NETSUITE INC
Form 10-Q
November 07, 2011
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark one)

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

For the quarterly period ended September 30, 2011

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 001-33870

NetSuite Inc.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	94-3310471 (I.R.S. Employer Identification No.)
2955 Campus Drive, Suite 100 San Mateo, California (Address of principal executive offices)	94403-2511 (Zip Code)

(650) 627-1000
(Registrant's telephone number, including area code)

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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). (Check one): Yes S No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "accelerated filer, large accelerated filer and a smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer¨		Accelerated filer	x
Non-accelerated filer ¨	(do not check if a smaller reporting company)	Smaller reporting company	¨

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

On October 31, 2011, 67,882,362 shares of the registrant's Common Stock, $0.01 par value, were issued and outstanding.

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NetSuite Inc.

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PART I – Financial Information

ITEM 1. Financial Statements

NetSuite Inc.
Condensed Consolidated Balance Sheets
(dollars in thousands)
(unaudited)

	September 30, 2011	December 31, 2010
Assets		
Current assets:		
Cash and cash equivalents	$126,777	$104,298
Accounts receivable, net of allowances of $374 and $456 as of September 30, 2011 and December 31, 2010, respectively	30,083	27,235
Deferred commissions	18,734	15,401
Other current assets	12,491	7,190
Total current assets	188,085	154,124
Property and equipment, net	21,843	19,847
Deferred commissions, non-current	2,403	1,389
Goodwill	27,564	27,340
Other intangible assets, net	13,049	12,507
Other assets	3,683	2,086
Total assets	$256,627	$217,293
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$2,393	$1,489
Deferred revenue	92,574	75,827
Accrued compensation	13,806	12,048
Accrued expenses	5,905	5,144
Other current liabilities (including note payable to related party of $2,729 and $1,117 as of September 30, 2011 and December 31, 2010, respectively)	11,542	5,599
Total current liabilities	126,220	100,107
Long-term liabilities:		
Deferred revenue, non-current	4,458	5,312
Other long-term liabilities (including note payable to related party of $2,375 and $3,535 as of September 30, 2011 and December 31, 2010, respectively)	6,048	5,590
Total long-term liabilities	10,506	10,902
Total liabilities	136,726	111,009
Commitments and contingencies (Note 4)		
Stockholders' equity:		
Common stock, par value $0.01, 500,000,000 shares authorized; 67,837,397 and 64,887,677 shares issued and outstanding at September 30, 2011 and December 31, 2010, respectively	678	649
Additional paid-in capital	454,794	416,582
Accumulated other comprehensive income	346	578
Accumulated deficit	(335,917)	(311,525)
Total equity	119,901	106,284
Total liabilities and stockholders' equity	$256,627	$217,293

See accompanying Notes to Condensed Consolidated Financial Statements.

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NetSuite Inc.
Condensed Consolidated Statements of Operations
(dollars in thousands, except per share data)
(unaudited)

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2011	2010	2011	2010
Revenue:				
Subscription and support	$145,388	$119,735	$51,334	$41,834
Professional services and other	26,845	21,347	9,625	7,909
Total revenue	172,233	141,082	60,959	49,743
Cost of revenue:				
Subscription and support	24,342	20,038	8,627	6,848
Professional services and other	27,450	26,090	9,658	8,546
Total cost of revenue	51,792	46,128	18,285	15,394
Gross profit	120,441	94,954	42,674	34,349
Operating expenses:				
Product development	31,615	26,451	11,257	9,482
Sales and marketing	88,209	66,623	30,279	24,363
General and administrative	23,839	21,773	7,622	7,110
Total operating expenses	143,663	114,847	49,158	40,955
Operating loss	(23,222)	(19,893)	(6,484)	(6,606)
Other income / (expense), net:				
Interest income	127	159	36	66
Interest expense	(104)	(100)	(39)	(43)
Other expense, net	(130)	(499)	(114)	(130)
Total other expense, net	(107)	(440)	(117)	(107)
Loss before income taxes	(23,329)	(20,333)	(6,601)	(6,713)
Provision for income taxes	1,063	702	328	245
Net loss	(24,392)	(21,035)	(6,929)	(6,958)
Less: net loss attributable to noncontrolling interest	—	14	—	—
Net loss attributable to NetSuite Inc. common stockholders	$(24,392)	$(21,021)	$(6,929)	$(6,958)
Net loss per common share, basic and diluted attributable to NetSuite Inc. common stockholders	$(0.37)	$(0.33)	$(0.10)	$(0.11)
Weighted average number of shares used in computing net loss per share	66,459	63,513	67,477	63,965

See accompanying Notes to Condensed Consolidated Financial Statements.

NetSuite Inc.
Condensed Consolidated Statements of Cash Flows
(dollars in thousands)
(unaudited)

	Nine Months Ended September 30,	
	2011	2010
Cash flows from operating activities:		
Net loss attributable to NetSuite Inc. common stockholders	$(24,392)	$(21,021)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	6,745	5,758
Amortization of other intangible assets	2,884	3,549
Provision for accounts receivable allowances	243	377
Stock-based compensation	28,166	23,038
Amortization of deferred commissions	24,954	16,814
Noncontrolling interests	—	(14)
Changes in operating assets and liabilities, net of acquired assets and assumed liabilities:		
Accounts receivable	(3,003)	896
Deferred commissions	(29,300)	(17,301)
Other current assets	146	(1,478)
Other assets	247	448
Accounts payable	911	1,093
Accrued compensation	1,821	(884)
Deferred revenue	15,864	2,823
Other current liabilities	(18)	41
Other long-term liabilities	(691)	(468)
Net cash provided by operating activities	24,577	13,671
Cash flows from investing activities:		
Purchases of property and equipment	(7,156)	(4,366)
Capitalized internal use software	(406)	(67)
Cash paid in business combination	(1,775)	—
Net cash used in investing activities	(9,337)	(4,433)
Cash flows from financing activities:		
Payments under capital leases and long-term debt	(1,080)	(1,182)
Repurchase of noncontrolling interest	—	(1,370)
RSUs acquired to settle employee withholding liability	(205)	(5,587)
Proceeds from issuance of common stock	8,662	3,590
Net cash provided by / (used in) financing activities	7,377	(4,549)
Effect of exchange rate changes on cash and cash equivalents	(138)	74
Net change in cash and cash equivalents	22,479	4,763
Cash and cash equivalents at beginning of period	104,298	96,355
Cash and cash equivalents at end of period	$126,777	$101,118
Supplemental cash flow disclosure:		
Cash paid for interest to related parties	$82	$88
Cash paid for interest to other parties	$22	$12
Cash paid for income taxes, net of tax refunds	$900	$631
Noncash financing and investing activities:		
Fixed assets and other acquired under capital lease	$1,791	$6,090

Funds held for customers and customer funds obligations	$4,294	$—
Common stock issued in connection with business combination	$1,400	$—

See accompanying Notes to Condensed Consolidated Financial Statements.

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NetSuite Inc.
Notes to Condensed Consolidated Financial Statements
(unaudited)

Note 1. Organization
NetSuite Inc. (the “Company”) provides cloud-based financials/ Enterprise Resource Planning (“ERP”) software suites. In addition to financials/ERP software suites, the Company offers a broad suite of applications, including accounting, Customer Relationship Management (“CRM”), Professional Services Automation (“PSA”) and Ecommerce that enable companies to manage most of their core business operations in its single integrated suite. The Company delivers its suite over the Internet as a subscription service using the software-as-a-service (“SaaS”) model. The Company’s headquarters are located in San Mateo, California. The Company conducts its business worldwide, with international locations in Canada, Europe, Asia, and Australia.

Note 2. Basis of Presentation

The Condensed Consolidated Financial Statements as of and for the nine and three month periods ended September 30, 2011 included in this Quarterly Report on Form 10-Q have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”). The condensed consolidated balance sheet data as of December 31, 2010 was derived from the audited consolidated financial statements included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2010 filed on March 3, 2011. Certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with generally accepted accounting principles in the United States of America (“GAAP”) have been condensed or omitted pursuant to such rules and regulations. However, the Company believes that the disclosures contained in this Quarterly Report comply with the requirements of Section 13(a) of the Securities Exchange Act of 1934, as amended, for a Quarterly Report on Form 10-Q and are adequate to make the information presented not misleading. These Condensed Consolidated Financial Statements are meant to be, and should be, read in conjunction with the Consolidated Financial Statements and the notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2010 filed on March 3, 2011.

The unaudited Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q reflect all adjustments (which include only normal, recurring adjustments and those items discussed in these Notes) that are, in the opinion of management, necessary to state fairly the financial position and results for the dates and periods presented. The results for such periods are not necessarily indicative of the results to be expected for the full fiscal year.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its majority- and wholly-owned subsidiaries. Intercompany balances and transactions have been eliminated.

As of September 30, 2011 and December 31, 2010, the Company owned a 100% interest in NetSuite Kabushiki Kaisha (“NetSuite KK”), a Japanese corporation. During the three months ended March 31, 2010, the Company purchased the remaining outstanding equity in NetSuite KK for aggregate consideration of $1.4 million in cash. Prior to the Company’s purchase of the remaining outstanding equity of NetSuite KK, given the Company’s majority ownership interest, the accounts of NetSuite KK were consolidated with the accounts of the Company, and a noncontrolling interest was recorded for the other investors’ interests in the net assets and operations of NetSuite KK to the extent of the noncontrolling investors’ individual investments.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make certain estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, as well as reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

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Recent Accounting Pronouncements

In September 2011, the FASB issued Accounting Standards Update, Testing Goodwill for Impairment (the revised standard). The revised standard is intended to reduce the cost and complexity of the annual goodwill impairment test by providing entities an option to perform a “qualitative” assessment to determine whether further impairment testing is necessary. The revised standard is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted provided that the entity has not yet performed its 2011 annual impairment test or issued its financial statements. An entity has the option to first assess qualitative factors to determine whether it is necessary to perform the current two-step test. If an entity believes, as a result of its qualitative assessment, that it is more-likely-than-not that the fair value of a reporting unit is less than its carrying amount, the quantitative impairment test is required. Otherwise, no further testing is required. The Company plans to adopt this update in the first quarter of fiscal year 2012. The Company does not expect the adoption of this update to have an impact on its consolidated results of operations and financial condition.

In June 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update, Presentation of Comprehensive Income. The new guidance eliminates the current option to report other comprehensive income and its components in the statement of changes in equity. Instead, an entity will be required to present either a continuous statement of net income and other comprehensive income or two separate but consecutive statements and will result in presentation changes for our consolidated financial statements. The updated guidance is effective on a retrospective basis for financial statements issued for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2011. Early adoption is permitted. The Company plans to adopt this update in the first quarter of fiscal year 2012. The Company does not anticipate adoption to have a material impact on its consolidated financial statements.

In December 2010, the FASB issued Accounting Standards Update, Disclosure of Supplementary Pro Forma Information for Business Combinations (Topic 805)-Business Combinations, to improve consistency in how the pro forma disclosures are calculated. Additionally, the update enhances the disclosure requirements and requires description of the nature and amount of any material, nonrecurring pro forma adjustments directly attributable to a business combination. The guidance is effective for the Company in the first quarter of fiscal 2012 and should be applied prospectively to business combinations for which the acquisition date is after the effective date. Early adoption is permitted. The Company plans to adopt this update in the first quarter of fiscal year 2012. The Company does not anticipate adoption to have a material impact on its consolidated financial statements.

Business Combination

On August 2, 2011, the Company completed the purchase of substantially all of the assets of a small private company ("SPC") that provides on-demand software. Accordingly, the assets and operating results of SPC are reflected in the Company’s condensed consolidated financial statements from the date of acquisition. As consideration on the closing date, the Company paid $1.1 million in cash and issued 38,102 shares of the Company's common stock valued at $1.4 million on the closing date. Additional consideration of $375,000 in cash is being withheld for a year following the close of the transaction as protection against certain losses the Company may incur in the event of certain breaches of representations and warranties covered in the purchase agreement. Third-party costs associated with this transaction were negligible. The Company will integrate SPC's technology into its product suite to enhance the functionality of its suite.

Under the acquisition method of accounting, the Company allocated the purchase price to the identifiable assets based on their estimated fair value at the date of acquisition. To determine the value of the intangible assets, the Company made various estimates and assumptions. Critical estimates in valuing the intangible assets include but are not limited to the expected costs to recreate the assets. The excess of the purchase price over the total identifiable assets has been recorded as goodwill. The Company did not record any in-process research and development charges in connection with the acquisition.

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The allocation of the SPC consideration to the assets acquired was as follows:

	(dollars in thousands)
Developed technology	$2,513
Customer relationships	183
Unbilled receivables	47
Goodwill	157
Total purchase price	$2,900
Cash	$1,500
Fair value common stock issued	1,400
Total purchase price	$2,900

The Company will amortize the developed technology and customer relationships intangible assets ratably on a straight-line basis over a four year term. The SPC's operating results are not material for pro forma disclosure.

Revenue Recognition

The Company generates revenue from two sources: (1) subscription and support; and (2) professional services and other. Subscription and support revenue includes subscription fees from customers accessing its on-demand application suite and support fees from customers purchasing support. Arrangements with customers do not provide the customer with the right to take possession of the software supporting the on-demand application service at any time. Professional services and other revenue include fees from consultation services to support the business process mapping, configuration, data migration, integration and training. Amounts that have been invoiced are recorded in accounts receivable and in deferred revenue or revenue, depending on whether the revenue recognition criteria have been met.

Generally, the Company enters into subscription and support agreements for 12 months. In aggregate, more than 90% of the professional services component of the arrangements with customers is performed within 300 days of entering into a contract with the customer.

The subscription agreements provide service level commitments of 99.5% uptime per period, excluding scheduled maintenance. The failure to meet this level of service availability may require the Company to credit qualifying customers up to the value of an entire month of their subscription and support fees. In light of the Company’s historical experience with meeting its service level commitments, the Company does not currently have any reserves on its balance sheet for these commitments.

The Company commences revenue recognition when all of the following conditions are met:
- There is persuasive evidence of an arrangement;
- The service is being provided to the customer;
- The collection of the fees is reasonably assured; and
- The amount of fees to be paid by the customer is fixed or determinable.

In most instances, revenue from new customer acquisition is generated under sales agreements with multiple elements, comprised of subscription and support fees from customers accessing its on-demand application suite and professional services associated with consultation services. The Company evaluates each element in a multiple-element arrangement to determine whether it represents a separate unit of accounting. An element constitutes a separate unit of accounting when the delivered item has standalone value and delivery of the undelivered element is probable and within the Company's control. Subscription and support have standalone value because they are routinely sold separately by the Company. Professional services have standalone value because the Company has sold professional services separately and there are several third party vendors that routinely provide similar professional services to its customers on a standalone basis.

The Company allocates revenue to each element in an arrangement based on a selling price hierarchy. The selling price for a deliverable is based on its vendor-specific objective evidence ("VSOE"), if available, third-party evidence ("TPE"), if VSOE is not available, or estimated selling price ("ESP"), if neither VSOE nor TPE is available. As the Company has been

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unable to establish VSOE or TPE for the elements of its arrangements, the Company establishes the ESP for each element primarily by considering the weighted average of actual sales prices of professional services sold on a standalone basis and subscription and support including various add-on modules when sold together without professional services, and other factors such as gross margin objectives, pricing practices and growth strategy. The consideration allocated to subscription and support is recognized as revenue over the contract period commencing when the subscription service is made available to the customer. The consideration allocated to professional services is recognized as revenue using the percentage-of-completion method.
The total arrangement fee for a multiple element arrangement is allocated based on the relative ESP of each element. However, since the professional services are generally completed prior to completion of delivery of subscription and support services, the revenue recognized for professional services in a given reporting period does not include fees subject to delivery of subscription and support services. This results in the recognition of revenue for professional services that is generally no greater than the contractual fees for those professional services.

For single element sales agreements, subscription and support revenue is recognized ratably over the contract term beginning on the provisioning date of the contract. The Company recognizes professional services revenue using the percentage-of-completion method for single element arrangements.

Sales and other taxes collected from customers to be remitted to government authorities are excluded from revenues.

Cross Patent License Agreement
In July 2011, the Company entered into a patent cross licensing agreement ("the Agreement") with a large technology company, which includes payments from the Company totaling $3.0 million with an initial installment of $1.0 million and the remaining amount payable by the Company over approximately the next two years. The Agreement provides the Company with the right to use the large technology company's patents over a period that is slightly in excess of six years and resolves any claims relating to alleged past usage of the large technology company's patents. The Agreement also provides the large technology company with the right to use the Company's existing and future patents. The Company estimated the total present value of the historical patent rights to be approximately $679,000 and recorded this amount as general and administrative expense in its condensed consolidated statement of operations for the second quarter of 2011. During the third quarter of 2011, the Company paid the initial $1.0 million installment to the large technology company and recorded a long-term asset and corresponding long-term liability for the remaining payments.

Funds Held for Customers and Customer Funds Obligations

During the first quarter of 2011, the Company took over the provisioning of the NetSuite Premier Payroll Service (“Payroll Services”), for its NetSuite Basic Payroll service customers, from Perquest, its previous strategic partner, as Perquest terminated its business. As a result of providing the Payroll Services directly to its customers, the Company receives a significant amount of cash from Payroll Services customers and holds the funds for purposes of paying the appropriate taxing authorities on the customer’s behalf. At the time the Company collects the funds, legal ownership transfers to the Company. The Company holds Payroll Services customers’ tax filing deposits for the period between collection from Payroll Services customers and remittance to the applicable tax authorities. During the third quarter of 2011, the Company entered into an agreement to outsource Payroll Services to a third-party payroll processor and began the process of transitioning its existing customers to the outsourced service. The Company expects to complete this transition in the fourth quarter of 2011. As of September 30, 2011, the Company held $4.3 million on behalf of Payroll Services customers. This amount was classified as other current assets with the corresponding customer tax obligation in other current liabilities in the financial statements.

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Comprehensive Loss

Comprehensive loss consists of net loss and other comprehensive loss. Other comprehensive loss is comprised of foreign currency translation gains and (losses) and a benefit obligation related to a statutory retirement plan for its employees in the Philippines. These items have been excluded from net loss and are reflected instead in stockholders' equity. The Company's comprehensive loss was as follows for the periods presented:

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2011	2010	2011	2010
	(dollars in thousands)			
Net loss	$(24,392)	$(21,035)	$(6,929)	$(6,958)
Other comprehensive income / (loss):				
Foreign currency translation gains / (losses), net of taxes	(105)	(160)	(322)	179
Statutory retirement pay - Philippines	(127)	—	(127)	—
Comprehensive loss	(24,624)	(21,195)	(7,378)	(6,779)
Less: comprehensive loss attributable to noncontrolling interests	—	16	—	—
Comprehensive loss attributable to NetSuite Inc.	$(24,624)	$(21,179)	$(7,378)	$(6,779)

Concentration of Credit Risk and Significant Customers

Financial instruments potentially exposing the Company to concentration of credit risk consist primarily of cash and cash equivalents, restricted cash and trade accounts receivable. The Company maintains an allowance for doubtful accounts receivable balances. The allowance is based upon historical loss patterns and an evaluation of the potential risk of loss associated with problem accounts. The Company generally charges off the receivable balances of uncollectible accounts when accounts are 120 days past-due based on the account's contractual terms. Credit risk arising from accounts receivable is mitigated due to the large number of customers comprising the Company's customer base and their dispersion across various industries. As of September 30, 2011 and December 31, 2010, there were no customers that represented more than 10% of the net accounts receivable balance. There were no customers that individually exceeded 10% of the Company's revenue in any of the periods presented. As of September 30, 2011 and December 31, 2010, long-lived assets located outside the United States were not significant.

Revenue by geographic region, based on the billing address of the customer, was as follows for the periods presented:

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2011	2010	2011	2010
	(dollars in thousands)			
United States	$126,031	$105,248	$45,210	$36,041
International	46,202	35,834	15,749	13,702
Total revenue	$172,233	$141,082	$60,959	$49,743
Percentage of revenue generated outside of the United States	27%	25%	26%	28%

No single country outside the United States represented more than 10% of revenue during the nine and three months ended September 30, 2011 or 2010.

The Company maintains cash balances at several banks. Accounts located in the United States are insured by the Federal Deposit Insurance Corporation (“FDIC”), up to $250,000. Certain operating cash accounts may exceed the FDIC limits.

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Intellectual Property Rights Indemnification

The Company's arrangements include provisions indemnifying customers against liabilities if our products infringe a third-party's intellectual property rights. The Company has not incurred any costs as a result of such indemnifications and has not accrued any liabilities related to such obligations in the accompanying condensed consolidated financial statements.

Note 3. Financial Instruments

Fair Value Measurements

The Company measures certain financial assets at fair value on a recurring basis based on a fair value hierarchy that requires us to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A financial instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The three levels of inputs that may be used to measure fair value:

- Level 1 - Quoted prices in active markets for identical assets or liabilities.
- Level 2 - Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets with insufficient volume or infrequent transactions (less active markets); or model-derived valuations in which all significant inputs are observable or can be derived principally from or corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 - Unobservable inputs to the valuation methodology that are significant to the measurement of fair value of assets or liabilities.

The fair value of the Company's investments in certain money market funds approximates their face value. Such instruments are classified as Level 1 and are included in cash and cash equivalents.

The fair value of the Company's foreign currency forward contracts is based on foreign currency rates quoted by banks or foreign currency dealers and other public data sources. Such instruments are classified as Level 2 and are included in other current assets and liabilities.

For certain other financial instruments, including accounts receivable, accounts payable and other current liabilities, the carrying amounts approximate their fair value due to the relatively short maturity of these balances.

As of September 30, 2011, financial assets stated at fair value on a recurring basis were comprised of money market funds included within cash and equivalents and foreign exchange forward contracts included within other current assets and liabilities. The fair value of these financial assets was determined using the following inputs as of September 30, 2011 and December 31, 2010:

	September 30, 2011				December 31, 2010			
	Fair value measurements at reporting date using				Fair value measurements at reporting date using			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
	(in thousands)				(in thousands)			
Assets:								
Money market funds	$72,329	$—	$—	$72,329	$72,256	$—	$—	$72,256
Foreign exchange contracts	—	378		378				—
Total	$72,329	$378	$—	$72,707	$72,256	$—	$—	$72,256

Liabilities:								
Foreign exchange contracts	$—	$8	$—	$8	$—	$243	$—	$243
Total	$—	$8	$—	$8	$—	$243	$—	$243

Restricted Cash

Restricted cash totaled $509,000 and $508,000 as of September 30, 2011 and December 31, 2010, respectively, and is included in other assets. These restricted cash accounts secure letters of credit applied against certain of the Company's facility

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lease agreements. Of the $509,000 restricted cash balance as of September 30, 2011, $265,000 is classified as current other assets and $244,000 is classified as long-term other assets. The $508,000 restricted cash balance as of December 31, 2010 was classified as long-term other assets.

Balance Sheet Hedging - Hedging of Foreign Currency Assets and Liabilities

During the nine months ended September 30, 2011, the Company hedged certain of its nonfunctional currency denominated assets and liabilities to reduce the risk that earnings would be adversely affected by changes in exchange rates. Gains and losses from these forward contracts are recorded each period as a component of other income / (expense) in the consolidated statements of operations. The notional amount of derivative instruments acquired during the period was $11.8 million. The Company accounts for derivative instruments as other current assets and liabilities on the balance sheet and measures them at fair value with changes in the fair value recorded as other income / (expense). These derivative instruments do not subject the Company to material balance sheet risk due to exchange rate movements because gains and losses on these derivatives are intended to offset gains and losses on the assets and liabilities being economically hedged.

As of September 30, 2011 and December 31, 2010, the Company had the following outstanding foreign exchange forward contracts:

	September 30, 2011		December 31, 2010	
	Notional Value Sold	Notional Value Purchased	Notional Value Sold	Notional Value Purchased
	(US dollars in thousands)		(US dollars in thousands)	
British pound	$4,690	$398	$2,048	$976
Australian dollar	3,128	183	4,056	1,324
Japanese yen	200	—	3,480	—
Canadian dollar	1,051	1,087	1,658	227
Euro	528	268	410	194
Czech crown	250	—	—	—
New Zealand dollar	—	—	52	—
Total	$9,847	$1,936	$11,704	$2,721

The fair value of the derivative instruments reported on the Company's Condensed Consolidated Balance Sheet were as follows:

	Asset Derivatives			Liability Derivatives		
Derivatives and forward contracts	Balance Sheet Location	September 30, 2011 Fair Value	December 31, 2010 Fair Value	Balance Sheet Location	September 30, 2011 Fair Value	December 31, 2010 Fair Value
	(in thousands)			(in thousands)		
Foreign exchange contracts	Other current assets	$378	—	Other current liabilities	$8	$243
Total		$378	—		$8	$243

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The effect of derivative instruments on the Statement of Operations was as follows for the periods presented:

Derivatives and forward contracts	Location of net gain (loss) recognized in income on derivatives	Amount of net gain (loss) recognized in income on derivatives during the			
		Nine Months Ended September 30,		Three Months Ended September 30,	
		2011	2010	2011	2010
		(in thousands)			
Foreign exchange contracts	Other income/ (expense), net	$65	$(498)	$373	$(595)
Total		$65	$(498)	$373	$(595)

The Company has entered into all of its foreign exchange contracts with a single counterparty. During the periods such contracts are open, the Company is subject to a potential maximum amount of loss due to credit risk equal to the gross fair value of the derivative instruments if the counterparty to the instruments failed completely to perform according to the terms of the contracts. Generally, we have the right of offset for gains earned and losses incurred under these agreements. Our agreements with the counterparty do not require either party to provide collateral to mitigate the credit risk of the agreements.

Note 4. Commitments and Contingencies

The Company is involved in various legal proceedings and receives claims from time to time, arising from the normal course of business activities. The Company has accrued for estimated losses in the accompanying condensed consolidated financial statements for matters with respect to which it believes the likelihood of an adverse outcome is probable and the amount of the loss is reasonably estimable.

Note 5. Stock-based Compensation

During the first quarter of 2011, the Company granted 162,558 performance share units ("PSUs") to selected executives and other key employees. These PSUs were divided into two sets: PSUs whose vesting is based upon the Company's stock performance in relation to a group of peer companies (market-based) and PSUs whose vesting is contingent upon meeting certain company-wide performance goals (performance-based). The following company-wide performance goals were set for 2011: 60% of the shares are contingent upon meeting revenue goals, 15% of the shares are contingent upon meeting a non-GAAP measure of operating margin and 25% are contingent upon meeting a non-GAAP measure of operating cash flows. These shares are subject to term vesting conditions. The fair value and the related stock-based compensation expense of performance-based PSUs are determined based on the value of the underlying shares on the date of grant and recognized over the vesting term. During the 2011 interim financial periods, management estimates the probable number of PSUs that will be granted until the achievement of the performance goals is known by year end.

The $36.40 per share fair value of market-based PSUs on the date of grant (measurement date) is calculated using a Monte Carlo valuation model that estimates the distribution of the potential outcomes of the PSU grants based on simulated future stock prices of the peer group.

In connection with the Company's acquisition of SPC in the third quarter of 2011, the Company entered into employment agreements with SPC's two stockholders. Each of the employment agreements includes a 60,000 restricted stock unit grant which vests over the next four years in accordance with the terms of the Company' equity compensation plan. On August 2, 2011, the Company granted the new employees a total of 120,000 restricted stock units with a fair value of $4.4 million. The costs of the equity grants will be recognized as product development expense in the Company's statement of operations over the four year vesting period.

Note 6. Income Taxes

The Company has incurred annual operating losses since inception. As a result of those continuing losses, management has determined insufficient evidence exists to support that it is more likely than not that the Company will realize the benefits of its U.S. net deferred tax assets and therefore has recorded a valuation allowance to reduce the net carrying value of these deferred tax assets to zero. Accordingly, the Company has not recorded a provision for income taxes for any of the periods presented other than provisions for state and foreign income taxes.

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As of September 30, 2011, the Company had net deferred tax assets in certain foreign jurisdictions of approximately $339,000 included in other assets. Based on all available evidence, both positive and negative, management believes that it is more likely than not that the benefits of those foreign deferred tax assets will be realized in full. The Company also had deferred tax assets of $5.4 million for Japan where it had a full valuation allowance as of September 30, 2011 reducing its carrying value to zero.

The Company does not anticipate a material change in the total amount or composition of its unrecognized tax benefits within 12 months of the reporting date.
The Company files federal, state and foreign income tax returns in jurisdictions with varying statutes of limitations. Due to its net operating loss carryforwards, the Company's income tax returns generally remain subject to examination by federal and most state tax authorities. In most of the Company's significant foreign jurisdictions, the 2006 through 2010 tax years remain subject to examination by their respective tax authorities. In addition, the 2004 and 2005 tax years remain open to examination in Canada.

Note 7. Net Loss Per Common Share

Basic net loss per common share is computed by dividing net loss attributable to common stockholders by the weighted-average number of common shares outstanding during the period less the weighted-average number of unvested common shares subject to the Company’s right of repurchase. Diluted net loss per common share is computed by giving effect to all potential dilutive common shares, including options, common stock subject to repurchase and warrants. Basic and diluted net loss per common share were the same for all periods presented as the impact of all potentially dilutive securities outstanding was anti-dilutive.

The following table presents the calculation of the numerator and denominator used in the basic and diluted net loss per common share:

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2011	2010	2011	2010
	(dollars and shares in thousands, except per share amounts)			
Numerator:				
Net loss attributable to NetSuite Inc. common stockholders	$(24,392)	$(21,021)	$(6,929)	$(6,958)
Denominator:				
Weighted-average number of common shares outstanding	66,459	63,519	67,477	63,971
Less: Weighted-average number of common shares subject to repurchase	—	(6)	—	(6)
Weighted-average number of common shares outstanding used in computing basic and diluted net loss per common share	66,459	63,513	67,477	63,965
Net loss per common share, basic and diluted	$(0.37)	$(0.33)	$(0.10)	$(0.11)

The Company’s unvested restricted stock and restricted stock units (“RSUs”) do not contain non-forfeitable rights to dividends and dividend equivalents. As such, unvested shares of restricted stock and RSUs are not participating securities and the Company is not required to use the two-class method to calculate diluted earnings per share in periods when the Company has net income.

Outstanding common stock owned by employees and subject to repurchase by the Company is not included in the calculation of the weighted-average shares outstanding for basic and diluted earnings per share.

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The following table presents the weighted average potential shares that are excluded from the computation of diluted net loss per common share for the periods presented because including them would have had an anti dilutive effect:

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2011	2010	2011	2010
	(Shares in thousands)			
Options to purchase shares of common stock	5,552	6,611	5,035	6,611
Unvested RSUs, PSUs and restricted stock awards	4,243	4,118	4,204	4,391
Warrants to purchase shares of common stock	—	7	—	—
Common stock subject to repurchase	—	6	—	6
Total	9,795	10,742	9,239	11,008

Note 8. Related Party Transactions

In November 2009 the Company entered into a license agreement with Trustwave Holdings Inc. (“Trustwave”). The Company's President and Chief Executive Officer, Zachary Nelson became a member of TrustWave's board of directors in June 2011. The Company and Trustwave have renewed the license agreement and the Company has sold additional services to Trustwave at various points in time. In September 2011, Trustwave renewed the license and support services for another year for $138,000. During the third quarter of 2011, Trustwave paid the Company $31,000 for license and support services.

In September 2007, the Company entered into an agreement with IRON Solutions LLC under which IRON Solutions became a partner and reseller of the NetSuite product. In June 2008, IRON Solutions was acquired in part by StarVest Partners LLC. Deborah Farrington, a member of the Company's board of directors, is also a founding principal of StarVest Partners. IRON Solutions also has a preexisting services agreement with the Company. In the third quarter of 2011, IRON Solutions purchased additional subscription and professional services from the Company for $125,000. The Company will provide these services to IRON Solutions over the next three years. During the third quarter of 2011, the Company received a $49,000 payment for subscription and professional services provided to IRON Solutions.

In March 2008 the Company entered into a license agreement with Ideeli Inc. (“Ideeli”). A member of the Company's board of directors, Deborah Farrington, is a general partner of StarVest Partners, L.P and in December 2009 another general partner of StarVest Partners, L.P. became a member of the board of directors of Ideeli. The Company and Ideeli have renewed the license agreement and the Company has sold additional services to Ideeli at various points in time. In September 2011, Ideeli renewed the license and support services for seven months for $171,000. During the third quarter of 2011, Ideeli paid the Company $15,000 for license and support services.

In August 2006, the Company entered into a license agreement with SolarWinds, Inc. (“SolarWinds”). A member of the Company’s board of directors, Kevin Thompson, is the President and Chief Executive Officer of SolarWinds. The Company and SolarWinds have renewed the licensing agreement and the Company has sold to SolarWinds additional services at various points in time. In March 2011, SolarWinds renewed the license and support services for two years with an option to extend for a third year. SolarWinds will pay the Company $1.1 million in the aggregate over two years for its services. During the second quarter of 2011, the Company received a $560,000 payment for the license and support agreement renewed in the first quarter of 2011.

In August 2006, the Company entered into a license agreement with a division of MetLife, Inc. (“MetLife”). A member of the Company’s Board of Directors, Catherine R. Kinney, became a member of MetLife’s board in April 2009. In March 2011, MetLife entered into a professional services agreement with the Company for which MetLife will pay the Company approximately $97,500. During the third quarter of 2011, the Company received a $30,000 payment from MetLife.

In April 2011, the Company amended its sponsorship agreement with the Oakland Athletics ("the Athletics"). Under the terms of the amendment, the Company will pay the Athletics $473,000 over the three year term of the agreement to extend certain sponsorship benefits through 2013. During the first nine months of 2011, the Company paid the Athletics $408,000 in accordance with the terms of its sponsorship agreement with the organization. William Beane III, the General Manager of the Athletics, became a member of the Company's board of directors in January 2007.

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In January 2011, the Company's Chief Technology Officer and Chairman of the Board, purchased property from an entity affiliated with a principal stockholder ("seller") for $8.0 million. The seller financed the transaction with a nine year loan. The Company analyzed the transaction and determined that the fair value of the property approximated the fair value of the loan. Consequently, the Company determined there is no compensation expense or a related capital contribution associated with this transaction.

In May 2011, the Company purchased an integrated database storage system from Oracle USA, Inc., an affiliate of Oracle Corporation, for $456,000. During the third quarter of 2011, the Company paid the $456,000 outstanding balance in full. Additionally, during the nine months ended September 30, 2011, the Company paid Oracle Financing $2.0 million which included $1.2 million related to a support services agreement renewed in May 2011, $734,000 related to software licenses and $82,000 related to interest in connection with a related party note entered into in May of 2010. Lawrence J. Ellison, who beneficially owns a majority of the Company's common stock, is the Chief Executive Officer, a director and a principal stockholder of Oracle Corporation.

Additional related party transactions entered into prior to December 31, 2010 are described in the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2010 filed on March 3, 2011.

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

The following discussion and analysis is intended to provide greater details of our results of operations and financial condition and should be read in conjunction with our condensed consolidated financial statements and the notes thereto included elsewhere in this document and the discussion contained in our Annual Report on Form 10-K for the year ended December 31, 2010 as filed with the SEC on March 3, 2011. Certain statements in this Quarterly Report constitute forward-looking statements and as such, involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. Such forward-looking statements include any expectation of earnings, revenues or other financial items; any statements of the plans, strategies and objectives of management for future operations; factors that may affect our operating results; statements concerning new products or services; statements related to adding employees; statements related to future capital expenditures; statements related to future economic conditions or performance; statements related to the integration of acquired companies; statements as to industry trends and other matters that do not relate strictly to historical facts or statements of assumptions underlying any of the foregoing. These statements are often identified by the use of words such as "anticipate," "believe," "continue," "could," "estimate," "exp "intend," "may," or "will," and similar expressions or variations. Such forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to those discussed in the section titled "Risk Factors" included in Item 1A of Part II of this Quarterly Report on Form 10-Q, and the risks discussed in our other SEC filings.

We urge you to consider these factors carefully in evaluating the forward-looking statements contained in this Quarterly Report on Form 10-Q. These statements are based on the beliefs and assumptions of our management based on information currently available to management. The forward-looking statements included in this Quarterly Report are made only as of the date of this Quarterly Report. All subsequent written or oral forward-looking statements attributable to our company or persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. We do not undertake, and specifically disclaim, any obligation to update any forward-looking statements to reflect the occurrence of events or circumstances after the date of such statements except as required by law.

Overview

We are the industry's leading provider of cloud-based financials/ ERP software suites. In addition to financials/ERP software suites, we offer a broad suite of applications, including accounting, CRM, PSA and Ecommerce that enable companies to manage most of their core business operations in our single integrated suite. Our "real-time dashboard" technology provides an easy-to-use view into up-to-date, role-specific business information. We also offer customer support and professional services related to supporting and implementing our suite of applications. We deliver our suite over the Internet as a subscription service using the software-as-a-service ("SaaS") model.

In 1999, we released our first application, NetLedger, focused on accounting applications. We then released Ecommerce functionality in 2000 and CRM and sales force automation functionality in 2001. In 2002, we released our next generation suite under the name NetSuite and we have regularly added features and functionality. In 2008, we acquired OpenAir and in 2009 we acquired QuickArrow, both of which offer professional services automation and project portfolio management products.

Our headquarters are located in San Mateo, California. We were incorporated in California in September 1998 and reincorporated in Delaware in November 2007. We conduct our business worldwide, with international locations in Canada, Europe, Asia and Australia.

Key Components of Our Results of Operations

Revenue

Our revenue has grown from $17.7 million during the year ended December 31, 2004 to $193.1 million during the year ended December 31, 2010.

We generate sales directly through our sales team and, to a lesser extent, indirectly through channel partners. We sell our service to customers across a broad spectrum of industries, and we have tailored our service for wholesalers/distributors, manufacturers, e-tailers, services companies and software companies. The primary target customers for our service are medium-sized businesses and divisions of large companies. An increasing percentage of our customers and our revenue have been derived from larger businesses within this market. For the nine and three months ended September 30, 2011 , we did not have any single customer that accounted for more than 3% of our revenue.

We are pursuing a number of strategies that we believe will enable us to continue to grow. The goals of those strategic objectives are to continue to move up-market; to increase use of NetSuite as a platform; and to extend the verticalization of our product line. Although we have made progress towards our goals in recent periods, there are still many areas where we believe that we can continue to grow. To achieve these goals, we are focused on the following initiatives:

- Growth of sales of OneWorld, our platform for ERP, CRM and Ecommerce capabilities in multi-currency environments across multiple subsidiaries and legal entities, which supports the needs of large, standalone companies, and divisions of very large enterprises;
- Strengthening our professional services automation verticalization with the continued expansion of functionality for Services Resource Planning (SRP) in NetSuite OpenAir, NetSuite and NetSuite OneWorld products; and
- Developing our SuiteCloud ecosystem to enable third parties to extend our offerings with their vertical expertise.

We experience competitive pricing pressure where our products are compared with solutions that address a narrower range of customer needs or are not fully integrated (for example, when compared with Ecommerce or CRM stand-alone solutions). In addition, since we sell primarily to medium-sized businesses, we also face pricing pressure in terms of the more limited financial resources or budgetary constraints of many of our target customers. We do not currently experience significant pricing pressure from competitors that offer a similar on-demand, integrated business management suite.

We sell our application suite pursuant to subscription agreements. The duration of these agreements is generally one year. We rely in part on a large percentage of our customers to renew their agreements to drive our revenue growth. Our customers have no obligation to renew their subscriptions after the expiration of their subscription period. In the aggregate, more than 90% of the professional services component of the arrangements with customers is performed within 300 days of entering into a contract with the customer.

Our subscription agreements provide service level commitments of 99.5% uptime per period, excluding scheduled maintenance. The failure to meet this level of service availability may require us to credit qualifying customers up to the value of an entire month of their subscription and support fees. In light of our historical experience with meeting our service level commitments, we do not currently have any reserves on our balance sheet for these commitments.

We generally invoice our customers in advance in annual or quarterly installments, and typical payment terms provide that our clients pay us within 30 to 60 days of invoice. Amounts that have been invoiced where the customer has a legal obligation to pay are recorded in accounts receivable and deferred revenue. As of September 30, 2011, we had deferred revenue of $97.0 million.

In most instances, revenue from a new customer acquisition is generated under sales agreements with multiple elements comprised of subscription and support revenue for access to our application suite and customer support, and professional service and other revenue for consulting services. We evaluate each element in a multiple-element arrangement to determine whether it represents a separate unit of accounting. An element constitutes a separate unit of accounting when the delivered item has standalone value and delivery of the undelivered element is probable and within our control. Subscription and support have standalone value because we routinely sell it separately. Professional services have standalone value because we have sold professional services separately and there are several third party vendors that routinely provide similar professional services to our customers on a standalone basis. We allocate revenue to each element in an arrangement based on a selling price hierarchy. The selling price for a deliverable is based on its vendor-specific objective evidence (“VSOE”), if available, third-party evidence (“TPE”), if VSOE is not available, or estimated selling price (“ESP”), if neither VSOE nor TPE is available. We have been unable to establish VSOE or TPE for the elements of our sales arrangements. Therefore, we establish the ESP for each element primarily by considering the weighted average of actual sales prices of professional services sold on a standalone basis and subscription and support including various add-on modules when sold together without professional services, and other factors such as gross margin objectives, pricing practices and growth strategy. The consideration allocated to subscription and support is recognized as revenue over the contract period. The consideration allocated to professional services and other revenue is recognized using the percentage-of-completion method.

The total arrangement fee for a multiple element arrangement is allocated based on the relative ESP of each element. However, since the professional services are generally completed prior to completion of delivery of subscription and support services, the revenue recognized for professional services in a given reporting period does not include fees subject to delivery of subscription and support services. This results in the recognition of revenue for professional services that is generally no greater than the contractual fees for those professional services.

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For single element sales agreements, subscription and support revenue is recognized ratably over the contract term beginning on the provisioning date of the contract, and professional services revenue is recognized using the percentage-of-completion method.

As part of our overall growth, we expect the percentage of our revenue generated outside of the United States to increase as we invest in and enter new markets. Revenue by geographic region, based on the billing address of the customer, was as follows for the periods presented:

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2011	2010	2011	2010
	(dollars in thousands)			
United States	$ 126,031	$ 105,248	$ 45,210	$ 36,041
International	46,202	35,834	15,749	13,702
Total revenue	$ 172,233	$ 141,082	$ 60,959	$ 49,743
Percentage of revenue generated outside of the United States	27 %	25 %	26 %	28 %

Employees

The number of full-time employees as of September 30, 2011 was 1,243 as compared to 1,084 at December 31, 2010 and 1,022 at September 30, 2010. As of September 30, 2011, our headcount included 376 employees in sales and marketing; 510 employees in operations; professional services, training and customer support; 231 employees in product development; and 126 employees in a general and administrative capacity.

Cost of Revenue

Subscription and support cost of revenue primarily consists of costs related to hosting our application suite, providing customer support, data communications expenses, personnel and related costs of operations, stock-based compensation, software license fees, outsourced subscription services, costs associated with website development activities, allocated overhead, intangible asset amortization expense associated with capitalized internal use software and acquired developed technology and related plant and equipment depreciation and amortization expenses.

Professional services and other cost of revenue primarily consists of costs related to personnel and related costs of operations, external consultants, stock-based compensation and allocated overhead.

We allocate overhead such as rent, information technology costs and employee benefit costs to all departments based on headcount. As such, general overhead expenses are reflected in cost of revenue and each operating expense category.
We expect cost of revenue to remain flat as a percentage of revenue over the near term; however, it could fluctuate period to period depending on the growth of our professional services business and any associated increased costs relating to the delivery of professional services and the timing of significant expenditures.

Operating Expenses - Product Development

Product development expenses primarily consist of personnel and related costs for our product development employees and executives, including salaries, stock-based compensation, employee benefits and allocated overhead. Our product development efforts have been devoted primarily to increasing the functionality and enhancing the ease of use of our on-demand application suite, as well as localizing our product for international use. A key component of our strategy is to expand our business internationally. This will require us to conform our application suite to comply with local regulations and languages, causing us to incur additional expenses related to translation and localization of our application for use in other countries.

We expect product development expenses to increase in absolute dollars and remain flat as a percentage of revenue as we continue to extend our service offerings in other countries and as we expand and enhance our application suite technologies. Such expenses may vary due to the timing of these offerings and technologies.

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Operating Expenses - Sales and Marketing

Sales and marketing expenses primarily consist of personnel and related costs for our sales and marketing employees and executives, including wages, benefits, bonuses, commissions and training, stock-based compensation, commissions paid to our channel partners, the cost of marketing programs such as on-line lead generation, promotional events, webinars and other meeting costs, amortization of intangible assets related to trade name and customer relationships and allocated overhead. We market and sell our application suite worldwide through our direct sales organization and indirect distribution channels such as strategic resellers. We capitalize and amortize our direct and channel sales commissions over the period the related revenue is recognized.
We believe we have sufficient sales and marketing staff to meet our revenue goals for the remainder of 2011. We expect to continue to invest in sales and marketing to pursue new customers and expand relationships with existing customers. As such, we expect our sales and marketing expenses to increase in terms of absolute dollars, but slightly decrease as a percentage of total revenue for the remainder of 2011.

Operating Expenses - General and Administrative

General and administrative expenses primarily consist of personnel and related costs for executive, finance, human resources and administrative personnel, stock-based compensation, legal and other professional fees, other corporate expenses and allocated overhead.
We expect our general and administrative expenses to increase in terms of absolute dollars and decrease as a percentage of total revenue as we continue to expand our business.

Income Taxes

Since inception, we have incurred annual operating losses and, accordingly, have not recorded a provision for income taxes for any of the periods presented other than provisions for state and foreign income taxes.

Critical Accounting Policies and Judgments

Our condensed consolidated financial statements are prepared in accordance with GAAP. The preparation of these condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, costs and expenses and related disclosures. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. In many instances, we could have reasonably used different accounting estimates, and in other instances changes in the accounting estimates are reasonably likely to occur from period-to-period. Accordingly, actual results could differ significantly from the estimates made by our management. To the extent that there are material differences between these estimates and actual results, our future financial statement presentation, financial condition, results of operations and cash flows will be affected.

In many cases, the accounting treatment of a particular transaction is specifically dictated by GAAP and does not require management's judgment in its application, while in other cases, significant judgment is required in selecting among available alternative accounting standards that allow different accounting treatment for similar transactions. We consider these policies requiring significant management judgment to be critical accounting policies. These critical accounting policies are:

- Revenue recognition;
- Internal use software and website development costs;
- Deferred commissions;
- Accounting for stock-based compensation; and
- Goodwill and other intangible assets

There have been no significant changes in our critical accounting policies and estimates during the first nine months of 2011 as compared to the critical accounting policies and estimates disclosed in "Management's Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies and Judgments" included in our Annual Report on Form 10-K for the year ended December 31, 2010 filed on March 3, 2011. In addition, please see Note 2 of Notes to the Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q and Note 2 of the Notes to Consolidated Financial Statements included in our 2010 Annual Report on Form 10-K filed on March 3, 2011 for a description of our accounting policies.

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Results of Operations

Revenue, Cost of Revenue and Gross Margin

Information about revenue, cost of revenue, gross profit and gross margin was as follows for the periods presented:

	Nine months ended September 30,		Three months ended September 30,	
	2011	2010	2011	2010
	(dollars in thousands)			
Revenue:				
Subscription and support	$ 145,388	$ 119,735	$ 51,334	$ 41,834
Professional services and other	26,845	21,347	9,625	7,909
Total revenue	172,233	141,082	60,959	49,743
Cost of revenue (1):				
Subscription and support	24,342	20,038	8,627	6,848
Professional services and other	27,450	26,090	9,658	8,546
Total cost of revenue	51,792	46,128	18,285	15,394
Gross profit	$ 120,441	$ 94,954	$ 42,674	$ 34,349
Gross margin	70 %	67 %	70 %	69 %

(1) Includes stock-based compensation expense and amortization of intangible assets of:				
Cost of revenue:				
Subscription and support	$ 2,698	$ 2,682	$ 807	$ 990
Professional services and other	3,055	2,785	1,067	1,042
	$ 5,753	$ 5,467	$ 1,874	$ 2,032

Nine Months Ended September 30, 2011 as Compared to the Nine Months Ended September 30, 2010

Revenue for the nine months ended September 30, 2011 increased $31.2 million, or 22%, compared to the same period in 2010.

Subscription and support revenue: Subscription and support revenue for the nine months ended September 30, 2011 increased $25.7 million, or 21%, compared to the same period in 2010. The increase was primarily the result of a $23.2 million increase in revenue resulting from the acquisition of new customers and the continued adoption of OneWorld and a $2.5 million increase in revenue from existing customers.

Professional services and other revenue: Professional services and other revenue for the nine months ended September 30, 2011 increased $5.5 million, or 26%, compared to the same period in 2010. The increase was primarily the result of an $18.0 million increase in revenue resulting from the acquisition of new customers, an increase in productivity, a slight increase in the average hourly rate charged to customers for professional services and the recognition of $541,000 in revenue on a single engagement where revenue recognition was delayed until the completion of the project during the nine months ended September 30, 2011 when compared to the same period in 2010. The increase in professional services and other revenue was partially offset by a $12.5 million decrease in revenue from existing customers related to services purchased in connection with the initial implementation of our product in 2010 that did not recur for those customers in 2011.

Revenue generated outside of the United States was $46.2 million, or 27%, of our revenue, during the nine months ended September 30, 2011, as compared to $35.8 million, or 25%, during the same period in 2010. Revenue generated outside of the United States increased primarily due to our increased international sales efforts particularly in Australia.

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Cost of revenue for the nine months ended September 30, 2011 increased $5.7 million, or 12%, compared to the same period in 2010.

Subscription and support cost of revenue: Subscription and support cost of revenue for the nine months ended September 30, 2011 increased $4.3 million, or 21%, compared to the same period in 2010. The increase was primarily the result of a $1.8 million increase in personnel costs resulting from an increase in headcount, an increase in annual salaries, a $1.2 million increase in data center expenses resulting from an increase in capacity, a $849,000 increase in depreciation expense related to data center equipment acquired over the past year and a $696,000 increase in overhead expense allocations resulting from an increase in headcount, partially offset by a $375,000 decrease in amortization expense resulting from certain intangible assets becoming fully amortized.

Professional services and other cost of revenue: Professional services and other cost of revenue for the nine months ended September 30, 2011 increased $1.4 million, or 5%, compared to the same period in 2010. The increase was primarily the result of a $771,000 increase in external consultant costs partially related to outsourced subscription services payments,a $382,000 increase in billable travel and a $238,000 increase in personnel costs related to an increase in headcount, payroll taxes, employee benefits and incentive bonuses.

Our gross margin increased to 70% during the nine months ended September 30, 2011 compared to 67% for the same period in 2010. The increase resulted primarily from professional services. The profitability of our professional service engagements increased during the first nine months of 2011 compared to the same period in the prior year primarily due to an increase in productivity and an increase in the average hourly rate charged to customers. We also recognized revenue on an engagement where revenue was delayed until completion of the project.

Three Months Ended September 30, 2011 as Compared to the Three Months Ended September 30, 2010

Revenue for the three months ended September 30, 2011 increased $11.2 million, or 23%, compared to the same period in 2010.

Subscription and support revenue: Subscription and support revenue for the three months ended September 30, 2011 increased $9.5 million, or 23%, compared to the same period in 2010. The increase was primarily the result of a $8.2 million increase in revenue resulting from the acquisition of new customers and the continued adoption of OneWorld, and a $1.3 million increase in revenue from existing customers.

Professional services and other revenue: Professional services and other revenue for the three months ended September 30, 2011 increased $1.7 million, or 22%, compared to the same period in 2010. The increase was primarily the result of a $6.5 million increase in revenue resulting from the acquisition of new customers and a slight increase in the average hourly rate charged to customers for professional services. The increase in professional services and other revenue was partially offset by a $4.7 million decrease in revenue from existing customers related to services purchased in connection with the initial implementation of our product in 2010 that did not recur for those customers in 2011.

Revenue generated outside of the United States was $15.7 million, or 26%, of our revenue, during the three months ended September 30, 2011, as compared to $13.7 million, or 28%, during the same period in 2010. Revenue generated outside of the United States increased primarily due to our increased international sales efforts particularly in Australia.

Cost of revenue for the three months ended September 30, 2011 increased $2.9 million, or 19%, compared to the same period in 2010.

Subscription and support cost of revenue: Subscription and support cost of revenue for the three months ended September 30, 2011 increased by $1.8 million, or 26%, compared to the same period in 2010. The increase was primarily the result of a $951,000 increase in personnel costs resulting from an increase in headcount and an increase in annual salaries, a $604,000 increase in data center expenses resulting from an increase in capacity and outsourced subscription service costs, a $378,000 increase in depreciation expense related to the development of our data center infrastructure and a $116,000 increase in overhead and other expenses, partially offset by a $249,000 decrease in amortization expense resulting from certain intangible assets becoming fully amortized.

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Professional services and other cost of revenue: Professional services and other cost of revenue for the three months ended September 30, 2011 increased by $1.1 million, or 13%, compared to the same period in 2010. The increase was primarily the result of a $451,000 increase in personnel costs related to payroll taxes and employee benefits, a $435,000 increase in external consultant costs and a $271,000 increase in overhead allocations including other operational expenses. We view professional services as an investment in customer success to ensure that we continue to receive recurring subscription and support revenue.

Our gross margin was 70% during the three months ended September 30, 2011, a 1% increase from the same period in 2010.

Operating Expenses

Operating expenses were as follows for the periods presented:

	Nine months ended September 30,					
	2011			2010		
	Amount	% of revenue		Amount	% of revenue	
	(dollars in thousands)					
Operating expenses (1):						
Product development	$31,615	18	%	$26,451	19	%
Sales and marketing	88,209	51	%	66,623	47	%
General and administrative	23,839	14	%	21,773	15	%
Total operating expenses	$143,663	83	%	$114,847	81	%

	Three months ended September 30,					
	2011			2010		
	Amount	% of revenue		Amount	% of revenue	
	(dollars in thousands)					
Operating expenses (1):						
Product development	$11,257	18	%	$9,482	19	%
Sales and marketing	30,279	50	%	24,363	49	%
General and administrative	7,622	13	%	7,110	14	%
Total operating expenses	$49,158	81	%	$40,955	82	%

(1) Includes stock-based compensation expense, amortization of acquisition-related intangible, transaction costs for business combinations and costs associated with the settlement of a patent dispute as follows:

	Nine months ended September 30,		Three months ended September 30,	
	2011	2010	2011	2010
	(dollars in thousands)			
Product development	$8,699	$7,328	$3,422	$2,724
Sales and marketing	9,909	7,349	3,402	2,753
General and administrative	7,408	6,575	2,089	2,028
Total	$26,016	$21,252	$8,913	$7,505

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Nine Months Ended September 30, 2011 as Compared to the Nine Months Ended September 30, 2010

Product development expenses for the nine months ended September 30, 2011 increased $5.2 million, or 20%, as compared to the same period in 2010. The increase was primarily the result of a $5.8 million increase in personnel costs resulting from an increase in the number of employees, annual salary increases, incentive bonuses and an increase in stock-based compensation. The increase in personnel costs includes a $1.4 million increase in stock-based compensation resulting primarily from the issuance of annual equity awards to employees during the nine months ended September 30, 2011. The increase in headcount also increased the overhead expense allocation to product development by $575,000. These cost increases were partially offset by a $956,000 decrease in external consulting costs which resulted from a language translation project completed in 2010, and a $368,000 increase in capitalized product development costs associated with the release of new product functionality.

Sales and marketing expenses for the nine months ended September 30, 2011 increased $21.6 million, or 32%, as compared to the same period in 2010. The increase was primarily the result of a $19.2 million increase in personnel costs, a $1.9 million increase in overhead allocation expense and a $1.2 million increase in marketing expenses. The increase in personnel costs related primarily to increases in payroll and commission expenses resulting from an increase in headcount and better than expected sales performance. Additionally, personnel costs include a $2.9 million increase in stock-based compensation resulting primarily from the issuance of annual equity awards to employees during the nine months ended September 30, 2011. These increases were partially offset by a $662,000 decrease in primarily other marketing and amortization expense. Amortization expense decrease because certain intangible assets becamefully amortized during the period.

General and administrative expenses for the nine months ended September 30, 2011 increased $2.1 million, or 9%, as compared to the same period in 2010. The increase was primarily the result of a $1.7 million increase in personnel costs, a $1.3 million increase in overhead costs primarily related to our facility operations, $720,000 in costs associated with the settlement of a patent dispute and $580,000 in other operational costs partially offset by $2.2 million in overhead allocations to other departments which increased from the prior year due to increased headcount in other departments. The increase in personnel costs resulted from annual salary increases, incentive bonuses and increases in other payroll costs.

Three Months Ended September 30, 2011 as Compared to the Three Months Ended September 30, 2010

Product development expenses for the three months ended September 30, 2011 increased $1.8 million, or 19%, as compared to the same period in 2010. The increase was primarily the result of a $2.3 million increase in personnel costs. Personnel costs increased due to an increase in headcount, employee benefits and recruiting costs. The increase in personnel costs was partially offset by a $749,000 decrease in external consultant costs which resulted from a language translation project completed in 2010.

Sales and marketing expenses for the three months ended September 30, 2011 increased $5.9 million, or 24%, as compared to the same period in 2010. The increase was primarily the result of a $6.0 million increase in personnel costs and a $413,000 increase in overhead allocation expenses, partially offset by a $271,000 decrease in marketing and other operational expenses. The increase in personnel costs related to an increase in headcount, commission expenses associated with better than expected sales and stock-based compensation expense associated with the issuance of annual equity awards to employees.

General and administrative expenses for the three months ended September 30, 2011 increased $512,000, or 7%, as compared to the same period in 2010. The increase was primarily due to a $408,000 increase in personnel costs that resulted from an increase in headcount, annual salaries and payroll taxes.

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Non-operating Items

Non-operating items, including interest income and expense, other expense, net, income taxes and the effect of noncontrolling interest, was as follows for the periods presented:

	Nine months ended September 30,			
	2011		2010	
	Amount	% of revenue	Amount	% of revenue
	(dollars in thousands)			
Interest income	$127	—%	$159	—%
Interest expense	(104)	—%	(100)	—%
Other expense, net	(130)	—%	(499)	—%
Provision for income taxes	1,063	1%	702	—%
Noncontrolling interest	—	—%	14	—%

	Three Months Ended September 30,			
	2011		2010	
	Amount	% of revenue	Amount	% of revenue
	(dollars in thousands)			
Interest income	$36	—%	$66	—%
Interest expense	(39)	—%	(43)	—%
Other expense, net	(114)	—%	(130)	—%
Provision for income taxes	328	1%	245	—%

Net other expense for the nine months ended September 30, 2011 decreased $369,000 as compared to the same period in 2010. The decrease in net other expense is primarily related to a write-off of a loan for a principal amount of $250,000 to a partner in 2010.

Liquidity and Capital Resources

As of September 30, 2011, our primary sources of liquidity were our cash and cash equivalents totaling $126.8 million and $30.1 million in accounts receivable, net of allowance.

In the nine months ended September 30, 2011, cash flows from operations were $24.6 million. Although we have had positive operating cash flows for 10 consecutive quarters, the possibility remains that we could return to a position of negative operating cash flows in a future period. Despite the possibility of such fluctuations in operating cash outflows, management believes its current cash and cash equivalents are sufficient for the next 12 months and into the foreseeable future to meet our operating cash flow needs.

We intend to use our cash for general corporate purposes, including potential future acquisitions or other transactions. Further, we expect to incur additional expenses in connection with our international expansion. We believe that our cash and cash equivalents are adequate to fund those anticipated activities.

While we believe that our uncommitted current working capital and anticipated cash flows from operations will be adequate to meet our cash needs for daily operations and capital expenditures for at least the next 12 months, we may elect to raise additional capital through the sale of additional equity or debt securities, obtain a credit facility or sell certain assets. If additional funds are raised through the issuance of additional debt securities, these securities could have rights, preferences and privileges senior to holders of common stock, and terms of any debt could impose restrictions on our operations. The sale of additional equity or convertible debt securities could result in additional dilution to our stockholders and additional financing may not be available in amounts or on terms acceptable to us. As we believe that our cash and cash equivalents are adequate to fund our operating and investing cash flow needs for at least the next 12 months, we have not found it necessary to reassess our capacity to generate cash from financing cash flows in the current economic climate. If additional financing becomes necessary

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and we are unable to obtain the additional funds, we may be required to reduce the scope of our planned product development and marketing efforts, potentially harming our business, financial condition and operating results. In the meantime, we intend to continue to manage our cash in a manner designed to ensure that we have adequate cash and cash equivalents to fund our operations as well as future acquisitions, if any.

Restricted cash consisting of letters of credit for our facility lease agreements is included in other assets which totaled $509,000 and $508,000 as of September 30, 2011 and December 31, 2010, respectively. Of the $509,000 restricted cash balance as of September 30, 2011, $265,000 is classified as short-term other assets and $244,000 is classified as current other assets. The $508,000 restricted cash balance as of December 31, 2011 was classified as long-term other assets.

As of September 30, 2011, we had an accumulated deficit of $335.9 million. We have funded this deficit primarily through the net proceeds raised from the sale of our capital stock and proceeds from operations.

A summary of our cash flow activities were as follows for the periods presented:

	Nine months ended September 30,	
	2011	2010
	(dollars in thousands)	
Net cash provided by operating activities	$ 24,577	$ 13,671
Net cash used in investing activities	(9,337)	(4,433)
Net cash provided by / (used in) financing activities	7,377	(4,549)
Effect of exchange rate changes on cash and cash equivalents	(138)	74
Net change in cash and cash equivalents	$ 22,479	$ 4,763

Cash provided by operating activities was driven by sales of our application suite and costs incurred to deliver that service. The timing of our billings and collections relating to our sales and the timing of the payment of our liabilities have a significant impact on our cash flows. Cash flows from operations increased during the nine months ended September 30, 2011 as compared to the same period in 2010 primarily as a result of an increase in revenue and deferred revenue offset by an increase in commissions paid.

Cash used in investing activities during the nine months ended September 30, 2011 increased from the same period in 2010 primarily due to the acquisition of a small private company, developed product technology, an increase in capital expenditures for property and equipment and an increase in capitalized internal use software. During the third quarter of 2011, we paid $1.1 million in connection with the purchase of a small software on-demand company, and in the second quarter of 2011, we paid $650,000 in connection with the purchase of an on-line property, plant and equipment solution from a small private company.

The net cash provided by financing activities for the nine months ended September 30, 2011 was primarily related to proceeds from the issuance of common stock as a result of the exercise of stock options. During the nine months ended September 30, 2010, financing activities included a payment for the purchase of the remaining ownership equity in NetSuite KK, payments to acquire shares upon vesting of RSUs to settle employee withholding liability and payments on capital leases.

Off Balance Sheet Arrangements and Contractual Obligations

During the nine months ended September 30, 2011 and 2010, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off balance sheet arrangements or other contractually narrow or limited purposes.

During the third quarter of 2011, we entered into a patent cross licensing agreement with a large technology company, which includes payments from us totaling $3.0 million. In the third quarter of 2011, we paid $1.0 million relating to this agreement and over the next two years, we will pay the remaining two $1.0 million annual payments.

During the second quarter of 2011, we entered into a lease agreement for a product development facility in the Czech Republic. Total lease payments of approximately $2.5 million related to this facility will be recorded as an operating expense over the next eight years unless we exercise our option to terminate the lease after five years.

During the second quarter of 2011, we entered into a lease agreement to relocate our Japan sales and operations office to another building within Japan. Total lease payments of approximately $394,000 related to this facility will be recorded as an operating expense over the next two years.

During the first quarter of 2011, we entered into a lease agreement for equipment to be placed in service in our data operations. The agreement requires total payments of approximately $758,000 over the next three years. Of the $758,000 in total payments, $729,000 will be capitalized in property and equipment and depreciated over three years.

ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Sensitivity

We had cash and cash equivalents of $126.8 million as of September 30, 2011. These amounts were held primarily in money market funds.

Cash and cash equivalents are held for working capital purposes, and restricted cash amounts are held as security against various lease obligations. Due to the short term nature of these investments, we believe that we do not have any material exposure to changes in the fair value of our investment portfolio as a result of changes in interest rates.

Foreign Currency Risk

Our results of operations and cash flows are subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the British Pound Sterling, Canadian Dollar, Australian Dollar, Philippine Peso and the Czech Koruna. Our revenue is generally denominated in the local currency of the contracting party. The majority of our invoicing relates to sales occurring in the United States and therefore is denominated in U.S. dollars. We have an increasing percentage of sales denominated in foreign currencies including, but not limited to, the local currencies of Australia, the United Kingdom and Canada. Our expenses are incurred primarily in the United States, Canada, the Philippines, Australia and the United Kingdom, with a small portion of expenses incurred in other countries where our international sales and operations offices are located. Our results of operations and cash flows are, therefore, subject to fluctuations due to changes in foreign currency exchange rates. During the nine and three months ended September 30, 2011, the U.S. dollar weakened against the foreign currencies that our invoicing and operational expenses are denominated in by approximately 7% and 5%, respectively, when compared to the same period in the prior year. For the three months ended September 30, 2011, the fluctuation in foreign currency rates positively affected our income by approximately $172,000; however, for nine months ended September 30, 2011, the fluctuation in foreign currency rates negatively affected our income by approximately $553,000. Even though the U.S. dollar weakened against foreign currencies during third quarter of 2011 compared to the same period in the prior year, the effect on our income was positive because third quarter 2011 revenue denominated in foreign currencies exceeded expenses denominated in foreign currencies resulting in a net gain related to the changes in the foreign currency rate.

During the nine and three months ended September 30, 2011, we continued a hedging program initiated in 2008 to limit the exposure of foreign currency risk resulting from the revaluation of foreign denominated assets and liabilities through the use of forward exchange contracts. See “Balance Sheet Hedging - Hedging of Foreign Currency Assets and Liabilities” in Note 3 (Financial Instruments) under the heading “Notes to Condensed Consolidated Financial Statements” of Part 1, Item 1, “Financial Statements” herein for further disclosures.

Fair Value of Financial Instruments

We do not have material exposure to market risk with respect to investments, as our investments consist primarily of highly liquid investments purchased with a remaining maturity of three months or less. We do not use derivative financial instruments for speculative or trading purposes. However, this does not preclude our adoption of specific hedging strategies in the future.

ITEM 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

An evaluation was performed by management, with the participation of our CEO and our Chief Financial Officer (“CFO”), of the effectiveness of our disclosure controls and procedures as of September 30, 2011 (as defined in Rules 13a-15(e) and 15d - 15(e) under the Securities Exchange Act of 1934, as amended). Disclosure controls and procedures are controls

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and procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the 1934 Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Based on that evaluation, our CEO and CFO have concluded that as of September 30, 2011, our disclosure controls and procedures are effective, to provide reasonable assurance that information required to be disclosed by us in reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the SEC's rules and forms and that such information is accumulated and communicated to management including the CEO and CFO, as appropriate, to allow timely decisions regarding required disclosures.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations of Internal Controls

Our management, including our CEO and CFO, does not expect that our disclosure controls and procedures or our internal controls will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of a simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

PART II – OTHER INFORMATION

ITEM 1. Legal Proceedings

We are involved in various legal proceedings and receives claims from time to time, arising from the normal course of business activities. We have accrued for estimated losses in the accompanying condensed consolidated financial statements for matters with respect to which we believe the likelihood of an adverse outcome is probable and the amount of the loss is reasonably estimable.

ITEM 1A. Risk Factors

A description of the risks and uncertainties associated with our business is set forth below. This description includes any material changes to and supersedes the description of the risks and uncertainties associated with our business previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2010 filed on March 3, 2011. You should carefully consider such risks and uncertainties, together with the other information contained in this report, our Annual Report on Form 10-K for the fiscal year ended December 31, 2010 and in our other public filings. If any of such risks and uncertainties actually occurs, our business, financial condition or operating results could differ materially from the plans, projections and other forward-looking statements included in the section titled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and elsewhere in this report and in our other public filings. In addition, if any of the following risks and uncertainties, or if any other risks and uncertainties, actually occurs, our business, financial condition or operating results could be harmed substantially, which could cause the market price of our stock to decline, perhaps significantly.

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Risks Related to Our Business

Continued adverse economic conditions or reduced investments in cloud-based applications and information technology spending may harm our business.

Our business depends on the overall demand for cloud-based applications and information technology spending and on the economic health and general willingness of our current and prospective customers to make capital commitments. If the conditions in the U.S. and global economic environment remain uncertain or continue to be volatile, or if they deteriorate further, our business, operating results, and financial condition may be materially adversely affected. Continued weak or volatile economic conditions, or a reduction in spending for cloud-based applications and information technology even if economic conditions improve, would likely harm our business and operating results in a number of ways, including longer sales cycles, extended payment terms, lower prices for our products and services, reduced sales, and lower customer retention rates.

We have a history of losses, and we may not achieve profitability in the future.

We have not been profitable on a generally accepted accounting principles ("GAAP") basis during any quarterly or annual period since our formation. We experienced a net loss of $24.4 million for the nine months ended September 30, 2011. As of that date, our accumulated deficit was $335.9 million. We expect to make significant future expenditures related to the development and expansion of our business. As a result of these increased expenditures, we will have to generate and sustain increased revenue to achieve and maintain future profitability. While historically our revenue has grown, this growth may not be sustainable and we may not achieve sufficient revenue to achieve or maintain profitability. We may incur significant losses in the future for a number of reasons, including due to the other risks described in this Quarterly Report, and we may encounter unforeseen expenses, difficulties, complications and delays and other unknown factors. Accordingly, we may not be able to achieve or maintain profitability and we may continue to incur significant losses for the foreseeable future.

Our customers are medium sized businesses and divisions of large companies, which may result in increased costs as we attempt to reach, acquire and retain customers.

We market and sell our application suite primarily to medium-sized businesses and divisions of large companies. To grow our revenue quickly, we must add new customers, sell additional services to existing customers and encourage existing customers to renew their subscriptions. However, selling to and retaining medium-sized businesses can be more difficult than selling to and retaining large enterprises because medium-sized business customers:

- are more price sensitive;
- are more difficult to reach with broad marketing campaigns;
- have high churn rates in part because of the nature of their businesses;
- often lack the staffing to benefit fully from our application suite's rich feature set; and
- often require higher sales, marketing and support expenditures by vendors that sell to them per revenue dollar generated for those vendors.

If we are unable to cost effectively market and sell our service to our target customers, our ability to grow our revenue quickly and become profitable will be harmed.

Our business depends substantially on customers renewing, upgrading and expanding their subscriptions for our services. Any decline in our customer renewals, upgrades and expansions would harm our future operating results.

We sell our application suite pursuant to service agreements that are generally one year in length. Our customers have no obligation to renew their subscriptions after their subscription period expires, and these subscriptions may not be renewed at the same or higher levels. Moreover, under specific circumstances, our customers have the right to cancel their service agreements before they expire. In addition, in the first year of a subscription, customers often purchase a higher level of professional services than they do in renewal years. As a result, our ability to grow is dependent in part on customers purchasing additional subscriptions and modules after the first year of their subscriptions. We have limited historical data with respect to rates of customer subscription renewals, upgrades and expansions so we may not accurately predict future trends in customer renewals. Our customers' renewal rates may decline or fluctuate because of several factors, including their satisfaction or dissatisfaction with our services, the prices of our services, the prices of services offered by our competitors or reductions in our customers' spending levels due to the macroeconomic environment or other factors. If our customers do not renew their subscriptions for our services, renew on less favorable terms, or do not purchase additional functionality or

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subscriptions, our revenue may grow more slowly than expected or decline and our profitability and gross margin may be harmed.

Our services are delivered primarily out of a single data center. Any disruption of service at this facility could interrupt or delay our ability to deliver our service to our customers.

We host our services, serve our customers and support our operations primarily from California based data centers, which we operate in conjunction with SAVVIS. Our OpenAir applications are hosted from a Massachusetts based data center, which we also operate in conjunction with SAVVIS. Our QuickArrow applications are hosted from a Texas based data center, which we operate in conjunction with Sunguard. We do not have sole control over the operations of these facilities. These facilities are vulnerable to damage or interruption from earthquakes, hurricanes, floods, fires, terrorist attacks, power losses, telecommunications failures and similar events. The occurrence of a natural disaster or an act of terrorism, a decision to close the facilities without adequate notice or other unanticipated problems could result in lengthy interruptions in our services. In particular, our California based data facilities are located in an area known for seismic activity, increasing our susceptibility to the risk that an earthquake could significantly harm the operations of these facilities. The facilities also could be subject to break ins, computer viruses, sabotage, intentional acts of vandalism and other misconduct.

Our data center facilities providers have no obligations to renew their agreements with us on commercially reasonable terms, or at all. If we are unable to renew our agreements with the facilities providers on commercially reasonable terms or if in the future we add additional data center facility providers, we may experience costs or downtime in connection with the transfer to, or the addition of, new data center facilities.

Any errors, defects, disruptions or other performance problems with our services could harm our reputation and may damage our customers' businesses. Interruptions in our services might reduce our revenue, cause us to issue credits to customers, subject us to potential liability, cause customers to terminate their subscriptions and harm our renewal rates.

We may become liable to our customers and lose customers if we have defects or disruptions in our service or if we provide poor service.

Because we deliver our application suite as a service, errors or defects in the software applications underlying our service, or a failure of our hosting infrastructure, may make our service unavailable to our customers. Since our customers use our suite to manage critical aspects of their business, any errors, defects, disruptions in service or other performance problems with our suite, whether in connection with the day to day operation of our suite, upgrades or otherwise, could damage our customers' businesses. If we have any errors, defects, disruptions in service or other performance problems with our suite, customers could elect not to renew, or delay or withhold payment to us, we could lose future sales or customers may make warranty claims against us, which could result in an increase in our provision for doubtful accounts, an increase in collection cycles for accounts receivable or costly litigation.

The market for cloud-based applications may develop more slowly than we expect.

Our success will depend, to a large extent, on the willingness of medium-sized businesses to accept cloud-based services for applications that they view as critical to the success of their business. Many companies have invested substantial effort and financial resources to integrate traditional enterprise software into their businesses and may be reluctant or unwilling to switch to a different application or to migrate these applications to cloud-based services. Other factors that may affect market acceptance of our application include:

- the security capabilities, reliability and availability of cloud-based services;
-

customer concerns with entrusting a third party to store and manage their data, especially confidential or sensitive data;

- our ability to minimize the time and resources required to implement our suite;
- our ability to maintain high levels of customer satisfaction;
- our ability to implement upgrades and other changes to our software without disrupting our service;
- the level of customization or configuration we offer;
- our ability to provide rapid response time during periods of intense activity on customer websites; and
- the price, performance and availability of competing products and services.

The market for these services may not develop further, or may develop more slowly than we expect, either of which would harm our business.

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If our security measures are breached and unauthorized access is obtained to a customer's data, we may incur significant liabilities, our service may be perceived as not being secure and customers may curtail or stop using our suite.

The services we offer involve the storage of large amounts of our customers' sensitive and proprietary information. If our security measures are breached as a result of third party action, employee error, malfeasance or otherwise, and someone obtains unauthorized access to our customers' data, we could incur significant liability to our customers and to individuals or businesses whose information was being stored by our customers, our business may suffer and our reputation will be damaged. Because techniques used to obtain unauthorized access to, or to sabotage, systems change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventive measures. If an actual or perceived breach of our security occurs, the market perception of the effectiveness of our security measures could be harmed and we could lose sales and customers. Such an actual or perceived breach could also cause a significant and rapid decline in our stock price.

We provide service level commitments to our customers, which could cause us to issue credits for future services if the stated service levels are not met for a given period and could significantly harm our revenue.

Our customer agreements provide service level commitments. If we are unable to meet the stated service level commitments or suffer extended periods of unavailability for our service, we may be contractually obligated to provide these customers with credits for future services. Our revenue could be significantly impacted if we suffer unscheduled downtime that exceeds the allowed downtimes under our agreements with our customers. In light of our historical experience with meeting our service level commitments, we do not currently have any reserves on our balance sheet for these commitments. Our service level commitment to all customers is 99.5% uptime per period, excluding scheduled maintenance. The failure to meet this level of service availability may require us to credit qualifying customers for the value of an entire month of their subscription fees, not just the value of the subscription fee for the period of the downtime. As a result, a failure to deliver services for a relatively short duration could cause us to issue these credits to all qualifying customers. Any extended service outages could harm our reputation, revenue and operating results.

Assertions by a third party that we infringe its intellectual property, whether successful or not, could subject us to costly and time consuming litigation or expensive licenses.

The software and technology industries are characterized by the existence of a large number of patents, copyrights, trademarks and trade secrets and by frequent and an increasing amount of litigation based on allegations of infringement or other violations of intellectual property rights. As we continue to grow, the possibility of intellectual property rights claims against us may increase. Our technologies may not be able to withstand any third party claims or rights against their use. Additionally, although we have licensed from other parties proprietary technology covered by patents, we cannot be certain that any such patents will not be challenged, invalidated or circumvented. Furthermore, many of our service agreements require us to indemnify our customers for certain third party intellectual property infringement claims, which could increase our costs as a result of defending such claims and may require that we pay damages if there were an adverse ruling related to any such claims. These types of claims could harm our relationships with our customers, may deter future customers from subscribing to our services or could expose us to litigation for these claims. Even if we are not a party to any litigation between a customer and a third party, an adverse outcome in any such litigation could make it more difficult for us to defend our intellectual property in any subsequent litigation in which we are a named party.

Any intellectual property rights claim against us or our customers, with or without merit, could be time consuming, expensive to litigate or settle and could divert management attention and financial resources. An adverse determination also could prevent us from offering our suite to our customers and may require that we procure or develop substitute services that do not infringe.

For any intellectual property rights claim against us or our customers, we may have to pay damages, license fees and/or stop using technology found to be in violation of a third party's rights. We may have to seek a license for the technology. Such license may not be available on reasonable terms, if at all, and may significantly increase our operating expenses or may require us to restrict our business activities and limit our ability to deliver certain products and services. As a result, we may also be required to develop alternative non infringing technology, which could require significant effort and expense and/or cause us to alter our product and service offerings which could negatively affect our business.

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Our success depends in large part on our ability to protect and enforce our intellectual property rights.

We rely on a combination of patent, copyright, service mark, trademark and trade secret laws, as well as confidentiality procedures and contractual restrictions, to establish and protect our proprietary rights, all of which provide only limited protection. We cannot assure you that any patents will issue from our currently pending patent applications in a manner that gives us the protection that we seek, if at all, or that any future patents issued to us will not be challenged, invalidated or circumvented. We do not have any issued patents and currently have eight patent applications pending. Any patents that may issue in the future from pending or future patent applications may not provide sufficiently broad protection or they may not prove to be enforceable in actions against alleged infringers. Also, we cannot assure you that any future service mark or trademark registrations will be issued for pending or future applications or that any registered service marks or trademarks will be enforceable or provide adequate protection of our proprietary rights.

We endeavor to enter into agreements with our employees and contractors and agreements with parties with whom we do business to limit access to and disclosure of our proprietary information. The steps we have taken, however, may not prevent unauthorized use or the reverse engineering of our technology. Moreover, others may independently develop technologies that are competitive to ours or infringe our intellectual property. Enforcement of our intellectual property rights also depends on our successful legal actions against these infringers, but these actions may not be successful, even when our rights have been infringed.

Furthermore, effective patent, trademark, service mark, copyright and trade secret protection may not be available in every country in which our services are available. In addition, the legal standards relating to the validity, enforceability and scope of protection of intellectual property rights in Internet related industries are uncertain and still evolving.

We have experienced rapid growth in recent periods. If we fail to manage our growth effectively, we may be unable to execute our business plan, maintain high levels of service or address competitive challenges adequately.

We have increased our annual revenue from $17.7 million during the year ended December 31, 2004 to $193.1 million during the year ended December 31, 2010. We have increased our number of full time employees from 296 as of December 31, 2004 to 1,243 as of September 30, 2011.

Our expansion has placed, and our anticipated growth may continue to place, a significant strain on our managerial, administrative, operational, financial and other resources. We intend to further expand our overall business, customer base, headcount and operations. We also intend to continue expanding our operations internationally. Creating a global organization and managing a geographically dispersed workforce will require substantial management effort and significant additional investment in our infrastructure. We will be required to continue to improve our operational, financial and management controls and our reporting procedures and we may not be able to do so effectively. As such, we may be unable to manage our expenses effectively in the future, which may negatively impact our gross margin or operating expenses in any particular quarter.

Our quarterly operating results may fluctuate in the future. As a result, we may fail to meet or exceed the expectations of research analysts or investors, which could cause our stock price to decline.

Our quarterly and annual operating results may fluctuate as a result of a variety of factors, many of which are outside of our control. A decline in general macroeconomic conditions could adversely affect our customers' ability or willingness to purchase our application suite, which could adversely affect our operating results or financial outlook. Fluctuations in our quarterly operating results or financial outlook may also be due to a number of additional factors, including the risks and uncertainties discussed elsewhere in this Quarterly Report.

Fluctuations in our operating results could cause our stock price to decline rapidly, may lead analysts to change their long term model for valuing our common stock, may impact our ability to retain or attract key personnel, or cause other unanticipated issues. If our operating results or financial outlook fall below the expectations of research analysts or investors, the price of our common stock could decline substantially.

We believe that our revenue and operating results may vary significantly in the future and that period to period comparisons of our operating results may not be meaningful. You should not rely on the results of one quarter as an indication of future performance.

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Our limited operating history makes it difficult to evaluate our current business and future prospects, and may increase the risk of your investment.

Our company has been in existence since 1998, and much of our growth has occurred since 2004, with our revenue increasing from $17.7 million during the year ended December 31, 2004 to $193.1 million during the year ended December 31, 2010. Our limited operating history may make it difficult to evaluate our current business and our future prospects. We have encountered and will continue to encounter risks and difficulties frequently experienced by growing companies in rapidly changing industries. If we do not address these risks successfully, our business may be harmed.

The markets in which we compete are intensely competitive, and if we do not compete effectively, our operating results may be harmed.

The markets for financials/ERP, CRM, PSA and Ecommerce applications are intensely competitive and rapidly changing with relatively low barriers to entry. With the introduction of new technologies and market entrants, we expect competition to intensify in the future. In addition, pricing pressures and increased competition generally could result in reduced sales, reduced margin or the failure of our service to achieve or maintain more widespread market acceptance. Often we compete to sell our application suite against existing systems that our potential customers have already made significant expenditures to install. Competition in our market is based principally upon service breadth and functionality; service performance, security and reliability; ability to tailor and customize services for a specific company, vertical or industry; ease of use of the service; speed and ease of deployment, integration and configuration; total cost of ownership, including price and implementation and support costs; professional services implementation; and financial resources of the vendor.

We face competition from both traditional software vendors and SaaS providers. Our principal competitors include Epicor Software Corporation, Intuit Inc., Microsoft Corporation, SAP, The Sage Group plc and salesforce.com, inc. Many of our actual and potential competitors enjoy substantial competitive advantages over us, such as greater name recognition, longer operating histories, more varied products and services and larger marketing budgets, as well as substantially greater financial, technical and other resources. In addition, many of our competitors have established marketing relationships and access to larger customer bases, and have major distribution agreements with consultants, system integrators and resellers. If we are not able to compete effectively, our operating results will be harmed.

Our brand name and our business may be harmed by aggressive marketing strategies of our competitors.

Because of the early stage of development of our markets, we believe that building and maintaining brand recognition and customer goodwill is critical to our success. Our efforts in this area have, on occasion, been complicated by the marketing efforts of our competitors, which may include incomplete, inaccurate and false statements about our company and our services that could harm our business. Our ability to respond to our competitors' misleading marketing efforts may be limited under certain circumstances by legal prohibitions on permissible public communications by us as a public company.

Many of our customers are price sensitive, and if the prices we charge for our services are unacceptable to our customers, our operating results will be harmed.

Many of our customers are price sensitive, and we have limited experience with respect to determining the appropriate prices for our services. As the market for our services matures, or as new competitors introduce new products or services that compete with ours, we may be unable to renew our agreements with existing customers or attract new customers at the same price or based on the same pricing model as previously used. As a result, it is possible that competitive dynamics in our market may require us to change our pricing model or reduce our prices, which could harm our revenue, gross margin and operating results.

If we are unable to develop new services or sell our services into new markets, our revenue growth will be harmed and we may not be able to achieve profitability.

Our ability to attract new customers and increase revenue from existing customers will depend in large part on our ability to enhance and improve our existing application suite and to introduce new services and sell into new markets. The success of any enhancement or new service depends on several factors, including the timely completion, introduction and market acceptance of the enhancement or service. Any new service we develop or acquire may not be introduced in a timely or cost effective manner and may not achieve the broad market acceptance necessary to generate significant revenue. Any new markets into which we attempt to sell our application, including new vertical markets and new countries or regions, may not be receptive. If we are unable to successfully develop or acquire new services, enhance our existing services to meet customer requirements or sell our services into new markets, our revenue will not grow as expected and we may not be able to achieve

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profitability.

Because we are a global organization and our long term success depends, in part, on our ability to expand the sales of our services to customers located outside of the United States, our business is susceptible to risks associated with international sales and operations.

We currently maintain offices outside of the United States and have sales personnel or independent consultants in several countries. Approximately one quarter of our employees are located in an office in the Philippines. We have limited experience operating in foreign jurisdictions and are rapidly building our international operations. Managing a global organization is difficult, time consuming and expensive. Our inexperience in operating our business outside of the United States increases the risk that any international expansion efforts that we may undertake will not be successful. In addition, conducting international operations subjects us to new risks that we have not generally faced in the United States. These risks include:

- localization of our services, including translation into foreign languages and adaptation for local practices and regulatory requirements;
- lack of familiarity with and unexpected changes in foreign regulatory requirements;
- longer accounts receivable payment cycles and difficulties in collecting accounts receivable;
- difficulties in managing and staffing international operations;
- fluctuations in currency exchange rates;
- potentially adverse tax consequences, including the complexities of foreign value added tax systems and restrictions on the repatriation of earnings;
- dependence on certain third parties, including channel partners with whom we do not have extensive experience;
- the burdens of complying with a wide variety of foreign laws and legal standards;
- increased financial accounting and reporting burdens and complexities;
- political, social and economic instability abroad, terrorist attacks and security concerns in general; and
- reduced or varied protection for intellectual property rights in some countries.

Operating in international markets also requires significant management attention and financial resources. The investment and additional resources required to establish operations and manage growth in other countries may not produce desired levels of revenue or profitability.

We rely on third party software, including Oracle database software, that may be difficult to replace or could cause errors or failures of our service that could lead to lost customers or harm to our reputation.

We rely on software licensed from third parties to offer our service, including database software from Oracle. This software may not continue to be available to us on commercially reasonable terms, or at all. Any loss of the right to use any of this software could result in delays in the provisioning of our service until equivalent technology is either developed by us, or, if available, is identified, obtained and integrated, which could harm our business. Any errors or defects in third party software could result in errors or a failure of our service which could harm our business.

If we fail to maintain proper and effective internal controls, our ability to produce accurate and timely financial statements could be impaired and investors' views of us could be harmed.

Ensuring that we have adequate internal financial and accounting controls and procedures in place so that we can produce accurate financial statements on a timely basis is a costly and time consuming effort that needs to be re evaluated frequently. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with generally accepted accounting principles. Although we have completed the process of documenting, reviewing and improving our internal controls and procedures for compliance with Section 404 of the Sarbanes Oxley Act of 2002, for the year ended December 31, 2010, there can be no assurances that control deficiencies will not be identified in the future.

Implementing any additional required changes to our internal controls may distract our officers and employees, entail substantial costs to modify our existing processes and add personnel and take significant time to complete. These changes may not, however, be effective in maintaining the adequacy of our internal controls. Any failure to maintain that adequacy, or consequent inability to produce accurate financial statements on a timely basis, could increase our operating costs and harm our business. In addition, investors' perceptions that our internal controls are inadequate or that we are unable to produce accurate

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financial statements on a timely basis may harm our stock price and make it more difficult for us to effectively market and sell our service to new and existing customers.

Our business is subject to changing regulations regarding corporate governance and public disclosure that will increase both our costs and the risk of noncompliance.

As a public company, we incur significant legal, accounting and other expenses associated with compliance with applicable laws, rules, regulations and listing requirements. In addition, the Sarbanes-Oxley Act, the Dodd-Frank Act, and rules subsequently implemented by the SEC and The New York Stock Exchange, have imposed a variety of compliance requirements on public companies, including requiring changes in corporate governance practices. In addition, the SEC and the U.S. Congress may continue to increase the scope of applicable disclosure and corporate governance-related rules. Our management and other personnel may need to devote a substantial amount of time to the compliance requirements associated with being a public company. Moreover, these laws, rules and regulations have increased and may continue to increase the scope, complexity and cost of our corporate governance, reporting and disclosure practices.

Because we recognize subscription revenue over the term of the applicable agreement, the lack of subscription renewals or new service agreements may not be reflected immediately in our operating results.

The majority of our quarterly revenue is attributable to service agreements entered into during previous quarters. A decline in new or renewed service agreements in any one quarter will not be fully reflected in our revenue in that quarter but will harm our revenue in future quarters. As a result, the effect of significant downturns in sales and market acceptance of our services in a particular quarter may not be fully reflected in our operating results until future periods. Our subscription model also makes it difficult for us to rapidly increase our revenue through additional sales in any period, because revenue from new customers must be recognized over the applicable subscription term.

Material defects or errors in the software we use to deliver our services could harm our reputation, result in significant costs to us and impair our ability to sell our services.

The software applications underlying our services are inherently complex and may contain material defects or errors, particularly when first introduced or when new versions or enhancements are released. We have from time to time found defects in our service, and new errors in our existing service may be detected in the future. Any defects that cause interruptions to the availability of our services could result in:

- a reduction in sales or delay in market acceptance of our services;
- sales credits or refunds to our customers;
- loss of existing customers and difficulty in attracting new customers;
- diversion of development resources;
- harm to our reputation; and
- increased warranty and insurance costs.

After the release of our services, defects or errors may also be identified from time to time by our internal team and by our customers. The costs incurred in correcting any material defects or errors in our services may be substantial and could harm our operating results.

Government regulation of the Internet and Ecommerce is evolving, and unfavorable changes or our failure to comply with regulations could harm our operating results.

As Internet commerce continues to evolve, increasing regulation by federal, state or foreign agencies becomes more likely. For example, we believe increased regulation is likely in the area of data privacy, and laws and regulations applying to the solicitation, collection, processing or use of personal or consumer information could affect our customers' ability to use and share data, potentially reducing demand for financials/ERP, CRM, PSA and Ecommerce solutions and restricting our ability to store, process and share our customers' data. In addition, taxation of services provided over the Internet or other charges imposed by government agencies or by private organizations for accessing the Internet may also be imposed. Any regulation imposing greater fees for Internet use or restricting information exchange over the Internet could result in a decline in the use of the Internet and the viability of Internet based services, harming our business and operating results.

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Privacy concerns and laws or other domestic or foreign regulations may reduce the effectiveness of our application suite and harm our business.

Our customers can use our service to store personal or identifying information regarding their customers and contacts. Federal, state and foreign government bodies and agencies, however, have adopted or are considering adopting laws and regulations regarding the collection, use and disclosure of personal information obtained from consumers and other individuals. The costs of compliance with, and other burdens imposed by, such laws and regulations that are applicable to the businesses of our customers may limit the use and adoption of our service and reduce overall demand for it.

In addition to government activity, privacy advocacy groups and the technology and other industries are considering various new, additional or different self regulatory standards that may place additional burdens on us. If the gathering of personal information were to be curtailed, financials/ERP, CRM, PSA and Ecommerce solutions would be less effective likely reducing demand for our service and harm our business.

Changes in financial accounting standards or practices may cause adverse, unexpected financial reporting fluctuations and harm our operating results.

A change in accounting standards or practices could harm our operating results and may even affect our reporting of transactions completed before the change is effective. New accounting pronouncements and varying interpretations of accounting pronouncements have occurred and may occur in the future. Changes to existing rules or the questioning of current practices may harm our operating results or the way we conduct our business.

Unanticipated changes in our effective tax rate could harm our future operating results.

We are subject to income taxes in the United States and various foreign jurisdictions, and our domestic and international tax liabilities are subject to the allocation of expenses in differing jurisdictions. Our tax rate is affected by changes in the mix of earnings and losses in countries with differing statutory tax rates, certain non deductible expenses arising from the requirement to expense stock options and the valuation of deferred tax assets and liabilities, including our ability to utilize our net operating losses. Increases in our effective tax rate could harm our operating results.

We may be unable to integrate acquired businesses and technologies successfully or to achieve the expected benefits of such acquisitions. We may acquire or invest in additional companies, which may divert our management’s attention, result in additional dilution to our stockholders and consume resources that are necessary to sustain our business.

We have undertaken acquisitions in the past and may continue to evaluate and consider potential strategic transactions, including acquisitions and dispositions of businesses, technologies, services, products and other assets in the future. An acquisition, investment or business relationship may result in unforeseen operating difficulties and expenditures. In particular, we may encounter difficulties assimilating or integrating the businesses, technologies, products, personnel or operations of the acquired companies, particularly if the key personnel of the acquired company choose not to work for us, the company’s software is not easily adapted to work with ours or we have difficulty retaining the customers of any acquired business due to changes in management or otherwise. Acquisitions may also disrupt our business, divert our resources and require significant management attention that would otherwise be available for development of our business. Moreover, the anticipated benefits of any acquisition, investment or business relationship may not be realized or we may be exposed to unknown liabilities.

We may in the future seek to acquire or invest in additional businesses, products, technologies or other assets. We also may enter into relationships with other businesses to expand our service offerings or our ability to provide service in foreign jurisdictions, which could involve preferred or exclusive licenses, additional channels of distribution, discount pricing or investments in other companies. Negotiating these transactions can be time consuming, difficult and expensive, and our ability to close these transactions may often be subject to approvals that are beyond our control. Consequently, these transactions, even if undertaken and announced, may not close. For one or more of those transactions, we may:

- issue additional equity securities that would dilute our stockholders;
- use cash that we may need in the future to operate our business;
- incur debt on terms unfavorable to us or that we are unable to repay;
- incur large charges or substantial liabilities;
- encounter difficulties retaining key employees of the acquired company or integrating diverse software codes or business cultures; and
- become subject to adverse tax consequences, substantial depreciation or deferred compensation charges.

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Any of these risks could harm our business and operating results.

We rely on our management team and need additional personnel to grow our business, and the loss of one or more key employees or our inability to attract and retain qualified personnel could harm our business.

Our success and future growth depends to a significant degree on the skills and continued services of our management team, especially Zachary Nelson, our President and Chief Executive Officer, and Evan M. Goldberg, our Chief Technology Officer and Chairman of the Board. We do not maintain key man insurance on any members of our management team, including Messrs. Nelson and Goldberg. Our future success also depends on our ability to attract, retain and motivate highly skilled technical, managerial, sales, marketing and service and support personnel, including members of our management team. Competition for sales, marketing and technology development personnel is particularly intense in the software and technology industries. As a result, we may be unable to successfully attract or retain qualified personnel. Our inability to attract and retain the necessary personnel could harm our business.

Risks Related to Ownership of our Common Stock

Lawrence J. Ellison or members of his family, and related entities, beneficially own a majority of our outstanding shares of common stock, which may limit your ability to influence or control certain of our corporate actions. This concentration of ownership may also reduce the market price of our common stock and impair a takeover attempt of us.

Entities beneficially owned by Lawrence J. Ellison held an aggregate of approximately 47.1% of our common stock as of September 30, 2011. Further, Mr. Ellison, his family members, trusts for their benefit, and related entities together beneficially owned an aggregate of approximately 53.9% of our common stock as of that date. Mr. Ellison is able to exercise control over approval of significant corporate transactions, including a change of control or liquidation. In addition, if the voting restrictions that apply to NetSuite Restricted Holdings LLC, the investment entity to which Mr. Ellison has transferred his shares, lapse or are amended, Mr. Ellison will be able to exercise control over additional corporate matters, including elections of our directors. So long as Mr. Ellison continues to be either an officer or director of Oracle, these voting restrictions cannot be changed without the approval of an independent committee of Oracle's board of directors. Mr. Ellison's interests and investment objectives may differ from our other stockholders. Mr. Ellison is also the Chief Executive Officer, a principal stockholder and a director of Oracle Corporation. Oracle supplies us with database software on which we rely to provide our service and is also a potential competitor of ours.

Our Board of Directors adopted resolutions which renounce and provide for a waiver of the corporate opportunity doctrine as it relates to Mr. Ellison. As a result, Mr. Ellison will have no fiduciary duty to present corporate opportunities to us. In addition, Mr. Ellison's indirect majority interest in us could discourage potential acquirers or result in a delay or prevention of a change in control of our company or other significant corporate transactions, even if a transaction of that sort would be beneficial to our other stockholders or in our best interest.

Our failure to raise additional capital or generate the cash flows necessary to expand our operations and invest in our application services could reduce our ability to compete successfully.

We may need to raise additional funds, and we may not be able to obtain additional debt or equity financing on favorable terms, if at all. If we raise additional equity financing, our stockholders may experience significant dilution of their ownership interests and the per share value of our common stock could decline. If we engage in debt financing, we may be required to accept terms that restrict our ability to incur additional indebtedness and force us to maintain specified liquidity or other ratios. If we need additional capital and cannot raise it on acceptable terms, we may not be able to, among other things:

- develop or enhance our application and services;
- continue to expand our product development, sales and marketing organizations;
- acquire complementary technologies, products or businesses;
- expand operations, in the United States or internationally;
- hire, train and retain employees; or
- respond to competitive pressures or unanticipated working capital requirements.

Future sales of shares by existing stockholders could cause our stock price to decline.

If our existing stockholders sell or otherwise dispose of, or indicate an intention to sell or dispose of, substantial

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amounts of our common stock in the public market, the trading price of our common stock could decline. As of September 30, 2011, we had a total of 67,837,397 shares of our common stock outstanding. Although shares that are held by NetSuite Restricted Holdings LLC are subject to certain restrictions on disposition and a portion of the remaining shares are subject to our Insider Trading Compliance Policy during certain periods of each quarter, substantially all of the shares held by parties other than NetSuite Restricted Holdings LLC, representing 52.9% of our outstanding shares as of September 30, 2011, are freely tradable, subject to our quarterly black-out periods that apply to shares held by our directors, officers, employees and consultants. If a significant number of these shares are sold, or if it is perceived that they will be sold, in the public market, the trading price of our common stock could decline.

Anti takeover provisions contained in our amended and restated certificate of incorporation and amended and restated bylaws, as well as provisions of Delaware law, could impair a takeover attempt.

Our amended and restated certificate of incorporation, amended and restated bylaws and Delaware law contain provisions that could have the effect of rendering more difficult or discouraging an acquisition deemed undesirable by our Board of Directors. Our corporate governance documents include provisions:

- authorizing blank check preferred stock, which could be issued with voting, liquidation, dividend and other rights superior to our common stock;
- limiting the liability of, and providing indemnification to, our directors and officers;
- limiting the ability of our stockholders to call and bring business before special meetings and to take action by written consent in lieu of a meeting;
- requiring advance notice of stockholder proposals for business to be conducted at meetings of our stockholders and for nominations of candidates for election to our Board of Directors;
- controlling the procedures for the conduct and scheduling of board and stockholder meetings;
- providing the Board of Directors with the express power to postpone previously scheduled annual meetings and to cancel previously scheduled special meetings;
- limiting the determination of the number of directors on our board and the filling of vacancies or newly created seats on the board to our board of directors then in office; and
- providing that directors may be removed by stockholders only for cause.

These provisions, alone or together, could delay hostile takeovers and changes in control or changes in our management.

As a Delaware corporation, we are also subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation law, which prevents some stockholders holding more than 15% of our outstanding common stock from engaging in certain business combinations without approval of the holders of substantially all of our outstanding common stock. Under Section 203, our majority stockholder, which is beneficially owned by Lawrence J. Ellison, and our current stockholders associated with members of Mr. Ellison's family are not subject to the prohibition from engaging in such business combinations.

Any provision of our amended and restated certificate of incorporation or bylaws or Delaware law that has the effect of delaying or deterring a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our common stock, and could also affect the price that some investors are willing to pay for our common stock.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

On August 2, 2011, we completed the purchase of substantially all of the assets of a small private company ("SPC") that provides on-demand software. As part of the consideration for the acquisition, on the closing date, we issued 38,102 shares of our common stock to SPC (the "SPC Shares"). At the close of business on August 2, 2011, the SPC shares were worth an aggregate of $1.4 million. The issuance of the SPC Shares was deemed to be exempt from registration under the Securities Act in reliance on Section 4(2) of the Securities Act or Regulation D promulgated thereunder. SPC and the stockholders of SPC represented their intention to acquire the SPC Shares for investment only and not with a view to or for sale in connection with any distribution thereof and the appropriate legend was affixed to the stock certificate representing the SPC Shares. SPC and the stockholders of SPC had adequate access, through their relationships with us, to information about us.

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ITEM 6. Exhibits

The exhibits listed below are filed or incorporated by reference as part of this Report.

Exhibit No	Description of Exhibits
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act.
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act.
32.1	Certification of the Chief Executive Officer and the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act.
101.INS**	XBRL Instance Document
101.SCH**	XBRL Taxonomy Extension Schema Document
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF**	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB**	XBRL Taxonomy Extension Label Linkbase Document
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document

** Users of this data are advised that, pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934 and otherwise are not subject to liability under these sections.

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SIGNATURES

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

Date:	November 4, 2011	NETSUITE INC.
	By:	/S/ RONALD GILL Ronald Gill Chief Financial Officer