to the 1991 plan, which will take effect in December 2001 following the scheduled expiration of the existing plan.

Our stockholder rights plan and certain provisions of our Restated Certificate of Incorporation and Amended and Restated Bylaws may discourage, delay or prevent an actual or potential change in control of Borland even if such a change in control would be beneficial to and in the best interests of our stockholders. These limitations may limit our stockholders' ability to approve transactions that they may deem to be in their best interests. In addition, our Board of Directors has the authority to fix the rights and preferences of, and issue shares of, preferred stock without action by our stockholders.

Potential Dilutive Effect of Conversion and Additional Issuance of Series C Preferred Stock ("Series C Stock")

Each share of our Series C Stock, all of which is held by Microsoft Corporation, is presently convertible, at the option of the holder, into fully paid and non-assessable shares of Borland common stock based upon a fixed conversion ratio. In the event of a reorganization, reclassification or other change (other than a stock dividend, stock split or reverse stock split), each share of Series C Stock would be convertible, at the option of the holder, into the kind and amount of shares of stock and other securities and property receivable upon such events. Upon transfer by the holder to an unaffiliated third party, each share of Series C Stock would automatically convert into fully-paid and non-assessable shares of our common stock based upon a fixed conversion ratio. In the event of a merger, consolidation, tender offer, agreement to sell, or sale of all or substantially all of our assets, each share of Series C Stock would automatically convert into the right to receive the same consideration as if the Series C Stock had been converted into common stock immediately prior to such events. In the event of liquidation, dissolution or winding up of Borland, the holders of shares of Series C Stock would receive the same consideration as if the Series C Stock had been converted into common stock immediately prior to such event. The conversion ratio is subject to certain adjustments in the event of a stock split and other capital reorganizations. On or about August 29, 2001, Microsoft Corporation converted 170 shares of Series C Stock into 1,827,957 shares of common stock. At September 30, 2001, the remaining 455 shares of Series C Stock issued and outstanding were convertible into 4,892,473 shares of common stock.

Risk of Natural Disasters, Power Shortages and Other Unexpected Events

Our corporate headquarters, including most of our research and development operations, are located in the Greater San Francisco Bay Area of California, an area known for significant seismic activity. Seismic activity, such as a major earthquake, could have a material adverse effect on our business, financial condition and operating results. Over the past year, there has been a shortage of electricity in California. As a result, many regions, including the Greater San Francisco Bay Area, have experienced rolling power outages as capacity has failed to satisfy demand. Continued power shortages, a power failure or other similar unexpected events could impair our ability to operate our business, which could also significantly disrupt our operations.

Recent terrorist attacks upon the United States have added (or exacerbated) economic, political and other uncertainties, which could adversely affect our revenue growth. Additional terrorist acts or acts of war (wherever located around the world) may cause damage or disruption to Borland, our employees, facilities, partners, suppliers, distributors and resellers and customers which could have a material adverse effect on our operations and financial results.

We Are Currently Party to Various Legal Proceedings

Although litigation is subject to inherent uncertainties, management does not believe that the ultimate outcome of these legal proceedings will have a material adverse effect on our financial position or overall trends in results of operations. However, if an unfavorable ruling were to occur in any specific period, there exists the possibility of a material adverse impact on the results of operations of that period. Management believes that, given our current liquidity and cash and investment balances, even were we to receive an adverse judgment with respect to litigation that we are currently a party to, such a judgment would not have a material impact on our cash and investments or liquidity.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risks relating to our operations result primarily from changes in interest rates and foreign currency exchange rates, as well as credit risk concentrations. To address the foreign currency exchange rate risk we enter into various hedging transactions as described below. We do not use financial instruments for trading purposes.

Foreign Currency Risk

We transact business in various foreign countries and have established a foreign currency hedging program utilizing foreign currency forward exchange contracts to hedge intercompany balances and other monetary assets denominated in foreign currencies. The goal of the hedging program is to offset the earnings impact of foreign denominated balances. We do not use foreign currency forward exchange contracts for trading purposes. At month-end, foreign denominated balances and the forward exchange contracts are marked-to-market and unrealized gains and losses are included in current period net income. Unrealized gains and losses on long term foreign denominated intercompany balances are reported as part of cumulative other comprehensive income.

During the three and nine months ending September 30, 2001, we have recorded net foreign exchange losses of $0.2 million and $ 0.7 million, respectively. The foreign exchange losses were generated primarily due to changes in the Euro to U.S. dollar exchange rate. It is uncertain whether these currency trends will continue. If these currency trends continue, we will continue to experience foreign exchange losses on our intercompany receivables to the extent that we have not hedged the exposure with foreign currency forward exchange contracts. Such foreign exchange losses could have a material adverse affect on our operating results and cash flows.

The table below provides information about our derivative financial instruments, comprised of foreign currency forward exchange contracts. The information is provided in U.S. dollar equivalent amounts, as presented in our financial statements. For foreign currency forward exchange contracts, the table presents the notional amounts (at the contract exchange rates), the weighted average contractual foreign currency exchange rates and the estimated fair value as of September 30, 2001. All instruments mature within twelve months.

	September 30, 2001		
	Notional Amount	**Average Contract Rate**	**Estimated Fair Value**
Foreign currency forward exchange contracts:			
Australian Dollar	$ 3,214	2.02	$ (32)
Hong Kong Dollar	1,607	7.78	(4)
New Taiwan Dollar	695	34.56	(11)
Singapore Dollar	6,791	1.77	(24)
Total	$ 12,307		$ (71)

Interest Rate Risk

Our exposure to market risk for changes in interest rates relate primarily to our investment portfolio. We do not use derivative financial instruments in our investment portfolio. We place our cash equivalents and short-term investments in a variety of financial instruments such as commercial paper. We, by corporate policy, limit the amount of our credit exposure to any one financial institution or commercial issuer.

We mitigate default risk by investing in only safe and high credit quality securities and by constantly positioning our portfolio to respond appropriately to a significant reduction in the credit rating of any investment issuer. The portfolio includes only marketable securities with active secondary and resale markets to ensure portfolio liquidity.

We have no interest rate exposure due to rate changes for long-term obligations.

The table below presents principal (or notional) amounts and related weighted average interest rates by year of maturity for our investment portfolio and debt obligations (dollar amounts in thousands).

	2001	2002	2003	2004 (In thousands)	2005	Thereafter	Total
Cash equivalents							
Fixed rate	$ 269,703	—	—	—	—	—	$ 269,703
Average interest rate	3.82%	—	—	—	—	—	3.82%
Short-term investments							
Fixed rate	$ 10,907	—	—	—	—	—	$ 10,907
Average interest rate	2.26%	—	—	—	—	—	2.26%

Credit Risks

Our financial instruments that are exposed to concentrations of credit risk consist primarily of cash equivalents, short-term investments and trade receivables. Our cash equivalents and short-term investments are in high quality securities placed with major banks and financial institutions. Credit risk with respect to receivables is limited due to the large number of customers and their dispersion across geographic areas. We perform periodic credit evaluations of our customers' financial condition and generally do not require collateral. As of September 30, 2001, no group or single customer represents greater than 10% of total accounts receivable.

PART II
OTHER INFORMATION

Item 1. Legal Proceedings

Although litigation is subject to inherent uncertainties, management does not believe that the ultimate outcome of these legal proceedings will have a material adverse effect on our financial position or overall trends in results of operations. However, if an unfavorable ruling were to occur in any specific period, there exists the possibility of a material adverse impact on the results of operations of that period. Management believes that, given our current liquidity and cash and investment balances, even were we to receive an adverse judgment with respect to litigation that we are currently a party to, such a judgment would not have a material impact on cash and investments or liquidity.

Item 2. Changes in Securities and Use of Proceeds

Successor Rights Agreement

On October 26, 2001, Borland's Board of Directors approved and adopted a successor stockholder rights plan under which all Borland stockholders on the record date for the rights distribution will receive rights to purchase shares of Borland's Series D Junior Participating Preferred Stock, a newly-authorized series of preferred stock.

The terms of the new rights plan are substantially similar to the terms of Borland's existing rights plan which is due to expire later this year. The record date for the distribution of the rights will be the close of business on December 20, 2001 or, if earlier, the date on which the existing rights are redeemed. Under the new rights plan, the rights will be distributed as a non-taxable dividend and will expire ten years from the record date. In general, the rights will be exercisable only if a person or group acquires 15% or more of Borland's common stock. If a person or group acquires 15% or more of Borland's common stock while the rights plan remains in place, all rights holders, except the acquiror, will be entitled to acquire Borland common stock having a value equal to two times the exercise price of the rights, which has been set at $80.

The rights will trade with Borland's common stock, unless and until they are separated upon the occurrence of certain future events. Borland's board of directors may terminate the rights plan at any time or redeem the rights until ten days after the time a person or group acquires more than 15% of Borland's common stock

The rights agreement is filed as Exhibit 1 to Borland's Registration Statement on Form 8-A which was filed with the SEC on October 31, 2001 and the foregoing description of the plan is qualified in its entirety by reference to such Exhibit 1.

Item 6. Exhibits and Reports on Form 8-K

A. Exhibits

The following exhibits are filed as part of, or incorporated by reference into, this Form 10-Q.

Exhibit No.	**Description of Exhibit**
4	Rights Agreement by and between Borland Software Corporation and Mellon Investor Services LLC, as Rights Agent, dated as of October 26, 2001, (filed with the Commission on October 31, 2001 as Exhibit 1 to Borland's Registration Statement on Form 8-A and incorporated herein by reference).

A copy of any exhibit referenced above will be furnished (at a reasonable cost) to any stockholder of Borland upon receipt of a written request. Such request should be sent to Borland Software Corporation, 100 Enterprise Way, Scotts Valley, California 95066-3249, Attention: Lynne Farris, Director of Investor Relations.

B. Reports on Form 8-K

During the quarter ended September 30, 2001, Borland did not file any Current Reports on Form 8-K with the Securities and Exchange Commission.

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.

BORLAND SOFTWARE CORPORATION
(Registrant)

Date: November 13, 2001

/ s / FREDERICK A. BALL

Frederick A. Ball
Executive Vice President and Chief Financial Officer
(Principal Financial Officer and Duly Authorized Officer)