Motorola Solutions, Inc.
Form 10-K
February 15, 2012
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
December 31, 2011 For the fiscal year ended December 31, 2011

or

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission File number 1-7221

MOTOROLA SOLUTIONS, INC.

(Exact name of registrant as specified in its charter)

DELAWARE	**36-1115800**
(State of Incorporation)	**(I.R.S. Employer Identification No.)**

1303 East Algonquin Road, Schaumburg, Illinois 60196

(Address of principal executive offices)

(847) 576-5000

(Registrant s telephone number)

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

Title of Each Class	**Name of Each Exchange on Which Registered**
Common Stock, $.01 Par Value per Share	**New York Stock Exchange**
	Chicago Stock Exchange

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

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No ¨

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes ¨ No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

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

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

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

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

The aggregate market value of voting and non-voting common equity held by non-affiliates of the registrant as of July 2, 2011 (the last business day of the Registrant s most recently completed second quarter) was approximately $16.0 billion.

The number of shares of the registrant s Common Stock, $.01 par value per share, outstanding as of January 31, 2012 was 317,969,760.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s definitive Proxy Statement to be delivered to stockholders in connection with its Annual Meeting of Stockholders to be held on April 30, 2012, are incorporated by reference into Part III.

Table of Contents

Table of Contents

	Page
PART I	**1**
Item 1. Business	1
General	1
Government Segment	1
Enterprise Segment	3
Other Information	4
Financial Information About Segments	4
Financial Information About Geographic Areas	4
Payment Terms	5
Research and Development	5
Regulatory Matters	5
Intellectual Property Matters, Patents, and Trademarks	6
Inventory, Raw Materials, and Right of Return and Seasonality	7
Environmental Quality	7
Employees	7
Available Information	7
Item 1A. Risk Factors	9
Item 1B. Unresolved Staff Comments	22
Item 2. Properties	22
Item 3. Legal Proceedings	23
Item 4. Mine Safety Disclosures	26
Executive Officers of the Registrant	27
PART II	**29**
Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	29
Item 6. Selected Financial Data	31
Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations	32
Item 7A. Quantitative and Qualitative Disclosures About Market Risk	57
Item 8. Financial Statements and Supplementary Data	59
Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	109
Item 9A. Controls and Procedures	109
Item 9B. Other Information	111
PART III	**111**
Item 10. Directors, Executive Officers and Corporate Governance	111
Item 11. Executive Compensation	111
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	111
Item 13. Certain Relationships and Related Transactions, and Director Independence	111
Item 14. Principal Accounting Fees and Services	111
PART IV	**112**
Item 15. Exhibits and Financial Statement Schedules	112
15(a)(1) Financial Statements	112
15(a)(2) Financial Statement Schedule and Independent Auditors Report	112
15(a)(3) Exhibits	112

Table of Contents

PART I

Throughout this 10-K report we incorporate by reference certain information in parts of other documents filed with the Securities and Exchange Commission (the SEC). The SEC allows us to disclose important information by referring to it in that manner. Please refer to such information.

We are making forward-looking statements in this report. In Item 1A: Risk Factors we discuss some of the risk factors that could cause actual results to differ materially from those stated in the forward-looking statements.

Motorola Solutions (which may be referred to as the Company, we, us, or our) means Motorola Solutions, Inc. or Motorola Solutions, Inc. and its subsidiaries, or one of our segments, as the context requires. MOTOROLA, MOTO, MOTOROLA SOLUTIONS and the Stylized M Logo, as well as iDEN are trademarks or registered trademarks of Motorola Trademark Holdings, LLC and are used under license.

During 2011, we reclassified the historical financial results of the following businesses as discontinued operations: (i) Motorola Mobility Holdings, Inc. (Motorola Mobility), (ii) Point-to-Point (Orthogon) and Point-to-Multipoint (Canopy) wireless broadband businesses (Wireless Broadband businesses), and (iii) the amateur, marine and airband radio businesses. Also during 2011, we completed the sale of certain assets and liabilities of the Networks business to Nokia Siemens Networks B.V. (NSN), which was reclassified to discontinued operations during 2010. The results from discontinued operations are discussed in further detail in the Discontinued Operations footnote to our financial statements included in Item 8.

Item 1: Business

General

We are a leading provider of mission-critical communication infrastructure, devices, software and services. Our communications-focused products and services help government and enterprise customers improve their operations through increased effectiveness and efficiency of their mobile workforces. Our customers benefit from our global footprint and thought leadership. We are positioned for success with sales in more than 100 countries, an industry leadership position, an unmatched portfolio of products and services and a strong patent portfolio.

We report financial results for two operating segments:

Government: The Government segment includes sales of public safety mission-critical communications systems, commercial two-way radio systems and devices, software and services.

Enterprise: The Enterprise segment includes sales of rugged and enterprise-grade mobile computers and tablets, laser/imaging/RFID-based data capture products, wireless local area network (WLAN) and integrated digital enhanced network (iDEN) infrastructure, software and services.

Motorola Solutions is a corporation organized under the laws of the State of Delaware as the successor to an Illinois corporation, Motorola, Inc., organized in 1928. The Company s principal executive offices are located at 1303 East Algonquin Road, Schaumburg, Illinois 60196.

Government segment

The Government segment designs, manufactures, sells, and provides services around voice and data communications systems, devices, security products and applications. These products and services are sold to a wide range of customers, including government, public safety and first responder agencies as well as commercial customers who operate private communications networks and manage a mobile workforce. In 2011, this segment s net sales represented approximately 65% of our consolidated net sales.

Our Industry, Products, and Services

Our government, public safety and first responder customers demand mission-critical and interoperable communications to effectively serve and protect the public. Our commercial customers demand business-critical communications to effectively run their business. Our customers are facing efficiency challenges which are driving technology transitions and equipment upgrades. Our sales growth is driven by helping our customers address their communication needs.

Table of Contents

2

We offer an extensive portfolio of network infrastructure, devices, applications and services, based on APCO 25 (Association for Public Safety Communications Officials), TETRA (terrestrial trunked radio), and DMR (digital mobile radio) standards, as well as broadband technologies (Long-Term Evolution (LTE), and WiFi). Our products and services are sold stand alone as well as part of an integrated system. In addition, we offer critical applications in the public safety command center, including voice, computer aided dispatch and multimedia/video. Our comprehensive service offering in this segment includes mobility consulting, system design and installation, network and device management and product support.

Our Strategy

Our strategy in the Government segment is to partner with our customers to enable them to deliver reliable services efficiently through innovative products and best-in-class services. Thought leadership and innovation are core to the effective partnership with our customers. We deliver innovation by: (i) developing next-generation public safety solutions including devices, Public Safety LTE systems, and critical command center applications; (ii) leading the ongoing migration to digital products; (iii) managing the potential public/private convergence of 700MHz public safety systems in the U.S. and digital dividend spectrum worldwide; (iv) continuing to be an industry leader in APCO 25 and TETRA standards-based voice and data communication systems around the world; and (v) enhancing our services offering through network and application integration. We continue to actively manage our product and services portfolio, investing to expand into attractive and complementary segments to strengthen our customer relationships.

Our Customers

We address the communication needs of government agencies, state and local public safety and first responder agencies, and commercial and industrial customers. Our largest customer is the U.S. Government (through its various branches and agencies, including the armed services), which represented approximately 11% of this segment s net sales, and 7% of the Company s net sales in 2011. The loss of this customer could have a material adverse effect on our revenue and earnings over several quarters, because some of our contracts with the U.S. Government are long-term. All contracts with the U.S. Government are subject to cancellation at the convenience of the U.S. Government. Net sales to customers in North America represented 63% of this segment s net sales in 2011.

We believe that there remain a large number of government and commercial customers globally who have yet to experience the benefits of converged wireless communications, mobility and/or effectiveness and efficiencies realized through applications enabled by mobile broadband. In addition to serving our existing customers, we believe that we have opportunities to pursue profitable growth by extending our reach across new segments and geographies.

Our sales model includes both direct-sales by our in-house sales force, which tends to focus on our largest accounts, and sales through our channel partner program. Our channel partners include distributors, value added resellers and independent software vendors. Resellers and distributors each have their own sales organizations that complement and extend the reach of our sales force. With deep expertise about specific customers operations, resellers are very effective in promoting sales of our product portfolio. The independent software vendors in our channel partner program offer customized applications that meet specific needs in each segment we serve. We believe this dual sales approach allows us to meet customer needs effectively, build strong, lasting relationships and broaden our penetration across segments and geographies.

Our Competition

The markets in which we operate are highly competitive. Continued evolution in our industry and technology shifts are creating opportunities for established and new competitors. Key competitive factors include product performance; product features; product quality, availability and warranty; price; availability of vendor financing; quality and availability of service; company reputation and financial strength, including investment grade rating; partner community; and relationship with key customers. Our strong relationships with customers and partners, technology leadership, breadth of portfolio, product performance and support position us well for success.

We experience widespread competition from a growing number of existing and new competitors, including: large system integrators and manufacturers of private and public wireless network equipment and devices. Major competitors include: Cassidian/EADS, Harris, Hytera,

Kenwood, Sepura and Tait.

Table of Contents

Large system integrators are seeking to move further into the state and local government market segment. We and our competitors may serve as subcontractors to large system integrators and are selected based on a number of competitive factors and customer requirements. Where favorable, we may partner with large system integrators or other third parties to make available our portfolio of advanced mission-critical network infrastructure, devices, applications and services.

Several other competitive factors may have an impact on our Government segment, including: the consolidation among telecommunications equipment providers; evolving developments in the 700 MHz band; increasing encroachment by broadband and IP solution providers; and new low-tier vendors. As demand for fully integrated voice, data, and broadband systems continue, we may face additional competition from public telecommunications carriers and telecommunications equipment providers.

Backlog

Our backlog position was approximately $2.0 billion as of December 31, 2011 and 2010. The 2011 order backlog is believed to be generally firm and only includes received product and system installation labor orders from customers. Service orders such as maintenance and extended warranty contracts are excluded from backlog. Approximately 73% of that amount is expected to be recognized as revenue during 2012. The forward-looking estimate of the firmness of such orders is subject to future events that may cause the amount recognized to change.

Enterprise segment

The Enterprise segment designs, manufactures, sells and provides services around WLAN infrastructure, rugged and enterprise-grade advanced data capture and mobile computing devices, security products and applications. These are sold to a wide range of enterprise customers, including those in retail and hospitality, transportation and logistics, manufacturing, energy and utilities, education and healthcare. In 2011, this segment s net sales represented approximately 35% of our consolidated net sales.

Our Industry, Products and Services

Our enterprise customers are continuously looking to improve their operational efficiency as well as to increase their sales through superior customer service. In 2011, we saw an increase in technology spend by our customers, driven primarily by retail and transportation and logistics customers. We believe that long-term growth opportunities exist within the Enterprise segment, as the global workforce continues to become more mobile and enterprise customers continue to focus on improving their workforce efficiency and productivity. The segment also provides products and systems for the advanced exchange of information at the point of business activity. Our sales growth is driven by helping our customers to mobilize their workforce and improve customer service.

We offer an extensive portfolio of devices, infrastructure, applications and services. These include rugged and enterprise-grade mobile computers and tablets, laser/imager/RFID based data capture devices and kiosks, WLAN switches/controllers and access points, network and device management software, network and device security software, voice-based devices and software, and systems based iDEN technology. Our service offerings in this segment have been primarily related to product support. However, we are expanding our services offerings to also include network integration and network and mobile device management, as well as mobility consulting.

Our Strategy

Our strategy in the Enterprise segment is to deliver the next generation of enterprise mobility to empower the mobile worker, enable real-time asset visibility and engage the smart consumer. We have identified key areas of innovation to enable successful implementation of this strategy. These include advanced devices, enhanced information capture and analysis, adaptive networking solutions, integrated voice and data communications, advanced applications and services. We are expanding our devices portfolio to address the needs of an increasingly mobile workforce. Our products and services are designed to improve our customers operations through real-time asset visibility and integrated/adaptive communications networking solutions. Our portfolio of infrastructure and device products is complemented by customized applications and services, which are designed to help our customers achieve their specific business objectives. We are seeking to further expand our services offerings over the lifecycle of these products.

Table of Contents

Our Customers

We address the communication and data capture needs of enterprise customers primarily in retail and hospitality, transportation and logistics, manufacturing, energy and utilities, education and healthcare. These customers operate a large and diverse mobile workforce and are continuously focused on improving their operations through greater employee efficiency, greater asset visibility and superior customer service. Our product and services portfolio delivers attractive return on technology investment for our customers. In addition to serving our existing customers, we believe that we have opportunities to pursue profitable growth by extending our reach across new segments and geographies.

Our sales model includes both direct-sales by our in-house sales force and sales through our channel partner program. Our channel partners include distributors, value added resellers and independent software vendors. Resellers and distributors each have their own sales organizations that complement and extend the reach of our sales force. With deep expertise about specific customers operations, resellers are very effective in promoting sales of our product portfolio. The independent software vendors in our channel partner program offer customized applications, in addition to those that we offer, that meet specific needs in each market we serve. Our Enterprise segment utilizes our channel partners extensively, as the products of this segment generally support a broad range of applications. We believe this dual sales approach allows us to meet customer needs effectively, build strong, lasting relationships and broaden our penetration across segments and geographies.

Our Competition

The segments in which we operate are highly competitive. Continued evolution in our industry and technology shifts are creating opportunities for established and new competitors. Key competitive factors include product performance; product features; product quality, availability and warranty; price; availability of vendor financing; quality and availability of service; company reputation and financial strength; partner community; and relationship with key customers. Our strong relationships with customers and partners, technology leadership, breadth of portfolio, product performance and support position us well to provide customized solutions for our customers that drive our success.

We experience widespread competition from a growing number of existing and new competitors, including present manufacturers of laser/imager/RFID based data capture devices, optical instruments, notebook computers and tablets, smart phones, cordless phones, and cellular/WLAN/wired infrastructure equipment. Major competitors include: Apple, Aruba, Bluebird, Cisco, Datalogic, Honeywell, Hewlett Packard, Intermec, Psion, Panasonic, and Samsung.

Backlog

Our backlog position at December 31, 2011, was approximately $480 million, compared to $570 million at December 31, 2010. Our order backlog is believed to be generally firm and only includes received product and system installation labor orders from customers. Service orders such as maintenance and extended warranty contracts are excluded from backlog. Approximately 97% of that amount is expected to be recognized as revenue during 2012. The forward-looking estimate of the firmness of such orders is subject to future events that may cause the amount recognized to change.

Other Information

Financial Information About Segments

The response to this section of Item 1 incorporates by reference Note 12, Information by Segment and Geographic Region, of Part II, Item 8: Financial Statements and Supplementary Data of this document.

Financial Information About Geographic Areas

The response to this section of Item 1 incorporates by reference Note 11, Commitments and Contingencies and Note 12, Information by Segment and Geographic Region of Part II, Item 8: Financial Statements and Supplementary Data of this document, the Results of

Operations 2011 Compared to 2010 and Results of

Table of Contents

Operations 2010 Compared to 2009 sections of Part II, Item 7: Management s Discussion and Analysis of Financial Condition and Results of Operations and Item 1A: Risk Factors of this document.

Payment Terms

Payment terms vary worldwide, depending on the arrangement. Generally, contract payment terms range from 30 to 45 days from the invoice date within North America and are typically limited to 90 days in regions outside of North America. A portion of the contracts with our government and public safety customers include implementation milestones, such as delivery, installation and system acceptance, which generally take 30 to 180 days to complete. Invoicing the customer is dependent on completion of the milestone.

We generally do not grant extended payment terms. As required for competitive reasons, we may provide long-term financing in connection with system purchases. Financing may cover all or a portion of the purchase price.

Research and Development

We participate in very competitive industries with constant changes in technology. Throughout our history, we have relied, and continue to rely, primarily on our research and development (R&D) programs for the development of new products, and on our production engineering capabilities for the improvement of existing products. Management believes, looking forward, that our commitment to R&D programs are necessary to allow us to remain competitive.

R&D expenditures relating to new product development or product improvement were $1.0 billion in 2011, 2010 and 2009. We continue to believe that a strong commitment to R&D is required to drive long-term growth. As of December 31, 2011, approximately 7,000 professional employees were engaged in such R&D activities for us.

Regulatory Matters

The use of wireless voice, data and video communications systems requires radio spectrum, which is regulated by governmental agencies throughout the world. In the U.S., the Federal Communications Commission (FCC) and the National Telecommunications and Information Administration (NTIA) regulate spectrum use by non-federal entities and federal entities, respectively. Similarly, countries around the world have one or more regulatory bodies that define and implement the rules for use of the radio spectrum, pursuant to their respective national laws and international coordination under the International Telecommunications Union (ITU). Consequently, our results could be positively or negatively affected by the rules and regulations adopted by the FCC, NTIA or regulatory agencies in other countries from time to time. The availability of additional radio spectrum may provide new business opportunities and the loss of available radio spectrum may result in the loss of business opportunities.

We manufacture and market products in spectrum bands already made available by regulatory bodies. These include voice and data infrastructure, mobile radios and portable or handheld devices. Our products operate both on licensed and unlicensed spectrum.

As television transmission and reception technology transitions from analog to more efficient digital modes, various countries around the world are examining, and in some cases already pursuing, the redevelopment of portions of the television spectrum. In the U.S., pursuant to federal legislation, analog television stations ceased operation in the broadcast television spectrum on June 12, 2009. As a result of this transition, 108 MHz of spectrum historically used for broadcast television, now known as the 700MHz band, is being redeveloped and deployed for new uses (the so-called digital dividend spectrum), including broadband and narrowband wireless communications. Now that the 700 MHz band spectrum is open nationwide, FCC records indicate that so far over 135 public safety agencies throughout over 25 states have been deploying narrowband operations at 700 MHz and others are in the planning stages. Under rules adopted by the FCC, 24 MHz of the 700 MHz band already allocated by the FCC will support new public safety narrowband and broadband communications systems. The public safety community is also seeking legislation from Congress to obtain an additional 10 MHz of dedicated spectrum in the 700 MHz band (D-block). If successful, the legislation would double the broadband 700 MHz band spectrum dedicated for public safety.

Table of Contents

6

The FCC is also making provisions for a 700 MHz band nationwide public safety broadband network that may be built over the next 10-15 years. In May 2010, the FCC issued 21 conditional waiver grants to public safety agencies around the country to deploy 700 MHz broadband systems. Thirty-three additional waiver petitions are pending FCC decisions as of December 2011. Several of the broadband waiver grantees also benefit from federal Broadband Technology Opportunity Policy (BTOP) Grant Funds issued by the NTIA during 2010. In 2010, we were awarded a $50.6 million BTOP grant to deploy a broadband system in the greater San Francisco Bay area. We are also working with a number of customers in other areas who received FCC conditional waivers to use the 700 MHz broadband spectrum. For example, during 2011, we received an award to implement a 700 MHz (LTE) broadband system for the Mississippi Wireless Communication Commission. Public safety organizations and the FCC have endorsed the use of LTE technology, a technology in which we are investing, for this broadband network.

In November 2010, Canada also released a consultation requesting input on making broadband spectrum available for public safety use in the 700 MHz band. All full power TV broadcasters in Canada vacated the 700 MHz band by August 31, 2011. During 2011, the Radio Advisory Board of Canada (RABC), an influential industry association, recommended that Canadian decision-makers harmonize the band with that in the U.S. Further decisions regarding broadband use in Canada are expected to be released during 2012.

Internationally, the ITU World Radio Conference (WRC) is being held in Geneva during the first quarter of 2012. During this session, leaders from United Nation member countries will consider a number of initiatives, including whether to allocate additional spectrum for commercial broadband use as well as whether to allocate spectrum dedicated for public safety broadband. If the WRC agrees to consider spectrum for public safety broadband, studies would follow that would assess whether and how much spectrum is needed and recommendations for where in the spectrum range the spectrum should be allocated (taking into account regional and global harmonization to the extent practicable). The result could be future allocations for dedicated broadband spectrum for public safety which will provide opportunities for us in the future. In addition, certain countries already have spectrum landscapes that would permit country administrations to allocate public safety spectrum today. A WRC initiative can spur individual countries to act sooner, which may also create opportunities for our broadband solutions in the nearer term.

Some of our operations use substances regulated under various federal, state, local and international laws governing the environment and worker health and safety, including those governing the discharge of pollutants into the ground, air and water, the management and disposal of hazardous substances and wastes and the cleanup of contaminated sites. Certain of our products are subject to various federal, state, local and international laws governing chemical substances in electronic products.

Intellectual Property Matters

Patent protection is extremely important to our operations. We have an extensive U.S. and international portfolio of patents relating to our products, systems, technologies and manufacturing processes, including research developments in scanning, information collection, mission-critical two-way radio communication, network communications and network management. We have also filed additional patent applications in the U.S. Patent and Trademark Office, as well as in foreign patent offices.

We license some of our patents to third parties, but this revenue is not significant. We are also licensed to use certain patents owned by others. In particular, Motorola Solutions has a royalty free license under all of the patents and patent applications assigned to Motorola Mobility at the time of the separation of the two businesses. Royalty and licensing costs vary from year to year and are subject to the terms of the agreements and sales volumes of our products subject to licenses.

We actively participate in the development of open standards for interoperable, mission-critical digital two-way radio systems. We have published our technology and licensed patents to signatories of the industry s two primary memorandums of understanding defined by the Telecommunications Industry Association (TIA), Project 25, European Telecommunications Standards Institute (ETSI), and TETRA.

Notwithstanding the transfer of patents to Motorola Mobility, the expiration of certain patents and the resulting potential for increased competition for some of our products in the future, we believe that our remaining

patent portfolio will continue to provide us with a competitive advantage in our core product areas. Furthermore, we believe we are not dependent upon a single patent or a few patents. Our success depends more upon our proprietary know-how, innovative skills, technical competence and marketing abilities. In addition, because of changing technology, our present intention is not to rely primarily on patents or other intellectual property rights to protect or establish our market position. However, we plan to continue to litigate against competitors to enforce our intellectual property rights in certain technologies when attempts to negotiate mutually agreeable licenses are not successful.

Patents and Trademarks

As of December 31, 2011, we owned approximately 6,013 patents in the U.S. and in foreign countries. As of December 31, 2011, we and our wholly owned subsidiaries had approximately 2,700 U.S. and foreign patent applications pending. These foreign patents and patent applications are mostly counterparts of our U.S. patents. During 2011, we and our wholly owned subsidiaries were granted 237 U.S. patents and 314 patents in other countries.

Inventory, Raw Materials, Right of Return and Seasonality

Our practice is to carry reasonable amounts of inventory to meet customers delivery requirements in a manner consistent with industry standards. We provide custom products which require the stocking of inventories and large varieties of piece parts and replacement parts in order to meet delivery and warranty requirements. To the extent our suppliers product life cycles are shorter than ours, stocking of lifetime-buy inventories is required to meet long-term warranty and contractual requirements. In addition, replacement parts are stocked for delivery on customer demand within a short delivery cycle. At December 31, 2011, our inventory balance decreased slightly compared to December 31, 2010.

Availability of materials and components required by the Company is generally dependable; however, fluctuations in supply and market demand have caused and could cause selective shortages and affect results. We currently procure certain materials and components from single-source vendors. A material disruption from a single-source vendor may have a material adverse impact on our results of operations. If certain single-source suppliers were to become capacity constrained or insolvent, it could result in a reduction or interruption in supplies or an increase in the price of supplies and adversely impact our financial results.

Natural gas, electricity and, to a lesser extent, oil are the primary sources of energy for our manufacturing operations. Each of these resources is currently in adequate supply for our operations. In addition, the cost to operate our facilities and freight costs are dependent on world oil prices. Labor is generally available in reasonable proximity to our manufacturing facilities. Difficulties in obtaining any of the aforementioned resources or a significant cost increase could affect our financial results.

Generally, our customer contracts do not include a right of return, other than for standard warranty provisions; however, certain distributor partners within the commercial enterprise markets do maintain limited stock rotation rights. Due to buying patterns in the markets we serve, sales tend to be somewhat higher in the fourth quarter.

Environmental Quality

During 2011, compliance with federal, state and local laws regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, did not have a material effect on our capital expenditures, earnings or the competitive position of the Company.

Employees

At December 31, 2011, we and our subsidiaries had approximately 23,000 employees, compared to 51,000 employees at December 31, 2010. Approximately 19,000 employees transferred as part of the distribution of Motorola Mobility on January 4, 2011, and approximately 7,000 employees transferred with the sale of certain assets and liabilities of the Networks business to NSN.

Available Information

We make available free of charge through our website, *www.motorolasolutions.com/investor*, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements, other

Table of Contents

8

reports filed under the Securities Exchange Act of 1934 (Exchange Act) and all amendments to those reports simultaneously or as soon as reasonably practicable after such material is electronically filed with, or furnished to, the Securities and Exchange Commission (SEC). Our reports are also available free of charge on the SEC s website, *www.sec.gov.* Also available free of charge on our website are the following corporate governance documents:

- Motorola Solutions, Inc. Restated Certificate of Incorporation
- Motorola Solutions, Inc. Amended and Restated Bylaws
- Motorola Solutions, Inc. Board Governance Guidelines
- Motorola Solutions, Inc. Director Independence Guidelines
- Principles of Conduct for Members of the Motorola Solutions, Inc. Board of Directors
- Motorola Solutions Code of Business Conduct, which is applicable to all Motorola Solutions employees, including the principal executive officers, the principal financial officer and the controller (principal accounting officer)
- Audit and Legal Committee Charter
- Compensation and Leadership Committee Charter
- Governance and Nominating Committee Charter

All of our reports and corporate governance documents may also be obtained without charge by contacting Investor Relations, Motorola Solutions, Inc., Corporate Offices, 1303 East Algonquin Road, Schaumburg, Illinois 60196, E-mail: *investors@motorolasolutions.com*. Our Annual Report on Form 10-K and Definitive Proxy Statement may also be requested in hardcopy by clicking on Printed Materials at *www.investor.motorolasolutions.com*. Our Internet website and the information contained therein or incorporated therein are not intended to be incorporated into this Annual Report on Form 10-K.

Table of Contents

9

Item 1A: Risk Factors

We wish to caution the reader that the following important risk factors, and those risk factors described elsewhere in this report or in our other Securities and Exchange Commission filings, could cause our actual results to differ materially from those stated in forward-looking statements contained in this document and elsewhere. These risks are not presented in order of importance or probability of occurrence.

The uncertainty of current economic and political conditions makes budgeting and forecasting very difficult and may reduce demand for our products.

Current conditions in the domestic and world economies remain uncertain. This is particularly true of U.S. government customers budgetary conditions. As a result of global economic conditions, U.S. and European unemployment levels, the ongoing recession in Europe and ongoing political conflicts in the Middle East and elsewhere have created many economic and political uncertainties that have impacted worldwide markets. As a result, it is difficult to estimate changes in various parts of the U.S. and world economy, including the markets in which we participate. Components of our budgeting and forecasting are dependent upon estimates of demand for our products, the prevailing economic uncertainties render estimates of future income and expenditures difficult.

We have sizeable operations in Europe, which have been and will be impacted by the ongoing financial situation in Europe and the weakening Euro. We have engineering resources in Israel that could be disrupted as a result of hostilities in the region. We also sell our products and services throughout the Middle East and demand for our products and services could be negatively impacted by political conflicts and hostilities in this region. The potential for future unrest, terrorist attacks, increased global conflicts and the escalation of existing conflicts has created worldwide uncertainties that have negatively impacted, and may continue to negatively impact, demand for certain of our products.

We continue to face a number of risks related to current global economic conditions, including adverse credit conditions, low economic growth, risk of sovereign defaults and high levels of unemployment.

Global economic conditions continue to be challenging for government and enterprise communications markets, as many economies and financial markets remain in a recession resulting from a number of factors, including adverse credit conditions, low economic growth rates, risk of sovereign defaults, particularly in certain European countries, continuing high rates of unemployment, reduced corporate capital spending and other factors. Economic growth in the U.S. and many other countries has remained low and the length of time these adverse economic conditions may persist are unknown. These global economic conditions have impacted and could continue to impact our business in a number of ways, including:

Potential Deferment or Cancellation of Purchases and Orders by Customers: Uncertainty about current and future global economic conditions may cause, and in some cases has caused businesses and governments to defer or cancel purchases in response to tighter credit and decreased cash availability and declining consumer confidence. If future demand for our products declines due to global economic conditions, it will negatively impact our financial results.

Customers Inability to Obtain Financing to Make Purchases from Motorola Solutions and/or Maintain Their Business: Some of our customers require substantial financing, including public financing or government grants, in order to fund their operations and make purchases from us. The inability of these customers to obtain sufficient credit or other funds to finance purchases of our products and/or meet their payment obligations to us could have, and in some cases has had, a negative impact on our financial results. In addition, if global economic conditions result in insolvencies for our customers, it will negatively impact our financial results.

Requests by Customers for Vendor Financing by Motorola Solutions: Certain of our customers, particularly, but not limited to, those who purchase large infrastructure systems, request that their suppliers provide financing in connection with equipment purchases or the provision of managed services. In response to reduced tax revenue at the state and local government level and ongoing tightening of credit for certain customers, these types of requests have increased in volume and scope. Motorola Solutions, particularly in its Government and Public Safety business, but also in connection with its Global Services offering, has continued to provide customer financing in light of these requests. A continuation of the credit market dislocation could force us to

Table of Contents

10

choose between further increasing our level of vendor financing or potentially losing sales to these customers, as some of our competitors, particularly in Asia, have been more willing to provide vendor financing. We also retain exposure to the credit quality of our customers who we finance.

Negative Impact from Increased Financial Pressures on Third-Party Dealers, Distributors and Retailers: We make sales in certain regions through third-party dealers, distributors and retailers. Although many of these third parties have significant operations and maintain access to available credit, others are smaller and more likely to be impacted by the significant decrease in available credit that resulted from the financial crisis that continues today. If credit pressures or other financial difficulties result in insolvency for important third parties and we are unable to successfully transition end-customers to purchase our products from other third parties or from us directly, it may cause, and in some cases has caused, a negative impact on our financial results.

Negative Impact from Increased Financial Pressures on Key Suppliers: Our ability to meet customers demands depends, in part, on our ability to obtain timely and adequate delivery of quality materials, parts and components from our suppliers. Certain of our components are available only from a single source or limited sources. If certain single-source or limited-source suppliers were to become capacity constrained or insolvent, it could result in a reduction or interruption in supplies or an increase in the price of supplies and negatively impact our financial results. In addition, credit constraints at single-source suppliers have resulted in accelerated payment of accounts payable by us, impacting our cash flow. If this trend continues, it will continue to negatively impact our cash flow.

Increased Risk of Financial Counterparty Failures Could Negatively Impact our Financial Position: We use derivative financial instruments to reduce our overall exposure to the effects of currency fluctuations on cash flows. We are exposed to credit loss in the event of nonperformance by the counterparties to these derivative financial instruments. Although the contracts are distributed among several leading financial institutions, all of whom presently have investment grade credit ratings, the default by one or more counterparty could have a material adverse impact on our financial statements.

Returns on Pension and Retirement Plan Assets and Interest Rate Changes Could Affect Our Earnings and Cash Flow in Future Periods: We have large underfunded pension obligations, in part resulting from the fact that we typically retain all of the U.S. pension liabilities and the majority of our non-U.S. pension liabilities following our divestitures, including the distribution of Motorola Mobility. The funding position of our pension plans is affected by the performance of the financial markets, particularly the equity and debt markets, and the interest rates used to calculate our pension obligations for funding and expense purposes. Annual pension contributions are determined by government regulations and calculated based upon our pension funding status, interest rates, and other factors. If the financial markets perform poorly, we could be and have been required to make additional large contributions. The equity markets can be volatile, and therefore our estimate of future contribution requirements can change dramatically in relatively short periods of time. Similarly, changes in interest rates can affect our contribution requirements. In a low interest rate environment like the one we are in, the likelihood of higher contributions in the future increases.

We have direct and indirect exposure to European sovereign and non-sovereign debt, European markets in terms of our revenues and cash flows and to fluctuations in the Euro.

We view our exposures to the Euro as follows as of December 31, 2011:

- Our cash and cash equivalents include approximately $300 million of Euro denominated currency
- Our accounts receivables balance includes approximately $230 million of Euro denominated receivables
- We estimate that approximately 10% of our total annual estimated 2012 sales are Euro denominated

- Company-sponsored defined benefit plans have no material exposure to Euro sovereign debt, approximately $50 million exposure to Euro corporate bonds, and approximately $220 million to Euro equity investments

A significant devaluation of, or movement away from, the use of the Euro could have a material adverse effect on our financial condition and results of operations.

Our success depends in part on our timely introduction of new products and technologies and our results can be impacted by the effectiveness of our significant investments in new products and technologies.

The markets for our products are characterized by rapidly changing technologies and evolving industry standards. We face intense competition in these markets and new products are expensive to develop and bring to market. Our success depends, in substantial part, on the timely and successful introduction of new products and upgrades of current products to comply with emerging industry standards and to address competing technological and product developments carried out by our competitors. The research and development of new, technologically-advanced products is a complex and uncertain process requiring high levels of innovation and investment, as well as the accurate anticipation of technology and market trends. Many of our products and systems are complex and we may experience delays in completing development and introducing new products or technologies in the future. We may focus our resources on technologies that do not become widely accepted or are not commercially viable or involve compliance obligations with additional areas of regulatory requirements. In addition, our products may contain defects or errors that are detected only after deployment. If our products are not competitive or do not work properly, our business will suffer.

Our results are subject to risks related to our significant investment in developing and introducing new products, such as integrated digital radios and integrated public safety systems. These risks include among others: (i) difficulties and delays in the development, production, testing and marketing of products; (ii) customer acceptance of products; (iii) the development of, approval of, and compliance with industry standards and regulatory requirements; (iv) the significant amount of resources we must devote to the development of new technologies; and (v) the ability to differentiate our products and compete with other companies in the same markets.

We are exposed to risks under large multi-year system and managed services contracts that may negatively impact our business.

We enter into large multi-year system contracts with large municipal, state, nation-wide government and enterprise customers. This exposes us to risks, including among others: (i) the technological risks of such contracts, especially when the contracts involve new technology, and (ii) financial risks under these contracts, including the estimates inherent in projecting costs associated with large contracts and the related impact on operating results. We are also facing increasing competition from traditional system integrators and the defense industry as system contracts become larger and more complicated.

Political developments also can impact the nature and timing of large government contracts. In addition, multi-year awards from governmental customers may often only receive partial funding initially and may typically be cancellable on short notice with limited penalties. The termination of funding for a government program would result in a loss of anticipated future revenue attributable to that program, which could have an adverse impact on our profitability.

In addition, we are increasingly providing managed services to our customers, particularly as we expand our Global Services organization, which requires that we partner with other systems and services providers, often on multi-year projects, to design, construct, manage and operate a public-safety system or other commercial system. From time to time such projects may require that we form a joint venture with our partners. Such arrangements may require us to assume the risk and agree to specific performance metrics that meet the customer s requirement for network availability, reliability, maintenance and support. In certain cases, if these performance metrics are not met we may not be paid. Depending on the nature of such projects, which are referred to as build-own-operate (BOO) and in some cases maintain (BOOM) or transfer (BOOT), we may be unable to recognize revenue from the sale of equipment for a period of time, which may be several years. Such BOO, BOOM and BOOT arrangements shift risk to us and may result in an adverse impact on our profitability if we are unable to meet the requirements of such contracts.

The expansion of our business into managed services creates new and increased areas of risk that we have not been exposed to in the past and that we may not be able to properly assess or mitigate against.

In July 2011, we announced the formation of our Global Services organization and we plan to expand our business by offering additional and expanded managed services for existing and new types of customers, such as designing, building and managing the network for emergency service organizations or enterprise customers. The

Table of Contents

offering of managed services involves the integration of multiple services, multiple vendors and multiple technologies. Such expansion will bring us into contact with new regulatory requirements and restrictions with which we will have to comply. This may increase the costs and delay or limit the range of new services which we will be able to offer.

The managed services business is one characterized by large subcontracting arrangements and we may not be able to obtain adequate indemnities or other protections from our subcontractors to adequately mitigate our risk to our customers.

We do not currently carry professional liability insurance, as such insurance is expensive to obtain for the amount of coverage typically requested by certain customers and we are therefore self insured for potential claims resulting from the managed services we provide.

A portion of our business is dependent upon U.S. Government contracts and grants, which are highly regulated and subject to oversight audits by U.S. Government representatives and subject to cancellations. Such audits could result in adverse findings and negatively impact our business.

Our government business is subject to specific procurement regulations with numerous compliance requirements. These requirements, although customary in U.S. Government contracting, increase our performance and compliance costs. These costs may increase in the future, thereby reducing our margins, which could have an adverse effect on our financial condition. Failure to comply with these regulations could lead to suspension or debarment from U.S. Government contracting or subcontracting for a period of time, and the inability to receive future grants. Among the causes for debarment are violations of various laws, including those related to procurement integrity, export control, U.S. Government security regulations, employment practices, protection of the environment, accuracy of records, proper recording of costs, foreign corruption and the False Claims Act.

Generally, U.S. Government contracts and grants are subject to oversight audits by U.S. Government representatives. Such audits could result in adjustments to our contracts or grants. Any costs found to be improperly allocated to a specific contract or grant may not be allowed, and such costs already reimbursed may have to be refunded. Future audits and adjustments, if required, may materially reduce our revenues or profits upon completion and final negotiation of audits. Negative audit findings could also result in investigations, termination of a contract or grant, forfeiture of profits or reimbursements, suspension of payments, fines and suspension or prohibition from doing business with the U.S. Government. All contracts with the U.S. Government are subject to cancellation at the convenience of the U.S. Government.

In addition, contacts with government officials and participation in political activities are areas that are tightly controlled by federal, state and local laws. Failure to comply with these laws could cost us opportunities to seek certain government sales opportunities or even result in fines, prosecution, or debarment.

We derive a portion of our revenue from government customers who award business through competitive bidding which can involve significant upfront costs and risks. This effort may not result in awards of business or we may fail to accurately estimate the costs to fulfill contracts awarded to us, which could have adverse consequences on our future profitability.

Many government customers, including most U.S. government customers, award business through a competitive bidding process, which results in greater competition and increased pricing pressure. The competitive bidding process involves significant cost and managerial time to prepare bids for contracts that may not be awarded to us. Even if we are awarded contracts, we may fail to accurately estimate the resources and costs required to fulfill a contract, which could negatively impact the profitability of any contract award to us. In addition, following a contract award, we have experienced and may continue to experience significant expense or delay, contract modification or contract rescission as a result of customer delay or our competitors protesting or challenging contracts awarded to us in competitive bidding.

Government regulation of radio frequencies may limit the growth of public safety broadband systems or reduce barriers to entry for new competitors.

Radio frequencies are required to provide wireless services. The allocation of frequencies is regulated in the U.S. and other countries and limited spectrum space is allocated to wireless services and specifically to public safety users. The growth of public safety broadband communications systems may be affected: (i)&nb J. Patrick Tinley......... - $ - 36,870 119,350 $ 58,005 $ 809,345 Robert B. Webster......... 3,750 18,900 5,300 83,200 1,760 580,490 Rick Marquardt............ - - 2,500 17,500 23,650 139,150 Eric W. Musser............ - - 11,300 23,700 51,797 164,352 Gary Nowacki............. 1,250 14,725 5,125 16,375 26,697 144,247 (1) Based upon the fair market value of one share of Ross' common stock on the date the option was exercised, less the exercise price per share multiplied by the number of shares received upon exercise of the option. (2) Value is based on the difference between the option exercise price and the fair market value at June 30, 2003 ($14.08 per share) multiplied by the number of shares underlying the option. 28 ROSS SYSTEMS, INC AND SUBSIDIARIES ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT The following table sets forth the beneficial ownership of Ross common stock as of September 24, 2003 by (a) each director, (b) each of the executive officers identified in the Summary Compensation Table, (c) all directors and executive officers as a group and (d) each person known by Ross to beneficially own more than 5% of any class of Ross' voting securities. Under the rules of the Securities and Exchange Commission, or Commission, beneficial ownership includes any shares as to which the individual has sole or shared voting power or investment power and also any shares which the individual has the right to acquire within 60 days of September 24, 2003 through the exercise of any stock option. COMMON STOCK SERIES A PREFERRED STOCK ---------------------------------- ------------------------- NUMBER OF NUMBER OF PERCENTAGE NUMBER OF PERCENTAGE NAME SHARES(1) OPTIONS(2) OF CLASS SHARES OF CLASS --- --------- ---------- ---------- --------- ---------- Alvin Johns 51,754 6,476 1.9% - - Robert B. Webster ** 52,401 133,500 6.0% - - J. Patrick Tinley ** 31,041 210,215 7.7% - - Oscar Pierre Prats 3,625 5,175 * - - Gary Nowacki 14,684 9,875 * - - Eric W. Musser 6,346 15,950 * - - Verome M. Johnston 3,986 10,500 * - - Bruce J. Ryan - 9,200 * - - Frank M. Dickerson - 13,000 * - - J. William Goodhew, III - 9,200 * - - Rick Marquardt 123 7,500 * - - Richard Thomas 1,448 2,375 * - - All officers and directors as a group (12 165,408 432,966 19.2% - - persons) Benjamin W. Griffith III 152,500 - 20.5% (3) 500,000 (4) 100% *Less than 1%. ** Number of options exercisable within 60 days includes accelerated vesting of certain options due to a change of control pursuant to the proposed merger. (1) The table is based upon information supplied by executive officers, directors and principal stockholders. Unless otherwise indicated, each of the stockholders named in the table has sole voting investment and/or dispositive power with respect to all shares of common stock shown as beneficially owned, subject to community property laws where applicable and to the information contained in the footnotes to this table (2) These are options which are exercisable for common stock within 60 days of September 24, 2003. (3) Mr. Griffith owns 4.9% of the total number of shares of outstanding common stock. (4) The 7.5% Series A Convertible Preferred Stock has one vote per share and votes with the common stock on most matters. These shares may be converted at the rate of one preferred share for one common stock share. These shares must be converted by June 29, 2006. EQUITY COMPENSATION PLAN INFORMATION The following table provides information as of June 30, 2003 about the common stock of Ross that may be issued upon the exercise of options, warrants and rights under all of Ross' existing equity compensation plans, including the Ross Systems Inc. 1988 Incentive Stock Plan, the 1998 Stock Option Plan and the 1991 Employee Stock Purchase Plan, each as amended. 29 ROSS SYSTEMS, INC AND SUBSIDIARIES NUMBER OF SECURITIES REMAINING AVAILABLE FOR FUTURE ISSUANCE UNDER NUMBER OF SECURITIES TO WEIGHTED-AVERAGE (1) EQUITY COMPENSATION PLANS BE ISSUED UPON EXERCISE EXERCISE PRICE OF (EXCLUDING SECURITIES OF OUTSTANDING OPTIONS, OUTSTANDING OPTIONS, REFLECTED IN THE FIRST WARRANTS AND RIGHTS WARRANT AND RIGHTS COLUMN) PLAN CATEGORY (#) ($)(1) (#) --------------------- ----------------------- -------------------- ------------------------- Equity compensation plans approved by security holders 576,063 $9.62 266,960 Equity compensation - - plans not approved by - security holders Total 576,063 $9.62 266,960 (1) Pursuant to a resolution passed by Ross stockholders at the annual meeting held November 15, 2001, the number of shares available for issuance under the 1991 Employee Stock Purchase Plan is automatically increased annually by the lesser of 35,000 shares or 1.5% of the outstanding shares of Ross common stock. 30 ROSS SYSTEMS, INC AND SUBSIDIARIES ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS CERTAIN TRANSACTIONS Under the terms of indemnification agreements with each of Ross' officers and directors, Ross is obligated to indemnify each officer and director against certain claims and expenses for which the director might be held liable in connection with past or future service on behalf of Ross. In addition, Ross' Certificate of Incorporation provide that, to the extent permitted by Delaware law, the officers and directors shall not be liable for monetary damages for breach of fiduciary duty as an officer or director. In fiscal 2003, Ross renewed and modified employment agreements with J. Patrick Tinley and Robert B. Webster. The employment agreements provide the executives with severance payments and accelerated vesting of stock options and other incentive awards if the executive's employment is terminated without "cause" at any time. If Mr. Tinley is terminated without "cause," he would be entitled to (1) a severance payment of 300% of his base compensation plus 300% of his targeted bonus, (2) employee benefit coverage applicable to the executive at the time of termination for three years following the termination and (3) ninety days to exercise all vested and unvested stock options and other incentive awards. If Mr. Webster is terminated without "cause," he would be entitled to (A) a severance payment of 200% of his base compensation plus 200% of his targeted bonus, (B) employee benefit coverage applicable to the executive at the time of termination for two years following the termination and (C) ninety days to exercise all vested and unvested stock options and other incentive awards. The employment agreements also provide the executives with severance payments and accelerated vesting of stock options and other incentive awards if the executive terminates his employment with Ross for "good reason" or is terminated for any reason other than "cause" or "disability" within nine months immediately following a "change of control" of Ross. In such a case, Mr. Tinley would be entitled to a severance payment of 300% of his base compensation plus 300% of his targeted bonus, each at the time of termination, and ninety days to exercise all vested and unvested stock options and other incentive awards, and Mr. Webster would be entitled to a severance payment of 200% of his base compensation plus 200% of his targeted bonus, each at the time of termination, and ninety days to exercise all vested and unvested stock options and other incentive awards. The employment agreements define "cause" to include a willful act by the executive which constitutes fraud and which is injurious to Ross, conviction of, or a plea of "guilty" or "no contest" to, a felony or the executive's continuing repeated willful failure or refusal to perform his material duties required by the employment agreement which is injurious to Ross. The employment agreements define "good reason" to include a material reduction in the executive's powers or duties, one or more reductions in the executive's base compensation in the cumulative amount of five percent (5%) or more or notifying the executive that his principal place of work

will be relocated by a distance of 50 miles or more. The employment agreements define "disability" as the executive's eligibility to receive immediate long-term disability benefits under Ross' long-term disability insurance plan or, if there is no such plan, under the federal Social Security program. The employment agreements define "change of control" to mean the occurrence of any of the following events: (a) any "person" (as such term in used in sections 13(d) and 14(d) of the Exchange Act) by the acquisition or aggregation of securities is or becomes the beneficial owner (within the meaning of Rule 13d-3 of the Exchange Act), directly or indirectly, of securities of Ross representing fifty percent (50%) or more of the combined voting power of Ross' then outstanding securities ordinarily (and apart from rights accruing under special circumstances) having the right to vote at elections of directors, referred to as "Base Capital Stock"; except that any change in the relative beneficial ownership of Ross' securities by any person resulting solely from a reduction in the aggregate number of outstanding shares of Base Capital Stock, and any decrease thereafter in such person's ownership of securities, shall be disregarded until such person increases in any manner, directly or indirectly, such person's beneficial ownership of any securities of Ross, or (b) the stockholders of Ross approve a definitive agreement: - to merge or consolidate Ross with or into another corporation in which the holders of the securities of Ross before such merger or reorganization will not, immediately following such merger or reorganization, hold as a group on a fully diluted basis both the ability to elect at least a majority of the directors of the surviving corporation and at least a majority in value of the surviving corporation's outstanding equity securities; or - to sell or otherwise dispose of all or substantially all of the assets of Ross or dissolve or liquidate Ross. 31 ROSS SYSTEMS, INC AND SUBSIDIARIES ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES AUDIT AND RELATED FEES BILLED TO ROSS DURING FISCAL 2003 AUDIT FEES BDO Seidman billed Ross an aggregate of $186,000 for expenses and professional services rendered for the (1) audit of the annual consolidated financial statements for fiscal year 2003 included in Ross' Annual Report on Form 10-K/A and (2) the review of the consolidated financial statements included in Ross' quarterly reports on Form 10-Q. FINANCIAL INFORMATION SYSTEMS DESIGN AND IMPLEMENTATION FEES Ross did not engage BDO Seidman to provide advice to it regarding financial information systems design and implementation during the fiscal year ended June 30, 2002. ALL OTHER FEES BDO Seidman billed Ross an aggregate of $92,000 for all other non-audit services rendered to it during fiscal 2003. The following table summarizes the approximate aggregate accounting fees billed to Ross for its 2003 fiscal year: Audit fees $ 186,000 Financial information systems design and implementation fees $ - All other fees:(1) $ 92,000 ---------- Total fees $ 278,000 (1) Includes fees for assistance with Commission filings and various accounting consultation ($11,000); various advisory services related principally to tax preparation services and tax consultation services associated with the development and implementation of international tax strategies and sales taxes ($67,000); and executive compensation analysis prepared at the request of independent board members ($14,000). 32 ROSS SYSTEMS, INC AND SUBSIDIARIES PART IV ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K (a) The following documents are filed as a part of this Report: 1. Consolidated Financial Statements. The following Consolidated Financial Statements of Ross Systems, Inc. are filed as part of this report: PAGE ---- Report of BDO Seidman , LLP, Independent Certified Public Accountants.. F-1 Fiscal 2001, and 2000 Report of Arthur Andersen LLP, Independent Public Accountants............................ F-2 Consolidated Balance Sheets at June 30, 2003 and 2002.. F-3 Consolidated Statements of Operations--Years Ended June 30, 2003, 2002, and 2001................................ F-4 Consolidated Statements of Cash Flows--Years Ended June 30, 2003, 2002, and 2001................................ F-5 Consolidated Statements of Shareholders' Equity--Years Ended June 30, 2003, 2002, and 2001...................... F-6 Notes to Consolidated Financial Statements.. F-7 2. Financial Statement Schedule. The following financial statement schedule of Ross Systems, Inc. for the Years Ended June 30, 2003, 2002, and 2001 is filed as part of this Report and should be read in conjunction with the Consolidated Financial Statements of Ross Systems, Inc. SCHEDULE PAGE -------- ---- II Valuation and Qualifying Accounts.. S-1 Schedules not listed above have been omitted because they are not applicable or are not required, or the information required to be set forth therein is included in the Consolidated Financial Statements or Notes thereto. 3. Exhibits. The Exhibits listed on the accompanying Index to Exhibits immediately following the financial statement schedules are filed as part of, or incorporated by reference into, this Report. (b) Reports on Form 8-K. None 33 ROSS SYSTEMS, INC AND SUBSIDIARIES SIGNATURES Pursuant to the requirements of Section 13 or 15(d) 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, in the City of Atlanta, State of Georgia, on the 22nd day of September, 2003. ROSS SYSTEMS, INC. By: /s/ J. Patrick Tinley --- J. Patrick Tinley Chairman and Chief Executive Officer POWER OF ATTORNEY KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints J. Patrick Tinley his attorney-in-fact, with the power of substitution, for him in any and all capacities, to sign any amendments to this Report on Form 10-K/A, and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that the said attorney-in-fact, or his substitute or substitutes, may do or cause to be done by virtue hereof. Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated. SIGNATURE TITLE DATE --------- ----- ---- /s/ J. Patrick Tinley Chairman and Chief Executive Officer September 22, 2003 ------------------------------- (Principal Executive Officer) J. Patrick Tinley /s/ Robert B. Webster Executive Vice President Operations, Company September 22, 2003 ------------------------------- Secretary and Director Robert B. Webster /s/ Verome M. Johnston Vice President and Chief Financial Officer September 22, 2003 ------------------------------- (Principal Financial and Accounting Verome M. Johnston Officer) /s/ J. William Goodhew III Director September 22, 2003 ------------------------------- J. William Goodhew III /s/ Frank M. Dickerson Director September 22, 2003 ------------------------------- Frank M. Dickerson /s/ Bruce J. Ryan Director September 22, 2003 ------------------------------- Bruce J. Ryan 34 ROSS SYSTEMS, INC AND SUBSIDIARIES ROSS SYSTEMS, INC. ANNUAL REPORT ON FORM 10-K/A YEAR ENDED JUNE 30, 2003 ROSS SYSTEMS, INC. INDEX TO EXHIBITS EXHIBIT NO. DESCRIPTION ----------- ----------- 2.1 Asset Sale Agreement between Registrant and Now Solutions LLC dated March 5, 2001 (1) 3.1 Certificate of Incorporation of the Registrant, as amended (2) 3.2 Bylaws of the Registrant, as amended (2) 3.3 Amendment to the Certificate of Incorporation of the Registrant, dated April 26, 2001, for the 1 for 10 Reverse Stock Split.(3) 4.1 Certificate of Designation of Rights, Preferences and Privileges of Series B Preferred Stock of the Registrant (4) 4.2 Form of the subordinated debenture agreement due February 6, 2003 issued by the Registrant to each investor (6) 4.3 Registration Rights Agreement between the Registrant and each Investor (6) 10.1 Preferred Share Rights Agreement, dated September 4, 1999 between the Registrant and Registrar and Transfer Company (5) 10.2 Employment

Agreement dated January 7, 1999, modified March 24, 2003, between Mr. Patrick Tinley and the Registrant (8) 10.3 Employment Agreement dated September 13, 1999, modified March 24, 2003, between Mr. Robert B. Webster and the Registrant (8) 10.4 Convertible Preferred Stock Purchase Agreement dated June 29, 2001 between Registrant and Benjamin W. Griffith, III (7) 10.5 Loan and Security Agreement dated September 24, 2002 between Registrant and Silicon Valley Bank (3) 21.1 Listing of Subsidiaries of Registrant 23.1 Consent of BDO Seidman, LLP 24.1 Power of Attorney (included on signature page) 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (1) Incorporated by reference to the exhibit filed with the Registrant's current Report on Form 8-K/A filed May 15, 2001. (2) Incorporated by reference to the exhibit filed with the Registrant's current Report on Form 8-K filed July 24, 1998. (3) Incorporated by reference to the exhibit filed with the Registrant's current Report on Form 10K/A filed October 2, 2002 (4) Incorporated by reference to the exhibit filed with the Registrant's Quarterly Report on Form 10-Q filed May 6, 1996. (5) Incorporated by reference to the exhibit filed with the Registrant's Registration Statement on Form 8-A filed September 4, 1998. (6) Incorporated by reference to the exhibit filed with the Registrant's current report on Form 8-K filed February 12, 1998. 35 ROSS SYSTEMS, INC AND SUBSIDIARIES (7) Incorporated by reference to the exhibit filed with the Registrant's Quarterly Report on Form 10K filed September 27, 2001. (8) Incorporated by reference to the exhibit filed with the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2003 filed May 14, 2003. 36 ROSS SYSTEMS, INC AND SUBSIDIARIES REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS To the Board of Directors and Shareholders of Ross Systems, Inc. We have audited the accompanying consolidated balance sheets of Ross Systems, Inc. and subsidiaries as of June 30, 2003 and 2002, and the related consolidated statements of operations, shareholders' equity and cash flows for the years then ended. We have also audited the financial statement schedule for the years ended June 30, 2003 and 2002 listed in the accompanying index. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits. The Company's consolidated financial statements and financial statement schedule as of and for the year ended June 30, 2001, prior to the adjustments discussed in the summary of significant accounting policies, were audited by auditors who have ceased operations. Those auditors expressed an unqualified opinion on those consolidated financial statements and schedule in their report dated August 17, 2001. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements and schedule are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and schedule. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Ross Systems, Inc. and subsidiaries as of June 30, 2003 and 2002, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the 2003 and 2002 schedules present fairly, in all material respects, the information set forth therein. As discussed in Note 1, during the year ended June 30, 2002 the company changed the manner in which it records reimbursement of out-of- pocket expenses upon the adoption of the accounting standards in of Emerging Issues Task Force Issue 01-14. As discussed in Note 1, the Company changed the manner in which it accounts for goodwill and other intangible assets upon adoption of the accounting standards in Statement of Financial Accounting Standards No. 142 on July 1, 2001, As discussed above, the financial statements of Ross Systems Inc. and subsidiaries as of June 30, 2001, and for each of the two years in the period ended June 30, 2001, were audited by other auditors who have ceased operations. As described in Note 1, these financial statements have been restated to reflect the adoption of Emerging Issues Task Force Issue 01-14 and revised to include the transitional disclosures required by SFAS No. 142. We audited the adjustments described in Note 1 that were applied to restate the 2001 financial statements to reflect the adoption of Emerging Issues Task Force Issue 01-14. We also audited the adjustments reflected in the transitional disclosures required by SFAS No. 142. In our opinion, such adjustments are appropriate and have been properly applied. However, we were not engaged to audit, review or apply any procedures to the 2001 financial statements of the company, other than with respect to such adjustments and, accordingly, we do not express an opinion or any other form of assurance on the 2001 financial statements taken as a whole. /s/ BDO Seidman, LLP Atlanta, Georgia August 20, 2003 (Except for Note 9 as to which the date is September 4, 2003) F - 1 ROSS SYSTEMS, INC AND SUBSIDIARIES THE FOLLOWING REPORT IS A COPY OF A PREVIOUSLY ISSUED REPORT BY ARTHUR ANDERSEN LLP AND IT HAS NOT BEEN REISSUED BY ARTHUR ANDERSEN LLP. ARTHUR ANDERSEN LLP HAS NOT CONSENTED TO ITS INCORPORATION BY REFERENCE INTO ROSS SYSTEMS INC.'S PREVIOUSLY FILED REGISTRATION STATEMENTS FILE NOS: 333-65660, 333-39348, 33-42036, 33-48226, 33-56584, 33-72168, 33-89128, 333-36745, 333-44665, 333-71005, 33-89504, 333-19619, 333-06053, 333-44363, 333-47877, 333-58639, AND 333-65065. THEREFORE, AN INVESTOR'S ABILITY TO RECOVER ANY POTENTIAL DAMAGE MAY BE LIMITED. REPORT OF PREVIOUS INDEPENDENT PUBLIC ACCOUNTANTS To Ross Systems, Inc.: We have audited the accompanying consolidated balance sheets of ROSS SYSTEMS, INC. (a Delaware corporation) AND SUBSIDIARIES as of June 30, 2001 and 2000* and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years ended June 30, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion. In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Ross Systems, Inc. and subsidiaries as of June 30, 2001 and 2000*, and the results of their operations and their cash flows for each of the three years ended June 30, 2001 in conformity with accounting principles generally accepted in the United States. Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedule listed in the

index of financial statements included in Item 14 is presented for purposes of complying with the Securities and Exchange Commission's rules and is not part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, fairly states in all material respects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole. ARTHUR ANDERSEN LLP Atlanta, Georgia August 17, 2001 * The 2000 and 2001 Consolidated Balance Sheet and the 1999 and 2000 Consolidated Statement of Operations, Shareholders Equity, and Cash Flows are not required to be present in the 2003 Annual Report. F - 2 ROSS SYSTEMS, INC AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS (IN THOUSANDS, EXCEPT SHARE DATA) JUNE 30, -------------------------- 2003 2002 -------- -------- ASSETS Current assets: Cash and cash equivalents .... $ 8,628 $ 5,438 Accounts receivable, less allowance for doubtful accounts of $1,532 and $3,379, at 2003, and 2002 respectively .... 12,880 12,319 Prepaid and other current assets .... 731 532 Note receivable from related party .... - 850 -------- -------- Total current assets .... 22,239 19,139 Property and equipment, net .... 1,406 1,450 Computer software costs, net .... 13,573 14,036 Other assets .... 2,993 2,993 -------- -------- Total assets .... $ 40,211 $ 37,618 ======== ======== LIABILITIES AND SHAREHOLDERS' EQUITY Current liabilities: Short term debt .... $ 2,800 $ 3,967 Accounts payable .... 2,978 2,682 Accrued expenses .... 4,940 4,476 Income taxes payable .... 261 15 Deferred revenues .... 12,203 12,535 -------- -------- Total liabilities .... 23,182 23,675 -------- -------- Commitments and Contingencies Shareholders' equity: Convertible Preferred stock, no par value 5,000,000 shares authorized; 500,000 shares issued and outstanding .... 2,000 2,000 Common stock, $0.001 par value; 15,000,000 shares authorized; 2,815,603 and 2,625,378 shares issued and outstanding .... 28 26 Additional paid-in capital .... 87,189 86,983 Accumulated deficit .... (69,094) (73,300) Accumulated other comprehensive deficit .... (1,749) (1,766) Treasury stock at cost, 158,977 shares .... (1,345) - -------- -------- Total shareholders' equity .... 17,029 13,943 -------- -------- Total liabilities and shareholders' equity .... $ 40,211 $ 37,618 ======== ======== See accompanying Notes to Consolidated Financial Statements F - 3 ROSS SYSTEMS, INC AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF OPERATIONS (IN THOUSANDS, EXCEPT SHARE DATA) YEARS ENDED JUNE 30, ------------------------------- 2003 2002 2001 -------- -------- -------- Revenues: Software product licenses .... $ 14,589 $ 13,026 $ 9,607 Consulting and other services .... 13,489 13,013 16,520 Maintenance .... 20,022 20,014 24,678 -------- -------- -------- Total revenues .... 48,100 46,053 50,805 -------- -------- -------- Operating expenses: Costs of software product licenses (inclusive of amortization and impairment of capitalized software) .... 6,997 19,992 8,349 Costs of consulting, maintenance and other services (inclusive of reimbursable expenses of $1,180, $834, and $1,307 for 2003, 2002, and 2001, respectively, and exclusive of non recurring expense of $353 for 2001) .... 17,193 17,023 17,595 Software product license sales and marketing (exclusive of non-recurring expense of $136 for 2001) .... 11,384 9,461 15,026 Product development, net of capitalized computer software costs (exclusive of non recurring expense of $301 for 2001) .... 2,528 3,057 4,127 General and administrative .... 4,376 4,393 4,737 Provision for uncollectible accounts .... 831 1,444 1,514 Amortization of goodwill .... - - 691 Non-recurring costs (benefit) .... - (650) 790 -------- -------- -------- Total operating expenses .... 43,309 54,720 52,829 -------- -------- -------- Operating profit (loss) .... 4,791 (8,667) (2,024) Other income (expense): Gain on sale of product line .... - - 2,372 Other financial, net .... (180) (625) (1,181) -------- -------- -------- Net income (loss) before income taxes .... 4,611 (9,292) (833) Income tax expense .... 405 132 9 -------- -------- -------- Net income (loss) .... 4,206 (9,424) (842) Preferred stock dividends (150) (150) - -------- -------- -------- Net income (loss) available to common shareholders .... $ 4,056 $ (9,574) $ (842) ======== ======== ======== Net income (loss) per common share--basic .... $ 1.54 $ (3.65) $ (0.33) ======== ======== ======== Net income (loss) per common share--diluted .... $ 1.28 $ (3.65) $ (0.33) ======== ======== ======== Shares used in per share computation--basic .... 2,641 2,625 2,566 ======== ======== ======== Shares used in per share computation--diluted .... 3,296 2,625 2,566 ======== ======== ======== See accompanying Notes to Consolidated Financial Statements F - 4 ROSS SYSTEMS, INC AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF CASH FLOWS (IN THOUSANDS) YEARS ENDED JUNE 30, --------------------------------- 2003 2002 2001 -------- -------- -------- Cash flows from operating activities: Net income (loss) .... $ 4,206 $ (9,424) $ (842) Adjustments to reconcile net loss to cash provided by operating activities: Non cash financing costs .... - - 60 Non-cash stock compensation costs .... 175 - - Impairment of capitalized software costs .... - 10,938 - Depreciation and amortization of property and equipment .... 766 984 1,592 Amortization of computer software costs .... 4,702 7,184 7,369 Amortization of goodwill .... - - 691 Provision for uncollectible accounts .... 831 1,444 1,514 Changes in operating assets and liabilities, net of sale of product line: Accounts receivable .... (1,246) (3,646) 9,911 Prepaid and other current assets .... (121) 575 (149) Income taxes recoverable/payable .... 271 185 92 Accounts payable .... 281 (2,218) (2,178) Accrued expenses .... 489 (881) (1,011) Deferred revenues .... (246) (66) (2,991) -------- -------- -------- Cash provided by operating activities .... 10,108 5,075 14,058 -------- -------- -------- Cash flows from investing activities: Purchases of property and equipment, net .... (722) (740) (277) Computer software costs capitalized .... (4,239) (4,307) (6,878) Note receivable from related party repaid .... 850 - - Sale of product line, net of assets disposed .... - - 1,567 Other

.... - 144 429 -------- -------- -------- Cash used in investing activities .... (4,111) (4,903) (5,159) -------- -------- -------- Cash flows from financing activities: Net cash paid on line of credit activity .... (1,167) (555) (5,353) Debt and capital lease payments .... - - (1,723) Repurchase of treasury stock .... (1,345) - - Proceeds from issuance of preferred stock .... - - 2,000 Proceeds from issuance of common stock .... 183 101 17 Preference dividend paid .... (150) (150) - -------- -------- -------- Cash used in financing activities .... (2,479) (604) (5,059) -------- -------- -------- Effect of exchange rate changes on cash .... (328) 154 (134) -------- -------- -------- Net increase (decrease) in cash and cash equivalents .... 3,190 (278) 3,706 -------- -------- -------- Cash and cash equivalents at beginning of fiscal year .... 5,438 5,716 2,010 -------- -------- -------- Cash and cash equivalents at end of fiscal year .... $ 8,628 $ 5,438 $ 5,716 ======== ======== ======== See accompanying Notes to Consolidated Financial Statements F - 5 ROSS SYSTEMS, INC AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (IN THOUSANDS) Accum- ulated Other Total Preferred Stock Common Stock Treasury Stock Accum- Compre- Share- Comprehen --------------- -------------- --------------- Paid in ulated hensive holders' -sive Shares Amount Shares Amount Shares Amount Capital Deficit Deficit Equity Loss ------ ------ ------ ------ ------ ------- ------- -------- ------- -------- --------- Balances as of June 30, 2000 - $ - 2,380 $ 24 - $ - $85,780 $(63,034) $(1,880) $ 20,890 ------ ------ ------ ------ ------ ------- ------- -------- ------- -------- Conversion of debentures ... 173 2 1,175 1,177 Issuance of stock pursuant to employee stock purchase plan............ 13 17 17 Effect of foreign currency translation............. (198) (198) $ (198) Issuance of preference shares 500 2,000 2,000 Issuance of warrants pursuant to cost of financing 60 60 Net loss................... (842) (842) (842) --------- Comprehensive Loss.......... (1,040) ========= ------ ------ ------ ------ ------ ------- ------- -------- ------- -------- Balances as of June 30, 2001 500 2,000 2,566 26 - - 87,032 (63,876) (2,078) 23,104 ====== ====== ====== ====== ====== ======= ======= ======== ======= ======== Issuance of stock pursuant to employee stock purchase and option plans.................... 59 101 101 Effect of foreign currency translation............. 312 312 312 Net loss................... (9,424) (9,424) (9,424) Dividends on preferred stock (150) (150) --------- Comprehensive Loss.......... (9,112) ========= ------ ------ ------ ------ ------ ------- ------- -------- ------- -------- Balances as of June 30, 2002 500 2,000 2,625 26 - - 86,983 (73,300) (1,766) 13,943 ====== ====== ====== ====== ====== ======= ======= ======== ======= ======== Issuance of stock pursuant to employee stock purchase and option plans.................... 71 1 357 358 Issuance of stock in fulfillment of 1996 acquisition of Spanish subsidiary 120 1 (1) Repurchase of treasury stock (159) (1,345) (1,345) Effect of foreign currency translation............. 17 17 17 Net profit (loss)........... 4,206 4,206 4,206 Dividends on preferred stock (150) (150) --------- Comprehensive Income........ $ 4,223 ========= ------ ------ ------ ------ ------ ------- ------- -------- ------- -------- Balances as of June 30, 2003 500 $2,000 2,816 $ 28 (159) $(1,345) $87,189 $(69,094) $(1,749) $ 17,029 ====== ====== ====== ====== ====== ======= ======= ======== ======= ======== See accompanying Notes to Consolidated Financial Statements F - 6 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (1) DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES Business of the Company Ross Systems, Inc. (NASDAQ: ROSS) delivers innovative software solutions that help manufacturers worldwide fulfill their business growth objectives through increased operational efficiencies, improved profitability, strengthened customer relationships and streamlined regulatory compliance. Focused on the food and beverage, life sciences, chemicals, metals and natural products industries and implemented by over 1,000 customer companies worldwide, the company's family of Internet-architected solutions is a comprehensive, modular suite that spans the enterprise, from manufacturing, financials and supply chain management to customer relationship management, performance management and regulatory compliance. Publicly traded on the NASDAQ since 1991, Ross' global headquarters are based in the U.S. in Atlanta, Georgia, with sales and support operations around the world. The Company operates in one business segment and no individual customer accounts for more than 10% of total revenues. The Company does not have a concentration of credit risk in any one industry. Approximately 60% of the Company's revenues are derived from the North American market. Basis of Presentation The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant inter-company balances and transactions have been eliminated in consolidation. Stock Based Compensation. The company measures compensation cost for its stock incentive and option plans using the intrinsic value-based method of accounting. Had the company used the fair value-based method of accounting to measure compensation expense for its stock incentive and option plans and charged compensation cost against income over the vesting periods, based on the fair value of options at the date of grant, net income and the related basic and diluted per common share amounts for the twelve months ended June 30, 2003, 2002, and 2001, would have been reduced to the following pro forma amounts: (In thousands, except per share data) FISCAL YEAR ENDED JUNE 30, ------------------------------------- 2003 2002 2001 --------- --------- --------- Net income (loss) available to common shareholders: As reported .... $ 4,056 $ (9,574) $ (842) Add: Stock-based compensation expense included in reported net income , net of tax .... 175 - - Deduct: Total stock-based employee compensation expense under fair value-based method, net of tax (699) (406) (460) --------- --------- --------- Pro forma net income (loss) available to common shareholders .... $ 3,532 $ (9,980) $ (1,302) --------- --------- --------- Basic net earnings per share: As reported .... $ 1.54 $ (3.65) $ (0.33) Pro forma .... 1.34 (3.80) (0.51) Diluted net earnings per share: As reported .... 1.28 (3.65) (0.33) Pro forma .... 1.07 (3.80) (0.51) F - 7 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS The following weighted average assumptions for the Company's Stock Option Plan were used to determine the pro forma amounts noted above: YEAR ENDED JUNE 30, ------------------------------------- 2003 2002 2001 --------- --------- --------- Expected life..................................... 5 5 5 Expected volatility............................... 48.6% 80.4% 121.6% Risk-free interest rate........................... 3.9% 5.0% 5.3% Expected dividend yield........................... None None None Revenue Recognition. In accordance with Securities and Exchange Commission Staff Accounting Bulletin No. 101 "Revenue Recognition in Financial Statements," the Company recognizes revenues from licenses of computer software "up-front" provided that a non-cancelable license agreement has been signed, the software and related documentation have been shipped, there are no material uncertainties regarding customer acceptance, collection of the resulting receivable is deemed probable, and no significant other vendor obligations exist. The revenue associated with any license agreements containing cancellation or refund provisions is deferred until such provisions lapse. Where the Company has future obligations, if such obligations are insignificant, related costs are accrued immediately. When the obligations are significant, the software product license revenues are deferred. Future contractual obligations can include software customization, requirements to provide additional products in the future and porting products to new platforms. Contracts which require

significant software customization are accounted for on the percentage-of-completion basis. Revenues related to significant obligations to provide future products or to port existing products are deferred until the new products or ports are completed. The Company's revenue recognition policies are designed to comply with American Institute of Certified Public Accountants Statement of Position ("SOP") 97-2, "Software Revenue Recognition," and with SEC Staff Accounting Bulletin ("SAB") No. 101, "Revenue Recognition in Financial Statements." Revenues recognized from multiple-element software license contracts are allocated to each element of the contracts based on the fair values of the elements, such as licenses for software products, maintenance, or professional services. The determination of fair value is based on objective evidence which is specific to the Company. The Company limits its assessment of objective evidence for each element to either the price charged when the same element is sold separately, or the price established by management having the relevant authority to do so, for an element not yet sold separately. If evidence of fair value of all undelivered elements exists but evidence does not exist for one or more delivered elements, then revenue is recognized using the residual method. Under the residual method, the fair value of the undelivered elements is deferred and the remaining portion of the arrangement fee is recognized as revenue. The Company utilizes distributors primarily in those geographic areas where the Company does not maintain a physical presence. The Company's revenue recognition policies with respect to sales by distributors complies with SOP 97-2 and SAB 101 in that all the revenue recognition criteria listed above are met. In addition, distributors do not have rights of return, price protections, rotation rights, or other features that would preclude revenue recognition. Generally, the value of software license sales to distributors is based on list selling prices to their customer less a discount at a predetermined rate. Similarly, the Company receives revenue from distributors based on a predetermined percentage of the maintenance fees billed by the distributor to the end customer. The distributor typically retains any fees earned by them for implementation services. Distributorships may or may not be geographically exclusive, and are generally subject to annual renewals by the Company. Service revenues generated from professional consulting and training services are recognized as the services are performed. Maintenance revenues, including revenues bundled with original software product license revenues, are deferred and recognized over the related contract period, generally 12 months. Computer Software Costs. The Company capitalizes computer software product development costs incurred in developing a product once technological feasibility has been established and until the product is available for general release to customers. Technological feasibility is established when the Company either (1) completes a detail program design that F - 8 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS encompasses product function, feature and technical requirements and is ready for coding and confirms that the product design is complete, that the necessary skills, hardware and software technology are available to produce the product, that the completeness of the detail program design is consistent with the product design by documenting and tracing the detail program design to the product specifications, and that the detail program design has been reviewed for high-risk development issues and any related uncertainties have been resolved through coding and testing or (2) completes a product design and working model of the software product, and the completeness of the working model and its consistency with the product design have been confirmed by testing. The Company evaluates realizability of the capitalized amounts based on expected revenues from the product over the remaining product life. Where future revenue streams are not expected to cover remaining amounts to be amortized, the Company either accelerates amortization or expenses remaining capitalized amounts. Amortization of such costs is computed as the greater of (1) the ratio of current revenues to expected revenues from the related product sales or (2) a straight-line basis over the expected economic life of the product (not to exceed five years). Software costs related to the development of new products incurred prior to establishing technological feasibility or after general release are expensed as incurred. As of June 30, 2003 and 2002, capitalized computer software costs approximated $63,945,000 and $61,587,000 respectively, and related accumulated amortization totaled $50,372,000 and $47,551,000 respectively. Cash and Cash Equivalents The Company considers all highly liquid investments purchased with an original maturity date of three months or less to be cash equivalents. Accounts Receivable and Allowance for Doubtful Accounts Accounts receivable comprise trade receivables that are credit based and do not require collateral. Generally, the Company's credit terms are 30 days but in some instances the Company offers extended payment terms to customers purchasing software licenses. The Company has a history of offering extended payment terms from time to time for competitive reasons. These terms are not offered in connection with any contingencies related to product acceptance, implementation, or any other service or contingency post-transaction, and the Company has not offered concessions as a result of these terms. Payment arrangements in these circumstances typically require payment of a significant portion of the total contract amount within 30 days of the sale, with 2 or 3 subsequent installments making up the balance payable within 6 months. The Company has not found collectibility to be compromised as a result of these terms. In no case have payment terms extended beyond 12 months. Based on historical results, the Company believes that all components of SOP 97-2 are met, including that the arrangement is fixed and determinable. The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. On an ongoing basis, the Company evaluates the collectibility of accounts receivable based upon historical collections and assessment of the collectibility of specific accounts. Ross specifically reviews the collectibility of accounts with outstanding accounts receivable balances in excess of 90 days outstanding. The Company evaluates the collectibility of specific accounts using a combination of factors, including the age of the outstanding balance(s), evaluation of the account's financial condition, recent payment history, and discussions with the account executive responsible for the specific customer and with the customer directly. Based upon this evaluation of the collectibility of accounts receivable, an increase or decrease required in the allowance for doubtful accounts is reflected in the period in which the evaluation indicates that a change is necessary. If actual results differ, this could have an impact on the Company's financial condition, results of operation and cash flows. Property and Equipment Property and equipment are stated at cost. Depreciation is accumulated using the straight-line method over the estimated useful lives of the respective assets, generally three to seven years. Leasehold improvements and equipment under capital leases are amortized using the straight-line method over the shorter of the terms of the related leases or the respective useful lives of the assets. F-9 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Long-lived Assets Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If the sum of the expected future undiscounted cash flows is less than the carrying amount of the asset, a loss is recognized for the difference between the fair value and the carrying value of the asset. Fair Value of Financial Instruments The carrying amounts reported on the balance sheet for accounts receivable, notes receivable, accounts payable and short term debt approximate their fair values. Net Earnings (Loss) Per Common Share Basic earnings (loss) per common share is computed by dividing net earnings or net loss by the weighted average number of common shares outstanding during the period. Shares issued or reacquired during the year are weighted for the

portion of the year that they were outstanding. Diluted earnings (loss) per common share is computed in a manner consistent with that of basic earnings (loss) per share while giving effect to all potentially dilutive common shares that were outstanding during the period. Potentially dilutive common shares used in computing diluted earnings per share are shown in the following table. As a result of the net losses incurred in the years ended June 30, 2002, and 2001, the potentially dilutive common shares for these fiscal years were not considered in the calculation as their impact would be antidilutive. Potentially dilutive common shares excluded in 2003, 2002 and 2001 were as follows: FISCAL YEAR ENDED JUNE 30, ------------------------- 2003 2002 2001 ---- ---- ---- Stock options .... 347 41 39 Warrants .... 47 Convertible Preferred shares .... 500 1 --- --- --- Total .... 347 588 40 --- --- --- The following is a reconciliation from basic earnings per share to diluted earnings per share for fiscal 2003 (in thousands) : EARNINGS AVAILABLE TO COMMON WEIGHTED AVERAGE EARNINGS SHAREHOLDERS SHARES OUTSTANDING PER SHARE ------------ ------------------ --------- Basic .... $4,056 2,641 $ 1.54 Stock options .... 108 Warrants .... 47 Convertible Preferred shares ...... 150 500 ------ ------ -------- Diluted .... $4,206 3,296 $ 1.28 ------ ------ -------- Goodwill In June 2001, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141, Business Combinations, and No. 142, Goodwill and Other Intangible Assets, effective for fiscal years beginning after December 15, 2001. The Company elected early adoption and applied the provisions of this statement, effective in the first quarter of fiscal 2002. Under the new rules, goodwill is no longer amortized but is subject to annual impairment tests. Other intangible assets will continue to be amortized over their useful lives. Goodwill attributable to each of the Company's reporting units was tested in June 2003 for impairment by comparing the fair value of each of the reporting units with its carrying value. The fair values of these reporting units were determined using a combination of discounted cash flow analysis and market multiples based on F-10 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS historical and projected financial information. It was determined that there was no impairment to goodwill in any period subsequent to the date the Company adopted SFAS 142. Net loss and loss per share for fiscal 2001, adding back goodwill amortization of $691,000 ($0.27 per basic and diluted share) would have been $(151,000), $(0.06) per basic and diluted share. Prior to July 1, 2001, goodwill was being amortized over periods ranging from 7 to 10 years. Reimbursable Expenses Prior to January 1, 2002, the Company recorded reimbursement by its customers for out-of-pocket expenses as a decrease to cost of services. The Company's results of operations for the fiscal years June 30, 2001, have been reclassified for comparable purposes in accordance with the Emerging Issues Task Force release 01-14, "Income Statement Characterization of Reimbursements Received for Out of Pocket Expenses Incurred." The effect of this reclassification was to increase both services revenues and cost of services by, $1,307,000 for fiscal year 2001. Income Taxes In accordance with Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" ("Statement 109"), the Company utilizes the asset and liability method of accounting for income taxes. Under the asset and liability method of Statement 109, deferred tax assets and liabilities are established to recognize the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Foreign Operations and Currency Translation The local currencies of the Company's foreign subsidiaries are the functional currencies. Assets and liabilities of foreign subsidiaries are translated into U.S. dollars at current exchange rates, and the resulting translation gains and losses are included as an adjustment to shareholders' equity as a component of comprehensive income. Transaction gains and losses that relate to U.S. dollar denominated intercompany short-term receivables recorded in the financial statements of the Company's foreign subsidiaries and are reflected in income. Where related intercompany balances have been designated as long-term, gains and losses are included as an adjustment to shareholders' equity as a component of comprehensive income. Reclassifications It is the Company's policy to reclassify prior year amounts to conform with current year financial statement presentation when necessary. Use of Estimates The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates. Advertising Costs The Company generally expenses advertising costs at the time the advertisement is published, or in the case of direct mail, when mailed. Advertising costs for the fiscal years ended June 30, 2003, 2002, and 2001 were approximately $574,000, $437,000, and $607,000 respectively. Segment Information SFAS No. 131 "Disclosures about Segments of an Enterprise and Related Information" established standards for the way that public business enterprises report information about operating segments in their financial statements. The standard defines operating segments as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding F-11 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS how to allocate resources and in assessing performance. Based on these standards the Company has determined that it operates in four geographical segments: Northern Europe, Spain the United Kingdom and North America. During fiscal 2001, the Company divested its French subsidiary and adopted an indirect sales approach in the French market. See further discussion of this matter under "Acquisitions and Divestitures" below. The Company has no customers that represent ten percent or more of annual revenues. For management purposes, the results of the Asian operations are included in the North American results since the costs associated with managing the Asian marketplace are born by the North American entities within the Group. Revenues in the Asian markets comprise less than 5% of total revenues reported for the North American segment. Selected balance sheet and income statement information pertaining to the various significant geographic areas of operation are as follows: As of and for the year ended June 30, 2003 (in thousands) : NET INCOME DEPRECIATION CAPITAL GROSS ASSETS REVENUE (LOSS) AND AMORTIZATION EXPENDITURES ------------ ------- ---------- --------------- ------------ Northern Europe .... $ 2,987 $ 5,000 $ 475 $ 60 $ 68 Spain .... 6,220 6,902 615 306 259 United Kingdom .... 2,569 5,545 387 54 39 North America .... 28,435 30,653 2,729 346 356 ------- ------- ------- ------- ------- Total .... $40,211 $48,100 $ 4,206 $ 766 $ 722 ======= ======= ======= ======= ======= As of and for the year ended June 30, 2002 (in thousands) : NET INCOME DEPRECIATION CAPITAL GROSS ASSETS REVENUE (LOSS) AND AMORTIZATION EXPENDITURES ------------ -------- ---------- --------------- ------------ Northern Europe .... $ 2,518 $ 5,579 $ 676 $ 60 $ 159 Spain .... 4,723 6,431 1,622 247 96 United Kingdom ..... 2,969 5,127 134 62 21 North America ...... 27,408 28,916 (11,856) 615 464 -------- -------- -------- -------- -------- Total .... $ 37,618 $ 46,053 $ (9,424) $ 984 $ 740 ======== ======== ======== ======== ======== As of and for the year ended June 30, 2001 (in thousands): NET INCOME DEPRECIATION CAPITAL GROSS ASSETS REVENUE (LOSS) AND AMORTIZATION EXPENDITURES ----------- ------- ---------- ---------------- ------------- Northern Europe .... $ 1,583 $ 4,947 $ (210) $ 80 $ 35 Spain .... 2,248 4,218 (56) 182 38 United Kingdom ..... 2,985 5,162 (1,014) 126 4 North America ......

43,646 36,478 438 1,895 200 ------- ------- ------- ------- ------- Total .... $50,462 $50,805 $ (842) $ 2,283 $ 277 ======= ======= ======= ======= ======= New Accounting Pronouncements In November 2002, the FASB issued FASB Interpretation ("FIN") No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others", which clarifies disclosure and recognition/measurement requirements related to certain guarantees. The disclosure requirements are effective for financial statements issued after December 15, 2002 and the recognition/measurement requirements are effective on a prospective basis for guarantees issued or modified after December 31, 2002. The application of the requirements of FIN 45 did not have a significant impact on our financial position or result of operations. F-12 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS In December 2002, the FASB issued Statement of Financial Accounting Standards No. 148, Accounting for Stock-Based Compensation--Transition and Disclosure--an amendment of FASB Statement No. 123 ("Statement 148"). This amendment provides two additional methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. Additionally, more prominent disclosures in both annual and interim financial statements are required for stock-based employee compensation. The transition guidance and annual disclosure provisions of Statement 148 are effective for fiscal years ending after December 15, 2002. The Company adopted the disclosure provisions of SFAS 148 during fiscal 2003. In January 2003, the FASB issued FASB Interpretation No. (FIN) 46, "Consolidation of Variable Interest Entities." This Interpretation of Accounting Research Bulletin No. 51, "Consolidated Financial Statements," addresses consolidation by business enterprises of variable interest entities which possess certain characteristics. The Interpretation requires that if a business enterprise has a controlling financial interest in a variable interest entity, the assets, liabilities, and results of the activities of the variable interest entity must be included in the consolidated financial statements with those of the business enterprise. This Interpretation applied immediately to variable interest entities created after January 31, 2003 and to variable interest entities in which an enterprise obtains an interest after that date. The Company does not have any ownership in any variable interest entities as of June 30, 2003. In April 2003, the FASB issued Statement of Financial Accounting Standards No. 149, Amendment of Statement 133 on Derivative Instruments and Hedging Activities ("Statement 149"). This Statement amends Statement 133 for decisions made (1) as part of the Derivatives Implementation Group process that effectively required amendments to Statement 133, (2) in connection with other Board projects dealing with financial instruments, and (3) in connection with implementation issues raised in relation to the application of the definition of a derivative, in particular, the meaning of an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors, the meaning of underlying, and the characteristics of a derivative that contains financing components. The Company does not have any derivative instruments or hedging activities. The application of Statement 149 did not have an impact on our financial statements. In May 2003, the FASB issued Statement of Financial Accounting Standards No. 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity ("Statement 150"). This Statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a financial instrument that is within its scope as a liability (or an asset in some circumstances). Many of those instruments were previously classified as equity. Statement 150 requires that certain mandatorily redeemable financial instruments issued in the form of shares are to be classified as liabilities rather than equity. The Company has no outstanding financial instruments that fall into the definitions covered by this Statement. The application of Statement 150 did not have a significant impact on our financial statements. Non-recurring items In October of 2000, the Company reorganized its European presence and adopted an indirect sales model in France by terminating its ownership and control of the French subsidiary due to the chronic and sustained losses and negative cash flows suffered by the French subsidiary. At that time, management recorded what they deemed to be adequate reserves related to the possible future costs for the change of presence in France by deferring the gain associated with divesting net liabilities in this liquidating transaction. In the fourth quarter of fiscal 2002, the Company experienced a favorable outcome relating to the French subsidiary liquidation transaction which rendered most of the reserve unnecessary. As a result the Company recorded a non-recurring gain of $650,000 in fiscal year 2002, arising from the reduction of the reserve described above. On September 12, 2000, the Company announced restructuring efforts aimed at reducing costs and improving efficiencies. Under the restructuring, the Company reduced 125 positions across the company as well as accelerated efforts to eliminate unneeded office space, improve productivity through the use of technology and focus on increased revenues through the use of distributors. As a result of these actions, during the first quarter of fiscal year 2001, the Company recorded a $790,000 expense to cover the liability arising from associated employee separation costs. The costs were accrued in accordance with EITF Issue 94-3, "Liability Recognition for Certain F-13 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Employee Terminations, Benefits and Other Costs to Exit an Activity". By March 31, 2001, all of the costs accrued in conjunction with both actions had been paid. Non-cash Impairment of Capitalized Software Cost In the fourth quarter of fiscal 2002, the Company made a major change in technology direction. The Internet-related functionality of the iRenaissance product was re-directed from the "java" based initial development used in the Resynt product line to the Microsoft ".net" technology. A new, formal development relationship with Microsoft was launched to support the requirements of the new technology direction. This strategic re-direction was based on the Company's belief that the .net technology will serve the Company and its customers better in the future, due to fuller market penetration, better standards of compatibility, and superior technical adaptability. The result of this change was that prior development in the former java environment became obsolete. Effective April 1, 2002, the amount of $5,488,000, representing all unamortized software-project balances relating to this, was expensed. On April 23, 2002, the Company announced the General Availability of Gembase Version 6.0. This version of Gembase, the 4GL language used for the development of the iRenaissance products, contained major functionality differences to prior versions, rendering all prior versions obsolete. As a result, development and maintenance of all versions prior to 6.0 were discontinued and no further sales using these versions would be contemplated. In addition, customers using these versions would be strongly encouraged to upgrade to version 6.0 because the Company no longer supports development of any Gembase release lower than version 6.0. Upgrades to the 6.0 version would be strongly supported and to encourage and facilitate customers' upgrading, the product was designed to make the transition straight-forward. Since Gembase versions lower than 6.0 would not contribute any further revenue to the Company, even in the short-term, the related unamortized software-project balances amounting to $943,000 were expensed. On May 22, 2002 the Company announced the release of iRenaissance version 5.7. This version was significantly changed from the prior versions. Previous to this release, upgrades from any version less than 4.4 to the latest version were technically challenging resulting in an environment not conducive to customer upgrades. Version 5.7 offered a straight-forward upgrade capability to customers on previous versions. In addition, version 5.7 contained a new

"engine" at its core, which significantly changed the way the software operated internally, and resulted in improved operating efficiencies. Since customers on versions lower than 4.4 could now upgrade without difficulty, the Company was able to discontinue the development and support of all versions prior to 4.4. No further sales using these versions would be contemplated. This had the effect of rendering all releases of iRenaissance which were lower than 4.4 obsolete. Since iRenaissance versions lower than 4.4 would not contribute any further license revenue to the Company, and renewable maintenance revenue would soon be in respect of the newly released version of the product rather than an older version, the related unamortized software-project balances amounting to $3,333,000 were expensed. During May 2002, the Company terminated further work on general enhancements of the COBOL technology based Renaissance Classic product line. Following prolonged, unfruitful attempts to garner interest in the proposed enhancements from the customer base, a twofold decision was made; to continue working with specific customers on custom product development, and to introduce a general sales program of free software license upgrade from the Classic product to the latest release of the iRenaissance product line for customers who remain on maintenance. The company will continue to support those customers who remain active users until they schedule their upgrade conversion to iRenaissance. Since no future revenue benefits are expected from the general enhancements capitalized to date, the aggregate, unamortized software-project balances amounting to $1,174,000 were expensed. The aggregate value of unamortized impaired software expensed in the fourth quarter of fiscal 2002 was $10,938,000. This action will have the effect of reducing software cost amortization in future years. If the Company had not recorded this expense, additional amortization expense of approximately $2,734,000 would be recorded during 2003. F-14 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (2) ACQUISITIONS AND NOTE RECEIVABLE FROM RELATED PARTY On December 30, 1996, the Company acquired a 100% ownership interest in Ross Systems Iberica, its distributor in Spain and Portugal for the prior five years, in exchange for shares of the Company's common stock valued at approximately $1,400,000. The acquisition was a non-cash stock exchange which was accounted for under the purchase method of accounting. Accordingly, the results of operations of the acquired business have been included in the Company's results of operations since the date of acquisition. The purchase agreement mandated that the purchase price be guaranteed based on security prices as of a date which had been mutually extended by the parties and coincided with the extension of the maturity to July 8, 2003 of a non-interest bearing, recourse note receivable, owed by the former majority shareholder of Ross Systems Iberica to the Company. The former majority shareholder is currently an employee of the Company. The Company, in its sole discretion, could make up any difference between the value of the shares originally tendered and the guaranteed purchase price of Ross Iberica either by issuing additional shares or by paying cash. The note receivable described herein totaled $850,000 and was satisfied in full during March 2003, in conjunction with the treasury stock transaction discussed below. At the time of acquisition, the seller was issued 10% of the purchase price in unrestricted shares with the remainder of the shares restricted. As of December 31, 2002, the former majority shareholder still held 20,000 restricted shares which were all the restricted shares that were issued to him at the time of acquisition. During January 2003, the Company sought and received a unanimous written consent from its Board of Directors to issue additional shares to the former majority shareholder to satisfy the guaranteed purchase price agreement. On the date of the Board consent, the share price was $9. Accordingly, the Company issued 120,000 additional shares to satisfy the purchase price agreement. Since the guaranteed purchase price was based on security prices and was not based on an earn out factor or any other performance measure, this share issuance resulted only in a change in the number of common shares outstanding. On the same day as the issuance of these additional shares, the Company entered into an agreement with the former majority shareholder that allowed the Company to repurchase the former majority shareholder's shares at $9 per share. During January, 2003, the Company purchased these shares into treasury stock at the agreed upon $9 per share. The Company anticipated that these treasury shares would be issued to satisfy conversions of its outstanding mandatorily convertible preferred shares which must occur prior to or on June 30, 2006. (3) PROPERTY AND EQUIPMENT A summary of property and equipment follows (in thousands) : JUNE 30, ------------------------ (IN THOUSANDS) 2003 2002 ------- ------- Computer equipment .... $ 5,747 $ 5,691 Furniture and fixtures .... 1,187 1,143 Leasehold improvements .... 838 1,508 ------- ------- 7,772 8,342 Less accumulated depreciation and amortization .... (6,366) (6,892) ------- ------- $ 1,406 $ 1,450 ======= ======= (4) OTHER ASSETS A summary of other assets follows (in thousands): JUNE 30, ------------------------ (IN THOUSANDS) 2003 2002 ------- ------- Goodwill.......................... $ 4,414 $ 4,414 Note receivable .... 750 750 Other .... 62 62 ------- ------- 5,226 5,226 Less accumulated amortization ..... (2,233) (2,233) ------- ------- $ 2,993 $ 2,993 ======= ======= F-15 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (5) ACCRUED EXPENSES A summary of accrued expenses follows (in thousands): JUNE 30, --------------------- (IN THOUSANDS) 2003 2002 ------ ------ Accrued vacation, salary and related compensation costs .... $1,583 $1,502 Sales, Use, VAT and GST taxes payable .... 1,334 1,159 Interest payable .... 38 63 Professional fees .... 244 281 Royalties .... 844 806 Other .... 897 665 ------ ------ $4,940 $4,476 ====== ====== (6) DEBT The Company has a revolving credit facility with an asset-based lender with a maximum credit line for up to $5,000,000, an expiration date of September 23, 2004, and an interest rate equal to the Prime Rate plus 2% (6.25% at June 30, 2003). Borrowings under the credit facility are collateralized by substantially all the assets of the Company. The revolving credit facility may be withdrawn if, amongst other things (a) the Company fails to pay any principal or interest amount due or (b) there is a material impairment of the Company's business which would prevent loan repayment and (c) any of these events are not remedied by the Company within allowable periods. At June 30, 2003, the Company had $2,131,000 outstanding against the $5,000,000 revolving credit facility and at June 30, 2002, approximately $3,370,000 was outstanding under the Company's revolving credit facility. The Company maintains other credit facilities in Spain with various expiration dates over a period of twelve months from June 30, 2003. Interest on these facilities ranges from 6% to 8% and the facilities are collateralized by various assets of the Spanish subsidiary. Balances outstanding under these agreements were approximately $669,000 and $597,000 at June 30, 2003 and 2002 respectively. (7) COMMITMENTS AND CONTINGENCIES Leases The Company leases facilities and certain equipment under operating leases which expire at various dates through fiscal 2016. Certain leases include renewal options and rental escalation clauses to reflect changes in price indices, real estate taxes, and maintenance costs. As of June 30, 2003, future minimum lease payments under non-cancelable operating leases were as follows (in thousands): FISCAL YEAR ----------- 2004.. 1,384 2005.. 816 2006.. 634 2007.. 442 Thereafter... 1,980 ------ Total future minimum lease payments.................... $5,256 ====== Rent expense approximated $1,189,000, $1,236,000, and $2,267,000, for fiscal 2003, 2002, and 2001,

respectively. F-16 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS Litigation a) On June 30, 1998, the Company entered into a distribution agreement with an existing Dutch systems integrator which entitled Ross to distribute a certain project accounting product the systems integrator was developing. The agreement contained certain minimum annual payments totaling $1,500,000 which, unless the agreement was properly canceled (as defined in the agreement) by Ross, would become due to the systems integrator if the Company did not achieve certain minimum annual sales quotas. The agreement also required that the Company use the systems integrator's personnel for certain implementation and maintenance activities. Over the next few years, the distributor, in Ross' view, failed to consistently successfully implement the project accounting product at multiple North American sites. These failures cost the Company between $300,000 and $400,000 in legal fees, uncollectible accounts receivable and settlement costs. In February 2001, the Company cancelled the agreement with the systems integrator. The parties were not able to reach mutual agreement regarding the terms of a settlement, and the systems integrator invoked the arbitration clause of the agreement in late 2001. The arbitration was commenced before the International Court of Arbitration in Paris, France, with the systems integrator ultimately seeking multiple damages aggregating more than $4,000,000. See note 14 for recent developments regarding the outcome of this matter. b) On February 28, 2001, the Company completed the sale of certain assets related to its Human Resource and Payroll product line to Now Solutions, LLC, (NOW), a majority owned subsidiary of Vertical Computer Systems Inc.(Vertical). Arglen Acquisitions (Arglen), was also a party to the transaction as a minority member of NOW. The gross asset sale price was $6,100,000. The purchase price consisted of cash of $5,100,000 and a note payable by NOW to Ross of $1,000,000. The note was non-interest bearing and was due in two installments; $250,000 due on February 28, 2002 and $750,000 due on February 28, 2003. NOW defaulted on the second installment of $750,000 which remains outstanding and is accruing interest at the rate of 10% per annum, the default interest rate as defined in the note. On February 27, 2003, the day before the final note installment was due, Vertical filed a derivative suit on behalf of NOW against Ross and others alleging breach of contract, fraud, conspiracy and breach of fiduciary duty. The suit alleges that Ross failed to schedule approximately $3,600,000 of liabilities related to maintenance agreements assumed by NOW. The suit also alleges that Ross failed to disclose to NOW a transaction brokerage fee of $600,000 that Ross was to pay to Arglen, whose CEO signed the fee agreement and who was also the CEO of NOW. The suit also alleges that Ross should be jointly and severally liable for certain alleged frauds committed by other defendants in which Ross allegedly conspired. The suit further seeks a setoff against the remaining note payment based on the above alleged damages, and the recovery of its attorneys' fees and costs. Ross denies and has contested each and every one of Vertical's claims. The Company does not believe currently that the outcome of range of outcomes is determinable, nor does it believe that should the outcome be unfavorable that it would be materially detrimental to the Company's liquidity. See note 14 for recent developments regarding the outcome of this matter. (8) CAPITAL STOCK Mandatorily Convertible Preferred Stock and Private Placement In fiscal 1991, the Company authorized a new class of no par value preferred stock consisting of 5,000,000 shares. The Board of Directors is authorized to issue the preferred stock in one or more series and to fix the rights, preferences, privileges and restrictions of such stock, including dividend rights, dividend rates, conversion rights, voting rights, terms of redemption, redemption prices, liquidation preferences and the number of shares constituting any series or the designation of such series, without further vote or action by the shareholders. All preferred stock was issued with a mandatory conversion feature. F-17 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS On June 29, 2001, the Company issued mandatorily convertible preferred stock to a qualified investor in a private placement transaction. In summary, the investor purchased 500,000 preferred shares at $4 per share yielding $2,000,000 for the Company. This price represented a premium to the market for the Company's common stock at the time of issuance. The average closing share price of the Company's common stock for the 30 trading days prior to the private placement was approximately $2.22. The preferred shares can be converted at $4.00 per share after June 29, 2002 but before June 29, 2006, on a one for one basis. The shares earn dividends at the rate of 7.5%. In conjunction with this transaction, the Company issued warrants to the broker who assisted in securing the investor. These warrants were fairly valued at $60,000 on the date of issuance and the expense has been recorded in the statement of operations as a component of other expense (net) in the quarter ended June 30, 2001. On April 27, 2001 the Company executed a reverse stock split on the basis of 1 share for 10 shares. (9) SUBSEQUENT EVENTS Announcement of Proposed Merger In early September 2003, the Company announced that it signed a definitive agreement whereby chinadotcom Software (CDC) will acquire Ross Systems in a merger. See note 14 for recent developments regarding the merger. (10) EMPLOYEE STOCK PLANS (a) Stock Option Plan The Company has reserved 210,000 shares of common stock for issuance under its 1988 Incentive Stock Plan and 810,000 shares of common stock for issuance under its 1998 Incentive Stock Plan (collectively the "Plans"). The 1988 Incentive Stock Plan is closed and may not be used for further issues of options. Under the Plans, the Company may issue options to purchase shares of the Company's common stock to eligible employees, officers, directors, independent contractors and consultants. The term of the options issued under the Plans cannot exceed ten years from the date of grant. Options granted to date generally become exercisable over four to five years based on the grantees' continued service with the Company. A summary of the status of the Company's Plan as of June 30, 2003, 2002 and 2001 and activity for the fiscal years then ended is presented below: NUMBER OF WEIGHTED AVERAGE SHARES EXERCISE PRICE EXERCISABLE ---------- ----------------- ----------- Balance as of June 30, 2000 .... 203,600 $ 28.70 102,800 Granted (at market value) .... 165,219 $ 4.90 Cancelled/forfeited .... (77,148) $ 21.80 -------- Balance as of June 30, 2001 .... 291,671 $ 16.91 112,255 Granted (at market value) .... 137,333 $ 4.91 Exercised .... (10,243) $ 2.32 Cancelled/forfeited .... (91,966) $ 20.34 -------- Balance as of June 30, 2002 .... 326,795 $ 10.78 113,494 Granted (at market value) .... 252,828 $ 8.01 Exercised .... (31,048) $ 3.23 Cancelled /forfeited .... (19,756) $ 18.27 -------- Balance as of June 30, 2003 .... 528,819 $ 9.62 154,615 ======= F-18 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS The weighted average estimated grant date fair value of options granted during fiscal 2003, 2002, and 2001 was $4.44, $3.73, and $4.49, respectively. The following table summarizes information about the stock options outstanding at June 30, 2003: OPTIONS OUTSTANDING -- WEIGHTED AVERAGE OPTIONS EXERCISABLE REMAINING ------------------------------ RANGE OF EXERCISE SHARES CONTRACTUAL WEIGHTED AVERAGE SHARES WEIGHTED AVERAGE PRICES OUTSTANDING LIFE EXERCISE PRICE EXERCISABLE EXERCISE PRICE ------------------ ----------- ----------- ----------------- ----------- ---------------- $1.88-$1.88 .... 50,613 7.5 years $ 1.88 16,041 $ 1.88 $3.25-$3.25 .... 5,738 8.1 years 3.25 5,738 3.25 $3.50-$3.50 .... 63,441 7.4 years 3.50 12,750 3.50 $3.75-$5.40 .... 34,514 6.5 years 4.71 26,639 4.74 $7.25-$11.88 .... 275,428 9.1 years 7.89 9,987 9.62 $12.99-$25.00 .... 39,615 7.0 years 16.35 25,040 17.28 $25.94-$25.94 .... 39,350 4.1 years 25.94 39,350 25.94 $26.56-$52.50 ....

17,715 4.1 years 33.35 16,665 33.46 $65.00-$65.00 .... 2,100 3.5 years 65.00 2,100 65.00 $67.50-$67.50 .... 305 1.4 years 67.50 305 67.50 ------- --------- --------- ------- --------- Totals .... 528,819 7.8 years $ 9.62 154,615 $ 16.06 ======= ========= ========= ======= ========= (b) Employee Stock Purchase Plan The Company initially reserved 80,000 shares of common stock for issuance under its 1991 Employee Stock Purchase Plan ("ESPP"). In fiscal 1999, the stockholders approved an amendment to the plan whereby the number of shares reserved for issuance was increased to 95,000. An amendment in fiscal 2002 provided that beginning in fiscal 2001 and each year thereafter, the amount reserved for issuance is increased by the lesser of 20,000 shares or 1% of total outstanding common stock. Under the ESPP, the Company's employees may purchase, through payroll deductions of 1% to 10% of compensation, shares of common stock at a price per share that is the lesser of 85% of its fair market value as of the beginning or end of the offering period. Under the ESPP, the Company sold 19,507 shares, 29,146 shares, and 11,409 shares, to employees in fiscal 2003, 2002, and 2001 respectively. The weighted average fair value of those purchase rights granted in fiscal 2003, and 2002, was $2.85 and $0.83, respectively. As of June 30, 2003, 182,922 shares had been issued under the ESPP. (11) INCOME TAXES Gains and losses before income taxes include foreign gains before income taxes of $1,507,000, and foreign losses before income taxes of $30,000 for fiscal 2003. Foreign gains before income taxes were $2,425,000 for fiscal 2002 and foreign losses before income taxes were $(1,280,000) for fiscal year 2001. Income tax expense for the years ended June 30, 2003, 2002 and 2001 consists of the following (in thousands): 2003 2002 2001 ----- ----- ----- Current: Federal .... $ 142 $ - $(140) Foreign .... - 112 123 State .... 263 20 26 ----- ----- ----- 405 132 9 ----- ----- ----- Deferred: Federal .... -- -- -- Foreign .... -- -- -- State .... -- -- -- ----- ----- ----- -- -- -- ----- ----- ----- $ 405 $ 132 $ 9 ===== ===== ===== F-19 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS For the years ended June 30, 2003, 2002, and 2001, the reconciliation between the amounts computed by applying the United States federal statutory tax rate of 34% to loss before income taxes and the actual tax expense follows (in thousands): 2003 2002 2001 ------- ------- ------- Income tax expense (benefit) at statutory rate .... $ 1,568 $(3,159) $ (283) State income tax expense (benefit), net of federal income tax benefit ..... 170 (13) (37) Change in beginning of year valuation allowance .... (1,195) 3,028 3,063 Losses for which no benefit is recognized (foreign loss and rate) .... - - 435 Rate differential related to foreign income and foreign tax withholdings .... - 843 485 Amortization of other assets and other permanent differences .... (138) (567) (3,654) ------- ------- ------- $ 405 $ 132 $ 9 ======= ======= ======= The tax effects of temporary differences that give rise to significant portions of deferred tax assets and deferred tax liabilities at June 30, 2003 and 2002 were as follows (in thousands): 2003 2002 -------- -------- Accruals and reserves .... $ 428 $ 670 Net operating loss carryforward (federal) .... 11,686 11,502 Net operating loss carryforward (state) .... 1,521 2,386 Net operating loss carryforward (foreign) .... 2,300 2,748 Tax credit carryforwards .... 3,802 3,802 Fixed assets depreciation differences .... 407 399 -------- -------- Total gross deferred tax assets .... 20,144 21,507 Less valuation allowance .... (14,698) (15,893) -------- -------- Net deferred tax assets .... 5,446 5,614 -------- -------- Capitalized computer software costs .... (5,446) (5,614) -------- -------- Total gross deferred liabilities .... (5,446) (5,614) -------- -------- Net deferred taxes .... $ - $ - ======== ======== The net change in total valuation allowance for the year ended June 30, 2003, was a decrease of approximately $1,195,000. The valuation allowance has been established to recognize the uncertainty of utilizing loss and credit carryovers and certain deferred assets. At June 30, 2003, the Company had net operating loss carry-forwards of approximately $34,370,000, $25,354,000 and $7,187,000 for federal, state and foreign tax purposes, respectively. At June 30, 2003, the Company also had unused research and other credit carry-forwards of approximately $3,368,000 and $208,000 for federal and California tax purposes, respectively. The loss and research credit carry-forwards, if not utilized, will expire between fiscal 2005 and 2020. (12) SUPPLEMENTAL CASH FLOW INFORMATION Supplemental cash flow information for the years ended June 30, 2003, 2002, and 2001 follows (in thousands): 2003 2002 2001 ------ ------ ------ Cash payments: Interest .... $ 349 $ 642 $1,228 Income taxes .... $ 121 $ 319 $ 75 Non-cash investing and financing activities: Conversion of convertible debentures into stock (non-cash transaction) .... $ - $ - $1,177 F-20 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (13) SELECTED UNAUDITED QUARTERLY INFORMATION (IN THOUSANDS, EXCEPT PER SHARE DATA) QUARTER ENDED JUNE 30 MARCH 31 DEC.31 SEPT. 30 FISCAL YEAR 2003 2003 2003 2003 2003 ------- -------- ------- -------- Total net revenues $12,988 $11,513(a) $12,173 $11,426 Cost of software product licenses 979 449 521 346 Net income 1,306 719 1,430 601 Earnings per share - basic 0.49 0.27 0.54 0.23 Earnings per share - diluted 0.40 0.22 0.45 0.20 Number of shares used in per share computation - diluted 3,362 3,387 3,260 3,267 (a) As originally stated, third quarter revenues of $11,420,000 excluded $93,000 of revenue which was recorded originally as a reduction of Costs of consulting, maintenance and other services. QUARTER ENDED JUNE 30 MARCH 31 DEC.31 SEPT. 30 FISCAL YEAR 2002 2002 2002 2001 2001 -------- -------- -------- -------- Total net revenues $ 11,173 $ 11,456 $ 11,425 $ 11,165 Cost of software product licenses 761 403 311 396 Net income (loss) (10,857) 381 488 414 Charge for impairment of capitalized software (10,288) - - - Earnings (loss) per share - basic (4.14) 0.16 0.19 0.16 Earnings (loss) per share - diluted (4.14) 0.13 0.17 0.13 Number of shares used in per share computation - diluted 2,625 3,209 3,152 3,144 (14) RECENT DEVELOPMENTS (UNAUDITED) On November 17, 2003, the Arbitrator in the systems integrator matter described more fully in note 7, announced an award of approximately $2,000,000 in favor of the systems integrator. The Company paid the award before the end of calendar 2003 by funding the payment out of operating cash flows in the ordinary course of business. As a result, the Company recognized a charge of approximately $1,900,000 during the quarter ending December 31, 2003 as $104,000 was previously recorded in accordance with the contract in its normal course. On November 18, 2003, the Supreme Court of the State of New York dismissed all of Vertical Computer Systems (Vertical) claims against Ross described more fully in note 7. Vertical has filed a Notice of Appeal. The Company will continue to defend this matter vigorously. On January 8, 2004, the Company filed a current report on Form 8-K to announce changes to the terms of the previously announced merger with chinadotcom. Under the terms of the merger agreement, as amended, for each share of Ross common stock held, stockholders of Ross Systems may elect to receive either (i) $17.00 in cash or (ii) $19.00 in a combination of cash and CDC common shares for each share of the Company's common stock (the "Common Shares"). CDC common shares will be valued at the average closing price of such shares for the 10 trading days preceding the second trading day before the closing date. Both companies are listed on NASDAQ. F-21 SCHEDULE II ROSS SYSTEMS, INC. AND SUBSIDIARIES VALUATION AND QUALIFYING ACCOUNTS (IN THOUSANDS) ADDITIONS ---------------------- BALANCE AT CHARGED TO CHARGED BEGINNING COSTS AND TO OTHER BALANCE AT DESCRIPTION OF PERIOD EXPENSES ACCOUNTS DEDUCTIONS(1) END OF PERIOD ---------- ---------

-------- -------- ------------- ------------- Year ended June 30, 2003 allowance for doubtful accounts and returns .... $3,379 $ 831 $ - $2,676 $1,532 ------ ------ --- ------ ------ Year ended June 30, 2002 allowance for doubtful accounts and returns .... $2,930 $1,444 $ - $ 995 $3,379 ------ ------ --- ------ ------ Year ended June 30, 2001 allowance for doubtful accounts and returns .... $3,571 $1,514 $ - $2,155 $2,930 ------ ------ --- ------ ------ ------------- (1) Represents net charge-off of specific receivables. S-1