
UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended October 31, 2009

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 No. 0-49790

Verint Systems Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware

(State or Other Jurisdiction of Incorporation
or Organization)

11-3200514

(I.R.S. Employer Identification No.)

330 South Service Road, Melville, New York

(Address of Principal Executive Offices)

11747

(Zip Code)

(631) 962-9600

(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 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 (§232.40S of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes 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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

Small 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

There were 32,794,402 shares of the registrant's common stock outstanding on May 31, 2010.

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Explanatory Note

This report of Verint Systems Inc. (together with its consolidated subsidiaries, “Verint”, the “Company”, “we”, “us”, and “our”, unless the context indicates otherwise) is for the three months ended October 31, 2009.

This report has been delayed due to the previously announced accounting reviews and internal investigations at Verint and at our majority stockholder, Converse Technology, Inc. (“Converse”), together with the resulting restatement of certain items and the making of other corrective adjustments to our previously-filed historical financial statements for periods through January 31, 2005, all of which were described in our comprehensive Annual Report on Form 10-K for the years ended January 31, 2008, 2007, and 2006 filed with the Securities and Exchange Commission (“SEC”) on March 17, 2010 (the “Comprehensive Form 10-K”). The filing of this report was further delayed by the preparation of the Comprehensive Form 10-K, our Annual Report on Form 10-K for the year ended January 31, 2009, and our Annual Report on Form 10-K for the year ended January 31, 2010, covering five years of audited financial information, and the process of filing of these reports over the course of a two-month period from March 17, 2010 to May 19, 2010. Please see our Comprehensive Form 10-K for more information regarding the accounting reviews and internal investigations and the related restatement.

As noted above, since the filing of our Comprehensive Form 10-K, we have filed, among other things, our Annual Report on Form 10-K for the year ended January 31, 2009 (on April 8, 2010) and our Annual Report on Form 10-K for the year ended January 31, 2010 (on May 19, 2010) as well as our Quarterly Report on Form 10-Q for the three months ended April 30, 2010 (on June 9, 2010). As a result, because information for periods subsequent to the three months ended October 31, 2009 is already available in our Annual Report on Form 10-K for the year ended January 31, 2010 and Quarterly Report on Form 10-Q for the three months ended April 30, 2010, in certain sections of this report, we have included information for periods after October 31, 2009 and, in some instances, we have made reference to such reports. Please see our Annual Report on Form 10-K for the year ended January 31, 2010 for additional information.

Cautionary Note on Forward-Looking Statements

Certain statements discussed in this report constitute “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995, the provisions of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”) (which Sections were adopted as part of the Private Securities Litigation Reform Act of 1995). Forward-looking statements include financial projections, statements of plans and objectives for future operations, statements of future economic performance, and statements of assumptions relating thereto. Forward-looking statements are often identified by future or conditional words such as “will”, “plans”, “expects”, “intends”, “believes”, “seeks”, “estimates”, or “anticipates”, or by variations of such words or by similar expressions. There can be no assurances that forward-looking statements will be achieved. By their very nature, forward-looking statements involve known and unknown risks, uncertainties, and other important factors that could cause our actual results or conditions to differ materially from those expressed or implied by such forward-looking statements. Important risks, uncertainties, and other factors that could cause our actual results or conditions to differ materially from our forward-looking statements include, among others:

- risks relating to the filing of our SEC reports, including the occurrence of known contingencies or unforeseen events that could delay our filings, management distractions, and significant expense;
- risk associated with the SEC’s initiation of an administrative proceeding on March 3, 2010 to suspend or revoke the registration of our common stock under the Exchange Act due to our previous failure to file an annual report on either Form 10-K or Form 10-KSB since April 25, 2005 or quarterly reports on either Form 10-Q or Form 10-QSB since December 12, 2005;
- risk that our credit rating could be downgraded or placed on a credit watch based on, among other things, our financial results, delays in the filing of our periodic reports, or the results of the SEC’s administrative proceeding;
- risks associated with being a consolidated, controlled subsidiary of Comverse and formerly part of Comverse’s consolidated tax group, including risk of any future impact on us resulting from Comverse’s special committee investigation and restatement or related effects, and risks related to our dependence on Comverse to provide us with accurate financial information, including with respect to stock-based compensation expense and net operating loss carryforwards (“NOLs”), for our financial statements;
- uncertainty regarding the impact of general economic conditions, particularly in information technology spending, on our business;
- risk that our financial results will cause us not to be compliant with the leverage ratio covenant under our credit facility or that any delays in the filing of future SEC reports could cause us not to be compliant with the financial statement delivery covenant under our credit facility;

- risk that customers or partners delay or cancel orders or are unable to honor contractual commitments due to liquidity issues, challenges in their business, or otherwise;
- risk that we will experience liquidity or working capital issues and related risk that financing sources will be unavailable to us on reasonable terms or at all;
- uncertainty regarding the future impact on our business of our internal investigation, restatement, extended filing delay, and the SEC's administrative proceeding, including customer, partner, employee, and investor concern, and potential customer and partner transaction deferrals or losses;
- risks relating to the remediation or inability to adequately remediate material weaknesses in our internal controls over financial reporting and relating to the proper application of highly complex accounting rules and pronouncements in order to produce accurate SEC reports on a timely basis;
- risks relating to our implementation and maintenance of adequate systems and internal controls for our current and future operations and reporting needs;
- risk of possible future restatements if the processes used to produce the financial statements contained in this report or in future SEC reports are inadequate;
- risk associated with current or future regulatory actions or private litigations relating to our internal investigation, restatement, or delays in filing required SEC reports;
- risk that we will be unable to re-list our common stock on NASDAQ or another national securities exchange and maintain such listing;
- risks associated with Comverse controlling our board of directors and a majority of our common stock (and therefore the results of any significant stockholder vote);
- risks associated with significant leverage resulting from our current debt position;
- risks due to aggressive competition in all of our markets, including with respect to maintaining margins and sufficient levels of investment in the business and with respect to introducing quality products which achieve market acceptance;
- risks created by continued consolidation of competitors or introduction of large competitors in our markets with greater resources than us;
- risks associated with significant foreign and international operations, including exposure to fluctuations in exchange rates;
- risks associated with complex and changing local and foreign regulatory environments;

- risks associated with our ability to recruit and retain qualified personnel in all geographies in which we operate;
- challenges in accurately forecasting revenue and expenses;
- risks associated with acquisitions and related system integrations;
- risks relating to our ability to improve our infrastructure to support growth;
- risks that our intellectual property rights may not be adequate to protect our business or that others may make claims on our intellectual property or claim infringement on their intellectual property rights;
- risks associated with a significant amount of our business coming from domestic and foreign government customers;
- risk that we improperly handle sensitive or confidential information or perception of such mishandling;
- risks associated with dependence on a limited number of suppliers for certain components of our products;
- risk that we are unable to maintain and enhance relationships with key resellers, partners, and systems integrators; and
- risk that use of our NOLs or other tax benefits may be restricted or eliminated in the future.

These risks and uncertainties, as well as other factors, are discussed in greater detail in “Risk Factors” under Item 1A of our Annual Report on Form 10-K for the year ended January 31, 2010. Readers are cautioned not to place undue reliance on forward-looking statements, which reflect our management’s view only as of the filing date of this report. We make no commitment to revise or update any forward-looking statements in order to reflect events or circumstances after the date any such statement is made, except as otherwise required under the federal securities laws. If we were in any particular instance to update or correct a forward-looking statement, investors and others should not conclude that we would make additional updates or corrections thereafter except as otherwise required under the federal securities laws.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

VERINT SYSTEMS INC. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
October 31, 2009 and January 31, 2009
(Unaudited)

| (in thousands, except share and per share data) | October 31, 2009 | January 31, 2009 |
|--|---------------------|---------------------|
| Assets | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 161,184 | \$ 115,928 |
| Restricted cash and bank time deposits | 5,748 | 7,722 |
| Accounts receivable, net | 129,838 | 113,178 |
| Inventories | 15,933 | 20,455 |
| Deferred cost of revenue | 11,487 | 8,935 |
| Prepaid expenses and other current assets | 63,399 | 46,748 |
| Total current assets | 387,589 | 312,966 |
| Property and equipment, net | 25,603 | 30,544 |
| Goodwill | 729,545 | 709,984 |
| Intangible assets, net | 182,210 | 200,203 |
| Capitalized software development costs, net | 8,946 | 10,489 |
| Deferred cost of revenue | 37,364 | 47,913 |
| Other assets | 24,720 | 25,294 |
| Total assets | \$ 1,395,977 | \$ 1,337,393 |
| Liabilities, Preferred Stock, and Stockholders' Equity (Deficit) | | |
| Current Liabilities: | | |
| Accounts payable | \$ 38,757 | \$ 38,484 |
| Accrued expenses and other liabilities | 149,478 | 146,741 |
| Current maturities of long-term debt | 3,693 | 4,088 |
| Deferred revenue | 181,737 | 160,918 |
| Liabilities to affiliates | 1,751 | 1,389 |
| Total current liabilities | 375,416 | 351,620 |
| Long-term debt | 617,219 | 620,912 |
| Deferred revenue | 55,369 | 88,985 |
| Other liabilities | 59,446 | 66,404 |
| Total liabilities | 1,107,450 | 1,127,921 |
| Preferred Stock — \$0.001 par value; authorized 2,500,000 shares. Series A convertible preferred stock; 293,000 shares issued and outstanding; aggregate liquidation preference and redemption value of \$322,751 at October 31, 2009 | 285,542 | 285,542 |
| Commitments and Contingencies | | |
| Stockholders' Equity (Deficit): | | |
| Common stock — \$0.001 par value; authorized 120,000,000 shares. Issued 32,643,000 and 32,623,000 shares, respectively; outstanding 32,543,000 and 32,535,000 shares, as of October 31, 2009 and January 31, 2009 respectively | 32 | 32 |
| Additional paid-in capital | 443,142 | 419,937 |
| Treasury stock, at cost - 100,000 and 88,000 shares as of October 31, 2009 and January 31, 2009, respectively | (2,438) | (2,353) |
| Accumulated deficit | (401,547) | (435,955) |
| Accumulated other comprehensive loss | (37,912) | (58,404) |
| Total Verint Systems Inc. stockholders' equity (deficit) | 1,277 | (76,743) |
| Noncontrolling interest | 1,708 | 673 |
| Total stockholders' equity (deficit) | 2,985 | (76,070) |
| Total liabilities, preferred stock, and stockholders' equity (deficit) | \$ 1,395,977 | \$ 1,337,393 |

See notes to condensed consolidated financial statements.

VERINT SYSTEMS INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Operations
Three and Nine Months Ended October 31, 2009 and 2008
(Unaudited)

| (in thousands, except per share data) | Three Months Ended October 31, | | Nine Months Ended October 31, | |
|--|-----------------------------------|--------------------|----------------------------------|--------------------|
| | 2009 | 2008 | 2009 | 2008 |
| Revenue: | | | | |
| Product | \$ 98,467 | \$ 81,495 | \$ 283,645 | \$ 251,306 |
| Service and support | 88,013 | 76,372 | 247,252 | 227,540 |
| Total revenue | 186,480 | 157,867 | 530,897 | 478,846 |
| Cost of revenue: | | | | |
| Product | 35,718 | 31,983 | 98,675 | 94,084 |
| Service and support | 25,819 | 27,571 | 74,922 | 90,177 |
| Amortization of acquired technology and backlog | 1,973 | 2,228 | 6,049 | 6,851 |
| Total cost of revenue | 63,510 | 61,782 | 179,646 | 191,112 |
| Gross profit | 122,970 | 96,085 | 351,251 | 287,734 |
| Operating expenses: | | | | |
| Research and development, net | 21,461 | 21,963 | 61,000 | 69,897 |
| Selling, general and administrative | 72,398 | 69,977 | 199,882 | 218,089 |
| Amortization of other acquired intangible assets | 5,376 | 6,139 | 16,892 | 19,318 |
| Integration, restructuring and other, net | — | (7,393) | 24 | 1,168 |
| Total operating expenses | 99,235 | 90,686 | 277,798 | 308,472 |
| Operating income (loss) | 23,735 | 5,399 | 73,453 | (20,738) |
| Other income (expense), net: | | | | |
| Interest income | 336 | 481 | 581 | 1,557 |
| Interest expense | (6,178) | (9,794) | (18,900) | (29,400) |
| Other expense, net | (2,775) | (7,086) | (10,844) | (464) |
| Total other expense, net | (8,617) | (16,399) | (29,163) | (28,307) |
| Income (loss) before provision for income taxes | 15,118 | (11,000) | 44,290 | (49,045) |
| Provision for income taxes | 1,803 | 9,441 | 8,921 | 10,887 |
| Net income (loss) | 13,315 | (20,441) | 35,369 | (59,932) |
| Net income attributable to noncontrolling interest | 139 | 695 | 961 | 1,588 |
| Net income (loss) attributable to Verint Systems Inc. | 13,176 | (21,136) | 34,408 | (61,520) |
| Dividends on preferred stock | (3,443) | (3,301) | (10,111) | (9,728) |
| Net income (loss) attributable to Verint Systems Inc. common shares | \$ 9,733 | \$ (24,437) | \$ 24,297 | \$ (71,248) |
| Net income (loss) per share attributable to Verint Systems Inc. | | | | |
| Basic | \$ 0.30 | \$ (0.75) | \$ 0.75 | \$ (2.20) |
| Diluted | \$ 0.29 | \$ (0.75) | \$ 0.74 | \$ (2.20) |
| Weighted-average common shares outstanding | | | | |
| Basic | 32,471 | 32,387 | 32,465 | 32,385 |
| Diluted | 33,330 | 32,387 | 32,879 | 32,385 |

See notes to condensed consolidated financial statements.

VERINT SYSTEMS INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Stockholders' Equity (Deficit)
Nine Months Ended October 31, 2009 and 2008
(Unaudited)

| Verint Systems Inc. Stockholders' Equity (Deficit) | | | | | | | | | |
|---|---------------|--------------|-------------------|-------------------|---------------------|--------------------------|--------------------------------|-------------------------|--------------------------------|
| (in thousands) | Common Stock | | Additional | | Accumulated | | Total Verint | | Total |
| | Shares | Par Value | Paid-in Capital | Treasury Stock | Accumulated Deficit | Other Comprehensive Loss | Stockholders' Equity (Deficit) | Noncontrolling Interest | Stockholders' Equity (Deficit) |
| Balances as of January 31, 2008 | 32,526 | \$ 32 | \$ 387,537 | \$ (2,094) | \$ (355,567) | \$ (610) | \$ 29,298 | \$ 1,027 | \$ 30,325 |
| Comprehensive income (loss): | | | | | | | | | |
| Net income (loss) | — | — | — | — | (61,520) | — | (61,520) | 1,588 | (59,932) |
| Unrealized losses on available for sale securities, net | — | — | — | — | — | (24) | (24) | — | (24) |
| Currency translation adjustments | — | — | — | — | — | (38,956) | (38,956) | (36) | (38,992) |
| Total comprehensive income (loss) | — | — | — | — | (61,520) | (38,980) | (100,500) | 1,552 | (98,948) |
| Stock-based compensation expense | — | — | 24,934 | — | — | — | 24,934 | — | 24,934 |
| Common stock issued for stock awards | 20 | — | — | — | — | — | — | — | — |
| Forfeitures of restricted stock awards | (8) | — | 163 | (163) | — | — | — | — | — |
| Purchases of treasury stock | (5) | — | — | (93) | — | — | (93) | — | (93) |
| Tax effects from stock award plans | — | — | 165 | — | — | — | 165 | — | 165 |
| Balances as of October 31, 2008 | 32,533 | \$ 32 | \$ 412,799 | \$ (2,350) | \$ (417,087) | \$ (39,590) | \$ (46,196) | \$ 2,579 | \$ (43,617) |
| Balances as of January 31, 2009 | 32,535 | \$ 32 | \$ 419,937 | \$ (2,353) | \$ (435,955) | \$ (58,404) | \$ (76,743) | \$ 673 | \$ (76,070) |
| Comprehensive income: | | | | | | | | | |
| Net income | — | — | — | — | 34,408 | — | 34,408 | 961 | 35,369 |
| Unrealized gains on derivative financial instruments, net | — | — | — | — | — | 302 | 302 | — | 302 |
| Unrealized gains on available for sale securities, net | — | — | — | — | — | 32 | 32 | — | 32 |
| Currency translation adjustments | — | — | — | — | — | 20,158 | 20,158 | 74 | 20,232 |
| Total comprehensive income | — | — | — | — | 34,408 | 20,492 | 54,900 | 1,035 | 55,935 |
| Stock-based compensation expense | — | — | 23,170 | — | — | — | 23,170 | — | 23,170 |
| Common stock issued for stock awards | 20 | — | — | — | — | — | — | — | — |
| Forfeitures of restricted stock awards | (4) | — | 35 | (35) | — | — | — | — | — |
| Purchases of treasury stock | (8) | — | — | (50) | — | — | (50) | — | (50) |
| Balances as of October 31, 2009 | 32,543 | \$ 32 | \$ 443,142 | \$ (2,438) | \$ (401,547) | \$ (37,912) | \$ 1,277 | \$ 1,708 | \$ 2,985 |

See notes to condensed consolidated financial statements.

VERINT SYSTEMS INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
Nine Months Ended October 31, 2009 and 2008
(Unaudited)

| (in thousands) | Nine Months Ended October 31, | |
|---|--------------------------------------|------------------|
| | 2009 | 2008 |
| Cash flows from operating activities: | | |
| Net income (loss) | \$ 35,369 | \$ (59,932) |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | | |
| Depreciation and amortization | 37,424 | 41,901 |
| Stock-based compensation | 23,170 | 24,934 |
| Losses on derivative financial instruments not designated as hedges, net | 11,745 | 2,554 |
| Non-cash gains on sales of auction rate securities | — | (4,713) |
| Other non-cash items, net | (957) | 2,718 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (15,692) | 4,149 |
| Inventories | 4,511 | (8,221) |
| Deferred cost of revenue | 10,448 | 6,758 |
| Accounts payable and accrued expenses | (1,408) | (752) |
| Deferred revenue | (22,821) | 19,981 |
| Prepaid expenses and other assets | (13,675) | 3,392 |
| Other, net | (2,623) | (2,372) |
| Net cash provided by operating activities | 65,491 | 30,397 |
| Cash flows from investing activities: | | |
| Payments of contingent consideration associated with business combinations in prior periods | (96) | (2,021) |
| Purchases of property and equipment | (3,346) | (9,249) |
| Sales of investments | — | 1,800 |
| Settlements of derivative financial instruments not designated as hedges | (13,140) | (5,650) |
| Cash paid for capitalized software development costs | (1,897) | (3,259) |
| Other investing activities | 2,094 | (5,865) |
| Net cash used in investing activities | (16,385) | (24,244) |
| Cash flows from financing activities: | | |
| Repayments of borrowings and other financing obligations | (6,088) | (2,119) |
| Dividends paid to noncontrolling interest | (2,142) | — |
| Other financing activities | (202) | (243) |
| Net cash used in financing activities | (8,432) | (2,362) |
| Effect of exchange rate changes on cash and cash equivalents | 4,582 | (4,102) |
| Net increase (decrease) in cash and cash equivalents | 45,256 | (311) |
| Cash and cash equivalents, beginning of period | 115,928 | 83,233 |
| Cash and cash equivalents, end of period | \$ 161,184 | \$ 82,922 |
| Supplemental disclosures of cash flow information: | | |
| Cash paid for interest | \$ 18,839 | \$ 28,245 |
| Cash paid for income taxes | \$ 9,688 | \$ 2,462 |
| Non-cash investing and financing transactions: | | |
| Accrued but unpaid purchases of property and equipment | \$ 520 | \$ 639 |
| Inventory transfers to property and equipment | \$ 480 | \$ 654 |
| Business combination consideration earned, but paid in subsequent periods | \$ — | \$ 1,072 |
| Settlement of embedded derivative | \$ — | \$ 8,121 |

See notes to condensed consolidated financial statements.

VERINT SYSTEMS INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited)

I. BASIS OF PRESENTATION

Preparation of Condensed Consolidated Financial Statements

The condensed consolidated financial statements included herein have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and on the same basis as the audited consolidated financial statements included in our Annual Report on Form 10-K filed with the SEC for the year ended January 31, 2009. The condensed consolidated statements of operations, stockholders’ equity (deficit) and cash flows for the periods ended October 31, 2009 and 2008, and the condensed consolidated balance sheet as of October 31, 2009, are not audited but reflect all adjustments that are of a normal recurring nature and that are considered necessary for a fair presentation of the results of the periods shown. The condensed consolidated balance sheet as of January 31, 2009 is derived from the audited consolidated balance sheet presented in our Annual Report on Form 10-K for the year ended January 31, 2009. Certain information and disclosures normally included in annual consolidated financial statements have been omitted pursuant to the rules and regulations of the SEC. Because the condensed consolidated interim financial statements do not include all of the information and disclosures required by GAAP for a complete set of financial statements, they should be read in conjunction with the audited consolidated financial statements and notes included in our Annual Reports on Form 10-K filed with the SEC. The results for interim periods are not necessarily indicative of a full year’s results.

Unless the context otherwise requires, the terms “Verint”, “we”, “our”, and “us” and words of similar import as used in these notes to the condensed consolidated financial statements include Verint Systems Inc. and its consolidated subsidiaries.

Principles of Consolidation

The accompanying condensed consolidated financial statements include the accounts of Verint Systems Inc., our wholly owned subsidiaries, and a joint venture in which we hold a 50% equity interest. This joint venture functions as a systems integrator for Asian markets and is a variable interest entity in which we are the primary beneficiary. Investments in companies in which we have less than a 20% ownership interest and do not exercise significant influence are accounted for at cost. We include the results of operations of acquired companies from the date of acquisition. All significant intercompany transactions and balances are eliminated.

Use of Estimates

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

Recent Accounting Pronouncements

Standards Implemented:

In December 2007, the Financial Accounting Standards Board (“FASB”) revised their guidance on business combinations. This new guidance requires an acquiring entity to measure and recognize identifiable assets acquired and liabilities assumed, and contingent consideration at their fair values at the acquisition date with subsequent changes recognized in earnings. In addition, acquisition related costs and restructuring costs are recognized separately from the business combination and expensed as incurred. The new guidance also requires acquired in-process research and development costs to be capitalized as an indefinite-lived intangible asset and requires that changes in accounting for deferred tax asset valuation allowances and acquired income tax uncertainties after the measurement period be recognized as a component of the provision for income taxes. In April 2009, the FASB issued a new standard which clarified the accounting for pre-acquisition contingencies. This guidance was effective for us beginning on February 1, 2009.

In December 2007, the FASB issued a new accounting standard which establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and the noncontrolling interest, changes in a parent’s ownership interest and the valuation of retained noncontrolling equity investments when a subsidiary is deconsolidated. The new standard also establishes disclosure requirements that clearly identify and distinguish between the interests of the parent and the interests of the noncontrolling owners. On February 1, 2009, we adopted this standard, and the presentation and disclosure requirements of this standard were applied retrospectively to all periods presented, as required by the standard. The adoption of this standard did not have a material impact on our condensed consolidated financial statements, other than the following changes in presentation of the noncontrolling interest:

- Net income (loss) now includes net income (loss) attributable to both Verint Systems Inc. and the noncontrolling interest in the condensed consolidated statements of operations. The presentation of net income (loss) in prior periods excluded the noncontrolling interest in the net income of our joint venture. Net income (loss) excluding the noncontrolling interest in the net income of our joint venture is now presented after net income (loss), with the caption net income (loss) attributable to Verint Systems Inc.

- The noncontrolling interest, which was previously reflected in other liabilities, is now presented in stockholders' deficit, separate from Verint Systems Inc.'s stockholders' deficit, in the condensed consolidated balance sheets.
- The condensed consolidated statements of cash flows now begin with net income (loss), including the noncontrolling interest, instead of net income (loss) attributable to Verint Systems Inc.

In March 2008, the FASB amended the disclosure requirements for derivative instruments and hedging activities. This new guidance requires enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. This guidance was effective for us beginning on February 1, 2009.

In April 2009, the FASB issued staff positions that require enhanced fair value disclosures, including interim disclosures, on financial instruments, determination of fair value in turbulent markets, and recognition and presentation of other than temporary impairments. These staff positions were effective beginning with our quarter ended July 31, 2009. These staff positions did not have a material impact on our consolidated financial statements.

In May 2009, the FASB issued a new accounting standard that establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued. In February 2010, the FASB issued an amendment to this guidance that removed the requirement for an SEC filer to disclose a date through which subsequent events have been evaluated in both issued and revised financial statements. This standard, as amended, was effective for us beginning with our interim period ended July 31, 2009. The adoption of this standard, as amended, did not have a material impact on our consolidated financial statements.

During the three months ended October 31, 2009, we adopted the new Accounting Standards Codification ("ASC") as issued by the FASB. The ASC has become the source of authoritative U.S. GAAP recognized by the FASB to be applied by nongovernmental entities. The ASC is not intended to change or alter existing GAAP. The adoption of the ASC had no impact on our consolidated financial statements.

New Standards to be Implemented:

In June 2009, the FASB issued a new accounting standard related to the consolidation of variable interest entities, requiring a company to perform an analysis to determine whether its variable interests give it a controlling financial interest in a variable interest entity. This analysis requires a company to assess whether it has the power to direct the activities of the variable interest entity and if it has the obligation to absorb losses or the right to receive benefits that could potentially be significant to the variable interest entity. This standard requires an ongoing reassessment of whether a company is the primary beneficiary of a variable interest entity, eliminates the quantitative approach previously required for determining the primary beneficiary of a variable interest entity, and significantly enhances disclosures. The standard may be applied retrospectively to previously issued financial statements with a cumulative-effect adjustment to retained earnings as of the beginning of the first year restated. This standard is effective for us for the fiscal year beginning on February 1, 2010. The adoption of this standard is not expected to have a material impact on our consolidated financial statements.

In October 2009, the FASB issued guidance that applies to multiple-deliverable revenue arrangements. This guidance also provides principles and application guidance on whether a revenue arrangement contains multiple deliverables, how the arrangement should be separated, and how the arrangement consideration should be allocated. The guidance requires an entity to allocate revenue in a multiple-deliverable arrangement using estimated selling prices of the deliverables if a vendor does not have vendor specific objective evidence of fair value (“VSOE”) or third-party evidence of selling price. It eliminates the use of the residual method and, instead, requires an entity to allocate revenue using the relative selling price method. It also expands disclosure requirements with respect to multiple-deliverable revenue arrangements.

Also in October 2009, the FASB issued guidance related to multiple-deliverable revenue arrangements that contain both software and hardware elements, focusing on determining which revenue arrangements are within the scope of existing software revenue guidance. This additional guidance removes tangible products from the scope of the software revenue guidance and provides guidance on determining whether software deliverables in an arrangement that includes a tangible product are within the scope of the software revenue guidance. The above guidance related to revenue recognition should be applied on a prospective basis for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. It will be effective for us in our fiscal year beginning February 1, 2011, although early adoption is permitted. Alternatively, an entity can elect to adopt the provisions of these issues on a retrospective basis. We are assessing the impact that the application of this new guidance, and the new guidance discussed in the preceding paragraph, may have on our consolidated financial statements.

In January 2010, the FASB issued amended standards that require additional fair value disclosures. These disclosure requirements are effective in two phases. Effective in our fiscal year beginning February 1, 2010, the amended standards will require enhanced disclosures about inputs and valuation techniques used to measure fair value as well as disclosures about significant transfers. Effective in our fiscal year beginning February 1, 2011, the amended standards will require presentation of disaggregated activity within the reconciliation for fair value measurements using significant unobservable inputs (Level 3). These amended standards are not expected to significantly impact our consolidated financial statements.

2. NET INCOME (LOSS) PER SHARE ATTRIBUTABLE TO VERINT SYSTEMS INC.

The following table summarizes the calculation of basic and diluted net income (loss) per share attributable to Verint Systems Inc. for the three and nine months ended October 31, 2009 and 2008:

| (in thousands, except per share amounts) | Three Months Ended October 31, | | Nine Months Ended October 31, | |
|--|-----------------------------------|--------------------|----------------------------------|--------------------|
| | 2009 | 2008 | 2009 | 2008 |
| Net income (loss) | \$ 13,315 | \$ (20,441) | \$ 35,369 | \$ (59,932) |
| Net income attributable to noncontrolling interest | 139 | 695 | 961 | 1,588 |
| Net income (loss) attributable to Verint Systems Inc. | 13,176 | (21,136) | 34,408 | (61,520) |
| Dividends on preferred stock | (3,443) | (3,301) | (10,111) | (9,728) |
| Net income (loss) attributable to Verint Systems Inc. for basic net income (loss) per share | 9,733 | (24,437) | 24,297 | (71,248) |
| Dilutive effect of dividends on preferred stock | — | — | — | — |
| Net income (loss) attributable to Verint Systems Inc. for diluted net income (loss) per share | \$ 9,733 | \$ (24,437) | \$ 24,297 | \$ (71,248) |
| Weighted-average shares outstanding: | | | | |
| Basic | 32,471 | 32,387 | 32,465 | 32,385 |
| Dilutive effect of employee equity award plans | 859 | — | 414 | — |
| Dilutive effect of assumed conversion of preferred stock | — | — | — | — |
| Diluted | <u>33,330</u> | <u>32,387</u> | <u>32,879</u> | <u>32,385</u> |
| Net income (loss) per share attributable to Verint Systems Inc. | | | | |
| Basic | \$ 0.30 | \$ (0.75) | \$ 0.75 | \$ (2.20) |
| Diluted | \$ 0.29 | \$ (0.75) | \$ 0.74 | \$ (2.20) |

We excluded the following weighted-average shares underlying stock-based awards and convertible preferred stock from the calculations of diluted net income (loss) per share because their inclusion would have been anti-dilutive:

| (in thousands) | Three Months Ended October 31, | | Nine Months Ended October 31, | |
|---|-----------------------------------|-------|----------------------------------|-------|
| | 2009 | 2008 | 2009 | 2008 |
| Shares excluded from calculation: | | | | |
| Stock options and restricted stock-based awards | 4,666 | 7,514 | 4,982 | 7,431 |
| Convertible preferred stock | 9,882 | 9,508 | 9,788 | 9,417 |

Diluted weighted-average shares outstanding include the dilutive effect, if applicable, of in-the-money options and unvested restricted stock awards and restricted stock units, which is calculated based on the average share price for each period using the treasury stock method. Under the treasury stock method, the exercise price of the award, any unrecognized future service costs, and tax benefits that would be recorded as additional paid-in capital when the award becomes deductible are assumed to be used to repurchase shares.

Diluted weighted-average shares outstanding also include the dilutive effect, if applicable, of common shares issuable from the assumed conversion of our preferred stock.

In periods in which we report a net loss applicable to Verint Systems Inc., weighted-average shares outstanding for determining basic and diluted net loss per share are identical since the effect of potential common shares is antidilutive and therefore excluded.

3. INVENTORIES

Inventories consist of the following as of October 31, 2009 and January 31, 2009:

| (in thousands) | October 31, 2009 | January 31, 2009 |
|--------------------------|---------------------|---------------------|
| Raw materials | \$ 6,817 | \$ 6,389 |
| Work-in-process | 5,131 | 5,070 |
| Finished goods | 3,985 | 8,996 |
| Total inventories | \$ 15,933 | \$ 20,455 |

4. INTANGIBLE ASSETS AND GOODWILL

Acquisition-related intangible assets consist of the following as of October 31, 2009 and January 31, 2009:

| (in thousands) | October 31, 2009 | | |
|----------------------------|-------------------------|-------------------------------------|-------------------|
| | Cost | Accumulated Amortization | Net |
| Customer relationships | \$ 199,298 | \$ (50,251) | \$ 149,047 |
| Acquired technology | 54,889 | (26,567) | 28,322 |
| Trade names | 9,612 | (7,742) | 1,870 |
| Non-competition agreements | 3,440 | (2,106) | 1,334 |
| Distribution network | 2,440 | (803) | 1,637 |
| Total | \$ 269,679 | \$ (87,469) | \$ 182,210 |

| (in thousands) | January 31, 2009 | | |
|----------------------------|-------------------------|-------------------------------------|-------------------|
| | Cost | Accumulated Amortization | Net |
| Customer relationships | \$ 194,076 | \$ (34,420) | \$ 159,656 |
| Acquired technology | 53,781 | (20,134) | 33,647 |
| Trade names | 9,350 | (5,926) | 3,424 |
| Non-competition agreements | 3,416 | (1,760) | 1,656 |
| Distribution network | 2,440 | (620) | 1,820 |
| Total | \$ 263,063 | \$ (62,860) | \$ 200,203 |

Total amortization expense recorded for acquisition-related intangible assets was \$7.3 million and \$22.9 million for the three and nine months ended October 31, 2009, respectively, and \$8.4 million and \$26.2 million for the three and nine months ended October 31, 2008, respectively.

Estimated future finite-lived acquisition-related intangible asset amortization expense is as follows:

| (in thousands) | Amount |
|--------------------------------|-------------------|
| Years Ended January 31, | |
| 2010 (Remainder of year) | \$ 7,372 |
| 2011 | 29,487 |
| 2012 | 28,555 |
| 2013 | 27,776 |
| 2014 | 22,792 |
| 2015 and thereafter | 66,228 |
| Total | \$ 182,210 |

Goodwill activity for the nine months ended October 31, 2009, in total and by reportable segment, was as follows:

| (in thousands) | Total | Reportable Segment | | |
|--|-------------------|-------------------------------|---------------------------|------------------------------------|
| | | Workforce Optimization | Video Intelligence | Communications Intelligence |
| Goodwill, gross, at January 31, 2009 | \$ 776,849 | \$ 681,140 | \$ 65,726 | \$ 29,983 |
| Accumulated impairment losses at January 31, 2009 | (66,865) | (30,791) | (36,074) | — |
| Goodwill, net, at January 31, 2009 | 709,984 | 650,349 | 29,652 | 29,983 |
| Additional consideration — previous acquisitions (1) | 89 | — | — | 89 |
| Foreign currency translation | 19,472 | 17,196 | 2,276 | — |
| Goodwill, net, at October 31, 2009 | <u>\$ 729,545</u> | <u>\$ 667,545</u> | <u>\$ 31,928</u> | <u>\$ 30,072</u> |
| Balance at October 31, 2009 | | | | |
| Goodwill, gross, at October 31, 2009 | \$ 796,410 | \$ 698,336 | \$ 68,002 | \$ 30,072 |
| Accumulated impairment losses at October 31, 2009 | (66,865) | (30,791) | (36,074) | — |
| Goodwill, net, at October 31, 2009 | <u>\$ 729,545</u> | <u>\$ 667,545</u> | <u>\$ 31,928</u> | <u>\$ 30,072</u> |

(1) Contingent consideration for acquisitions completed in prior years.

We test our goodwill for impairment at least annually as of November 1, or more frequently if an event occurs indicating the potential for impairment. No events or circumstances indicating the potential for goodwill impairment were identified during either the nine months ended October 31, 2009 or the nine months ended October 31, 2008.

5. LONG-TERM DEBT

On May 25, 2007, to partially finance the acquisition of Witness Systems Inc. (“Witness”), we entered into a \$675.0 million secured credit facility comprised of a \$650.0 million seven-year term loan facility and a \$25.0 million six-year revolving credit facility.

The following is a summary of our outstanding financing arrangements as of October 31, 2009 and January 31, 2009:

| (in thousands) | October 31, 2009 | January 31, 2009 |
|---------------------------|-------------------------|-------------------------|
| Term loan facility | \$ 605,912 | \$ 610,000 |
| Revolving credit facility | 15,000 | 15,000 |
| Total debt | <u>620,912</u> | <u>625,000</u> |
| Less: current portion | 3,693 | 4,088 |
| Long-term debt | <u>\$ 617,219</u> | <u>\$ 620,912</u> |

The interest rates on the term loan were 3.50% and 3.59% as of October 31, 2009 and January 31, 2009, respectively.

Our \$25.0 million revolving line of credit facility was reduced to \$15.0 million during the three months ended October 31, 2008 as a result of the bankruptcy of Lehman Brothers. During the three months ended January 31, 2009, we borrowed the full \$15.0 million available under the revolving credit facility. Repayment of these borrowings is required upon expiration of the facility in May 2013. The interest rates on the revolving line of credit borrowings were 3.50% and 3.64% as of October 31, 2009 and January 31, 2009, respectively.

On May 25, 2007, concurrently with entry into our credit facility, we entered into a receive-variable/pay-fixed interest rate swap agreement with a multinational financial institution on a notional amount of \$450.0 million to mitigate a portion of the risk associated with variable interest rates on the term loan. This interest rate swap agreement terminates in May 2011. See Note 10, "Fair Value Measurements and Derivative Financial Instruments" for further details regarding the interest rate swap agreement.

We incurred interest expense on borrowings under our credit facilities of \$5.6 million and \$17.0 million during the three and nine months ended October 31, 2009, respectively, and \$9.3 million and \$27.8 million during the three and nine months ended October 31, 2008, respectively. We also recorded amortization of our deferred debt issuance costs of \$0.5 million and \$1.4 million during the three and nine months ended October 31, 2009, respectively, which is reported within interest expense. Amortization of our deferred debt issuance costs during the three and nine months ended October 31, 2008 was \$0.4 million and \$1.2 million, respectively.

In May 2009, we made a \$4.1 million mandatory "excess cash flow" prepayment of the term loan based upon our operating results for the year ended January 31, 2009, which was applied to the three immediately following principal payments.

The credit agreement also includes a requirement that we submit audited consolidated financial statements to the lenders within 90 days of the end of each fiscal year, beginning with the financial statements for the year ended January 31, 2010. Should we fail to deliver such audited consolidated financial statements as required, the agreement provides a thirty day period to cure such default, or an event of default occurs.

On April 27, 2010, we entered into an amendment to our credit agreement to extend the due date for delivery of audited consolidated financial statements and related documentation for the year ended January 31, 2010 from May 1, 2010 to June 1, 2010. See Note 14, "Subsequent Events" for further details regarding this amendment.

6. CONVERTIBLE PREFERRED STOCK

On May 25, 2007, in connection with our acquisition of Witness, we entered into a Securities Purchase Agreement with Comverse, whereby Comverse purchased, for cash, an aggregate of 293,000 shares of our Series A Convertible Preferred Stock, for an aggregate purchase price of \$293.0 million. Proceeds from the issuance of the preferred stock were used to partially finance the acquisition.

The terms of the preferred stock provide that upon a fundamental change, as defined, the holders of the preferred stock would have the right to require us to repurchase the preferred stock for 100% of the liquidation preference then in effect. Therefore, the preferred stock has been classified as mezzanine equity on our condensed consolidated balance sheets as of October 31, 2009 and January 31, 2009, separate from permanent equity, because the occurrence of these fundamental changes, and thus potential redemption of the preferred stock, however remote in likelihood, is not solely under our control. Fundamental change events include the sale of substantially all of our assets and certain changes in beneficial ownership, board of directors' representation, and business reorganizations.

We concluded that, as of October 31, 2009 and January 31, 2009, there were no indications that the occurrence of a fundamental change and the associated redemption of the preferred stock were probable. We therefore have not adjusted the initial carrying amount of the preferred stock to its redemption amount, which is its liquidation preference. Through October 31, 2009, cumulative, undeclared dividends on the preferred stock were \$29.8 million and as a result, the liquidation preference of the preferred stock was \$322.8 million at that date. If it were convertible at October 31, 2009, the preferred stock could be converted into approximately 9.9 million shares of our common stock.

7. STOCKHOLDERS' DEFICIT

Accumulated Other Comprehensive Loss

The following table summarizes, as of each balance sheet date, the components of our accumulated other comprehensive loss. Income tax effects on unrealized gains and losses on available-for-sale marketable securities and derivative financial instruments were not significant.

| (in thousands) | October 31, 2009 | January 31, 2009 |
|---|---------------------|---------------------|
| Foreign currency translation losses, net | \$ (38,318) | \$ (58,476) |
| Unrealized gains on derivative financial instruments | 403 | 101 |
| Unrealized gains (losses) on available-for-sale marketable securities | 3 | (29) |
| Total accumulated other comprehensive loss | \$ (37,912) | \$ (58,404) |

Foreign currency translation losses, net, primarily reflect the strengthening of the U.S. dollar against the British pound sterling since our acquisition of Witness in May 2007, which has resulted in lower U.S. dollar translated balances of British pound sterling denominated goodwill and intangible assets associated with the acquisition of Witness. The British pound sterling was weaker against the U.S. dollar at January 31, 2009 compared to October 31, 2009, resulting in larger net foreign currency translation losses at January 31, 2009 compared to October 31, 2009.

8. INTEGRATION, RESTRUCTURING AND OTHER, NET

Integration, restructuring and other, net, is comprised of the following for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | Three Months Ended October 31, | | Nine Months Ended October 31, | |
|--|-----------------------------------|-------------------|----------------------------------|-----------------|
| | 2009 | 2008 | 2009 | 2008 |
| Restructuring expenses | \$ — | \$ 1,284 | \$ 24 | 2,492 |
| Integration expenses | — | 844 | — | 2,979 |
| Other legal recoveries, net | — | (9,521) | — | (4,303) |
| Total integration, restructuring and other, net | \$ — | \$ (7,393) | \$ 24 | \$ 1,168 |

Restructuring and Integration Expenses

During the three months ended January 31, 2009, we implemented a global cost reduction plan in order to reduce our operating costs in response to uncertainty in the global economic environment. The associated restructuring charges consisted predominantly of severance and related employee payments resulting from terminations.

During the three and nine months October 31, 2008, we also recorded activity related to the following restructuring plans:

- During the three months ended July 31, 2008, as a result of reduced demand for our consulting services in Europe, we implemented a cost reduction plan in this sector of our Workforce Optimization segment. The associated restructuring charges consisted predominantly of severance and related employee payments related to terminations;
- Following the acquisition of Witness in May 2007, we implemented a plan to integrate the Witness business with our existing Workforce Optimization segment, which included actions to reduce fixed costs and eliminate redundancies; and
- During the year ended January 31, 2008, we implemented a restructuring plan in our Video Intelligence segment to reduce our overall cost structure, predominantly in our North American and Hong Kong locations.

The following table summarizes our restructuring expenses, by restructuring activity, for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | Three Months Ended October 31, | | Nine Months Ended October 31, | |
|--------------------------------|-----------------------------------|-----------------|----------------------------------|-----------------|
| | 2009 | 2008 | 2009 | 2008 |
| Restructuring activity: | | | | |
| Global cost reduction plan | \$ — | \$ — | \$ 24 | \$ — |
| Consulting business in Europe | — | 879 | — | 1,370 |
| Acquisition of Witness | — | 238 | — | 858 |
| Video Intelligence plan | — | 167 | — | 264 |
| Total | \$ — | \$ 1,284 | \$ 24 | \$ 2,492 |

The following table summarizes the activity during the nine months ended October 31, 2009 in accrued restructuring expenses:

| | Global Cost Reduction Plan | Video Intelligence Plan | Total |
|---|-------------------------------|----------------------------|---------------|
| Accrued restructuring costs — January 31, 2009 | \$ 531 | \$ 10 | \$ 541 |
| Expenses accrued | 24 | — | 24 |
| Payments and settlements | (548) | (10) | (558) |
| Accrued restructuring costs — October 31, 2009 | \$ 7 | \$ — | \$ 7 |

In addition to the aforementioned restructuring expenses, we also incurred integration expenses of \$0.8 million and \$3.0 million during the three and nine months ended October 31, 2008, respectively, resulting from the integration of the Witness and Verint businesses following our May 2007 acquisition of Witness. The process of integrating the Witness and Verint businesses was substantially complete as of January 31, 2009.

Other Legal Recoveries, Net

During the three months ended October 31, 2008, an ongoing patent infringement litigation matter was settled in our favor, for which we received a \$9.7 million settlement payment. The \$9.7 million settlement was partially offset by \$0.2 million and \$5.4 million of related legal fees incurred during the three and nine months ended October 31, 2008, respectively. The resulting net recovery was \$9.5 million and \$4.3 million for three and nine months ended October 31, 2008, respectively.

9. INCOME TAXES

Our quarterly provision for (benefit from) income taxes is measured using an estimated annual effective tax rate for the period, adjusted for discrete items that occurred within the periods presented. For the three months ended October 31, 2009, we recorded an income tax provision of \$1.8 million, which represents an effective tax rate of 11.9%. This rate is lower than the U.S. federal statutory rate of 35% primarily because we recorded an income tax provision on income from certain foreign subsidiaries taxed at rates lower than the U.S. federal statutory rate, but did not record a U.S. federal income tax benefit because we maintain a valuation allowance against our U.S. deferred tax assets. The comparison of our effective tax rate between periods is significantly impacted by the level and mix of earnings and losses by taxing jurisdiction, foreign income tax rate differentials, relative impact of permanent book to tax differences, and the effects of valuation allowances.

For the three months ended October 31, 2008, we recorded an income tax expense of \$9.4 million, which represents an effective tax rate of (85.8%). The tax rate for the period is negative since we recorded income tax expense on a consolidated pre-tax loss. We recorded a valuation allowance against certain domestic and foreign pre-tax losses and recorded an income tax provision in certain profitable jurisdictions. The rate is higher than the U.S. federal statutory rate primarily due to the mix of income and losses by jurisdiction and the impact of permanent book to tax differences.

For the nine months ended October 31, 2009, we recorded an income tax provision of \$8.9 million, which represents an effective tax rate of 20.1%. This rate is lower than the U.S. federal statutory rate of 35% primarily because we recorded an income tax provision on income from certain foreign subsidiaries taxed at rates lower than the U.S. federal statutory rate. We did not record significant U.S. federal income tax expense because we maintain a valuation allowance against our U.S. deferred tax assets. The comparison of our effective tax rate between periods is significantly impacted by the level and mix of earnings and losses by taxing jurisdiction, foreign income tax rate differentials, relative impact of permanent book to tax differences, and the effects of valuation allowances.

For the nine months ended October 31, 2008, we recorded an income tax provision of \$10.9 million, which represents an effective tax rate of (22.2%). The tax rate for the period is negative since we recorded income tax expense on a consolidated pre-tax loss. We recorded a valuation allowance against certain domestic and foreign pre-tax losses and an income tax provision in certain profitable jurisdictions.

As required by the authoritative guidance on accounting for income taxes, we evaluate the realizability of deferred tax assets on a jurisdictional basis at each reporting date. Accounting for income taxes requires that a valuation allowance be established when it is more likely than not that all or a portion of the deferred tax assets will not be realized. In circumstances where there is sufficient negative evidence indicating that the deferred tax assets are not more-likely-than-not realizable, we establish a valuation allowance. We determined there is sufficient negative evidence to maintain the valuation allowances against our federal and certain state and foreign deferred tax assets as a result of historical losses in the U.S. and certain foreign jurisdictions. We intend to maintain a valuation allowance against these assets until sufficient positive evidence exists to support its reversal.

As of October 31, 2009, we had unrecognized tax benefits of \$37.8 million (excluding interest and penalties) of which the total amount, if recognized, would impact the effective tax rate was approximately \$32.8 million. We regularly assess the adequacy of our provisions for income tax contingencies in accordance with the applicable authoritative guidance on accounting for income taxes. As a result, we may adjust the reserves for unrecognized tax benefits for the impact of new facts and developments, such as changes to interpretations of relevant tax law, assessments from taxing authorities, settlements with taxing authorities, and lapses of statutes of limitation. We believe that it is reasonably possible that the total amount of unrecognized tax benefits at October 31, 2009 could decrease by approximately \$1.7 million in the next twelve months as a result of settlement of certain tax audits or lapses of statutes of limitation. Such decreases may involve the payment of additional taxes, the adjustment of certain deferred taxes including the need for additional valuation allowances, and the recognition of tax benefits. Our income tax returns are subject to ongoing tax examinations in several jurisdictions in which we operate. We also believe that it is reasonably possible that new issues may be raised by tax authorities or developments in tax audits may occur which would require increases or decreases to the balance of reserves for unrecognized tax benefits; however, an estimate of such changes cannot reasonably be made.

10. FAIR VALUE MEASUREMENTS AND DERIVATIVE FINANCIAL INSTRUMENTS

Fair value is defined as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required to be recorded at fair value, we consider the principal or most advantageous market in which we would transact and consider assumptions that market participants would use when pricing the asset or liability, such as inherent risk, transfer restrictions, and risk of nonperformance.

Accounting guidance establishes a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. An instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. This fair value hierarchy consists of 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: inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices in active markets for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; or

Level 3: unobservable inputs that are supported by little or no market activity.

Assets and liabilities are classified based on the lowest level of input that is significant to the fair value measurements. We review the fair value hierarchy classification of our applicable assets and liabilities on a quarterly basis. Changes in the observability of valuation inputs may result in transfers within the fair value measurement hierarchy. We did not identify any transfers between levels of the fair value measurement hierarchy during the nine months ended October 31, 2009.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

Our assets and liabilities measured at fair value on a recurring basis consisted of the following as of October 31, 2009 and January 31, 2009:

| (in thousands) | October 31, 2009 | | |
|------------------------------------|--------------------------------------|------------------|----------------|
| | Fair Value Hierarchy Category | | |
| | Level 1 | Level 2 | Level 3 |
| Assets: | | | |
| Money market funds | \$ 31,217 | \$ — | \$ — |
| Foreign currency forward contracts | — | 437 | — |
| Total assets | \$ 31,217 | \$ 437 | \$ — |
| Liabilities: | | | |
| Foreign currency forward contracts | \$ — | \$ 1,491 | \$ — |
| Interest rate swap agreement | — | 32,568 | — |
| Total liabilities | \$ — | \$ 34,059 | \$ — |
| | January 31, 2009 | | |
| | Fair Value Hierarchy Category | | |
| | Level 1 | Level 2 | Level 3 |
| Assets: | | | |
| Money market funds | \$ 34,292 | \$ — | \$ — |
| Foreign currency forward contracts | — | 146 | — |
| Total assets | \$ 34,292 | \$ 146 | \$ — |
| Liabilities: | | | |
| Foreign currency forward contracts | \$ — | \$ 2,000 | \$ — |
| Interest rate swap agreement | — | 33,114 | — |
| Total liabilities | \$ — | \$ 35,114 | \$ — |

Fair Value Measurements

Money Market Funds - We value our money market funds using quoted market prices for such funds.

Foreign Currency Forward Contracts - The estimated fair value of foreign currency forward contracts is based on quotes received from the counterparty. These quotes are reviewed for reasonableness by discounting the future estimated cash flows under the contracts, considering the terms and maturities of the contracts and market exchange rates.

Interest Rate Swap Agreement - The fair value of our interest rate swap agreement is based in part on data received from a third party financial institution. These fair values represent the estimated amount we would receive or pay to settle the swap agreement, taking into consideration current and projected interest rates as well as the creditworthiness of the parties.

Derivative Financial Instruments

Interest Rate Swap Agreement

The interest rates applicable to borrowings under our credit facilities are variable, and we are exposed to risk from changes in the underlying index interest rates, which affect our cost of borrowing. To partially mitigate this risk, and in part because we were required to do so by the lenders, when we entered into our credit facilities in May 2007, we executed a pay-fixed, receive-variable interest rate swap with a high credit-quality multinational financial institution under which we pay fixed interest at 5.18% and receive variable interest of the three-month London Interbank Offering Rate ("LIBOR") on a notional amount of \$450.0 million. This instrument is settled with the counterparty on a quarterly basis, and matures on May 1, 2011. As of October 31, 2009, of the \$620.9 million of borrowings which were outstanding under the term loan facility, the interest rate on \$450.0 million of such borrowings was substantially fixed by utilization of this interest rate swap. Interest on the remaining \$170.9 million of borrowings was variable.

The interest rate swap is not designated as a hedging instrument under derivative accounting guidance, and gains and losses from changes in its fair value are therefore reported in other income (expense), net.

Foreign Currency Forward Contracts

Under our risk management strategy, we periodically use derivative instruments to manage our short-term exposures to fluctuations in foreign currency exchange rates. We utilize foreign exchange forward contracts to hedge certain operational cash flow exposures resulting from changes in foreign currency exchange rates. These cash flow exposures result from portions of our forecasted operating expenses, primarily compensation and related expenses, which are transacted in currencies other than the U.S. dollar, primarily the Israeli shekel and the Canadian dollar. Our joint venture, which has a Singapore dollar functional currency, also utilizes foreign exchange forward contracts to manage its exposure to exchange rate fluctuations related to settlement of liabilities denominated in U.S. dollars. These foreign currency forward contracts are reported at fair value on our consolidated balance sheets and have maturities of no longer than twelve months. We enter into these foreign currency forward contracts in the normal course of business to mitigate risks and not for speculative purposes.

The counterparties to our derivative financial instruments consist of several major international financial institutions. We regularly monitor the financial strength of these institutions. While the counterparties to these contracts expose us to credit-related losses in the event of a counterparty's non-performance, the risk would be limited to the unrealized gains on such affected contracts. We do not anticipate any such losses.

Certain of these foreign currency forward contracts are not designated as hedging instruments under derivative accounting guidance, and gains and losses from changes in their fair values are therefore reported in other income (expense), net. Changes in the fair value of foreign currency forward contracts that are designated and effective as cash flow hedges are recorded net of related tax effects in accumulated other comprehensive income (loss), and are reclassified to the statement of operations when the effects of the item being hedged are recognized in the statement of operations.

The total notional amounts for outstanding derivatives (recorded at fair value) as of October 31, 2009 and January 31, 2009 were as follows:

| (in thousands) | October 31, 2009 | January 31, 2009 |
|------------------------------------|-----------------------------|-----------------------------|
| Foreign currency forward contracts | \$ 49,359 | \$ 35,900 |
| Interest rate swap agreement | 450,000 | 450,000 |
| | <u>\$ 499,359</u> | <u>\$ 485,900</u> |

Fair Values of Derivative Financial Instruments

The fair values of our derivative financial instruments as of October 31, 2009 and January 31, 2009 were as follows:

| (in thousands) | October 31, 2009 | | | |
|---|--|---------------|--|------------------|
| | Assets | | Liabilities | |
| | Balance Sheet Classification | Fair Value | Balance Sheet Classification | Fair Value |
| Derivative financial instruments designated as hedging instruments: | | | | |
| Foreign currency forward contracts | Prepaid expenses and other current assets | \$ 437 | — | \$ — |
| Total derivative financial instruments designated as hedging instruments | | \$ 437 | | \$ — |
| Derivative financial instruments not designated as hedging instruments: | | | | |
| Foreign currency forward contracts | — | \$ — | Accrued expenses and other liabilities | \$ 1,491 |
| Interest rate swap — current portion | — | — | Accrued expenses and other liabilities | 20,549 |
| Interest rate swap — long-term portion | — | — | Other liabilities | 12,019 |
| Total derivative financial instruments not designated as hedging instruments | | \$ — | | \$ 34,059 |
| January 31, 2009 | | | | |
| (in thousands) | Assets | | Liabilities | |
| | Balance Sheet Classification | Fair Value | Balance Sheet Classification | Fair Value |
| | Derivative financial instruments designated as hedging instruments: | | | |
| Foreign currency forward contracts | Prepaid expenses and other current assets | \$ 146 | — | \$ — |
| Total derivative financial instruments designated as hedging instruments | | \$ 146 | | \$ — |
| Derivative financial instruments not designated as hedging instruments: | | | | |
| Foreign currency forward contracts | — | \$ — | Accrued expenses and other liabilities | \$ 2,000 |
| Interest rate swap — current portion | — | — | Accrued expenses and other liabilities | 14,851 |
| Interest rate swap — long-term portion | — | — | Other liabilities | 18,263 |
| Total derivative financial instruments not designated as hedging instruments | | \$ — | | \$ 35,114 |

The effects of derivative financial instruments in cash flow hedging relationships as of October 31, 2009 and January 31, 2009, and for the three and nine months ended October 31, 2009 and 2008 were as follows:

| (in thousands) | Gains Recognized in Accumulated Other Comprehensive Loss | | Classification of Gains Reclassified from Other Comprehensive Income (Loss) into the Condensed Statements of Operations | Gains Reclassified from Other Comprehensive Income (Loss) into the Condensed Statements of Operations | | | |
|------------------------------------|--|------------------|---|---|------|-------------------------------|------|
| | October 31, 2009 | January 31, 2009 | | Three Months Ended October 31, | | Nine Months Ended October 31, | |
| | | | | 2009 | 2008 | 2009 | 2008 |
| Foreign currency forward contracts | \$ 403 | \$ 101 | Operating Expenses | \$ 1,382 | \$ — | \$ 2,555 | \$ — |

There were no gains or losses from ineffectiveness of these financial instruments recorded for the three and nine months ended October 31, 2009 and 2008.

Losses recognized on derivative financial instruments not designated as hedging instruments in our condensed consolidated statements of operations for the three and nine months ended October 31, 2009 and 2008 were as follows:

| (in thousands) | Classification in Condensed Statements of Operations | Three Months Ended October 31, | | Nine Months Ended October 31, | |
|------------------------------------|--|--------------------------------|-----------------------------|-------------------------------|-------------------|
| | | 2009 | 2008 | 2009 | 2008 |
| | | Interest rate swap agreement | Other income (expense), net | \$ (4,434) | \$ (8,145) |
| Foreign currency forward contracts | Other income (expense), net | (276) | (1,128) | (740) | (1,249) |
| Total | | \$ (4,710) | \$ (9,273) | \$ (11,745) | \$ (2,554) |

Other Financial Instruments

The carrying amounts of accounts receivable, accounts payable and accrued liabilities approximate fair value due to their short maturities.

As of October 31, 2009, the estimated fair values of our outstanding term loan and revolving credit facility borrowings were \$554.4 million and \$15.0 million, respectively. As of January 31, 2009, the estimated fair values of our outstanding term loan and revolving credit facility borrowings were \$359.9 million and \$15.0 million, respectively. The estimated fair values of the term loan are based upon the estimated bid and asked prices as determined by the agent responsible for the syndication of our term loan. The fair value of the revolving credit facility is assumed to equal the principal amount outstanding for both October 31, 2009 and January 31, 2009.

Assets and Liabilities Not Measured at Fair Value on a Recurring Basis

In addition to assets and liabilities that are measured at fair value on a recurring basis, we also measure certain assets and liabilities at fair value on a nonrecurring basis. Our non-financial assets, including goodwill, intangible assets and property, plant and equipment, are measured at fair value when there is an indication of impairment and the carrying amount exceeds the asset's projected undiscounted cash flows. These assets are recorded at fair value only when an impairment charge is recognized.

II. STOCK -BASED COMPENSATION

We recognized stock-based compensation expense in the following line items on the condensed consolidated statements of operations for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | Three Months Ended October 31, | | Nine Months Ended October 31, | |
|---|-----------------------------------|-----------------|----------------------------------|------------------|
| | 2009 | 2008 | 2009 | 2008 |
| Cost of revenue — product | \$ 405 | \$ 152 | \$ 852 | \$ 427 |
| Cost of revenue — service and support | 1,241 | 1,247 | 3,268 | 3,974 |
| Research and development, net | 2,297 | 1,643 | 5,501 | 5,347 |
| Selling, general, and administrative | 7,739 | 6,731 | 21,759 | 18,810 |
| Total stock-based compensation expense | \$ 11,682 | \$ 9,773 | \$ 31,380 | \$ 28,558 |

Total stock-based compensation expense by classification was as follows for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | Three Months Ended October 31, | | Nine Months Ended October 31, | |
|---|-----------------------------------|-----------------|----------------------------------|------------------|
| | 2009 | 2008 | 2009 | 2008 |
| Equity-classified awards | \$ 7,638 | \$ 8,335 | \$ 23,170 | \$ 24,934 |
| Liability-classified awards | 4,044 | 1,438 | 8,210 | 3,624 |
| Total stock-based compensation expense | \$ 11,682 | \$ 9,773 | \$ 31,380 | \$ 28,558 |

Stock Options

We have not granted stock options subsequent to January 31, 2006. However, in connection with our acquisition of Witness on May 25, 2007, options to purchase Witness common stock were converted into options to purchase approximately 3.1 million shares of our common stock.

Restricted Stock Awards and Restricted Stock Units

We periodically award shares of restricted stock, as well as restricted stock units, to our directors, officers and other employees. These awards contain various vesting conditions, and are subject to certain restrictions and forfeiture provisions prior to vesting.

During the three months ended October 31, 2009 and 2008, we did not grant any restricted stock awards and restricted stock units. During the nine months ended October 31, 2009 and 2008, we granted 1.8 million and 0.9 million combined restricted stock awards and restricted stock units, respectively. Restricted stock awards and restricted stock units aggregating 0.1 million were forfeited in each nine-month period. As of October 31, 2009 and 2008, we had 3.5 million and 2.0 million of combined restricted stock awards and stock units outstanding, respectively with weighted-average grant date fair values of \$6.50 and \$18.07, respectively.

As of October 31, 2009, there was approximately \$16.1 million of total unrecognized compensation expense, net of estimated forfeitures, related to unvested restricted stock awards and restricted stock units, which is expected to be recognized over weighted-average periods of 0.3 years for restricted stock awards and 1.0 years for restricted stock units.

Phantom Stock Units

We issue phantom stock units to certain non-officer employees that settle, or are expected to settle, with cash payments upon vesting. Like equity-settled awards, phantom stock units are awarded with vesting conditions and are subject to certain forfeiture provisions prior to vesting.

Phantom stock units granted during the three months ended October 31, 2009 were not significant. During the nine months ended October 31, 2009, we granted 0.4 million phantom stock units. During the three and nine months ended October 31, 2008, we granted 0.8 million and 1.3 million phantom stock units, respectively. 0.1 million phantom stock units were forfeited during the nine months ended October 31, 2009 and forfeitures were not significant during the nine months ended October 31, 2008. Total cash payments made upon vesting of phantom stock units were \$2.3 million for the nine months ended October 31, 2009. There were no cash payments made during the three months ended October 31, 2009, and the three and nine months ended October 31, 2008. The total accrued liability for phantom stock units was \$9.9 million and \$4.0 million as of October 31, 2009 and January 31, 2009, respectively.

12. LEGAL PROCEEDINGS

There were no material legal proceedings which arose, or in which there were material developments, during the three months ended October 31, 2009.

13. SEGMENT INFORMATION

We conduct our business in three operating segments — Enterprise Workforce Optimization Solutions (“Workforce Optimization”), Video Intelligence Solutions (“Video Intelligence”), and Communications Intelligence and Investigative Solutions (“Communications Intelligence”).

We measure the performance of our operating segments based upon operating segment revenue and operating segment contribution. Operating segment contribution includes segment revenue and expenses incurred directly by the segment, including material costs, service costs, research and development and selling, marketing, and administrative expenses. We do not allocate certain expenses, which include the majority of general and administrative expenses, facilities and communication expenses, purchasing expenses, manufacturing support and logistic expenses, depreciation and amortization, amortization of capitalized software development costs, stock-based compensation, and special charges such as restructuring and integration expenses. These expenses are included in the unallocated expenses section of the table presented below. Revenue from transactions between our operating segments is not material.

With the exception of goodwill and acquired intangible assets, we do not identify or allocate our assets by operating segment. Consequently, it is not practical to present assets by operating segment. There were no material changes in the allocation of goodwill and acquired intangible assets by operating segment during the nine months ended October 31, 2009 and 2008.

Operating results by segment for the three and nine months ended October 31, 2009 and 2008 were as follows:

| (in thousands) | Three Months Ended October 31, | | Nine Months Ended October 31, | |
|--|-----------------------------------|---------------------------|----------------------------------|---------------------------|
| | 2009 | 2008 | 2009 | 2008 |
| Revenue: | | | | |
| Workforce Optimization | | | | |
| Segment Revenue | \$ 105,398 | \$ 90,786 | \$ 279,001 | \$ 271,805 |
| Revenue adjustment | — | 133 | — | 5,865 |
| | <u>105,398</u> | <u>90,653</u> | <u>279,001</u> | <u>265,940</u> |
| Video Intelligence | 33,985 | 30,893 | 116,548 | 94,665 |
| Communications Intelligence | 47,097 | 36,321 | 135,348 | 118,241 |
| Total revenue | <u>\$ 186,480</u> | <u>\$ 157,867</u> | <u>\$ 530,897</u> | <u>\$ 478,846</u> |
| Segment contribution: | | | | |
| Workforce Optimization | \$ 54,058 | \$ 36,449 | \$ 136,024 | \$ 101,334 |
| Video Intelligence | 11,916 | 6,767 | 50,073 | 18,174 |
| Communications Intelligence | 14,892 | 9,740 | 46,125 | 33,270 |
| Total segment contribution | 80,866 | 52,956 | 232,222 | 152,778 |
| Unallocated expenses, net: | | | | |
| Amortization of other acquired intangible assets | 7,349 | 8,367 | 22,941 | 26,169 |
| Stock-based compensation | 11,682 | 9,773 | 31,380 | 28,558 |
| Integration, restructuring and other, net | — | (7,393) | 24 | 1,168 |
| Other unallocated expenses | 38,100 | 36,810 | 104,424 | 117,621 |
| | <u>57,131</u> | <u>47,557</u> | <u>158,769</u> | <u>173,516</u> |
| Operating income (loss) | 23,735 | 5,399 | 73,453 | (20,738) |
| Other expense, net | (8,617) | (16,399) | (29,163) | (28,307) |
| Income (loss) before provision for income taxes | <u>\$ 15,118</u> | <u>\$ (11,000)</u> | <u>\$ 44,290</u> | <u>\$ (49,045)</u> |

For the three and nine months ended October 31, 2008, Workforce Optimization segment revenue includes \$0.1 million and \$5.9 million, respectively, of additional revenue, primarily related to deferred maintenance and service revenue, not recognizable in our GAAP revenue as a result of purchase accounting following our May 2007 acquisition of Witness. We include this additional revenue within our segment revenue because it better reflects our ongoing maintenance and service revenue stream.

14. SUBSEQUENT EVENTS

Wells Notices

On April 9, 2008, as we previously reported, we received a “Wells Notice” from the staff of the SEC arising from the staff’s investigation of our past stock option grant practices and certain unrelated accounting matters. These accounting matters were also the subject of our internal investigation. On March 3, 2010, the SEC filed a settled enforcement action against us in the United States District Court for the Eastern District of New York relating to certain of our accounting reserve practices. Without admitting or denying the allegations in the SEC’s Complaint, we consented to the issuance of a Final Judgment permanently enjoining us from violating Section 17(a) of the Securities Act of 1933, as amended (the “Securities Act”), Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act, and Rules 13a-1 and 13a-13 thereunder. The settled SEC action did not require us to pay any monetary penalty and sought no relief beyond the entry of a permanent injunction. The SEC’s related press release noted that, in accepting the settlement offer, the SEC considered our remediation and cooperation in the SEC’s investigation. The settlement was approved by the United States District Court for the Eastern District of New York on March 9, 2010.

On December 23, 2009, as we previously reported, we received an additional “Wells Notice” from the staff of the SEC relating to our failure to timely file periodic reports under the Exchange Act. Under the SEC’s Wells process, recipients of a Wells Notice have the opportunity to make a Wells Submission before the SEC staff makes a recommendation to the SEC regarding what action, if any, should be brought by the SEC. After considering our Wells Submission, on March 3, 2010, the SEC issued an Order Instituting Proceedings (“OIP”) pursuant to Section 12(j) of the Exchange Act to suspend or revoke the registration of our common stock because of our previous failure to file an annual report on either Form 10-K or Form 10-KSB since April 25, 2005 or quarterly reports on either Form 10-Q or Form 10-QSB since December 12, 2005. On May 28, 2010, we entered into an agreement in principle with the SEC’s Division of Enforcement regarding the terms of a settlement of the SEC’s Section 12(j) proceeding. Under the agreement in principle, the Division of Enforcement will recommend to the SEC that the Section 12(j) proceeding against us be dismissed if we file our Form 10-Q for the three months ended April 30, 2010 on a timely basis and file our Forms 10-Q for the three months ended April 30, 2009, July 31, 2009, and October 31, 2009 by 5:30 p.m. EDT on June 21, 2010. The agreement in principle is subject to approval by the SEC. As a result of the agreement in principle, on June 1, 2010, a joint motion by the parties to stay the Section 12(j) proceeding was granted by the administrative law judge hearing the case and a conference was scheduled for July 2, 2010 to discuss the status of settlement. If the proceeding is not dismissed, we intend to vigorously defend the matter. On June 9, 2010, we timely filed our Quarterly Report on Form 10-Q for the three months ended April 30, 2010.

Business Combination

On February 4, 2010, our wholly owned subsidiary, Verint Americas Inc., acquired all of the outstanding shares of Iontas Limited (“Iontas”), a privately held provider of desktop analytics solutions. Prior to this acquisition, we licensed certain technology from Iontas, whose solutions measure application usage and analyze workflows to help improve staff performance in contact center, branch, and back-office operations environments. We acquired Iontas, among other objectives, to expand the desktop analytical capabilities of our workforce optimization solutions.

We acquired Iontas for total consideration valued at \$21.9 million, including cash consideration of \$17.9 million, and additional milestone-based contingent payments of up to \$3.8 million, tied to certain performance targets being achieved over the next two years.

We have included the acquisition-date estimated fair value of the contingent consideration of \$3.2 million as a component of the purchase price of Iontas. The acquisition-date fair value of the contingent consideration was measured based on the probability-adjusted present value of the contingent consideration expected to be earned and transferred.

Our purchase price to acquire Iontas also includes \$1.5 million of prepayments for product licenses and support services procured from Iontas prior to the acquisition date, partially offset by \$0.7 million of trade accounts payable to Iontas as of the acquisition date.

The following table sets forth the components and the preliminary allocation of the purchase price of Iontas:

| (in thousands) | Amount |
|--|-------------------------|
| Components of Purchase Price: | |
| Cash | \$ 17,861 |
| Fair value of contingent consideration | 3,224 |
| Prepaid product licenses and support services | 1,493 |
| Trade accounts payable | (712) |
| Total purchase price | <u>\$ 21,866</u> |
| Preliminary Allocation of Purchase Price: | |
| Net tangible assets | \$ 1,740 |
| Identifiable intangible assets: | |
| Developed technology | 6,949 |
| Non-competition agreements | 278 |
| Total identifiable intangible assets | <u>7,227</u> |
| Goodwill | 12,899 |
| Total purchase price | <u>\$ 21,866</u> |

Among the factors that contributed to the recognition of goodwill in this transaction were the expansion of our desktop analytical capabilities, the expansion of our suite of products and services, and the addition of an assembled workforce. This goodwill has been assigned to our Workforce Optimization segment, and is not deductible for income tax purposes.

We incurred \$1.2 million of transaction costs, primarily professional fees, directly related to the acquisition of Iontas, which were expensed as incurred.

Amendment to Credit Agreement

On April 27, 2010, we entered into an amendment to our credit agreement to extend the due date for delivery of audited consolidated financial statements and related documentation for the year ended January 31, 2010 from May 1, 2010 to June 1, 2010. In consideration for this amendment, we paid \$0.9 million to our lenders. This payment will be amortized as additional interest expense over the remaining term of the credit agreement using the effective interest method. Legal fees and other out-of-pocket costs directly relating to the amendment, which were expensed as incurred, were not significant.

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

The following management's discussion and analysis of our financial condition and results of operations is designed to provide a better understanding of the significant factors related to our results of operations and financial condition. The following information should be read in conjunction with our audited consolidated financial statements and the notes thereto included in our Annual Report on Form 10-K for the year ended January 31, 2009 and our unaudited condensed consolidated financial statements and notes thereto contained in this report. In addition, because we have filed our Annual Report on Form 10-K for the year ended January 31, 2010, which contains information for periods subsequent to October 31, 2009, you should read the information presented below in conjunction with the Annual Report on Form 10-K for the year ended January 31, 2010. This discussion contains a number of forward-looking statements, all of which are based on our current expectations and all of which could be affected by uncertainties and risks. Our actual results may differ materially from the results contemplated in these forward-looking statements as a result of many factors including, but not limited to, those described under "Cautionary Note on Forward Looking Statements".

Business Overview

Verint is a global leader in Actionable Intelligence® solutions and value-added services. Our solutions enable organizations of all sizes to make timely and effective decisions to improve enterprise performance and make the world a safer place. More than 10,000 organizations in over 150 countries – including over 80% of the Fortune 100 – use Verint solutions to capture, distill, and analyze complex and underused information sources, such as voice, video, and unstructured text.

In the enterprise market, our Workforce Optimization solutions help organizations enhance customer service operations in contact centers, branches, and back-office environments to increase customer satisfaction, reduce operating costs, identify revenue opportunities, and improve profitability. In the security intelligence market, our video intelligence, public safety, and communications intelligence and investigative solutions are vital to government and commercial organizations in their efforts to protect people and property and neutralize terrorism and crime.

Critical Accounting Policies and Estimates

Note 1, “Summary of Significant Accounting Policies”, to the consolidated financial statements in our Annual Report on Form 10-K for the year ended January 31, 2009 describes the significant accounting policies and methods used in the preparation of our consolidated financial statements. The accounting policies that reflect our more significant estimates, judgments and assumptions in the preparation of our consolidated financial statements are described in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Item 7 of our Annual Report on Form 10-K for the year ended January 31, 2009, and include the following:

- revenue recognition;
- accounting for business combinations;
- impairment of goodwill and intangible assets;
- accounting for income taxes;
- contingencies;
- accounting for stock-based compensation; and
- allowance for doubtful accounts.

There were no material changes during the nine months ended October 31, 2009 to our critical accounting policies and estimates as disclosed in our Form 10-K for the year ended January 31, 2009.

Impact of Our VSOE/Revenue Recognition Policies on our Results of Operations

As we have previously reported in our filings with the SEC, we have not established VSOE for certain elements of our arrangements, primarily our product offerings. We recognize revenue under the Residual Method when VSOE does not exist for all delivered elements of an arrangement. Under the Residual Method, the value of our delivered products is derived by ascertaining the fair value of all undelivered elements (i.e., post-contract customer support (“PCS”) and other services) and subtracting the fair value of the undelivered elements from the total arrangement value to determine the appropriate amount of revenue to recognize upon delivery of our products. However, if the fair value of all undelivered elements cannot be determined, revenue recognition is deferred for all elements, including delivered elements, until all elements are delivered, except if the only undelivered element is PCS. If VSOE for PCS does not exist the entire arrangement fee is recognized ratably over the PCS period or the period that the customer is entitled to renew their PCS but not to exceed the estimated economic life of the product or contractual period (“Ratable Method”). In addition, several of our Communications Intelligence contracts require substantial customization, and are therefore accounted for under contract accounting methods, using either the percentage of completion method or completed contract method (“Contract Accounting Method”).

As we have previously reported in our filings with the SEC, we determined that for many of the arrangements we entered into during previously reported periods (including periods included in this report), we were unable to determine the fair value of all or some of the elements within multiple-element arrangements, as required by accounting guidance for revenue recognition. Further, for certain transactions occurring during periods reported herein, we were similarly unable to determine the fair value of all or some of the elements. Therefore, certain arrangements are being recognized ratably on a straight line basis over a period of time ranging from a couple of quarters to several years while other transactions are recognized as delivery occurs based on the ability to establish VSOE for the undelivered elements.

We believe that, in most cases, we have or will have changed our business processes and systems in a way that will enable us to establish fair value for each undelivered element in our offerings. These changes are intended to enable us to recognize revenue from products and services upon delivery instead of recognizing the entire arrangement fee over the PCS period. As a result, we expect the amount of revenue we will recognize in future periods that originated from transactions occurring in prior periods will diminish over time. However, we believe that we will, in certain situations, continue to enter into arrangements that will require revenue to be deferred over longer periods of time.

Results of Operations

Financial Overview

The following table sets forth summary financial information for the three and nine months ended October 31, 2009 and 2008:

| (in thousands, except per share data) | Three Months Ended October 31, | | Nine Months Ended October 31, | |
|---|-----------------------------------|-------------|----------------------------------|-------------|
| | 2009 | 2008 | 2009 | 2008 |
| Revenue | \$ 186,480 | \$ 157,867 | \$ 530,897 | \$ 478,846 |
| Operating income (loss) | \$ 23,735 | \$ 5,399 | \$ 73,453 | \$ (20,738) |
| Net income (loss) attributable to Verint Systems Inc. common shares | \$ 9,733 | \$ (24,437) | \$ 24,297 | \$ (71,248) |
| Net income (loss) per share attributable to Verint Systems Inc.: | | | | |
| Basic | \$ 0.30 | \$ (0.75) | \$ 0.75 | \$ (2.20) |
| Diluted | \$ 0.29 | \$ (0.75) | \$ 0.74 | \$ (2.20) |

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Our revenue increased approximately 18%, or \$28.6 million, to \$186.5 million in the three months ended October 31, 2009 from \$157.9 million in the three months ended October 31, 2008 due to revenue increases in all three of our operating segments. In our Workforce Optimization segment, revenue increased by \$14.7 million, or 16%, primarily due to the completion of a multi-site installation for a major customer for which revenue was recognized upon final customer acceptance. In our Video Intelligence segment, revenue increased \$3.1 million, or 10%, primarily due to an increase in Residual Method revenue. In our Communications Intelligence segment, revenue increased \$10.8 million, or 30%, primarily due to an increase of approximately \$6 million in Contract Accounting Method revenue associated with work performed on customized projects and an increase of approximately \$4 million in Residual Method revenue associated with the timing of the completion of customer installations. For more details on our revenue by segment, see “- Revenue by Operating Segment”. Revenue in the Americas, Europe, the Middle East, and Africa (“EMEA”), and the Asia Pacific Region (“APAC”) represented approximately 56%, 25%, and 19% of our total revenue, respectively, in the three months ended October 31, 2009 compared to approximately 57%, 27%, and 16%, respectively, in the three months ended October 31, 2008.

We had operating income of \$23.7 million in the three months ended October 31, 2009 compared to operating income of \$5.4 million in the three months ended October 31, 2008. The increased operating income was primarily due to an increase in gross profit of \$26.9 million to \$123.0 million, or 66%, from \$96.1 million, or 61%. The increase in gross profit was primarily due to higher revenue and higher gross profit in all three of our operating segments. Product margins increased primarily in our Video Intelligence and Workforce Optimization segments mainly as a result of a more favorable product mix. Service margins increased primarily in our Workforce Optimization segment due to our cost-saving initiatives, as well as the fact, that in certain cases, expenses associated with service revenue recognized in the three months ended October 31, 2009 under the Ratable Method were recorded in prior periods when the costs were incurred. The cost of revenue associated with services is generally expensed as incurred in the period in which the services were performed, which is not necessarily the period in which revenue was recognized, with the exception of certain transactions accounted for under Contract Accounting Method revenue. This increase in operating income was partially offset by \$9.5 million in recoveries associated with intellectual property litigation assumed in the Witness acquisition. The recovery lowered operating expenses during the three months ended October 31, 2008, but had no impact on our results during the three months ended October 31, 2009.

We had net income attributable to Verint Systems Inc. common shares of \$9.7 million and diluted net income per share of \$0.29 in the three months ended October 31, 2009, compared to a net loss attributable to Verint Systems Inc. common shares of \$24.4 million and a net loss per share of \$0.75 in the three months ended October 31, 2008. The increase in our net income attributable to Verint Systems Inc. common shares and income per share in the three months ended October 31, 2009 was due to our higher gross profit as described above, and to a reduction in interest and other expenses, net of \$7.8 million coupled with a reduction of income tax expense of \$7.6 million.

The strengthening of the U.S. dollar relative to the major foreign currencies where we do business (primarily the British pound sterling, the euro, Israeli shekel and Canadian dollar) in the three months ended October 31, 2009 compared to the three months ended October 31, 2008 had an unfavorable impact on our revenue and a favorable impact on our operating expenses. Had foreign exchange rates remained constant in these periods, our total revenue would have been approximately \$1 million higher and our operating expenses and cost of revenue would have been approximately \$4 million higher, or would have resulted in a net unfavorable impact of approximately \$3 million on our operating income.

As of October 31, 2009, we employed approximately 2,500 employees, including part-time employees and certain contractors, as compared to approximately 2,600 as of October 31, 2008.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Our revenue increased approximately 11%, or \$52.1 million, to \$530.9 million in the nine months ended October 31, 2009 from \$478.8 million in the nine months ended October 31, 2008 due to revenue increases in all of our operating segments. In our Video Intelligence segment, revenue increased \$21.8 million, or 23%, almost entirely due to the product delivery of an order from a major customer. In our Communications Intelligence segment, revenue increased \$17.1 million, or 14%, primarily due to an increase of approximately \$24 million in Contract Accounting Method revenue associated with work performed on customized projects, partially offset by a decrease of approximately \$8 million in Residual Method revenue associated with the timing of completion of customer installations. In our Workforce Optimization segment, revenue increased \$13.1 million, or 5%, primarily due to the completion of a multi-site installation for a major customer for which revenue was recognized upon final customer acceptance, coupled with an increase in maintenance renewal revenue recognized at full value as a result of the elimination of the impact of purchase accounting adjustments to support obligations assumed which amounted to \$5.2 million in the nine months ended October 31, 2008. We recorded an adjustment reducing support obligations assumed in the Witness acquisition to their estimated fair value at the acquisition date. As a result, as required by business combination accounting rules, revenue related to maintenance contracts in the amount of \$5.2 million that would have been otherwise recorded by Witness as an independent entity, was not recognized in the nine months ended October 31, 2008. Historically, substantially all of our customers, including customers from acquired companies, renew their maintenance contracts when such contracts are eligible for renewal. To the extent these underlying maintenance contracts are renewed, we will recognize the revenue for the full value of these contracts over the maintenance periods, the substantial majority of which are one year. For more details on our revenue by segment, see “- Revenue by Operating Segment”. Revenue in the Americas, EMEA, and APAC regions represented approximately 55%, 24%, and 21% of our total revenue, respectively, in the nine months ended October 31, 2009 compared to approximately 55%, 29%, and 16%, respectively, in the nine months ended October 31, 2008.

We had operating income of \$73.5 million in the nine months ended October 31, 2009 compared to an operating loss of \$20.7 million in the nine months ended October 31, 2008. The increase in operating income was due to an increase in gross profit of \$63.6 million to \$351.3 million, or 66%, from \$287.7 million, or 60%, coupled with a decrease in operating expenses of \$30.7 million. The increase in gross profit was primarily due to higher revenue and higher gross profit in all three of our operating segments. Product margins increased primarily in our Video Intelligence and Workforce Optimization segments mainly as a result of a more favorable product mix. Service margins increased in all three of our operating segments due to our cost-saving initiatives, as well as the fact, that in certain cases, expenses associated with service revenue recognized in the nine months ended October 31, 2009 under the Ratable Method were recorded in prior periods when the costs were incurred. The cost of revenue associated with services is generally expensed as incurred in the period in which the services were performed, which is not necessarily the period in which revenue was recognized, with the exception of certain transactions accounted for under Contract Accounting Method revenue. The decrease in our operating expenses was primarily due to our cost saving initiatives, \$9.5 million in recoveries associated with intellectual property litigation assumed in the Witness acquisition, a \$5.5 million decrease in integration and restructuring primarily related to the completion of the integration with Witness, and a decline in operating expenses as a result of the strengthening U.S. dollar relative to the major foreign currencies where we do business (primarily the British pound sterling, euro, Israeli shekel and Canadian dollar).

We had net income attributable to Verint Systems Inc. common shares of \$24.3 million and diluted net income per share of \$0.74 in the nine months ended October 31, 2009, compared to a net loss attributable to Verint Systems Inc. common shares of \$71.2 million and a net loss per share of \$2.20 in the nine months ended October 31, 2008. The increase in our net income applicable to Verint Systems Inc. common shares and income per share in the nine months ended October 31, 2009 was due to our higher gross profit and lower operating expenses as described above as well as a reduction in income taxes of \$2.0 million, partially offset by \$0.9 million of higher interest and other expenses.

The strengthening of the U.S. dollar relative to the major foreign currencies where we do business (primarily the British Pound, euro, Israeli shekel and Canadian dollar) in the nine months ended October 31, 2009 compared to the nine months ended October 31, 2008 had an unfavorable impact on our revenue and a favorable impact on our operating expenses. Had foreign exchange rates remained constant in these periods, our total revenue would have been approximately \$15 million higher and our operating expenses and cost of revenue would have been approximately \$21 million higher, or would have resulted in a net unfavorable impact of approximately \$6 million on our operating income.

Revenue by Operating Segment

The following table sets forth revenue for each of our three operating segments for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | <u>Three Months Ended October 31,</u> | | <u>% Change</u> 2009 - 2008 | <u>Nine Months Ended October 31,</u> | | <u>% Change</u> 2009 - 2008 |
|------------------------|---------------------------------------|--------------------------|--------------------------------|--------------------------------------|--------------------------|--------------------------------|
| | <u>2009</u> | <u>2008</u> | | <u>2009</u> | <u>2008</u> | |
| Workforce Optimization | \$ 105,398 | \$ 90,653 | 16% | \$ 279,001 | \$ 265,940 | 5% |
| Video Intelligence | 33,985 | 30,893 | 10% | 116,548 | 94,665 | 23% |
| Communications | | | | | | |
| Intelligence | 47,097 | 36,321 | 30% | 135,348 | 118,241 | 14% |
| Total revenue | <u>\$ 186,480</u> | <u>\$ 157,867</u> | 18% | <u>\$ 530,897</u> | <u>\$ 478,846</u> | 11% |

Workforce Optimization Segment

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Workforce Optimization revenue increased approximately 16%, or \$14.7 million, to \$105.4 million in the three months ended October 31, 2009 from \$90.7 million in the three months ended October 31, 2008. The increase was primarily due to the completion of a multi-site installation for a major customer for which revenue was recognized upon final customer acceptance.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Workforce Optimization revenue increased approximately 5%, or \$13.1 million, to \$279.0 million in the nine months ended October 31, 2009 from \$265.9 million in the nine months ended October 31, 2008. The increase was primarily due to the completion of a multi-site installation for a major customer for which revenue was recognized upon final customer acceptance. In addition, there was an increase in Residual Method revenue associated with product deliveries, thereby allowing for revenue recognition upon product delivery rather than upon the completion of installation, as well as an increase in maintenance renewal revenue recognized at full value as a result of the elimination of the impact of purchase accounting adjustments to support obligations assumed. We recorded an adjustment reducing support obligations assumed in the Witness acquisition to their estimated fair value at the acquisition date. As a result, as required by business combination accounting rules, revenue related to maintenance contracts in the amount of \$5.2 million that would have been otherwise recorded by Witness as an independent entity, was not recognized in the nine months ended October 31, 2008. Historically, substantially all of our customers, including customers from acquired companies, renew their maintenance contracts when such contracts are eligible for renewal. To the extent these underlying maintenance contracts are renewed, we will recognize the revenue for the full value of these contracts over the maintenance periods, the substantial majority of which are one year. These increases were partially offset by a decline in our performance management business of \$4.7 million primarily due to the completion of a large project in the nine months ended October 31, 2008 as well as the impact of the weakening British pound sterling relative to the U.S. dollar on our revenue in EMEA.

Video Intelligence Segment

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Video Intelligence revenue increased approximately 10%, or \$3.1 million, to \$34.0 million in the three months ended October 31, 2009 from \$30.9 million in the three months ended October 31, 2008. The increase was due to an increase in Residual Method revenue of approximately \$5 million primarily attributable to the overall product deliveries of orders from major customers, partially offset by a decrease in Ratable Method revenue of approximately \$2 million due to a decline in the volume of arrangements recognized ratably over the economic life of the product because of implied PCS. As a result of changes in our business practices we anticipate that the mix of revenue arrangements recognized ratably over the economic life of the product in our Video Intelligence segment will continue to decline.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Video Intelligence revenue increased approximately 23%, or \$21.8 million, to \$116.5 million in the nine months ended October 31, 2009 from \$94.7 million in the nine months ended October 31, 2008. The increase was almost entirely due to the product delivery of an order from a major customer.

Communications Intelligence Segment

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Communications Intelligence revenue increased approximately 30%, or \$10.8 million, to \$47.1 million in the three months ended October 31, 2009 from \$36.3 million in the three months ended October 31, 2008. This increase was primarily attributable to an increase of approximately \$6 million in Contract Accounting Method revenue due to work performed on customized projects as well as an increase of approximately \$4 million in Residual Method revenue associated with the timing of the completion of customer installations.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Communications Intelligence revenue increased approximately 14%, or \$17.1 million, to \$135.3 million in the nine months ended October 31, 2009 from \$118.2 million in the nine months ended October 31, 2008. This increase was primarily due to an increase of approximately \$24 million in Contract Accounting Method revenue due to work performed on customized projects, as well as an increase of approximately \$1 million in Ratable Method revenue associated with increased support revenue, partially offset by a decrease of approximately \$8 million in Residual Method revenue associated with the timing of completion of customer installations.

Volume and Price

We sell products in multiple configurations, and the price of any particular product varies depending on the configuration of the product sold. Due to the variety of customized configurations for each product we sell, we are unable to quantify the amount of any revenue increases attributable to a change in the price of any particular product and/or a change in the number of products sold.

Revenue by Product Revenue and Service and Support Revenue

We categorize and report our revenue in two categories — product revenue and service and support revenue. For multiple element arrangements for which we are unable to establish VSOE of one or more elements, we use various available indicators of fair value and apply our best judgment to reasonably classify the arrangement's revenue into product revenue and service and support revenue.

The following table sets forth revenue for products and services and support for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | Three Months Ended October 31, | | % Change 2009 - 2008 | Nine Months Ended October 31, | | % Change 2009 - 2008 |
|--------------------------------|--------------------------------|-------------------|-------------------------|-------------------------------|-------------------|-------------------------|
| | 2009 | 2008 | | 2009 | 2008 | |
| Product revenue | \$ 98,467 | \$ 81,495 | 21% | \$ 283,645 | \$ 251,306 | 13% |
| Service and support revenue | 88,013 | 76,372 | 15% | 247,252 | 227,540 | 9% |
| Total revenue | \$ 186,480 | \$ 157,867 | 18% | \$ 530,897 | \$ 478,846 | 11% |

Product Revenue

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Product revenue increased approximately 21%, or \$17.0 million, to \$98.5 million in the three months ended October 31, 2009 from \$81.5 million in the three months ended October 31, 2008. Product revenue increased in all three of our operating segments. In our Communications Intelligence segment product revenue increased \$7.6 million, in our Workforce Optimization segment product revenue increased \$6.6 million, and in our Video Intelligence segment product revenue increased \$2.8 million. For additional information see “- Revenue by Operating Segment”.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Product revenue increased approximately 13%, or \$32.3 million, to \$283.6 million in the nine months ended October 31, 2009 from \$251.3 million in the nine months ended October 31, 2008. Product revenue increased in all three of our operating segments. In our Video Intelligence segment product revenue increased \$20.4 million, in our Communications Intelligence segment product revenue increased \$8.7 million, and in our Workforce Optimization segment product revenue increased \$3.2 million. For additional information see “- Revenue by Operating Segment”.

Service and Support Revenue

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Service and support revenue increased approximately 15%, or \$11.6 million, to \$88.0 million in the three months ended October 31, 2009 from \$76.4 million in the three months ended October 31, 2008. Service and support revenue increased in all three of our operating segments. Service and support revenue in our Workforce Optimization segment increased \$8.1 million and in our Communications Intelligence segment service and support revenue increased \$3.2 million. For additional information see “- Revenue by Operating Segment”.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Service and support revenue increased approximately 9%, or \$19.8 million, to \$247.3 million in the nine months ended October 31, 2009 from \$227.5 million in the nine months ended October 31, 2008. Service and support revenue increased in all three of our operating segments. Service and support revenue in our Workforce Optimization segment increased \$9.8 million and in our Communications Intelligence segment service and support revenue increased \$8.4 million. The increase in our Workforce Optimization segment is partially a result of fair value adjustments relating to future support obligations under acquired Witness contracts which lowered revenue in the nine months ended October 31, 2008 but had no impact on our results during the nine months ended October 31, 2009. For additional information see “- Revenue by Operating Segment”.

Cost of Revenue

The following table sets forth cost of revenue by product and service and support as well as amortization of acquired technology and backlog for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | Three Months Ended October 31, | | | Nine Months Ended October 31, | | |
|---|---------------------------------------|------------------|---------------------------------|--------------------------------------|-------------------|---------------------------------|
| | 2009 | 2008 | % Change 2009 - 2008 | 2009 | 2008 | % Change 2009 - 2008 |
| Product cost of revenue | \$ 35,718 | \$ 31,983 | 12% | \$ 98,675 | \$ 94,084 | 5% |
| Service and support cost of revenue | 25,819 | 27,571 | (6%) | 74,922 | 90,177 | (17%) |
| Amortization of acquired technology and backlog | 1,973 | 2,228 | (11%) | 6,049 | 6,851 | (12%) |
| Total cost of revenue | \$ 63,510 | \$ 61,782 | 3% | \$ 179,646 | \$ 191,112 | (6%) |

Product Cost of Revenue

Product cost of revenue primarily consists of hardware material costs and royalties due to third parties for software components that are embedded in our software applications. When revenue is deferred, we also defer hardware material costs and third-party software royalties and recognize those costs over the same period that the product revenue is recognized. Product cost of revenue also includes amortization of capitalized software development costs, employee compensation and related expenses associated with our global operations, facility costs and other allocated overhead expenses. In our Communications Intelligence segment, product cost of revenue also includes employee compensation and related expenses, contractor and consulting expenses, and travel expenses, in each case relating to resources dedicated to the delivery of customized projects for which certain contracts are accounted for under the POC method.

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Product cost of revenue increased \$3.7 million, or 12%, to \$35.7 million in the three months ended October 31, 2009 from \$32.0 million in the three months ended October 31, 2008. Our overall product margins have increased to 64% in the three months ended October 31, 2009 from 61% in the three months ended October 31, 2008 as a result of an increase in product revenue and change in product mix. Product margins in our Video Intelligence segment increased to 58% in the three months ended October 31, 2009 from 51% in the three months ended October 31, 2008 primarily due to an increase in product revenue, resulting in a better absorption of overhead costs, coupled with a higher software component which carries a higher gross margin, in the overall product mix. Product margins in our Workforce Optimization segment increased to 84% in the three months ended October 31, 2009 from 82% in the three months ended October 31, 2008, as a result of product mix. These increases were partially offset by a decrease in product margins in our Communications Intelligence segment to 48% in the three months ended October 31, 2009 from 52% in the three months ended October 31, 2008 primarily due to an increase in Contract Accounting Method revenue which resulted in an increase in product costs attributable to more work performed on customized projects accounted for under the Contract Accounting Method.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Product cost of revenue increased \$4.6 million, or 5%, to \$98.7 million in the nine months ended October 31, 2009 from \$94.1 million in the nine months ended October 31, 2008. Our overall product margins have increased to 65% in the nine months ended October 31, 2009 from 63% in the nine months ended October 31, 2008 as a result of an increase in revenue and change in product mix. Product margins in our Video Intelligence segment increased to 63% in the nine months ended October 31, 2009 from 52% in the nine months ended October 31, 2008 primarily due to an increase in product revenue, resulting in a better absorption of overhead costs, coupled with a higher software component which carries a higher gross margin, in the overall product mix. Product margins in our Workforce Optimization segment increased to 85% in the nine months ended October 31, 2009 from 84% in the nine months ended October 31, 2008, as a result of product mix. These increases were partially offset by a decrease in product margins in our Communications Intelligence segment to 52% in the nine months ended October 31, 2009 from 56% in the nine months ended October 31, 2008 primarily due to a change in project mix, as Residual Method revenue declined and Contract Accounting Method revenue increased, which resulted in an increase in product costs attributable to more work performed on customized projects accounted for under the Contract Accounting Method.

Service and Support Cost of Revenue

Service and support cost of revenue primarily consist of employee compensation and related expenses, contractor costs, and travel expenses relating to installation, training, consulting, and maintenance services. Service and support cost of revenue also include stock compensation expenses, facility costs, and other overhead expenses.

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Service and support cost of revenue decreased approximately 6% to \$25.8 million in the three months ended October 31, 2009 from \$27.6 million in the three months ended October 31, 2008. Employee compensation and related expenses decreased \$1.2 million due to, in approximately equal measure, a decrease in employee headcount in our Workforce Optimization segment resulting from the elimination of redundancies and other cost saving initiatives following the Witness acquisition, and a decrease in employee headcount in our Video Intelligence and Communications Intelligence segments as a result of our cost saving initiatives. Other expenses totaling \$0.6 million were reduced as a result of our cost saving initiatives. Our overall service and support margins increase to 71% in the three months ended October 31, 2009 from 64% in the three months ended October 31, 2008 due to increased service and support revenue and the decrease in service and support expenses discussed above. Contributing to the increase in service and support margins was the fact that in certain cases expenses associated with service and support revenue recognized in the three months ended October 31, 2009 under the Ratable Method were recorded in prior periods when the costs were incurred. The cost of revenue associated with services is generally expensed as incurred in the period in which the services were performed, which is not necessarily the period in which revenue was recognized, with the exception of certain transactions accounted for under the Contract Accounting Method.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Service and support cost of revenue decreased approximately 17% to \$74.9 million in the nine months ended October 31, 2009 from \$90.2 million in the nine months ended October 31, 2008. Employee compensation and related expenses decreased \$7.8 million primarily in our Workforce Optimization segment due to a decrease in employee headcount resulting from the elimination of redundancies and other cost saving initiatives following the Witness acquisition and partially due to a decrease in employee headcount in our Video Intelligence and Communications Intelligence segments as a result of our cost saving initiatives. Other expense decreases included a decrease in travel expenses of \$3.4 million and other expense reductions totaling \$1.0 million, all of which were a result of our cost saving initiatives. In addition, in the nine months ended October 31, 2008 we completed certain projects in our performance management business included in our Workforce Optimization segment, which were accounted for under the Contract Accounting Method. As a result, we recognized deferred service revenue and attributable costs of \$3.1 million during the nine months ended October 31, 2008. Our overall service and support margins increased to 70% in the nine months ended October 31, 2009 from 60% in the nine months ended October 31, 2008 due to increased service and support revenue and the decrease in service and support expenses discussed above. Contributing to the increase in service and support margins was the fact that in certain cases expenses associated with service and support revenue recognized in the nine months ended October 31, 2009 under the Ratable Method were recorded in prior periods when the costs were incurred. The cost of revenue associated with services is generally expensed as incurred in the period in which the services were performed, which is not necessarily the period in which revenue was recognized, with the exception of certain transactions accounted for under the Contract Accounting Method.

Amortization of Acquired Technology and Backlog

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Amortization of acquired technology and backlog decreased approximately 11% to \$2.0 million in the three months ended October 31, 2009 from \$2.2 million in the three months ended October 31, 2008 primarily due to the weakening of the British pound sterling in which some of our intangible assets are denominated.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Amortization of acquired technology and backlog decreased approximately 12% to \$6.0 million in the nine months ended October 31, 2009 from \$6.9 million in the nine months ended October 31, 2008 primarily due to the weakening of the British pound sterling in which some of our intangible assets are denominated.

Research and Development, Net

Research and development expenses primarily consist of personnel and subcontracting expenses, facility costs, and other allocated overhead, net of certain software development costs that are capitalized as well as reimbursement under government programs. Software development costs are capitalized upon the establishment of technological feasibility and until related products are available for general release to customers.

The following table sets forth research and development, net expenses for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | Three Months Ended October 31, | | | Nine Months Ended October 31, | | |
|-------------------------------|---------------------------------------|-------------|-----------------|--------------------------------------|-------------|-----------------|
| | 2009 | 2008 | % Change | 2009 | 2008 | % Change |
| | 2009 - 2008 | | | 2009 - 2008 | | |
| Research and development, net | \$ 21,461 | \$ 21,963 | (2%) | \$ 61,000 | \$ 69,897 | (13%) |

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Research and development, net expenses decreased approximately 2% to \$21.5 million in the three months ended October 31, 2009 from \$22.0 million in the three months ended October 31, 2008. The decrease was due to lower expenses in our Communications Intelligence segment as a result of a smaller portion of employees' time devoted to generic product development rather than specific customization work for projects accounted for under the Contract Accounting Method, and lower expenses in our Workforce Optimization and Video Intelligence operating segments due to our cost saving initiatives. The above decreases include the effect of the strengthening of the U.S. dollar relative to the major foreign currencies where we do business.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Research and development, net expenses decreased approximately 13% to \$61.0 million in the nine months ended October 31, 2009 from \$69.9 million in the nine months ended October 31, 2008. Employee compensation and related expenses decreased \$5.3 million due to, in approximately equal measure, lower expenses in our Communications Intelligence segment as a result of a smaller portion of employees' time devoted to generic product development rather than specific customization work for projects accounted for under the Contract Accounting Method, and lower expenses in our Video Intelligence segment due to a decrease in employee headcount as a result of our cost saving initiatives. Contractor costs decreased \$3.6 million primarily in our Workforce Optimization segment and partially in our Video Intelligence and Communications Intelligence segments due to our cost saving initiatives. The above decreases include the effect of the strengthening of the U.S. dollar relative to the major foreign currencies where we do business.

Selling, General and Administrative Expenses

Selling, general and administrative expenses consist primarily of personnel costs and related expenses, professional fees, sales and marketing expenses, including travel, sales commissions and sales referral fees, facility costs, communication expenses, and other administrative expenses.

The following table sets forth selling, general and administrative expenses for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | Three Months Ended October 31, | | | Nine Months Ended October 31, | | |
|-------------------------------------|---------------------------------------|-------------|-----------------|--------------------------------------|-------------|-----------------|
| | 2009 | 2008 | % Change | 2009 | 2008 | % Change |
| | 2009 - 2008 | | | 2009 - 2008 | | |
| Selling, general and administrative | \$ 72,398 | \$ 69,977 | 3% | \$ 199,882 | \$ 218,089 | (8%) |

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Selling, general and administrative expenses increased approximately 3% to \$72.4 million in the three months ended October 31, 2009 from \$70.0 million in the three months ended October 31, 2008. Professional fees and related expenses associated with our restatement of previously filed financial statements and our extended filing delay status increased approximately \$4 million to approximately \$12 million in the three months ended October 31, 2009 compared to approximately \$8 million in the three months ended October 31, 2008. These increases were offset by decreases in travel, marketing, and other expenses totaling \$1.6 million which were a result of our cost saving initiatives.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Selling, general and administrative expenses decreased approximately 8% to \$199.9 million in the nine months ended October 31, 2009 from \$218.1 million in the nine months ended October 31, 2008. Employee compensation and related expenses decreased \$7.0 million attributable to lower headcount as a result of our cost saving initiatives. Employee sales commissions decreased \$1.5 million due to a decline in customer orders received during the nine months ended October 31, 2009. Other expense decreases include decreases in travel and entertainment expenses of \$4.5 million, marketing expenses of \$2.7 million, communication, personnel, rent and utility expenses of \$4.4 million, and other expense reductions totaling \$3.1 million all of which were due to our cost saving initiatives. Professional fees and related expenses associated with our restatement of previously filed financial statements and our extended filing delay status increased approximately \$5 million to approximately \$29 million in the nine months ended October 31, 2009 compared to approximately \$24 million in the nine months ended October 31, 2008. The above decreases include the effect of the strengthening of the U.S. dollar relative to the major foreign currencies where we do business.

Amortization of Other Acquired Intangible Assets

The following table sets forth amortization of acquisition related intangibles for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | Three Months Ended October 31, | | | Nine Months Ended October 31, | | |
|--|---------------------------------------|-------------|---------------------------------|--------------------------------------|-------------|---------------------------------|
| | 2009 | 2008 | % Change 2009 - 2008 | 2009 | 2008 | % Change 2009 - 2008 |
| Amortization of other acquired intangible assets | \$ 5,376 | \$ 6,139 | (12%) | \$ 16,892 | \$ 19,318 | (13%) |

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Amortization of other acquired intangible assets decreased approximately 12% to \$5.4 million in the three months ended October 31, 2009 from \$6.1 million in the three months ended October 31, 2008 primarily due to the weakening of the British pound sterling in which some of our intangible assets are denominated in.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Amortization of other acquired intangible assets decreased approximately 13% to \$16.9 million in the nine months ended October 31, 2009 from \$19.3 million in the nine months ended October 31, 2008 primarily due to the weakening of the British pound sterling in which some of our intangible assets are denominated in.

Integration, Restructuring, and Other, Net

The following table sets forth integration, restructuring, and other, net for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | Three Months Ended October 31, | | | Nine Months Ended October 31, | | |
|--|---------------------------------------|-------------------|---------------------------------|--------------------------------------|-----------------|---------------------------------|
| | 2009 | 2008 | % Change 2009 - 2008 | 2009 | 2008 | % Change 2009 - 2008 |
| Restructuring expenses | \$ — | \$ 1,284 | (100%) | \$ 24 | \$ 2,492 | (99%) |
| Integration expenses | — | 844 | (100%) | — | 2,979 | (100%) |
| Other legal recoveries, net | — | (9,521) | (100%) | — | (4,303) | (100%) |
| Integration, restructuring and other, net | \$ — | \$ (7,393) | (100%) | \$ 24 | \$ 1,168 | (98%) |

Integration and Restructuring Costs

Three Months Ended October 31, 2008. We continually review our business to manage costs and align our resources with market demand. In connection with such reviews, and also in conjunction with the acquisition of Witness, we continued to take several actions to reduce fixed costs, eliminate redundancies, strengthen areas needing operational focus, and better position us to respond to market pressures or unfavorable economic conditions. We incurred restructuring costs of \$1.3 million, consisting primarily of severance and personnel-related costs resulting from headcount reductions and retention, due to the acquisition of Witness and the restructuring of our Video Intelligence segment. As a result of the subsequent integration of the Witness and Verint businesses, and our enterprise resource planning re-engineering project, we incurred integration costs of \$0.8 million, the majority of which were consulting fees.

Nine Months Ended October 31, 2008. We incurred restructuring costs of \$2.5 million, consisting primarily of severance and personnel-related costs resulting from headcount reductions and retention, due to the acquisition of Witness and the restructuring of our Video Intelligence segment. As a result of the subsequent integration of the Witness and Verint businesses, and our enterprise resource planning re-engineering project, we incurred integration costs of \$3.0 million, the majority of which were consulting fees.

Other Legal Recoveries, Net

Three Months Ended October 31, 2008. On August 1, 2008, we reached a settlement agreement related to an ongoing patent infringement litigation matter, and recorded \$9.7 million in settlement gains in the three months ended October 31, 2008. This gain was partially offset by \$0.2 million of legal fees incurred during the three months ended October 31, 2008 resulting in a net recovery of \$9.5 million.

Nine Months Ended October 31, 2008. On August 1, 2008, we reached a settlement agreement related to an ongoing patent infringement litigation matter, and recorded \$9.7 million in settlement gains in the nine months ended October 31, 2008. This gain was partially offset by \$5.4 million of legal fees incurred during the nine months ended October 31, 2008 resulting in a net recovery of \$4.3 million.

Other Income (Expense), Net

The following table sets forth total other income (expense), net for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | Three Months Ended October 31, | | % Change | Nine Months Ended October 31, | | % Change |
|--------------------------------------|---------------------------------------|--------------------|--------------------|--------------------------------------|--------------------|--------------------|
| | 2009 | 2008 | 2009 - 2008 | 2009 | 2008 | 2009 - 2008 |
| Interest income | \$ 336 | \$ 481 | (30%) | \$ 581 | \$ 1,557 | (63%) |
| Interest expense | (6,178) | (9,794) | (37%) | (18,900) | (29,400) | (36%) |
| Other income (expense): | | | | | | |
| Gains on investments | — | 5,577 | (100%) | — | 4,712 | (100%) |
| Foreign currency gains (losses), net | 2,039 | (3,639) | (156%) | 1,700 | (2,418) | (170%) |
| Losses on derivatives, net | (4,710) | (9,273) | (49%) | (11,745) | (2,554) | 360% |
| Other, net | (104) | 249 | (142%) | (799) | (204) | 292% |
| Total other income (expense) | (2,775) | (7,086) | (61%) | (10,844) | (464) | 2,237% |
| Total other expense, net | \$ (8,617) | \$ (16,399) | (47%) | \$ (29,163) | \$ (28,307) | 3% |

Three Months Ended October 31, 2009 compared to Three Months Ended October 31, 2008. Total other expense, net, decreased \$7.8 million to an expense of \$8.6 million in the three months ended October 31, 2009, compared to an expense \$16.4 million in the three months ended October 31, 2008. Interest income decreased to \$0.3 million in the three months ended October 31, 2009 from \$0.5 million in the three months ended October 31, 2008 primarily due to lower interest rates. Interest expense on our term loan and revolving credit facility decreased to \$6.2 million in the three months ended October 31, 2009 from \$9.8 million in the three months ended October 31, 2008 due to lower interest rates during the three months ended October 31, 2009. We recorded a \$2.0 million gain on foreign currency in the three months ended October 31, 2009 compared to a \$3.6 million loss in the prior year quarter. Foreign currency gains in the three months ended October 31, 2009 resulted from the weakening of the U. S. dollar against the British pound sterling, euro, and Israeli shekel.

In the three months ended October 31, 2009, we recorded a net loss on derivatives of \$4.7 million. This loss was primarily attributable to a \$4.4 million loss in connection with a \$450.0 million interest rate swap contract entered into concurrently with our credit agreement. This interest rate swap is not designated as a hedging instrument under derivative accounting guidance, and accordingly gains and losses from changes in fair value are recorded in other income (expense), net. This loss was also partially due to a \$0.3 million loss on foreign currency derivatives, which represented the realized and unrealized portions of certain foreign currency derivatives.

In the three months ended October 31, 2008, we recorded a net loss on derivatives of \$9.3 million, primarily attributable to a \$450.0 million interest rate swap contract entered into concurrently with our credit agreement.

Nine Months Ended October 31, 2009 compared to Nine Months Ended October 31, 2008. Total other expense, net, increased \$0.9 million to an expense of \$29.2 million in the nine months ended October 31, 2009, compared to an expense of \$28.3 million in the nine months ended October 31, 2008. Interest income decreased to \$0.6 million in the nine months ended October 31, 2009 from \$1.6 million in the nine months ended October 31, 2008 primarily due to lower interest rates. Interest expense on our term loan and revolving credit facility decreased to \$18.9 million in the nine months ended October 31, 2009 from \$29.4 million in the nine months ended October 31, 2008 due to lower interest rates. We recorded a \$1.7 million gain on foreign currency in the nine months ended October 31, 2009 compared to a \$2.4 million loss in the prior year quarter. Foreign currency gains in the nine months ended October 31, 2009 resulted from the weakening of the U. S. dollar against the British pound sterling, euro, and Israeli shekel.

In the nine months ended October 31, 2009, we recorded a net loss on derivatives of \$11.7 million. This loss was primarily attributable to an \$11.0 million loss in connection with a \$450.0 million interest rate swap contract entered into concurrently with our credit agreement. This interest rate swap is not designated as a hedging instrument under derivative accounting guidance, and accordingly gains and losses from changes in fair value are recorded in other income (expense), net. This loss was also partially due to a \$0.7 million loss on foreign currency derivatives, which represented the realized and unrealized portions of certain foreign currency derivatives.

In the nine months ended October 31, 2008, we recorded a net loss on derivatives of \$2.6 million, primarily attributable to a \$450.0 million interest rate swap contract entered into concurrently with our credit agreement.

Income Tax Provision

The following table sets forth our income tax provision for the three and nine months ended October 31, 2009 and 2008:

| (in thousands) | <u>Three Months Ended October 31,</u> <u>2009</u> | <u>2008</u> | <u>% Change</u> <u>2009 - 2008</u> | <u>Nine Months Ended October 31,</u> <u>2009</u> | <u>2008</u> | <u>% Change</u> <u>2009 - 2008</u> |
|----------------------------|--|-------------|---------------------------------------|---|-------------|---------------------------------------|
| Provision for income taxes | \$ 1,803 | \$ 9,441 | (81%) | \$ 8,921 | \$ 10,887 | (18%) |

Three Months ended October 31, 2009 compared to the Three Months ended October 31, 2008. Our effective tax rate was 11.9% for the three months ended October 31, 2009, as compared to (85.8%) for the three months ended October 31, 2008. For the three months ended October 31, 2009, our effective tax rate was lower than the U.S. federal statutory rate because we recorded an income tax provision on income from certain foreign subsidiaries taxed at rates lower than the U.S. federal statutory rate, but did not record significant U.S. federal income tax benefit because we maintain a valuation allowance against our U.S. deferred tax assets. Our effective tax rate for the three months ended October 31, 2008 was negative due to the fact that we reported an income tax expense on a consolidated pre-tax loss. We recorded a valuation allowance against certain pre-tax losses and we recorded an income tax provision in profitable jurisdictions. The comparison of our effective tax rate between periods is significantly impacted by the level and mix of earnings and losses by taxing jurisdiction, foreign income tax rate differentials, relative impact of permanent book to tax differences, the effects of valuation allowances, and discrete items that occur within the period.

Nine Months ended October 31, 2009 compared to the Nine Months ended October 31, 2008. Our effective tax rate was 20.1% for the nine months ended October 31, 2009, as compared to (22.2%) for the nine months ended October 31, 2008. For the nine months ended October 31, 2009, our effective tax rate was lower than the U.S. federal statutory rate because we recorded an income tax provision on income from certain foreign subsidiaries taxed at rates lower than the U.S. federal statutory rate. We did not record significant U.S. federal income tax benefit because we maintain a valuation allowance against our U.S. deferred tax assets. Our effective tax rate for the nine months ended October 31, 2008 was negative due to the fact that we recorded income tax expense on a consolidated pre-tax loss. We recorded a valuation allowance against certain domestic and foreign pre-tax losses and an income tax provision in certain profitable jurisdictions. The comparison of our effective tax rate between periods is significantly impacted by the level and mix of earnings and losses by taxing jurisdiction, foreign income tax rate differentials, relative impact of permanent book to tax differences, the effects of the valuation allowances, and discrete items that occur within the period.

Backlog

The delivery cycles of most of our products are generally very short, ranging from days to several months, with the exception of certain projects with multiple deliverables over a longer period of time. Therefore, we do not view backlog as a meaningful indicator of future business activity and do not consider it a meaningful financial metric for evaluating our business.

Liquidity and Capital Resources

Overview

Our primary sources of cash have historically been collections of our accounts receivable for services and products as well as cash advances from our customers, and may in the future include cash raised from equity and/or debt financings. Our primary uses of cash have been for selling and marketing activities, research and development, interest expense and related interest rate swap settlements, professional fees and related expenses associated with our restatement of previously filed financial statements and our extended filing delay status, capital expenditures, acquisitions of businesses, repayments of borrowings and dividends paid to the noncontrolling stockholders of our joint venture.

Statements of Cash Flows

The following table sets forth, as of October 31, 2009 and January 31, 2009, cash and cash equivalents, preferred stock and long-term debt:

| (in thousands) | October 31, 2009 | January 31, 2009 |
|-------------------------------------|-----------------------------|-----------------------------|
| Cash and cash equivalents | \$ 161,184 | \$ 115,928 |
| Preferred stock (at carrying value) | \$ 285,542 | \$ 285,542 |
| Long-term debt | \$ 617,219 | \$ 620,912 |

At October 31, 2009, our cash and cash equivalents were \$161.2 million, an increase of \$45.3 million from January 31, 2009. This increase in cash is due to our strong operating performance.

The following table summarizes selected items from our condensed consolidated statements of cash flows for the nine months ended October 31, 2009 and 2008:

| (in thousands) | Nine Months Ended October 31, | |
|--|--------------------------------------|-----------------|
| | 2009 | 2008 |
| Net cash provided by operating activities | \$ 65,491 | \$ 30,397 |
| Net cash used in investing activities | (16,385) | (24,244) |
| Net cash used in financing activities | (8,432) | (2,362) |
| Effect of exchange rate changes on cash and cash equivalents | 4,582 | (4,102) |
| Net increase (decrease) in cash and cash equivalents | \$ 45,256 | \$ (311) |

Net cash provided by operating activities

During the nine months ended October 31, 2009, we generated \$65.5 million in cash in operating activities. This \$65.5 million in cash from operating activities was due to net income of \$35.4 million and non-cash items of \$71.4 million, primarily depreciation and amortization and stock-based compensation, and lower deferred cost of revenue of \$10.4 million. These increases were partially offset by lower deferred revenue of \$22.8 million, higher accounts receivable of \$15.7 million, and higher prepaid expenses and other assets of \$13.7 million.

During the nine-month period ended October 31, 2008, we reported a \$59.9 million net loss, which included \$67.4 million of net non-cash expenses. Net changes in operating assets and liabilities provided \$22.9 million of cash during this nine-month period which, when combined with the impact of the period's net loss and non-cash expenses, resulted in \$30.4 million of cash provided by operating activities. The primary non-cash expenses for the period were \$41.9 million of depreciation and amortization and \$24.9 million of stock-based compensation. The net changes in operating assets and liabilities during the period included a \$20.0 million increase in deferred revenue and a \$6.8 million decrease in deferred cost of revenue, partially offset by an \$8.2 million increase in inventories.

Net cash used by investing activities

During the nine months ended October 31, 2009, we used \$16.4 million in cash primarily due to settlements of derivative financial instruments not designated as hedges of \$13.1 million and capital expenditures of \$5.2 million.

During the nine months ended October 31, 2008, our investing activities used \$24.2 million of cash, including \$12.5 million of capital expenditures, \$5.7 million of settlements of derivative financial instruments not designated as hedges and an increase of \$5.9 million in restricted cash and bank time deposits, which is presented within Other investing activities on the condensed consolidated statement of cash flows.

Net cash used in financing activities

During the nine months ended October 31, 2009, we used \$8.4 million in cash, reflecting \$6.1 million in repayments of borrowings and other financing arrangements and \$2.1 million of dividends paid to the noncontrolling stockholders of our joint venture.

During the nine months ended October 31, 2008, our financing activities used \$2.4 million of cash, primarily reflecting \$2.1 million in repayments of borrowings and other financing arrangements.

Liquidity and Capital Resources Requirements

Based on past performance and current expectations, we believe that our cash and cash equivalents and cash generated from operations will be sufficient to meet anticipated operating costs, required payments of principal and interest, working capital needs, capital expenditures, research and development spending, and other commitments for at least the next 12 months. Currently, we have no plans to pay any dividends on our preferred or common stock, which are not permitted under our credit agreement.

Our liquidity could be negatively impacted by a decrease in demand for our products and service and support, including the impact of changes in customer buying behavior due to the general global economic downturn. We have incurred significant professional fees and related expenses in connection with our restatement of previously filed financial statements and our extended filing delay status, and we expect that we will continue to incur significant professional fees and costs through the first half of calendar 2010 and some related expenses remaining in the second half of the year. Our liquidity could be negatively impacted by these additional fees and costs. In the event we determine to make acquisitions, or otherwise require additional funds, we may need to raise additional capital, which could involve the issuance of equity or debt securities. There can be no assurance that we would be able to raise additional equity or debt in the private or public markets on terms favorable to us, or at all.

On May 25, 2007, we entered into a \$650.0 million term loan and a \$25.0 million revolving credit facility with a group of banks to fund a portion of the acquisition of Witness. As of October 31, 2009, our outstanding term loan balance was \$605.9 million. As of June 2010, our outstanding term loan balance has been reduced to \$583.2 million. The original \$25.0 million revolving credit facility was reduced to \$15.0 million in September 2008 due to the bankruptcy of Lehman Brothers and the termination of its commitment under the credit facility. We borrowed the entire \$15.0 million available to us in November 2008 and currently have no remaining balance available to us. The term loan matures on May 25, 2014 and the revolving credit facility matures on May 25, 2013.

The credit agreement requires mandatory prepayments from the proceeds of certain asset sales, excess cash flow as defined by the agreement (for the year ended January 31, 2009, we made a \$4.1 million prepayment in May 2009 and for the year ended January 31, 2010, we made a \$22.1 million prepayment in May 2010 as required by the annual excess cash flow requirement), proceeds of indebtedness, and quarterly principal repayments (we made a \$0.6 million required quarterly principal repayment in February 2010). Any re-borrowings under the revolving credit facility are dependent upon certain conditions including the absence of any material adverse effect or change on our business, as defined in the credit agreement.

The credit agreement contains one financial covenant that requires us to meet a certain consolidated leverage ratio, defined as our consolidated net total debt divided by consolidated earnings before interest, taxes, depreciation, and amortization (“EBITDA”) for the trailing four quarters. EBITDA is defined in our credit agreement as net income/(loss) plus income tax expense, interest expense, depreciation and amortization, losses related to hedge agreements, any extraordinary, unusual, or non-recurring expenses or losses, any other non-cash charges, and expenses incurred or taken prior to April 30, 2008 in connection with our acquisition of Witness, minus interest income, any extraordinary, unusual, or non-recurring income or gains, gains related to hedge agreements, and any other non-cash income. Under the credit agreement, the consolidated leverage ratio could not exceed 4.50:1 for the quarterly periods ended January 31, April 30, July 31, and October 31, 2009, and we were in compliance with such requirement as of such dates. For the quarterly periods ended January 31 and April 30, 2010, and the quarterly periods ending July 31 and October 31, 2010, the consolidated leverage ratio could not exceed 3:50:1. As of January 31, 2010 and April 30, 2010, we were in compliance with such requirement. For the quarterly periods ending January 31, April 30, July 31, and October 31, 2011, the consolidated leverage ratio cannot exceed 2.50:1. For the quarterly period ending January 31, 2012 and thereafter, the consolidated leverage ratio cannot exceed 2.00:1.

Based on debt levels as of the date of the filing of this report and our expectations for EBITDA, we may reduce our outstanding debt by the end of the year ending January 31, 2011 in order to maintain compliance with the consolidated leverage ratio covenant using available cash or we may attempt to raise cash from equity or debt financings. Alternatively, we may attempt to modify the credit agreement terms or refinance the bank debt. There can be no assurance that we will be successful with any such financing activities.

In addition, we are subject to a number of restrictive covenants, including limitations on our ability to incur indebtedness, create liens, make fundamental business changes, dispose of property, make restricted payments including dividends, make significant investments, enter into sale and leasebacks, enter new lines of business, provide negative pledges, enter into transactions with related parties and enter into any speculative hedges although there are limited exceptions to these covenants.

If we are unable to comply with any of these requirements, an event of default could occur which could cause or permit holders of the debt to declare all amounts outstanding to be immediately due and payable. In that event, we may be forced to sell assets, raise additional capital through a securities offering, or seek to refinance or restructure our debt. In such case, we may not be able to consummate such a sale, securities offering, or refinancing or restructuring on reasonable terms, or at all.

Contractual Obligations

There has been no material change in our contractual obligations or commercial commitments during the nine months ended October 31, 2009.

Off-Balance Sheet Arrangements

As of October 31, 2009, we did not have any off-balance sheet arrangements that we believe have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors. There were no material changes in our off-balance sheet arrangements during the nine months ended October 31, 2009.

Recent Accounting Pronouncements

Refer to Note 1, "Basis of Presentation" of the Notes to Condensed Consolidated Financial Statements included in Item 1 of this Form 10-Q for information regarding recent accounting pronouncements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk represents the risk of loss that may impact our financial condition due to adverse changes in financial market prices and rates. We are exposed to market risk related to changes in interest rates and foreign currency exchange rate fluctuations. To manage the volatility relating to interest rate and foreign currency risks, we periodically enter into derivative instruments including foreign currency forward exchange contracts and interest rate swap agreements. It is our policy to enter into derivative transactions only to the extent considered necessary to meet our risk management objectives. We use derivative instruments solely to reduce the financial impact of these risks and do not use derivative instruments for trading purposes.

Our Annual Report on Form 10-K for the year ended January 31, 2009, filed with the SEC on April 8, 2010 provides a detailed discussion of the market risks affecting our operations for the year ended January 31, 2009. We believe our exposure to these market risks did not materially change during the nine months ended October 31, 2009.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, are controls and other procedures designed to ensure that information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified by the rules and forms promulgated by the SEC. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. We conducted an evaluation, under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this report. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of October 31, 2009, our disclosure controls and procedures were not effective because of the material weaknesses in our internal control over financial reporting as described in our Annual Report on Form 10-K for the year ended January 31, 2009.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect every misstatement. An evaluation of effectiveness is subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with policies or procedures may decrease over time.

Changes in Internal Control over Financial Reporting

Under applicable SEC rules (Exchange Act Rules 13a-15(c) and 15d-15(c)) management is required to evaluate any change in internal control over financial reporting that occurred during each fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. As discussed in Item 9A of our Annual Report on Form 10-K for the year ended January 31, 2010, we have undertaken a broad range of remedial procedures to address the material weaknesses in our internal control over financial reporting identified as of January 31, 2009 in Item 9A of our Annual Report on Form 10-K for the year ended January 31, 2009. These remedial procedures entailed changes in our internal control over financial reporting throughout the course of the year ended January 31, 2010, including during the quarter ended October 31, 2009. However, as of October 31, 2009, these changes were not yet effective in remediating the material weaknesses identified in our Annual Report on Form 10-K for the year ended January 31, 2009. As discussed in Item 9A of our Annual Report on Form 10-K for the year ended January 31, 2010, the material weaknesses related to risk assessment and equity compensation, as well as certain areas of the financial reporting material weakness identified as of January 31, 2009, were remediated as of January 31, 2010.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

There were no material legal proceedings which arose, or in which there were material developments, during the three months ended October 31, 2009.

Please see Item 3, "Legal Proceedings", in our Annual Report on Form 10-K for the year ended January 31, 2010 for a discussion of all material legal proceedings as of the filing date of such report. Please see Part II, Item 1, "Legal Proceedings" in our Quarterly Report on Form 10-Q for the three months ended April 30, 2010 for a discussion of material updates, if any, to the disclosure in the Form 10-K as of the filing date of such quarterly report.

Item 1A. Risk Factors

Please see Item 1A, "Risk Factors", in our Annual Report on Form 10-K for the year ended January 31, 2010 for a discussion of the principal risks to our business, financial condition, and results of operations as of the filing date of such report. Please see Part II, Item 1A, "Risk Factors" in our Quarterly Report on Form 10-Q for the three months ended April 30, 2010 for a discussion of material updates, if any, to the disclosure in the Form 10-K as of the filing date of such quarterly report.

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

Equity Grants

As a result of our inability to file required SEC reports during our extended filing delay period, we ceased using our registration statement on Form S-8 to make equity grants to employees.

On May 24, 2007, we received a no-action letter from the SEC upon which we have relied to make broad-based equity grants to employees under a no-sale theory. We have also made equity grants to our directors, executive officers, and certain other executives who qualify as accredited investors in reliance upon a private placement exemption from the federal securities laws and have made a small number of equity grants to non-U.S. employees under the exemption provided by Regulation S of the Securities Act.

There were no equity awards approved by the stock option committee during the three months ended October 31, 2009. The following summarizes various time-based equity awards approved by the stock option committee since the three month period ended October 31, 2009 (excluding directors and executive officers) in the United States and elsewhere throughout the world under the application of the no sale theory or under the exemption provided by Regulation S of the Securities Act:

- March 17, 2010 — equity awards representing approximately 283,850 shares; and
- April 17, 2010 — equity awards representing approximately 209,900 shares.

The following summarizes various time-based and performance-based equity awards approved by the board of directors or the stock option committee since the three month period ended October 31, 2009 under a private placement exemption to directors, executive officers, or other employees qualifying as accredited investors (with officer performance awards included at target levels):

- March 17, 2010 — equity awards representing approximately 426,850 shares;
- March 18, 2010 — equity awards representing approximately 20,000 shares; and
- April 17, 2010 — equity awards representing approximately 37,600 shares.

All grants were made under a stockholder-approved equity compensation plan or contain vesting conditions which require that we receive stockholder approval of a new equity compensation plan or have additional share capacity under an existing stockholder-approved equity compensation plan for the awards to stock vest. All grants were compensatory in nature and were issued without cost to the employee.

Issuer Purchases of Equity Securities

Our board of directors has approved a program to repurchase shares of our common stock from our independent directors, and such other directors as may from time to time be designated by the board of directors, upon vesting of restricted stock grants during our extended filing delay period, in order to provide funds to the recipient for the payment of associated income taxes. From time to time, our board of directors has also approved repurchases from executive officers for the same purpose when a vesting has occurred during a blackout period and on November 24, 2009, the board of directors approved a repurchase program for our executive officers similar to the one for our directors. On June 4, 2010, the officer repurchase program was extended through the date of our next meeting of stockholders at which a new equity incentive plan is approved. We record any repurchases of common stock as treasury stock. During the three months ended October 31, 2009, we did not repurchase any common shares.

Item 3. Defaults upon Senior Securities

None.

Item 4. Removed and Reserved

Item 5. Other Information

None.

Item 6. Exhibits

The following exhibit list includes exhibits that we entered into or that became effective during the three months ended October 31, 2009.

| Number | Description | Filed Herewith / Incorporated by Reference from |
|---------------|---|--|
| 10.01 | Amended and Restated Employment Agreement, dated October 29, 2009, between Verint Systems Inc. and Elan Moriah* | Form 10-K filed on March 17, 2010 |
| 31.1 | Certification of Dan Bodner, Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. | Filed Herewith |
| 31.2 | Certification of Douglas E. Robinson, Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. | Filed Herewith |
| 32.1 | Certification of the Chief Executive Officer pursuant to Securities Exchange Act Rule 13a-14(b) and 18 U.S.C. Section 1350 ⁽¹⁾ | Filed Herewith |
| 32.2 | Certification of the Chief Financial Officer pursuant to Securities Exchange Act Rule 13a-14(b) and 18 U.S.C. Section 1350 ⁽¹⁾ | Filed Herewith |

(1) These exhibits are being “furnished” with this periodic report and are not deemed “filed” with the Securities and Exchange Commission and are not incorporated by reference in any filing of the Company under the Securities Act of 1933 or the Securities Exchange Act of 1934.

* Denotes a management contract or compensatory plan or arrangement required to be filed as an exhibit to this form pursuant to Item 6 of this report.

SIGNATURES

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

VERINT SYSTEMS INC.

June 18, 2010

/s/ Dan Bodner

Dan Bodner

President and Chief Executive Officer

June 18, 2010

/s/ Douglas E. Robinson

Douglas E. Robinson

Chief Financial Officer (Principal Financial Officer
and Accounting Officer)