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Total

\$103,015 \$63,064 \$39,951

| | As of December 31, 2007 | | |
|------------------------|--------------------------------------|-------------------------------------|------------------------------------|
| | Carrying Amount Gross | Accumulated Amortization | Carrying Amount Net |
| Customer relationships | \$ 57,327 | \$ 33,761 | \$ 23,566 |
| Non-compete agreements | 5,351 | 5,328 | 23 |
| Technology/tradename | 29,197 | 20,404 | 8,793 |
| Total | \$ 91,875 | \$ 59,493 | \$ 32,382 |

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Amortization expense for the three months ended March 31, 2008 and 2007 was \$2.2 million and \$2.7 million, respectively. Estimated amortization expense for the remaining life of the intangible assets, based on intangible assets as of March 31, 2008, is as follows (in thousands):

| Year | |
|--------------|------------------|
| 2008 | \$ 6,456 |
| 2009 | 7,751 |
| 2010 | 5,849 |
| 2011 | 4,551 |
| 2012 | 4,422 |
| 2013 | 2,723 |
| Thereafter | 8,199 |
| Total | \$ 39,951 |

4. STOCKHOLDERS EQUITY***Option and Restricted Stock Awards******2007 Plan***

Our stockholders approved the Digital River, Inc. 2007 Equity Incentive Plan (the "2007 Plan") at the Company's annual stockholder meeting held on May 31, 2007. The number of shares issuable under the 2007 Plan equals 2,000,000 shares of our common stock. In addition, shares not issued under the 1998 Plan shall become available for issuance under the 2007 Plan to the extent a stock option or other stock award under the 1998 Plan expires or terminates before shares of common stock are issued under the award. Under our 2007 Equity Incentive Plan we have the flexibility to grant incentive and non-statutory stock options, restricted stock awards, restricted stock unit awards and performance shares to our directors, employees, and consultants.

1998 Plan

Under our 1998 Equity Incentive Plan, as amended and restated (the "1998 Plan"), we have the flexibility to grant incentive and non-statutory stock options, restricted stock awards, restricted stock unit awards and performance shares to our directors, employees, and consultants.

General Stock Award Information

As of March 31, 2008, there were 733,770 and 1,123,250 shares available for future awards under our 1998 Plan and 2007 Plan, respectively. The number of shares available has been reduced by three shares for every two shares of restricted stock awards granted under the plans.

Options granted to employees typically expire no later than ten years after the date of grant. Incentive stock option grants must have an exercise price of at least 100% of the fair market value of a share of common stock on the grant date. Incentive stock options granted to employees who, immediately before such grant, owned stock directly or indirectly representing more than 10% of the voting power of our stock, will have an exercise price of 110% of the fair market value of a share of common stock on the grant date and will expire no later than five years from the date of grant. The 1998 Plan also provides for other stock-based awards as may be established by the Board of Directors or the Compensation Committee.

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A summary of the changes in outstanding options under the 1998 Plan and 2007 Plan is as follows:

| | Shares Available for Grant | Options Outstanding | Options Price Per Share | Weighted Average Price Per Share |
|---|---|--------------------------------|--|---|
| Balance, December 31, 2006 | 1,540,200 | 3,557,783 | \$ 2.59-\$57.36 | \$ 18.68 |
| Granted | (573,376) | 573,376 | 45.07 - 56.61 | 54.17 |
| Restricted stock effect on shares available for grant | (251,426) | N/A | N/A | N/A |
| Exercised | | (1,219,519) | 2.59 - 45.24 | 11.08 |
| Canceled/expired | 133,330 | (133,330) | 4.56 - 56.61 | 38.01 |
| Additional Shares Reserved | 2,000,000 | N/A | N/A | N/A |
| Balance, December 31, 2007 | 2,848,728 | 2,778,310 | \$ 2.59-\$57.36 | \$ 28.41 |
| Granted | (532,000) | 532,000 | 30.68- 31.86 | 31.79 |
| Restricted stock effect on shares available for grant | (489,789) | N/A | N/A | N/A |
| Exercised | | (129,871) | 4.56- 27.28 | 15.29 |
| Canceled/expired | 30,081 | (30,081) | 27.28- 56.61 | 46.91 |
| Balance, March 31, 2008 | 1,857,020 | 3,150,358 | \$ 2.59-\$57.36 | \$ 29.34 |

The total pretax intrinsic value of options exercised during the three months ended March 31, 2008, was \$2.3 million. The following table summarizes significant ranges of outstanding and exercisable options under our 1998 Plan and 2007 Plan as of March 31, 2008:

| Exercise Price | Options Outstanding | | | Options Exercisable | | | |
|-----------------------|-------------------------------|--|---|--|-------------------------------|---------------------------------------|--|
| | Number Outstanding | Weighted Average Remaining Life Price | Weighted Average Price Value | Aggregate Intrinsic Value | Number Exercisable | Weighted Average Price | Aggregate Intrinsic Value |
| \$2.59 - \$3.88 | 19,187 | 2.8 years | \$ 2.74 | \$ 541,554 | 19,187 | \$ 2.74 | \$ 541,554 |
| 4.56 - 7.55 | 201,244 | 3.3 years | 5.60 | 5,106,340 | 201,244 | 5.60 | 5,106,340 |
| 9.12 - 13.92 | 446,753 | 4.6 years | 11.72 | 8,602,082 | 374,441 | 11.87 | 7,150,780 |
| 16.72 - 22.98 | 427,204 | 5.5 years | 22.41 | 3,657,883 | 400,418 | 22.63 | 3,339,933 |
| 23.01 - 30.69 | 730,323 | 7.0 years | 28.00 | 2,167,029 | 457,603 | 28.02 | 1,349,781 |
| 31.84 - 57.36 | 1,325,647 | 8.6 years | 48.65 | | 244,055 | 46.45 | |

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| | | | | | | | |
|------------------|-----------|--------------|----------|---------------|-----------|----------|---------------|
| \$2.59 - \$57.36 | 3,150,358 | 6.5 years | \$ 28.87 | \$ 20,074,888 | 1,696,948 | \$ 22.89 | \$ 17,488,388 |
|------------------|-----------|--------------|----------|---------------|-----------|----------|---------------|

The aggregate intrinsic value in the preceding table represents the total pretax intrinsic value, based on options with an exercise price less than the Company's closing stock price of \$30.97 as of March 31, 2008, which would have been received by the option holders had those option holders exercised their options as of that date.

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A summary of the changes in restricted stock under our 1998 Plan and 2007 Plan as of March 31, 2008, is as follows:

| | Restricted Stock | | Weighted Average Intrinsic Value |
|---------------------------------------|-----------------------------|----|---|
| Non-Vested Balance, December 31, 2006 | 89,500 | \$ | 39.96 |
| Granted | 198,889 | | 53.75 |
| Vested | (23,713) | | 39.19 |
| Forfeited | (31,272) | | 48.54 |
| Non-Vested Balance, December 31, 2007 | 233,404 | \$ | 50.64 |
| Granted | 331,300 | | 31.82 |
| Vested | (52,054) | | 49.84 |
| Forfeited | (4,774) | | 50.46 |
| Non-Vested Balance, March 31, 2008 | 507,876 | \$ | 38.44 |

Inducement Equity Incentive Plan

Effective on December 14, 2005, in connection with our acquisition of Commerce5, Inc., we adopted an Inducement Equity Incentive Plan (the "Inducement Plan") initially for Commerce5, Inc. executives who joined Digital River as a result of the acquisition, or other personnel who join us after the date of the Inducement Plan adoption. A total of 87,500 restricted shares of Digital River stock may be issued under the Inducement Plan, subject to vesting. In accordance with the NASDAQ rules, no stockholder approval was required for the Inducement Plan.

Employee Stock Purchase Plan

We also sponsor an employee stock purchase plan ("ESPP") under which 1,200,000 shares have been reserved for purchase by employees. The purchase price of the shares under the ESPP is the lesser of 85% of the fair market value on the first or last day of the offering period. Offering periods are currently every six months ending on June 30 and December 31. Employees may designate up to ten percent of their compensation for the purchase of shares under the ESPP. Total shares purchased by employees under the ESPP were 76,436 shares and 71,183 shares in the years ended December 31, 2007 and 2006, respectively. There were 480,417 shares still reserved under the ESPP as of March 31, 2008.

Stock Repurchase Activity

In June 2007 our Board of Directors authorized a new stock buyback program to repurchase up to an aggregate of \$200 million of our common stock. This buyback program supersedes the prior buyback program. During the three months ended March 31, 2008 we repurchased 3,911,545 shares for \$137.9 million. None of the repurchased shares have been retired.

The Accelerated Share Repurchase agreement was entered into with Goldman Sachs (GS) on February 7, 2008 and calls for GS to repurchase \$127 million of Digital River, Inc. stock between February 7, 2008 and June 20, 2008. Based on the agreement, Digital River will receive a final share count based on a discount of the Volume Weighted Average Price of Digital River stock from February 21, 2008, through the end of the contract. As of March 31, 2008, Digital River has received 3,548,845 shares.

Rule 10b5-1 Trading Plans

Our Chief Executive Officer, Joel A. Ronning, has entered into a trading plan pursuant to Rule 10b5-1(c)(1) of the Securities Exchange Act of 1934, as amended. A trading plan is a written document that pre-establishes the amounts, prices and dates (or formula for determining the amounts, prices and dates) of future purchases or sales of the

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Company's stock including the exercise and sale of employee stock options and shares acquired pursuant to the Company's employee stock purchase plan and upon vesting of restricted stock.

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Expense Information under SFAS 123(R)

On January 1, 2006, we adopted SFAS 123(R) which requires measurement and recognition of compensation expense for all stock-based payments made to employees and directors including stock options, restricted stock grants and employee stock purchases made through our ESPP based on estimated fair values. The following table summarizes stock-based compensation expense, net of tax, related to employee stock options and employee stock purchases recognized under SFAS 123(R):

| | Three Months Ended | |
|---|---------------------------|-------------|
| | March 31, | |
| | 2008 | 2007 |
| Costs and expenses | | |
| Direct cost of services | \$ 192 | \$ 195 |
| Network and infrastructure | 32 | 72 |
| Sales and marketing | 1,102 | 1,268 |
| Product research and development | 262 | 552 |
| General and administrative | 1,443 | 1,389 |
| Stock-based compensation included in costs and expenses | 3,031 | 3,476 |
| Tax benefit | (668) | (1,047) |
| Stock-based compensation expense, net of tax | \$ 2,363 | \$ 2,429 |

Valuation Information under SFAS 123(R)

The weighted-average fair value of stock options granted during the three months ended March 31, 2008 and 2007 were \$11.23 and \$23.07 per share, respectively, using the Black-Scholes option pricing model with the following weighted average assumptions:

| | Three Months Ended | |
|-------------------------|---------------------------|-------------|
| | March 31, | |
| | 2008 | 2007 |
| Risk-free interest rate | 2.0% | 4.5% |
| Expected life (years) | 3.5 | 3.5 |
| Volatility factor | 0.46 | 0.51 |
| Expected dividends | | |

The risk-free interest rate assumption is based on observed interest rates appropriate for the term of our stock options. The expected life of stock options represents the weighted-average period the stock options are expected to remain outstanding and is based on historical exercise patterns. We used historical closing stock price volatility for a period equal to the expected term of the options granted. The dividend yield assumption is based on our history and expectation of future dividend payouts.

As stock-based compensation expense recognized in the Condensed Consolidated Statement of Income for the three months ended March 31, 2008 is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Forfeitures were estimated based on historical experience.

At March 31, 2008, there was approximately \$34.9 million of total unrecognized stock-based compensation expense, adjusted for estimated forfeitures, related to unvested share-based awards. Unrecognized stock-based compensation

expense is expected to be recognized over the next 4.2 years on a weighted average basis and will be adjusted for any future changes in estimated forfeitures.

5. INCOME TAXES

For the three months ended March 31, 2008 and 2007, our tax expense was \$7.8 million and \$9.3 million, respectively.

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For the three months ended March 31, 2008, our tax expense consisted of approximately \$6.4 million of U.S. tax expense and \$1.4 million of foreign tax expense.

In prior years, there was uncertainty of future realization of the deferred tax assets resulting from acquired U.S. tax loss carryforwards due to anticipated limitations, including limitations under Section 382 of the Internal Revenue Code. Therefore a valuation allowance was recorded against the tax effect of such tax loss carryforwards. We evaluated these deferred tax assets and concluded it is more likely than not that we will realize \$11.6 million of these deferred tax assets. This is based on conclusions of an IRC Section 382 analysis completed during 2007 as well as our expected future taxable income. The release of the valuation allowance was recorded in the second quarter of 2007 and was reflected as a reduction to goodwill. A valuation allowance remains on approximately \$1.4 million of deferred tax assets related to acquired operating losses and other tax attributes as we believe it is more likely than not that these deferred tax assets will not be realized. This valuation allowance is due to anticipated limitations on acquired losses and any future release of this valuation allowance will reduce goodwill.

As of March 31, 2008, we had \$5.9 million of unrecognized tax benefits. All of these unrecognized tax benefits would affect our effective tax rate if recognized. As of March 31, 2008, we had approximately \$120,000 of accrued interest related to uncertain tax positions.

Due to the potential resolution of examinations currently being performed by taxing authorities, and the expiration of various statutes of limitation, it is reasonably possible that the balance of our gross unrecognized tax benefits may change within the next twelve months by a range of zero to \$4.1 million.

6. DEBT

In 2004 we sold and issued \$195.0 million in aggregate principal amount of 1.25% convertible senior notes due January 1, 2024 (Notes), in a private, unregistered offering. The Notes were sold at 100% of their principal amount. We are required to pay interest on the Notes on January 1 and July 1 of each year so long as the Notes are outstanding. The Notes bear interest at a rate of 1.25% and, if specified conditions are met, are convertible into our common stock at a conversion price of \$44.063 per share. The Notes may be surrendered for conversion under certain circumstances, including the satisfaction of a market price condition, such that the price of our common stock reaches a specified threshold; the satisfaction of a trading price condition, such that the trading price of the Notes falls below a specified level; the redemption of the Notes by us, the occurrence of specified corporate transactions, as defined in the related indenture; and the occurrence of a fundamental change, as defined in the related indenture. The initial conversion price is equivalent to a conversion rate of approximately 22.6948 shares per \$1,000 of principal amount of the Notes. We will adjust the conversion price if certain events occur, as specified in the related indenture, such as the issuance of our common stock as a dividend or distribution or the occurrence of a stock subdivision or combination. If a fundamental change, such as a change in our control, as defined in the related indenture, occurs on or before January 1, 2009, we may also be required to purchase the Notes for cash and pay an additional make whole premium payable in our common stock upon the repurchase or conversion of the Notes in connection with the fundamental change.

Holders of the Notes have the right to require us to repurchase their Notes prior to maturity on January 1, 2009, 2014 and 2019. We have the right to redeem the Notes, under certain circumstances, on or after July 1, 2007 and prior to January 1, 2009, and we may redeem the Notes at any time on or after January 1, 2009. Through December 31, 2007, we classified the Notes as long-term debt. However, in light of the right of holders to require us to redeem the Notes on January 1, 2009, we have reclassified the Notes as short-term debt.

In each the first quarters of 2008 and 2007, we incurred interest expense of \$0.6 million on the Notes and made \$1.2 million interest payments in each of the first quarters of 2008 and 2007.

7. FAIR VALUE MEASUREMENTS

Effective January 1, 2008, we adopted the provisions of Statement of Financial Accounting Standards No. 157, Fair Value Measurements, (FAS 157) for financial instruments, as required. FAS 157 defines fair value, establishes a framework for measuring fair value in accordance with GAAP, and requires enhanced disclosures about fair value

measurements. FAS 157 does not require any new fair value measurements; rather it specifies valuation methods

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and disclosures to be applied when fair value measurements are required under existing or future accounting pronouncements.

FAS 157 clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, FAS 157 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

- Level 1 Observable inputs such as quoted prices in active markets;
-
- Level 2 Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly; and
-
- Level 3 Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumption.

As of March 31, 2008, we held certain assets that are required to be measured at fair value on a recurring basis. These included cash equivalents, short and long-term investments and convertible senior notes.

At March 31, 2008, we held approximately \$117.2 million of municipal debt classified as current assets, with an auction reset feature (auction rate securities) whose underlying assets are generally student loans which are FFELP (Federal Family Education Loan Program), over-collateralized, insured and backed by the Department of Education. As of May 1, 2008, auctions failed for all of our auction rate securities. A failed auction will occur if there is more selling than buying in a given auction. All of our auction rate securities, including those subject to the failure, are currently rated AAA, the highest rating, by a rating agency. If the issuers are unable to successfully close future auctions and their credit ratings deteriorate, we may in the future be required to record an other than temporary impairment charge on these investments.

We believe we will be able to liquidate our investment without loss within the next year. We currently believe the market liquidity for these securities will recover within the next twelve months and are not, other than temporarily, impaired, primarily due to the government guarantee of the underlying securities; however, there is no guarantee that it will not take until the final maturity of the underlying notes (up to 30 years) to realize our investments recorded value. Based on our expected operating cash flows, and our other sources of cash, we do not anticipate the potential lack of liquidity on these investments will affect our ability to execute our current business plan.

We have used a discounted cash flow model to determine the estimated fair value of our investment in auction rate securities as of March 31, 2008. The assumptions used in preparing the discounted cash flow model include estimates for interest rates, timing and amount of cash flows and expected holding periods of the auction rate securities. Based on this assessment of fair value, the delta between fair value and par value was not material and no unrealized loss was recorded. The Company believes that the market for these instruments will recover in the next twelve months. Any future fluctuation in fair value related to these instruments that the Company deems to be temporary, including any recoveries of previous write-downs, would be recorded to accumulated other comprehensive income. If the Company determines that any future valuation adjustment was other than temporary, it would record a charge to earnings as appropriate.

The table below presents our assets measured at fair value on a recurring basis as of March 31, 2008:

| | Fair Value Measurements | | | |
|------------------|--------------------------------|----------------|----------------|----------------|
| | As of March 31, 2008 | | | |
| | Total | Level 1 | Level 2 | Level 3 |
| Cash equivalents | \$ 305,800 | \$ 305,800 | \$ | \$ |

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|-------------------------------------|------------|------------|----|------------|
| Short-term investments | 289,612 | 172,412 | | 117,200 |
| Total assets measured at fair value | \$ 595,412 | \$ 478,212 | \$ | \$ 117,200 |

Based on market conditions, we have classified auction rate securities as Level 3 within FAS 157's hierarchy since our initial adoption of FAS 157 at January 1, 2008. As of March 31, 2008, the difference between fair value and par value of these securities was immaterial to our financial statements.

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8. LITIGATION

We are subject to legal proceedings, claims and litigation arising in the ordinary course of business. While the final outcome of these matters is currently not determinable, we believe there is no litigation pending against us that is likely to have, individually or in the aggregate, a material adverse effect on our consolidated financial position, results of operations or cash flows. Because of the uncertainty inherent in litigation, it is possible that unfavorable resolutions of these lawsuits, proceedings and claims could exceed the amount we have currently reserved for these matters.

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

The discussion in this Quarterly Report contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those discussed below. Additional factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section entitled Risk Factors, included in Item 1A of Part II of this Quarterly Report. When used in this document, the words believes, expects, anticipates, intends, plans, and similar expressions, are intended to identify certain of these forward-looking statements. However, these words are not the exclusive means of identifying such statements. In addition, any statements that refer to expectations, projections or other characterizations of future events or circumstances are forward-looking statements. The cautionary statements made in this document should be read as being applicable to all related forward-looking statements wherever they appear in this document.

Overview

We provide end-to-end global e-commerce solutions to a wide variety of companies in software, consumer electronics, computer and video games, and other markets. We were incorporated in 1994 and began building and operating online stores for our clients in 1996. We offer our clients a broad range of services that enable them to quickly and cost effectively establish an online sales channel capability and to subsequently manage and grow online sales on a global basis. Our offerings help our clients mitigate risk and grow their online revenues. Our services include design, development and hosting of online stores and shopping carts, store merchandising and optimization, order management, denied parties screening, export controls and management, tax compliance and management, digital product delivery via download, physical product fulfillment, subscription management, multi-lingual customer service, online marketing including e-mail marketing, management of paid search programs, website optimization, web analytics and reporting.

Our products and services allow our clients to focus on promoting and marketing their brands while leveraging our investments in technology and infrastructure to facilitate the purchase of products through their online websites. When shoppers visit one of our clients' websites and purchase goods, they are transferred to an e-commerce store and /or shopping cart operated by us on our e-commerce platform. Once on our system, shoppers can browse for products and make purchases online. We typically are the seller of record for transactions through our stores. After a purchase is made, we either deliver the product digitally via download over the Internet or transmit instructions to a third party for physical fulfillment of the order. We also process the buyer's payment as the merchant of record, including collection and remittance of applicable taxes, and can provide customer service in multiple languages to handle order-related questions. We believe we are an example of an emerging trend known as Software as a Service (SaaS). We have invested substantial resources to develop our e-commerce software platform and we provide access and use of it to our clients as a service as opposed to selling the software to be operated on their own in-house computer hardware. In addition to the services we provide that facilitate the completion of an online transaction, we also offer services designed to increase traffic to our clients' websites and the associated online stores and to improve the sales productivity of those stores. Our services include paid search advertising, search engine optimization, affiliate marketing, store optimization, and e-mail optimization. All of our services are designed to help our clients acquire customers more effectively, sell to those customers more often and more efficiently, and increase the lifetime value of each customer.

Our clients include many of the largest software, consumer electronics, and computer and video game companies and major retailers of these products, including Smith Micro Software, Inc., Autodesk, Inc., Computer Associates, Canon Inc., Electronic Arts, Inc., Hewlett Packard Company, Lexmark, Inc., Microsoft Corporation, Nuance Communications Inc, Symantec Corporation, and Trend Micro, Inc.

General information about us can be found at www.digitalriver.com under the Company/Investor Relations link. Our annual report on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, as well as any amendments or exhibits to those reports, are available free of charge through our website as soon as reasonably practicable after we file them with the Securities and Exchange Commission.

Our prospects must be considered in light of the risks, expenses and difficulties frequently encountered by companies in new and rapidly evolving markets such as e-commerce. See Item 1A of Part II for a discussion of the risk factors that could have a material adverse effect on our business, financial condition and results of operations.

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We prepare our consolidated financial statements in conformity with accounting principles generally accepted in the United States of America. As such, we are required to make certain estimates, judgments and assumptions that we believe are reasonable based upon the information available. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods presented. The significant accounting policies that we believe are the most critical in fully understanding and evaluating our reported financial results are the following:

Revenue Recognition. We recognize revenue from services rendered once all the following criteria for revenue recognition have been met: (1) pervasive evidence of an agreement exists; (2) the services have been rendered; (3) the fee is fixed and determinable and not subject to refund or adjustment; and (4) collection of the amounts due is reasonably assured.

We evaluate the criteria outlined in Emerging Issues Task Force, (EITF) Issues No. 99-19, Reporting Revenue Gross as a Principal versus Net as an Agent, in determining whether it is appropriate to record the gross amount of product sales and related costs or the net amount earned as net revenue. We act as the seller and merchant of record on most of the transactions processed and have contractual relationships with our clients, which obligate us to pay to the client a specified percentage of each sale. We derive our revenue primarily from transaction fees based on a percentage of the product sale price and fees from services rendered associated with the e-commerce and other services provided to our clients and end customers. Our revenue is recorded as net as generally our clients are subject to inventory risks and control customers' product choices. Clients do not have the right to take possession of the software applications used in the delivery of services.

We also provide customers with various proprietary software backup services. We recognize revenue for these backup services upon delivery or based upon historical usage within the contract period of the digital backup services when this information is available. Digital backup services are recognized straight-line over the life of the backup service when historical usage information is unavailable. Shipping revenues are recorded net of any associated costs.

We also, to a lesser extent, provide fee-based client services, which include website design and hosting, custom development and integration, analytical marketing and email marketing services. If we receive payments for fee-based services in advance of delivery, these amounts are deferred and recognized over the service period.

Provisions for doubtful accounts and transaction losses and authorized credits are made at the time of revenue recognition based upon our historical experience. The provision for doubtful accounts and transaction losses are recorded as charges to operating expense, while the provision for authorized credits is recognized as a reduction of net revenues.

In June 2006, the EITF reached a consensus on EITF Issue No. 06-3, How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That is, Gross versus Net Presentation) (EITF 06-3). EITF 06-3 provides that the presentation of taxes assessed by a governmental authority that is directly imposed on a revenue-producing transaction between a seller and a customer on either a gross basis (included in revenues and costs) or on a net basis (excluded from revenues) is an accounting policy decision that should be disclosed. The Company presents these taxes on a net basis.

Allowance for Doubtful Accounts. We must make estimates and assumptions that can affect the amount of assets and liabilities and the amounts of revenues and expenses we report in any financial reporting period. We use estimates in determining our allowance for doubtful accounts, which are based on our historical experience and current trends. We must estimate the collectability of our billed accounts receivable. We analyze accounts receivable and consider our historical bad debt experience, customer credit-worthiness, current economic trends and changes in our customer payment terms when evaluating the adequacy of the allowance for doubtful accounts. We must make significant judgments and estimates in connection with the allowance in any accounting period. There may be material differences in our operating results for any period if we change our estimates or if the estimates are not accurate.

Credit Card Chargeback Reserve. We use estimates based on historical experience and current trends to determine accrued chargeback expenses. Significant management judgments are used and estimates made in connection with the accrued expenses in any accounting period. There may be material differences in our operating results for any period if we change our estimates or if the estimates are not accurate.

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Goodwill, Intangibles and Other Long-Lived Assets. We depreciate property, plant and equipment; amortize certain intangibles and certain other long-lived assets with definite lives over their useful lives. Useful lives are based on our estimates of the period of time over which the assets will generate revenue or benefit our business. We review assets with definite lives for impairment whenever events or changes in circumstances indicate that the value we are carrying on our financial statements for an asset may not be recoverable. Our evaluation considers non-financial data such as changes in the operating environment and business strategy, competitive information, market trends and operating performance. If there are indications that impairment may be necessary, we use an undiscounted cash flow analysis to determine the impairment amount, if any. Assets with indefinite lives are reviewed for impairment annually in the fourth quarter (or more frequently if there are indications that an impairment may be necessary) utilizing the two-step approach prescribed in Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*. There have been no impairments of goodwill and other intangible assets for the three months ended March 31, 2008 and 2007.

Income Taxes and Deferred Taxes. Deferred income taxes reflect the tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. We record deferred tax assets for favorable tax attributes, including tax loss carryforwards. We currently have significant U.S. tax loss carryforwards consisting solely of acquired operating tax loss carryforwards, and a lesser amount of acquired foreign operating tax loss carryforwards. A portion of the benefit of the acquired tax loss carryforwards has been reserved by a valuation allowance pursuant to United States generally accepted accounting principles. These valuation reserves of the deferred tax asset will be reversed if and when it is more likely than not that the deferred tax asset will be realized. We evaluate the need for a valuation allowance of the deferred tax asset on a quarterly basis. If the benefit of these acquired tax loss carryforwards is recognized, we will not recognize the benefit in the statement of income. Rather, the benefit will be recognized as a reduction to goodwill.

On January 1, 2007, we adopted FASB Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109*. FIN 48 clarifies the accounting for uncertainty in income taxes recognized under SFAS No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and also provides guidance on various related matters such as derecognition, interest and penalties, and disclosure. As a result of the implementation of FIN 48, we recognized no material adjustment in the liability for unrecognized income tax benefits.

Fair Value Measurements. On January 1, 2008, we adopted FAS No. 157, *Fair Value Measurements* (FAS 157). This Statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. The Statement applies under other accounting pronouncements that require or permit fair value measurements and, accordingly, does not require any new fair value measurements. This Statement was initially effective as of January 1, 2008, but in February 2008, the FASB delayed the effective date for applying this standard to nonfinancial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. We adopted FAS 157 as of January 1, 2008 for assets and liabilities within its scope and the impact was immaterial to our financial statements.

Stock-Based Compensation Expense. On January 1, 2006, we adopted Statement of Financial Accounting Standards No. 123 (Revised 2004), *Share-Based Payment*, (SFAS 123(R)) which requires the measurement and recognition of compensation expense for all share-based payments made to employees and directors including stock options, restricted stock grants and employee stock purchases made through our Employee Stock Purchase Plan based on estimated fair values.

We have adopted SFAS 123(R) using the modified prospective transition method under which prior periods are not revised. Stock-based compensation expense recognized during the period is based on the value of the portion of share-based awards that are ultimately expected to vest during the period. Stock-based compensation expense recognized in our Condensed Consolidated Statement of Income for 2007 and 2008 includes compensation expense for share-based awards granted prior to, but not yet vested, as of December 31, 2005, as well as compensation expense for the share-based payment awards granted subsequent to December 31, 2005. The fair value of each stock option grant is estimated on the date of grant using the Black-Scholes option pricing model. The fair value of restricted stock

is determined based on the number of shares granted and the closing price of our common stock on the date of grant. Compensation expense for all share-based payment awards is recognized using the straight-line amortization method over the vesting period. As stock-based compensation expense recognized in our Condensed Consolidated Statement of Income is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

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SFAS 123(R) also requires the benefits of tax deductions in excess of recognized stock-based compensation expense be reported as a financing cash flow, rather than an operating cash flow as required prior to adoption of SFAS 123(R) in our Condensed Consolidated Statement of Cash Flows.

See Note 4 in the Condensed Consolidated Financial Statements in this Quarterly Report on Form 10-Q for further information regarding our stock-based compensation plans.

Results of Operations

The following table sets forth certain items from our condensed consolidated statements of income as a percentage of total revenue for the periods indicated.

| | Three Months Ended | |
|--|---------------------------|-------------|
| | March 31, | |
| | 2008 | 2007 |
| Revenue | 100.0% | 100.0% |
| Cost of Revenue (exclusive of depreciation and amortization expense shown separately below): | | |
| Direct cost of services | 4.0 | 2.8 |
| Network and infrastructure | 9.8 | 8.2 |
| Sales and marketing | 38.3 | 37.3 |
| Product research and development | 12.3 | 9.4 |
| General and administrative | 9.9 | 11.0 |
| Depreciation and amortization | 3.7 | 3.1 |
| Amortization of acquisition-related costs | 2.1 | 3.1 |
| Total costs and expenses | 80.1 | 74.9 |
| Income from operations | 19.9 | 25.1 |
| Interest Income | 6.0 | 8.6 |
| Other expense, net | (0.7) | (1.0) |
| Income before income tax expense | 25.2 | 32.7 |
| Income tax expense | 7.6 | 10.1 |
| Net income | 17.6% | 22.6% |

We acquired NetGiro Systems AB on September 1, 2007, and DigitalSwift Corporation and CustomCD, Inc. in January 2008. The results of these acquisitions must be factored into any comparison of our 2008 results to the results for 2007. See Note 3 of our Consolidated Financial Statements in this Form 10-Q for pro forma financial information as if these entities had been acquired on January 1, 2007.

REVENUE. Our revenue increased to \$103.6 million for the three months ended March 31, 2008, from \$91.6 million for the same period in the prior year, an increase of \$12.0 million, or 13.1%. The revenue increases were primarily attributable to increased traffic, increase in average order value offset by a reduction in close ratio, growth in the number of online game and consumer electronic clients we served, increased sales from international sites, expanded strategic marketing activities with a larger number of clients, and acquisitions. NetGiro, DigitalSwift and CustomCD accounted for \$4.9 million of total revenue as of March 31, 2008. Sales of security software products for PCs represent the largest contributor to our revenues.

International e-commerce sales were approximately 43.2% and 42.6% of total sales in the three month period ended March 31, 2008 and 2007, respectively. That growth is attributable to a larger number of international stores being operated for our clients.

DIRECT COST OF SERVICES. Our direct cost of services primarily include costs related to personnel, product fulfillment, physical on demand, our proprietary back-up CD production and client-specific costs. Direct cost of service expense was \$4.2 million for the three months ended March 31, 2008, up from \$2.6 million for the same period in the prior year. The increase was primarily due to \$1.3 million of increased CD supply and personnel related costs associated with higher gross sales from our January 2008 DigitalSwift Corporation and CustomCD, Inc. acquisitions. The remaining increases were attributable to higher CD supply and additional personnel costs to support our largest clients and handle increased sales volume. As a percentage of revenue, direct cost of services

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increased to 4.0% for the three months ended March 31, 2008 compared to 2.8% in the same period of the prior year. We currently believe that direct cost of services will increase in absolute dollars in 2008 compared to 2007 as a result of our acquisitions and as we continue to expand our worldwide fulfillment capacity to meet anticipated shipment volumes.

NETWORK AND INFRASTRUCTURE. Our network and infrastructure expenses primarily include personnel related expenses and costs to operate and maintain our technology platforms, customer service, data communication and data center operations. Network and infrastructure expenses were \$10.2 million and \$7.5 million for the three months ended March 31, 2008 and 2007, respectively. The increase in 2008 supported revenue growth and was comprised of approximately \$1.1 million in personnel related expenses, \$0.8 million in additional software license amortization expense and \$0.8 million of network and infrastructure costs related to our recent NetGiro Systems acquisition. As a percentage of revenue, direct cost of services increased to 9.8% for the three months ended March 31, 2008 compared to 8.2% in the same period of the prior year.

We currently believe that network and infrastructure expenses will increase in absolute dollars in 2008 compared to 2007 due to the impact of acquisitions and as we continue to expand our global data center and customer service capacity.

SALES AND MARKETING. Our sales and marketing expenses mainly include credit card transaction and other payment processing fees, personnel and related costs, advertising, promotional and product marketing expenses, credit card chargebacks and bad debt expense. Sales and marketing expenses increased to \$39.7 million for the three months ended March 31, 2008 from \$34.2 million for the same period in the prior year. The increase was primarily due to a \$3.0 million increase in credit card and other payment processing fees directly related to incremental gross revenue and the addition of new international payment methods, an additional \$1.2 million in personnel and related costs to support our global growth initiatives in strategic and product marketing and \$1.0 million in sales and marketing expenses incurred by our recent acquisition NetGiro Systems. As a percentage of revenue, sales and marketing expense was 38.3% in the three months ended March 31, 2008, compared to 37.3% for the same period in the prior year.

We currently believe sales and marketing expenses will increase in absolute dollars in 2008 compared to 2007, to support the expansion of our client relationships through increased investments in subscriptions, international payment processing and strategic marketing services. We also plan to invest in key vertical markets, in particular consumer electronics and games.

PRODUCT RESEARCH AND DEVELOPMENT. Our product research and development expenses include the costs of personnel and related expenses associated with developing and enhancing our technology platforms and related systems. Product research and development expense increased to \$12.7 million, for the three months ended March 31, 2008 from \$8.7 million for the same period in the prior year. The increase for the three months ended March 31, 2008 compared to the same period in 2007 was primarily due to strategic investments in our e-commerce infrastructure. These investments primarily impacted software development and quality assurance and comprised \$1.5 million of professional consulting fees, \$1.4 million in personnel related expenses and \$1.1 million of product research and development expenses related to our recent NetGiro Systems AB acquisition. These investments supported on-going initiatives in our e-commerce infrastructure to advance global system scalability, our e-marketing capabilities and client reporting. We expect these investments to drive long-term operational efficiencies across the organization and provide further competitive differentiation. We did not capitalize any significant costs related to software development during the three months ended March 31, 2008 and 2007. As a percentage of revenue, product research and development expense increased to 12.3% in the three months ended March 31, 2008 compared to 9.4% for the same period in the prior year.

We currently believe that product research and development expenses will increase in absolute dollars in 2008 compared to 2007, as a result of our completed 2007 NetGiro acquisition and continued investments in product development required to remain competitive.

GENERAL AND ADMINISTRATIVE. Our general and administrative expenses primarily include the costs of executive, accounting and administrative personnel and related expenses, professional fees for legal, tax and audit services, bank fees and insurance. General and administrative expenses increased to \$10.2 million for the three months

ended March 31, 2008 from \$10.1 million for the same period in the prior year. The increase resulted from approximately \$0.7 million higher personnel costs to support infrastructure investments and continued growth and

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\$0.4 million related to our recent NetGiro acquisition. These increases were partially offset by \$0.9 million lower legal expenses for the period ended March 31, 2008 compared to the prior year which included professional legal fees related to our internal review of historical stock option practices. As a percentage of revenue, general and administrative expenses decreased to 9.9% for the three months ended March 31, 2008 compared to 11.0% in the same period of the prior year.

We currently believe that general and administrative expenses will increase in absolute dollars in 2008 compared to 2007, as we continue to invest in our infrastructure to support our continued organic growth and expenses related to new acquisitions.

DEPRECIATION AND AMORTIZATION. Our depreciation and amortization expenses include the depreciation of computer equipment and office furniture and the amortization of purchased and internally developed software, leasehold improvements made to our leased facilities and debt financing costs. Computer equipment, software and furniture are depreciated under the straight-line method using three to seven year lives and leasehold improvements are amortized over the shorter of the life of the asset or the remaining length of the lease. Depreciation and amortization expense was \$3.8 million and \$2.9 million for the three months ended March 31, 2008 and 2007, respectively. The increase was primarily due to depreciation and amortization on new data center equipment, third party software licenses and facilities.

We currently believe that depreciation and amortization expense will increase in absolute dollars in 2008 compared to 2007 as we continue to expand our worldwide customer support capacity and expand the number of operating global data centers.

AMORTIZATION OF ACQUISITION-RELATED INTANGIBLES. Our amortization of acquisition-related intangibles line item consists of amortization of intangible assets recorded from eight of our acquisitions during the past four years. Amortization of acquisition-related intangible assets was \$2.2 million for the three months ended March 31, 2008, compared to \$2.7 million for the same period in the prior year. The decrease was due to lower expense from intangible assets that have become fully amortized partially offset by additional amortization from recent acquisitions. We have purchased, and expect to continue purchasing assets or businesses which may include the purchase of intangible assets.

INTEREST INCOME. Our interest income represents the total of interest income on our cash, cash equivalents, and short-term investments. Interest income was \$6.2 million and \$7.9 million in March 31, 2008 and 2007, respectively. The decrease in interest income was primarily due to the use of \$138 million in cash for our share repurchase during the quarter ended March 31, 2008. Interest income also declined due to lower interest rates during 2008.

OTHER EXPENSE, NET. Our other expense, net line includes the total of interest expense on our debt and foreign currency transaction gains and losses. Interest expense was \$0.7 and \$0.6 million for the three months ended March 31, 2008 and 2007, respectively. Foreign currency re-measurement was a loss of \$0.1 million for the three months ended March 31, 2008, compared to a loss of \$0.3 million for the same period in the prior year. Gains and losses from the sale of investments were immaterial for the three months ended March 31, 2008 and 2007.

INCOME TAXES. For the three months ended March 31, 2008 and 2007, our tax expense was \$7.8 million and \$9.3 million, respectively. For the three months ended March 31, 2008, our tax expense consisted of approximately \$6.4 million of U.S. tax expense and \$1.4 million of foreign tax expense.

In prior years, there was uncertainty of future realization of the deferred tax assets resulting from acquired U.S. tax loss carryforwards due to anticipated limitations, including limitations under Section 382 of the Internal Revenue Code. Therefore a valuation allowance was recorded against the tax effect of such tax loss carryforwards. We evaluated these deferred tax assets and concluded it is more likely than not that we will realize \$11.6 million of these deferred tax assets. This is based on conclusions of an IRC Section 382 analysis completed during 2007 as well as our expected future taxable income. The release of the valuation allowance was recorded in the second quarter of 2007 and was reflected as a reduction to goodwill. A valuation allowance remains on approximately \$1.4 million of deferred tax assets related to acquired operating losses and other tax attributes as we believe it is more likely than not that these deferred tax assets will not be realized. This valuation allowance is due to anticipated limitations on acquired losses and any future release of this valuation allowance will reduce goodwill.

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As of March 31, 2008, we had \$5.9 million of unrecognized tax benefits. All of these unrecognized tax benefits would affect our effective tax rate if recognized. As of March 31, 2008, we had approximately \$120,000 of accrued interest related to uncertain tax positions.

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Due to the potential resolution of examinations currently being performed by taxing authorities, and the expiration of various statutes of limitation, it is reasonably possible that the balance of our gross unrecognized tax benefits may change within the next twelve months by a range of zero to \$4.1 million.

Off Balance Sheet Arrangements

None

Table of Contents**Liquidity and Capital Resources**

As of March 31, 2008, we had \$305.8 million of cash and cash equivalents, \$289.6 million of short-term investments. Our primary source of internal liquidity is our operating activities. Net cash provided by operations during the first quarter of 2008 and 2007 was primarily the result of net income adjusted for non-cash expenses, and balance sheet changes such as an increase in accounts payable.

Net cash provided by investing activities for the three months ended March 31, 2008 was \$6.7 million and was the result of net sales of investments of \$27.3 million, cash paid for acquisitions net of cash received of \$16.5 million, and purchases of capital equipment of \$4.2 million. Net cash used in investing activities for the three months ended March 31, 2007 was \$35.1 million and was the result of net purchases of investments of \$27.3 million, cash paid for acquisitions net of cash received of \$4.3 million, and purchases of capital equipment of \$3.4 million.

Net cash used by financing activities during the three months ended March 31, 2008 was \$135.9 million. Proceeds of \$2.0 million were provided by the sale of stock through the exercise of stock options, cash used in the repurchase of restricted stock to satisfy tax withholding obligation was \$0.4, and proceeds of \$0.4 million were provided by the excess tax benefit from stock-based compensation. In February 2008, we repurchased \$137.9 million of common stock, which reduced our net cash provided by financing activities. Net cash provided by financing activities during the three months ended March 31, 2007, was \$13.9 million. Proceeds of \$5.6 million were provided by the sale of stock through the exercise of stock options and purchases through the employee stock purchase plan, cash used in the repurchase of restricted stock to satisfy tax withholding obligation was \$0.2, and proceeds of \$8.5 million were provided by the excess tax benefit from stock-based compensation.

At March 31, 2008, we held approximately \$117.2 million of municipal debt, classified as current assets, with an auction reset feature (auction rate securities) whose underlying assets are generally student loans which are FFELP (Federal Family Education Loan Program), over-collateralized, insured and backed by the Department of Education. As of May 1, 2008, auctions failed for all of our auction rate securities. A failed auction will occur if there is more selling than buying in a given auction. All of our auction rate securities, including those subject to the failure, are currently rated AAA, the highest rating, by a rating agency. If the issuers are unable to successfully close future auctions and their credit ratings deteriorate, we may in the future be required to record an impairment charge on these investments.

We believe we will be able to liquidate our investment without loss within the next year. We currently believe the market liquidity for these securities will recover within the next twelve months and are not, other than temporarily, impaired, primarily due to the government guarantee of the underlying securities; however, there is no guarantee that it will not take until the final maturity of the underlying notes (up to 30 years) to realize our investments recorded value. Based on our expected operating cash flows, and our other sources of cash, we do not anticipate the potential lack of liquidity on these investments will affect our ability to execute our current business plan.

We completed our review of Fair Value Measurements FAS 157 for the quarter ended March 31, 2008. Fair Market Value determination was based on level 3 of the fair value hierarchy of FAS 157. We did not record any fair value adjustments for the three months ended March 31, 2008. See Note 7 for further information.

Our principal commitments consist of interest and principal on our convertible senior notes and long-term obligations outstanding under operating leases. Although we have no material commitments for capital expenditures, we anticipate continued capital expenditures consistent with our anticipated growth in operations, infrastructure and personnel. We expect that our operating expenses will continue to grow as our overall business grows and that they will be a material use of our cash resources.

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The following table summarizes our principal contractual commitments as of March 31, 2008:

| Contractual Obligations | Total Amount Committed | Payment due by period (in thousands) | | | 2013 and Thereafter |
|--------------------------------|---------------------------------------|---|------------------|------------------|--------------------------------|
| | | Apr-Dec 2008 | 2009-2010 | 2011-2012 | |
| Operating Lease Obligations | \$ 18,007 | \$3,830 | \$ 6,140 | \$1,978 | \$ 6,058 |
| Convertible Senior Notes | \$234,000 | \$1,219 | \$ 4,875 | \$4,875 | \$223,031 |
| Total | \$252,007 | \$5,049 | \$11,015 | \$6,853 | \$229,089 |

We expect to continue to evaluate and consider a wide array of potential strategic transactions, including business combinations and acquisitions of businesses, products, services and other assets as well as licenses of technology related to our current business. At any given time, we may be engaged in discussions or negotiations with respect to one or more such transactions. Any such transactions could have a material impact on our financial position, results of operations, or cash flows. There is no assurance that any such discussions or negotiations will result in the consummation of any transaction. The process of integrating any acquisition may create unforeseen challenges for our operational, financial and management information systems, as well as unforeseen expenditures and other risks, including diversion of management's attention from other business concerns, the potential loss of key customers, employees and business partners, difficulties in managing facilities and employees in different geographic areas, and difficulties in entering markets in which we have no or limited direct prior experience and where competitors in such markets have stronger market positions. In addition, an acquisition may cause us to assume liabilities or become subject to litigation. Further, there can be no assurance that we will realize a positive return on any acquisition or that future acquisitions will not be dilutive to our current shareholders' percentage ownership or to earnings. We have allocated significant valuation in the form of goodwill and intangibles for the companies we acquired in the past, which is subject to impairment testing on a regular basis. If the individual businesses do not perform as expected at the acquisition dates, we may incur impairment charges for goodwill, accelerated amortization of definite-lived intangible assets due to shortened expected lives of those assets, immediate write-offs and restructuring or other related expenses.

With respect to our 1.25% convertible senior notes due January 1, 2024 (the "Notes"), we are required to pay interest on the Notes on January 1 and July 1 of each year so long as the Notes are outstanding. On January 2, 2008, we paid \$1.2 million in interest for the period July 1 through December 31, 2007. The Notes bear interest at a rate of 1.25% and, if specified conditions are met, are convertible into our common stock at a conversion price of \$44.063 per share. The Notes may be surrendered for conversion under certain circumstances, including the satisfaction of a market price condition, such that the price of our common stock reaches a specified threshold; the satisfaction of a trading price condition, such that the trading price of the Notes falls below a specified level; the redemption of the Notes by us, the occurrence of specified corporate transactions, as defined in the related indenture; and the occurrence of a fundamental change, as defined in the related indenture. The initial conversion price is equivalent to a conversion rate of approximately 22.6948 shares per \$1,000 of principal amount of the Notes. We will adjust the conversion price if certain events occur, as specified in the related indenture, such as the issuance of our common stock as a dividend or distribution or the occurrence of a stock subdivision or combination. In addition, contingent interest is required to be paid to holders if certain conditions are met. If a fundamental change, such as a change in our control, as defined in the related indenture, occurs on or before January 1, 2009, we may also be required to purchase the Notes for cash and pay an additional make whole premium payable in our common stock upon the repurchase or conversion of the Notes in connection with the fundamental change.

Holders of the Notes have the right to require us to repurchase their Notes prior to maturity on January 1, 2009, 2014 and 2019. We have the right to redeem the Notes, under certain circumstances, on or after July 1, 2007 and prior to January 1, 2009, and we may redeem the Notes at any time on or after January 1, 2009. Through December 31, 2007, we classified the Notes as long-term debt. However, in light of the right of holders to require us to redeem the Notes on January 1, 2009, we have reclassified the Notes as short-term debt.

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On June 25, 2007, the Board of Directors authorized a new share repurchase program of up to \$200.0 million of our outstanding shares of common stock (the 2007 Repurchase Program). This new program supersedes and replaces the \$50.0 million share repurchase program adopted in 2005. Under the 2007 Repurchase Program, the shares may be repurchased in the open market or in privately negotiated transactions. Repurchases are at our discretion based on ongoing assessments of the capital needs of the business, the market price of our common stock and general market conditions. No time limit was set for the completion of the 2007 Repurchase Program.

During the three months ended March 31, 2008, 3,911,545 shares were repurchased under the 2007 Repurchase Program. None of the repurchased shares have been retired.

We believe that existing sources of liquidity and the results of our operations will provide adequate cash to fund our

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operations, although we may seek to raise additional capital. In January 2005, we filed a registration statement to increase our available shelf registration amount and we have approximately \$82 million available for future use. In addition, we filed an acquisition shelf registration statement for up to approximately 1.5 million shares. In February 2006, we filed a shelf registration that would allow us to sell an undetermined amount of equity or debt securities in accordance with the recently approved rules applying to well known seasoned issuers. These filings were made to provide future flexibility for acquisition and financing purposes. The sale of additional equity or convertible debt securities could result in additional dilution to our stockholders. There can be no assurances that financing will be available in amounts or on terms acceptable to us, if at all.

Table of Contents**Item 3. Qualitative and Quantitative Disclosure about Market Risk****Interest Rate Risk**

Our portfolio of cash equivalents and short-term investments is maintained in a variety of securities, including government agency obligations and money market funds. Investments are classified as available-for-sale securities and carried at their market value with cumulative unrealized gains or losses recorded as a component of accumulated other comprehensive income/(loss) within stockholders' equity. At March 31, 2008, all securities held had maturities or reset dates of less than three years. A sharp rise in interest rates could have an adverse impact on the market value of certain securities in our portfolio. We do not currently hedge our interest rate exposure and do not enter into financial instruments for trading or speculative purposes or utilize derivative financial instruments.

At March 31, 2008, we had short-term debt of \$195.0 million associated with our Notes. The market value of our short-term debt will fluctuate with movements of interest rates, increasing in periods of declining rates of interest and declining in periods of increasing rates of interest.

Foreign Currency Risk

Our business has historically been transacted primarily in the U.S. dollar and, as such, has not been subject to material foreign currency exchange rate risk. However, the growth in our international operations has increased our exposure to foreign currency fluctuations as well as other risks typical of international operations, including, but not limited to, differing economic conditions, changes in political climate, differing tax structures and other regulations and restrictions. Further, we recently acquired NetGiro Systems, a payment processor based in Stockholm, Sweden that processes international transactions, and the anticipated growth of this company will increase our exposure to foreign currency fluctuations. Accordingly, our future results could be materially adversely impacted by changes in these or other factors.

Foreign exchange rate fluctuations may adversely impact our consolidated results of operations as exchange rate fluctuations on transactions denominated in currencies other than our functional currencies result in gains and losses that are reflected in our Consolidated Statement of Income. To the extent the U.S. dollar weakens against foreign currencies, the translation of these foreign currency-denominated transactions will result in increased net revenues and operating expenses. Conversely, our net revenues and operating expenses will decrease when the U.S. dollar strengthens against foreign currencies.

Transaction Exposure

The Company enters into short term foreign currency forward contracts to offset the foreign exchange gains and losses generated by the re-measurement of certain assets and liabilities recorded in non-functional currencies. Changes in the fair value of these derivatives, as well as re-measurement gains and losses, are recognized in current earnings in other expense, net.

Translation Exposure

Foreign exchange rate fluctuations may adversely impact our consolidated financial position as the assets and liabilities of our foreign operations are translated into U.S. dollars in preparing our consolidated balance sheet. These gains or losses are recognized as an adjustment to stockholders' equity through accumulated other comprehensive income/(loss) net of tax benefit or expense.

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Item 4. Controls and Procedures

- (a) We are committed to maintaining disclosure controls and procedures designed to ensure that information required to be disclosed in our periodic reports filed under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. Our management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of March 31, 2008. Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) promulgated under the Securities Exchange Act of 1934) were effective in providing reasonable assurance that material information required to be disclosed by us in this Form 10-Q was recorded, processed, summarized and reported in a timely manner.
- (b) During the quarter ended March 31, 2008, there was no change in our internal control over financial reporting that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Limitations on the Effectiveness of Controls

Our management, including the Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining an adequate system of internal control over financial reporting. This system of internal accounting controls is designed to provide reasonable assurance that assets are safeguarded, transactions are properly recorded and executed in accordance with management's authorization and financial statements are prepared in accordance with generally accepted accounting principles. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within our company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Table of Contents**PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

DDR Holdings, LLC has brought a claim against us and several other defendants regarding US Patents No. 6,629,135 and 6,993,572, which are owned by DDR Holdings. These patents claim e-commerce outsourcing systems and methods relating to the provision of outsourced e-commerce support pages having a common look and feel with a host's website. The case was filed in the U.S. District Court for the Eastern District of Texas on January 31, 2006. The complaint seeks injunctive relief, declaratory relief, damages and attorneys' fees. We have denied infringement of any valid claim of the patents-in-suit, and have asserted counter-claims which seek a judicial declaration that the patents are invalid and not infringed. In September 2006, DDR Holdings filed an application for reexamination of its patents based upon the prior art produced by us and the other defendants in the case. As part of that application, DDR Holdings asserted that this prior art raised a substantial question as to the patentability of the inventions claimed in the patents. In December 2006, the Court stayed the litigation pending a decision on the reexamination application. In February 2007, the US Patent and Trademark Office ordered reexamination of DDR's patents. We intend to vigorously defend ourselves in this matter.

NetRatings, Inc. has brought a claim against us regarding US Patents Nos. 5,675,510, 6,115,680, 6,108,637, 6,138,155 and 6,763,386, which are owned by NetRatings. These patents claim web analytic and reporting systems. The case was filed in the U.S. District Court for the District of Minnesota on October 5, 2006. The complaint seeks injunctive relief, declaratory relief, damages and attorney's fees. We have denied the allegations of infringement. Discovery in this matter is ongoing. In December 2007, the parties submitted briefs to the Court in connection with the Markman claim construction. No trial date is currently set for this case. We intend to continue our vigorous defense of this matter.

In December 2006, we announced that we had received an informal inquiry from the SEC relating to our historical stock option grant practices. We have cooperated with the SEC regarding this matter and intend to continue to do so. We are subject to legal proceedings, claims and litigation arising in the ordinary course of business. While the final outcome of these matters is currently not determinable, we believe there is no litigation pending against us that is likely to have, individually or in the aggregate, a material adverse effect on our consolidated financial position, results of operations or cash flows. Because of the uncertainty inherent in litigation, it is possible that unfavorable resolutions of these lawsuits, proceedings and claims could exceed the amount we have currently reserved for these matters. Third parties have from time-to-time claimed, and others may claim in the future, that we have infringed their intellectual property rights. We have been notified of several potential patent disputes, and expect that we will increasingly be subject to patent infringement claims as our services expand in scope and complexity. We have in the past been forced to litigate such claims. We also may become more vulnerable to third-party claims as laws, such as the Digital Millennium Copyright Act, the Lanham Act and the Communications Decency Act are interpreted by the courts and as we expand geographically into jurisdictions where the underlying laws with respect to the potential liability of online intermediaries like ourselves are either unclear or less favorable. These claims, whether meritorious or not, could be time-consuming and costly to resolve, cause service upgrade delays, require expensive changes in our methods of doing business, or could require us to enter into costly royalty or licensing agreements.

Item 1A. Risk Factors

The risks described below are not the only ones facing our company. Additional risks not presently known to us or that we currently deem immaterial also may impair our business operations. Our business financial condition or results of operations could be materially adversely affected by any of these risks and the value of our common stock could decline due to any of these risks. This quarterly report also contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including the risks faced by us described below and elsewhere in this report.

A loss of any client that accounts for a large portion of our revenue would cause our revenue to decline.

Sales of products for one software publisher client, Symantec Corporation, accounted for approximately 25.5% of our revenue during the first quarter of 2008. In addition, revenues derived from proprietary Digital River services sold to Symantec end-users and sales of Symantec products through our oneNetwork retail and affiliate channel

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together accounted for approximately 11.1% of total Digital River revenue. In addition, a limited number of other software and physical goods clients contribute a large portion of our annual revenue. Contracts with our clients are generally one or two years in length. If any one of these key contracts is not renewed or otherwise terminates, or if revenues from these clients decline for any other reason (such as competitive developments), our revenue would decline and our ability to sustain profitability would be impaired. If our contract with Symantec is not renewed or otherwise terminated, or if revenues from Symantec and Symantec-related services decline for any other reason, our revenue and our ability to sustain profitability could be materially adversely impaired. It is important to our ongoing success that we maintain our key client relationships and, at the same time, develop new client relationships.

Our future success cannot be predicted based upon our operating history.

The nature of our business and the e-commerce industry in which we operate has undergone rapid development and change. Accordingly, it is difficult to predict whether we will be successful. Thus, our chances of financial and operational success should be evaluated in light of the risks, uncertainties, expenses, delays and difficulties associated with operating a business in a relatively rapidly changing industry. If we are unable to address these issues, we may not be financially or operationally successful.

Failure to properly manage and sustain our expansion efforts could strain our management and other resources.

Through acquisitions and organic growth, we are rapidly and significantly expanding our operations, both domestically and internationally. We will continue to expand further to pursue growth of our service offerings and customer base. This expansion increases the complexity of our business and places a significant strain on our management, operations, technical performance, financial resources, and internal financial control and reporting functions, and there can be no assurance that we will be able to manage it effectively. Our personnel, systems, procedures and controls may not be adequate to effectively manage our future operations, especially as we employ personnel in multiple domestic and international locations. We may not be able to hire, train, retain and manage the personnel required to address our growth. Failure to effectively manage our growth opportunities could damage our reputation, limit our future growth, negatively affect our operating results and harm our business.

We intend to continue to expand our international operations and these efforts may not be successful in generating additional revenue.

We sell products and services to end-users outside the United States and we intend to continue expanding our international presence. In the first quarter of 2008, our e-commerce sales to international consumers represented approximately 43.2% of our total sales. Expansion into international markets, particularly the European and Asia-Pacific regions, requires significant resources that we may fail to recover by generating additional revenue. Conducting business outside of the United States is subject to risks, including:

- § Changes in regulatory requirements and tariffs;
- § Uncertainty of application of local commercial, tax, privacy and other laws and regulations;
- § Reduced protection of intellectual property rights;
- § Difficulties in physical distribution for international sales;
- § Higher incidences of credit card fraud and difficulties in accounts receivable collection;
- § The burden and cost of complying with a variety of foreign laws, rules and regulations;
- § The possibility of unionization of our workforce outside the United States, particularly in Europe;
- § Political, social and economic instability;
- §

Import and export license requirements and restrictions of the United States and every other country in which we operate; and

§ Political or economic constraints on international trade or instability.

Any of the factors described above may have a material adverse effect on our ability to increase or maintain foreign sales. These risks have grown with the acquisitions of Digital River GmbH, which has substantial operations outside the U.S. and with our expansion into the Asia-Pacific region. More recently, we acquired NetGiro Systems which is based in Stockholm, Sweden.

We may be unable to successfully and cost-effectively market, sell and distribute our services in foreign markets. This may be more difficult or take longer than anticipated especially due to international challenges, such as language barriers, currency exchange issues and the fact that the Internet infrastructure in foreign countries may be less advanced than the U.S. Internet infrastructure. If we are unable to successfully expand our international operations, or manage

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this expansion, our operating results and financial condition could be harmed. In addition, a significant portion of our cash and marketable securities are held in non-U.S. domiciled countries.

Our operating results are subject to fluctuations in demand for products and services offered by us or our clients.

Our quarterly and annual operating results are subject to fluctuations in demand for the products or services offered by us or our clients, such as anti-virus software and anti-spyware software. In particular, sales of anti-virus software represented a significant portion of our revenues in recent years, and continue to be very important to our business. Demand for anti-virus software is subject to the unpredictable introduction of significant computer viruses. To the extent that software publishers successfully introduce products or services not sold through our platform that are competitive with products and services sold by current Digital River clients (including anti-virus pro