

AMERICAN SOFTWARE INC

Form 10-Q

December 08, 2017

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended October 31, 2017

OR

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

For the transition period from _____ to _____

Commission File Number: 0-12456

AMERICAN SOFTWARE, INC.

(Exact name of registrant as specified in its charter)

Georgia
(State or other jurisdiction of

58-1098795
(IRS Employer

incorporation or organization)

Identification Number)

470 East Paces Ferry Road, N.E., Atlanta, Georgia
(Address of principal executive offices)

30305
(Zip Code)

(404) 261-4381

(Registrant's telephone number, including area code)

None

(Former name, former address and former fiscal year, if changed since last report)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the exchange act.

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

| Classes | Outstanding at December 5, 2017 |
|---------------------------------------|--|
| Class A Common Stock, \$.10 par value | 27,896,254 Shares |
| Class B Common Stock, \$.10 par value | 2,256,588 Shares |

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AMERICAN SOFTWARE, INC. AND SUBSIDIARIES

Form 10-Q

Quarter ended October 31, 2017

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Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****American Software, Inc. and Subsidiaries****Condensed Consolidated Balance Sheets (unaudited)****(in thousands, except share data)**

| | October 31, 2017 | April 30, 2017 |
|---|-----------------------------|---------------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 61,242 | \$ 66,001 |
| Investments | 19,221 | 19,332 |
| Trade accounts receivable, less allowance for doubtful accounts of \$124 at October 31, 2017 and \$171 at April 30, 2017: | | |
| Billed | 14,126 | 17,060 |
| Unbilled | 2,502 | 2,811 |
| Prepaid expenses and other current assets | 5,708 | 4,322 |
| Total current assets | 102,799 | 109,526 |
| Investments Noncurrent | 10,552 | 4,455 |
| Property and equipment, net of accumulated depreciation of \$28,392 at October 31, 2017 and \$28,153 at April 30, 2017 | 2,027 | 2,055 |
| Capitalized software, net of accumulated amortization of \$22,185 at October 31, 2017 and \$20,423 at April 30, 2017 | 9,468 | 8,614 |
| Goodwill | 19,549 | 19,549 |
| Other intangibles, net of accumulated amortization of \$7,110 at October 31, 2017 and \$6,406 at April 30, 2017 | 2,695 | 3,399 |
| Other assets | 1,548 | 1,176 |
| Total assets | \$ 148,638 | \$ 148,774 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 1,326 | \$ 1,541 |
| Accrued compensation and related costs | 3,706 | 3,329 |
| Dividends payable | 3,313 | 3,259 |
| Other current liabilities | 2,277 | 5,171 |
| Deferred revenue | 27,291 | 29,437 |
| Total current liabilities | 37,913 | 42,737 |
| Deferred income taxes | 2,755 | 1,994 |

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| | | |
|--|-------------------|-------------------|
| Long-term deferred revenue | 651 | 214 |
| Other long-term liabilities | 74 | 79 |
| Total liabilities | 41,393 | 45,024 |
| Shareholders' equity: | | |
| Common stock: | | |
| Class A, \$.10 par value. Authorized 50,000,000 shares: Issued 32,442,465 shares at October 31, 2017 and 31,821,508 shares at April 30, 2017 | 3,243 | 3,182 |
| Class B, \$.10 par value. Authorized 10,000,000 shares: Issued and outstanding 2,267,209 shares at October 31, 2017 and 2,393,336 shares at April 30, 2017; convertible into Class A shares on a one-for-one basis | 227 | 239 |
| Additional paid-in capital | 126,104 | 121,280 |
| Retained earnings | 3,230 | 4,608 |
| Class A treasury stock, 4,588,632 shares at October 31, 2017 and April 30, 2017, at cost | (25,559) | (25,559) |
| Total shareholders' equity | 107,245 | 103,750 |
| Commitments and contingencies | | |
| Total liabilities and shareholders' equity | \$ 148,638 | \$ 148,774 |

See accompanying notes to condensed consolidated financial statements unaudited.

Table of Contents**American Software, Inc. and Subsidiaries****Condensed Consolidated Statements of Operations (unaudited)****(in thousands, except earnings per share data)**

| | Three Months Ended October 31, | | Six Months Ended October 31, | |
|---|---|-------------|---|-------------|
| | 2017 | 2016 | 2017 | 2016 |
| Revenues: | | | | |
| License | \$ 2,449 | \$ 3,140 | \$ 6,464 | \$ 7,767 |
| Services and other | 13,049 | 12,349 | 25,091 | 24,570 |
| Maintenance | 10,839 | 10,657 | 21,667 | 21,242 |
| Total revenues | 26,337 | 26,146 | 53,222 | 53,579 |
| Cost of revenues: | | | | |
| License | 1,848 | 1,606 | 3,355 | 3,429 |
| Services and other | 8,195 | 9,044 | 16,122 | 18,097 |
| Maintenance | 2,288 | 2,478 | 4,515 | 5,239 |
| Total cost of revenues | 12,331 | 13,128 | 23,992 | 26,765 |
| Gross margin | 14,006 | 13,018 | 29,230 | 26,814 |
| Research and development | 2,643 | 3,169 | 5,151 | 6,269 |
| Sales and marketing | 4,437 | 5,202 | 9,670 | 10,672 |
| General and administrative | 3,616 | 3,690 | 7,155 | 7,201 |
| Amortization of acquisition-related intangibles | 68 | 249 | 391 | 317 |
| Total operating expenses | 10,764 | 12,310 | 22,367 | 24,459 |
| Operating income | 3,242 | 708 | 6,863 | 2,355 |
| Other income (expense): | | | | |
| Interest income | 354 | 278 | 717 | 595 |
| Other, net | 322 | (445) | 558 | (102) |
| Earnings before income taxes | 3,918 | 541 | 8,138 | 2,848 |
| Income tax expense | 1,438 | 129 | 2,933 | 748 |
| Net earnings | \$ 2,480 | \$ 412 | \$ 5,205 | \$ 2,100 |
| Earnings per common share ^(a) : | | | | |
| Basic | \$ 0.08 | \$ 0.01 | \$ 0.17 | \$ 0.07 |

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| | | | | |
|--|---------|---------|---------|---------|
| Diluted | \$ 0.08 | \$ 0.01 | \$ 0.17 | \$ 0.07 |
| Cash dividends declared per common share | \$ 0.11 | \$ 0.11 | \$ 0.22 | \$ 0.22 |
| Shares used in the calculation of earnings per common share: | | | | |
| Basic | 29,906 | 29,135 | 29,788 | 29,037 |
| Diluted | 30,229 | 29,548 | 30,110 | 29,398 |

- (a) Basic per share amounts are the same for Class A and Class B shares. Diluted per share amounts for Class A shares are shown above. Diluted earnings per share for Class B shares under the two-class method are \$0.08 and \$0.01 for the three months ended October 31, 2017 and 2016, and \$0.17 and \$0.07 for the six months ended October 31, 2017 and 2016, respectively. See Note D to the Condensed Consolidated Financial Statements.

See accompanying notes to condensed consolidated financial statements unaudited.

Table of Contents**American Software, Inc. and Subsidiaries****Condensed Consolidated Statements of Cash Flows (unaudited)****(in thousands)**

| | Six Months Ended October 31, | |
|---|---|-------------|
| | 2017 | 2016 |
| Cash flows from operating activities: | | |
| Net earnings | \$ 5,205 | \$ 2,100 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | |
| Depreciation and amortization | 2,705 | 3,043 |
| Stock-based compensation expense | 793 | 778 |
| Net gain on investments | (381) | (394) |
| Deferred income taxes | 761 | (262) |
| Changes in operating assets and liabilities, net of effects of acquisition: | | |
| Purchases of trading securities | (14,057) | (2,509) |
| Proceeds from maturities and sales of trading securities | 8,452 | 7,654 |
| Accounts receivable, net | 3,243 | 5,692 |
| Prepaid expenses and other assets | (1,758) | (1,231) |
| Accounts payable and other liabilities | (2,734) | (2,277) |
| Deferred revenue | (1,709) | (2,959) |
| Net cash provided by operating activities | 520 | 9,635 |
| Cash flows from investing activities: | | |
| Capitalized computer software development costs | (2,617) | (1,606) |
| Purchases of property and equipment, net of disposals | (212) | (329) |
| Purchase of business, net of cash acquired | | (4,441) |
| Net cash used in investing activities | (2,829) | (6,376) |
| Cash flows from financing activities: | | |
| Proceeds from exercise of stock options | 4,079 | 2,203 |
| Payment for accrued acquisition consideration | | (200) |
| Dividends paid | (6,529) | (6,097) |
| Net cash used in financing activities | (2,450) | (4,094) |
| Net change in cash and cash equivalents | (4,759) | (835) |
| Cash and cash equivalents at beginning of period | 66,001 | 49,004 |
| Cash and cash equivalents at end of period | \$ 61,242 | \$ 48,169 |

See accompanying notes to condensed consolidated financial statements unaudited.

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AMERICAN SOFTWARE, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements Unaudited

October 31, 2017

A. Basis of Presentation and Principles of Consolidation

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required for complete financial statements. In the opinion of our management, these condensed consolidated financial statements contain all normal recurring adjustments considered necessary for a fair presentation of the Company's financial position at October 31, 2017, the results of operations for the three and six months ended October 31, 2017 and 2016 and cash flows for the six months ended October 31, 2017 and 2016. The Company's results for the three and six months ended October 31, 2017 are not necessarily indicative of the results expected for the full year. You should read these statements in conjunction with our audited consolidated financial statements and management's discussion and analysis and results of operations included in our Annual Report on Form 10-K for the fiscal year ended April 30, 2017.

The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities, at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Note 1 in the Notes to the Consolidated Financial Statements for the fiscal year ended April 30, 2017 describes the significant accounting policies that we have used in preparing our financial statements. On an ongoing basis, we evaluate our estimates, including but not limited to those related to revenue/vendor specific objective evidence (VSOE), capitalized software costs, goodwill, intangible assets, stock-based compensation, income taxes and contingencies. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Our actual results could differ materially from these estimates under different assumptions or conditions.

Principles of Consolidation

The accompanying unaudited condensed consolidated financial statements include the accounts of American Software, Inc. and its wholly-owned subsidiaries (American Software or the Company). All significant intercompany balances and transactions have been eliminated in consolidation.

B. Revenue Recognition

We recognize revenue in accordance with the Software Revenue Recognition Topic of the Financial Accounting Standards Board's (FASB) Accounting Standards Codification.

License. We recognize license revenue in connection with license agreements for standard proprietary software upon delivery of the software, provided we consider collection to be probable, the fee is fixed or determinable, there is evidence of an arrangement, and VSOE exists with respect to any undelivered elements of the arrangement. For

multiple-element arrangements, we recognize revenue under the residual method, whereby (1) the total fair value of the undelivered elements, as indicated by VSOE, is deferred and subsequently recognized and (2) the difference between the total arrangement fee and the amount deferred for the undelivered elements is recognized as revenue related to the delivered elements. We record revenues from sales of third-party products in accordance with Principal Agent Considerations within the Revenue Recognition Topic of the FASB's Accounting Standards Codification. Furthermore, we evaluate sales through our indirect channel on a case-by-case basis to determine whether the transaction should be recorded gross or net, including but not limited to assessing whether or not we: (1) act as principal in the transaction, (2) take title to the products, (3) have risks and rewards of ownership, such as the risk of loss for collection, delivery, or returns, and (4) act as an agent or broker with compensation on a commission or fee basis. Accordingly, in most cases we record our sales through the Demand Management, Inc. (DMI) channel on a gross basis.

Maintenance. Revenue derived from maintenance contracts primarily includes telephone consulting, product updates, and releases of new versions of products previously purchased by the customer, as well as error reporting and correction services. Maintenance contracts are typically sold for a separate fee with initial contractual periods ranging from one to three years with renewal for additional periods thereafter. Maintenance fees are generally billed annually in advance. We recognize maintenance revenue ratably over the term of the maintenance agreement. In situations where we bundle all or a portion of the maintenance fee with the license fee, VSOE for maintenance is determined based on prices when sold separately.

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Services. Revenue derived from services primarily includes consulting, implementation, and training. We primarily bill fees under time and materials arrangements and recognize them as we perform the services. In accordance with the other presentation matters within the Revenue Recognition Topic of the FASB's Accounting Standards Codification, we recognize amounts received for reimbursement of travel and other out-of-pocket expenses incurred as revenue in the condensed consolidated statements of operations under services and other. These amounts totaled approximately \$421,000 and \$947,000 for the three and six months ended October 31, 2017, respectively, and approximately \$534,000 and \$1.2 million for the three and six months ended October 31, 2016, respectively.

Software-as-a-Service (SaaS) revenues include fees for the right to use the software for a limited period of time in a hosted environment by the Company or by a third party and the customer accesses and uses the software on an as-needed basis over the Internet or via a dedicated line; however, the customer has no ability to take delivery of the software. The underlying arrangements typically include a single fee for the service that is billed monthly, quarterly or annually. SaaS revenues are recognized ratably over the subscription (which rolls into Services Revenue) over the committed services period once the services commence.

Indirect Channel Revenue. We recognize revenues for sales made through indirect channels principally when the distributor makes the sale to an end-user, the license fee is fixed or determinable, the license fee is nonrefundable, and the sale meets all other conditions for revenue recognition.

Deferred Revenue. Deferred revenue represents advance payments or billings for software licenses, services, and maintenance billed in advance of the time revenue is recognized.

Sales Taxes. We account for sales taxes collected from customers on a net basis.

Unbilled Accounts Receivable. The unbilled receivable balance consists of amounts generated from license fee and services revenues. At October 31, 2017 and April 30, 2017, unbilled license fees were approximately \$76,000 and \$1.0 million, respectively, and unbilled services revenues were approximately \$2.4 million and \$1.8 million, respectively. Unbilled license fee accounts receivable represents revenue that has been recognized, but under the terms of the license agreement, which include specified payment terms that are considered normal and customary, certain payments have not yet been invoiced to the customers. Unbilled services revenues primarily occur due to the timing of the respective billings, which occur subsequent to the end of each reporting period.

C. Declaration of Dividend Payable

On August 24, 2017, our Board of Directors declared a quarterly cash dividend of \$0.11 per share of our Class A and Class B Common Stock. The cash dividend is payable on December 4, 2017 to Class A and Class B shareholders of record at the close of business on November 10, 2017.

D. Earnings Per Common Share

We have two classes of common stock, of which Class B Common Shares are convertible into Class A Common Shares at any time, on a one-for-one basis. Under our Articles of Incorporation, if we declare dividends, holders of Class A Common Shares shall receive a \$0.05 dividend per share prior to the Class B Common Shares receiving any dividend and holders of Class A Common Shares shall receive a dividend at least equal to Class B Common Shares dividends on a per share basis. As a result, we have computed the earnings per share in accordance with Earnings Per Share within the Presentation Topic of the FASB's Accounting Standards Codification, which requires companies that have multiple classes of equity securities to use the two-class method in computing earnings per share.

For our basic earnings per share calculation, we use the two-class method. Basic earnings per share are calculated by dividing net earnings attributable to each class of common stock by the weighted average number of shares outstanding. All undistributed earnings are allocated evenly between Class A and B Common Shares in the earnings per share calculation to the extent that earnings equal or exceed \$0.05 per share. This allocation is based on management's judgment after considering the dividend rights of the two classes of common stock, the control of the Class B shareholders and the convertibility rights of the Class B Common shares to Class A Common shares.

The calculation of diluted earnings per share is similar to the calculation of basic earnings per share, except that the calculation includes the dilutive effect of the assumed exercise of options issuable under our stock incentive plans. For our diluted earnings per share calculation for Class A Common Shares, we use the if-converted method. This calculation assumes that all Class B Common Shares are converted into Class A Common Shares (if antidilutive) and, as a result, assumes there are no holders of Class B Common Shares to participate in undistributed earnings.

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For our diluted earnings per share calculation for Class B Common Shares, we use the two-class method. This calculation does not assume that all Class B Common Shares are converted into Class A Common Shares. In addition, this method assumes the dilutive effect if Class A stock options were converted to Class A Common Shares and the undistributed earnings are allocated evenly to both Class A and B Common Shares including Class A Common Shares issued pursuant to those converted stock options. This allocation is based on management's judgment after considering the dividend rights of the two classes of common stock, the control of the Class B shareholders and the convertibility rights of the Class B Common Shares into Class A Common Shares.

The following tables set forth the computation of basic earnings per common share and diluted earnings per common share (in thousands except for per share amounts):

Basic earnings per common share:

| | Three Months Ended October 31, 2017 | | Six Months Ended October 31, 2017 | |
|--|--|----------------|--|----------------|
| | Class A | Class B | Class A | Class B |
| Distributed earnings | \$ 0.11 | \$ 0.11 | \$ 0.22 | \$ 0.22 |
| Undistributed losses | (0.03) | (0.03) | (0.05) | (0.05) |
| Total | \$ 0.08 | \$ 0.08 | \$ 0.17 | \$ 0.17 |
| Distributed earnings | \$ 3,064 | \$ 249 | \$ 6,078 | \$ 505 |
| Undistributed losses | (768) | (65) | (1,269) | (109) |
| Total | \$ 2,296 | \$ 184 | \$ 4,809 | \$ 396 |
| Basic weighted average common shares outstanding | 27,589 | 2,317 | 27,448 | 2,340 |

| | Three Months Ended October 31, 2016 | | Six Months Ended October 31, 2016 | |
|--|--|----------------|--|----------------|
| | Class A | Class B | Class A | Class B |
| Distributed earnings | \$ 0.11 | \$ 0.11 | \$ 0.21 | \$ 0.21 |
| Undistributed losses | (0.10) | (0.10) | (0.14) | (0.14) |
| Total | \$ 0.01 | \$ 0.01 | \$ 0.07 | \$ 0.07 |
| Distributed earnings | \$ 2,943 | \$ 268 | \$ 5,609 | \$ 511 |
| Undistributed losses | (2,565) | (234) | (3,680) | (340) |
| Total | \$ 378 | \$ 34 | \$ 1,929 | \$ 171 |
| Basic weighted average common shares outstanding | 26,703 | 2,432 | 26,580 | 2,457 |

Diluted EPS for Class A Common Shares Using the If-Converted Method

Three Months Ended October 31, 2017

| | Undistributed & Distributed Earnings to Class A Common | Class A Common Shares | EPS* |
|---------------------------------------|---|--------------------------------------|-------------|
| Per Basic | \$ 2,296 | 27,589 | \$ 0.08 |
| Common Stock Equivalents | | 323 | |
| | 2,296 | 27,912 | 0.08 |
| Class B Conversion | 184 | 2,317 | |
| Diluted EPS for Class A Common Shares | \$ 2,480 | 30,229 | \$ 0.08 |

Table of Contents**Six Months Ended October 31, 2017**

| | Undistributed & Distributed Earnings to Class A Common | Class A Common Shares | EPS* |
|---------------------------------------|---|--------------------------------------|-------------|
| Per Basic | \$ 4,809 | 27,448 | \$ 0.17 |
| Common Stock Equivalents | | 322 | |
| | 4,809 | 27,770 | 0.17 |
| Class B Conversion | 396 | 2,340 | |
| Diluted EPS for Class A Common Shares | \$ 5,205 | 30,110 | \$ 0.17 |

Three Months Ended October 31, 2016

| | Undistributed & Distributed Earnings to Class A Common | Class A Common Shares | EPS |
|---------------------------------------|---|--------------------------------------|------------|
| Per Basic | \$ 378 | 26,703 | \$ 0.01 |
| Common Stock Equivalents | | 413 | |
| | 378 | 27,116 | 0.01 |
| Class B Conversion | 34 | 2,432 | |
| Diluted EPS for Class A Common Shares | \$ 412 | 29,548 | \$ 0.01 |

Six Months Ended October 31, 2016

| | Undistributed & Distributed Earnings to Class A Common | Class A Common Shares | EPS |
|--------------------------|---|--------------------------------------|------------|
| Per Basic | \$ 1,929 | 26,580 | \$ 0.07 |
| Common Stock Equivalents | | 361 | |
| | 1,929 | 26,941 | 0.07 |
| Class B Conversion | 171 | 2,457 | |

| | | | | |
|---------------------------------------|----|-------|--------|---------|
| Diluted EPS for Class A Common Shares | \$ | 2,100 | 29,398 | \$ 0.07 |
|---------------------------------------|----|-------|--------|---------|

Diluted EPS for Class B Common Shares Using the Two-Class Method

Three Months Ended October 31, 2017

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| | Undistributed & Distributed Earnings to Class B Common | Class B Common Shares | EPS* |
|---|---|--------------------------------------|-------------|
| Per Basic | \$ 184 | 2,317 | \$ 0.08 |
| Reallocation of undistributed earnings to Class A Common Shares from Class B Common Shares | | | |
| Diluted EPS for Class B Common Shares | \$ 184 | 2,317 | \$ 0.08 |

Six Months Ended October 31, 2017

| | Undistributed & Distributed Earnings to Class B Common | Class B Common Shares | EPS* |
|---|---|--------------------------------------|-------------|
| Per Basic | \$ 396 | 2,340 | \$ 0.17 |
| Reallocation of undistributed earnings to Class B Common Shares from Class A Common Shares | 1 | | |
| Diluted EPS for Class B Common Shares | \$ 397 | 2,340 | \$ 0.17 |

Three Months Ended October 31, 2016

| | Undistributed & Distributed Earnings to Class B Common | Class B Common Shares | EPS |
|---|---|--------------------------------------|------------|
| Per Basic | \$ 34 | 2,432 | \$ 0.01 |
| Reallocation of undistributed earnings to Class A Common Shares from Class B Common Shares | 4 | | |
| Diluted EPS for Class B Common Shares | \$ 38 | 2,432 | \$ 0.01 |

Six Months Ended October 31, 2016

| | Undistributed & Distributed Earnings to Class B Common | Class B Common Shares | EPS |
|--|---|--------------------------------------|------------|
| Per Basic | \$ 171 | 2,457 | \$ 0.07 |
| Reallocation of undistributed earnings to Class A shares from Class B shares | 5 | | |
| Diluted EPS for Class B | \$ 176 | 2,457 | \$ 0.07 |

* Amounts adjusted for rounding

For the three and six months ended October 31, 2017, we excluded options to purchase 1,184,124 and 1,105,521 Class A Common Shares, respectively, and for the three and six months ended October 31, 2016, we excluded options to purchase 345,891 and 302,628 Class A Common Shares, respectively, from the computation of diluted earnings per Class A Common Shares. We excluded these option share amounts because the exercise prices of those options were greater than the average market price of the Class A Common Shares during the applicable period. As of October 31, 2017, we had a total of 3,440,512 options outstanding and, as of October 31, 2016, we had a total of 3,517,317 options outstanding.

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E. Stock-Based Compensation

During the six months ended October 31, 2017 and 2016, we granted options to purchase 884,000 and 342,000 shares of common stock, respectively. We recorded stock option compensation cost of approximately \$477,000 and \$389,000 and related income tax benefits of approximately \$137,000 and \$145,000 during the three months ended October 31, 2017 and 2016, respectively. We recorded stock option compensation cost of approximately \$793,000 and \$778,000 and related income tax benefits of approximately \$275,000 and \$285,000 during the six months ended October 31, 2017 and 2016, respectively. We recorded stock-based compensation expense on a straight-line basis over the vesting period directly to additional paid-in-capital.

During the six months ended October 31, 2017 and 2016, we issued 482,000 and 314,000 shares of common stock, respectively, resulting from the exercise of stock options. The total intrinsic value of options exercised during the six months ended October 31, 2017 and 2016 based on market value at the exercise dates was approximately \$1.3 million and \$1.1 million, respectively. As of October 31, 2017, unrecognized compensation cost related to unvested stock option awards approximated \$3.3 million, which we expect to recognize over a weighted average period of 1.79 years.

F. Fair Value of Financial Instruments

We measure our investments based on a fair value hierarchy disclosure framework that prioritizes and ranks the level of market price observability used in measuring assets and liabilities at fair value. A number of factors affect market price observability, including the type of asset or liability and its characteristics. This hierarchy prioritizes the inputs into three broad levels as follows:

Level 1 Quoted prices in active markets for identical instruments.

Level 2 Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets.

Level 3 Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

The following is a general description of the valuation methodologies we use for financial assets and liabilities measured at fair value, including the general classification of such assets and liabilities pursuant to the valuation hierarchy.

Cash Equivalents Cash equivalents include investments in government obligation based money-market funds, other money market instruments and interest-bearing deposits with initial terms of three months or less. The fair value of cash equivalents approximates its carrying value due to the short-term nature of these instruments.

Marketable Securities Marketable securities utilizing Level 1 inputs include active exchange-traded equity securities and equity index funds, and most U.S. Government debt securities, as these securities all have quoted prices in active markets. Marketable securities utilizing Level 2 inputs include municipal bonds. We value these securities using market-corroborated pricing or other models that use observable inputs such as yield curves.

The following tables present our assets and liabilities that we measured at fair value on a recurring basis as of October 31, 2017 and April 30, 2017, respectively, and indicates the fair value hierarchy of the valuation techniques we used to determine such fair value (in thousands):

| | October 31, 2017 | | | |
|-----------------------|--|---|--|-----------|
| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Balance |
| Cash equivalents | \$ 56,832 | \$ | \$ | \$ 56,832 |
| Marketable securities | 11,298 | 18,475 | | 29,773 |
| Total | \$ 68,130 | \$ 18,475 | \$ | \$ 86,605 |

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| April 30, 2017 | | | | |
|-----------------------|---|--|--|------------------|
| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Balance |
| Cash equivalents | \$ 62,647 | \$ | \$ | \$ 62,647 |
| Marketable securities | 8,984 | 14,803 | | 23,787 |
| Total | \$ 71,631 | \$ 14,803 | \$ | \$ 86,434 |

G. Stock Repurchases

On August 19, 2002, our Board of Directors approved a resolution authorizing the repurchase of up to an additional 2.0 million shares of our Class A common stock. We have made and will make these repurchases through open market purchases at prevailing market prices. The timing of any repurchase will depend upon market conditions, the market price of our common stock and management's assessment of our liquidity and cash flow needs. Under this repurchase plan, through October 31, 2017, we have repurchased 1,053,679 shares of common stock at a cost of approximately \$6.2 million. As of October 31, 2017, under all repurchase plans previously authorized, including this most recent plan, we have repurchased a total of 4,588,632 shares of common stock at a cost of approximately \$25.6 million.

H. Comprehensive Income

We have not included condensed consolidated statements of comprehensive income in the accompanying unaudited condensed consolidated financial statements since comprehensive income and net earnings presented in the accompanying condensed consolidated statements of operations would be substantially the same.

I. Industry Segments

We provide our software solutions through three major business segments, which are further broken down into a total of four major product and service groups. The three business segments are (1) Enterprise Resource Planning (ERP), (2) Supply Chain Management (SCM), and (3) Information Technology (IT) Consulting.

The ERP segment consists of (i) American Software ERP, which provides purchasing and materials management, customer order processing, financial, e-commerce and traditional manufacturing solutions, and (ii) New Generation Computing (NGC), which provides industry-specific business software to both retailers and manufacturers in the apparel, sewn products and furniture industries. The SCM segment, which consists of Logility, Inc. (Logility), a wholly-owned subsidiary, as well as its subsidiary, DMI¹, provides collaborative supply chain solutions to streamline and optimize the forecasting, inventory, production, supply, allocation, distribution and management of products between trading partners. The IT Consulting segment consists of The Proven Method, Inc., an IT staffing and consulting services firm. We also provide support for our software products, such as software enhancements, documentation, updates, customer education, consulting, systems integration services, maintenance and support services.

Our chief operating decision maker is the Principal Executive Officer (PEO). While the PEO is apprised of a variety of financial metrics and information, we manage our business primarily on a segment basis, with the PEO evaluating performance based upon segment operating profit or loss that includes an allocation of common expenses, but excludes certain unallocated expenses, which are included in the ERP segment.

¹ Term previously defined page 6.

All of our revenues are derived from external customers. We do not have any inter-segment revenue. Our income taxes and dividends are paid at a consolidated level. Consequently, it is not practical to show these items by operating segment.

In the following table, we have broken down the intersegment transactions applicable to the three and six months ended October 31, 2017 and 2016:

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| | Three Months Ended October 31, | | Six Months Ended October 31, | |
|--|---|-------------|---|-------------|
| | 2017 | 2016 | 2017 | 2016 |
| Revenues: | | | | |
| Enterprise Resource Planning | \$ 3,088 | \$ 2,757 | \$ 5,893 | \$ 5,765 |
| Collaborative Supply Chain Management | 18,653 | 18,125 | 38,364 | 37,536 |
| IT Consulting | 4,596 | 5,264 | 8,965 | 10,278 |
| | \$ 26,337 | \$ 26,146 | \$ 53,222 | \$ 53,579 |
| Operating income (loss) before intersegment eliminations: | | | | |
| Enterprise Resource Planning | \$ (1,333) | \$ (1,614) | \$ (2,849) | \$ (3,029) |
| Collaborative Supply Chain Management | 4,218 | 2,164 | 9,121 | 5,016 |
| IT Consulting | 357 | 158 | 591 | 368 |
| | \$ 3,242 | \$ 708 | \$ 6,863 | \$ 2,355 |
| Intersegment eliminations: | | | | |
| Enterprise Resource Planning | \$ (879) | \$ (880) | \$ (1,834) | \$ (1,759) |
| Collaborative Supply Chain Management | 885 | 897 | 1,840 | 1,792 |
| IT Consulting | (6) | (17) | (6) | (33) |
| | \$ | \$ | \$ | \$ |
| Operating income (loss) after intersegment eliminations: | | | | |
| Enterprise Resource Planning | \$ (2,212) | \$ (2,495) | \$ (4,683) | \$ (4,788) |
| Collaborative Supply Chain Management | 5,103 | 3,061 | 10,961 | 6,808 |
| IT Consulting | 351 | 142 | 585 | 335 |
| | \$ 3,242 | \$ 708 | \$ 6,863 | \$ 2,355 |
| Capital expenditures: | | | | |
| Enterprise Resource Planning | \$ 23 | \$ 121 | \$ 138 | \$ 166 |
| Collaborative Supply Chain Management | 51 | 65 | 68 | 163 |
| IT Consulting | 4 | | 6 | |
| | \$ 78 | \$ 186 | \$ 212 | \$ 329 |
| Capitalized software: | | | | |
| Enterprise Resource Planning* | \$ | \$ | \$ | \$ |
| Collaborative Supply Chain Management | 1,330 | 969 | 2,617 | 1,606 |
| IT Consulting | | | | |
| | \$ 1,330 | \$ 969 | \$ 2,617 | \$ 1,606 |
| Depreciation and amortization: | | | | |

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| | | | | |
|---------------------------------------|----------|----------|----------|----------|
| Enterprise Resource Planning | \$ 55 | \$ 183 | \$ 111 | \$ 326 |
| Collaborative Supply Chain Management | 1,264 | 1,453 | 2,591 | 2,713 |
| IT Consulting | 2 | 2 | 3 | 4 |
| | \$ 1,321 | \$ 1,638 | \$ 2,705 | \$ 3,043 |

Earnings (loss) before income taxes:

| | | | | |
|---------------------------------------|----------|------------|------------|------------|
| Enterprise Resource Planning* | \$ (706) | \$ (1,743) | \$ (1,785) | \$ (2,471) |
| Collaborative Supply Chain Management | 4,267 | 2,126 | 9,332 | 4,951 |
| IT Consulting | 357 | 158 | 591 | 368 |
| | \$ 3,918 | \$ 541 | \$ 8,138 | \$ 2,848 |

* includes certain unallocated expenses.

Major Customer

No one customer accounted for more than 10% of total revenues for the three and six months ended October 31, 2017 and 2016.

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J. Contingencies

We more often than not indemnify our customers against damages and costs resulting from claims of patent, copyright or trademark infringement associated with use of our products. We have historically not been required to make any payments under such indemnifications. However, we continue to monitor the conditions that are subject to the indemnifications to identify whether it is probable that a loss has occurred, and would recognize any such losses under the indemnifications when those losses are estimable. In addition, we warrant to our customers that our products operate substantially in accordance with the software products specifications. Historically, we have incurred no costs related to software product warranties and we do not expect to incur such costs in the future, and as such we have made no accruals for software product warranty costs. Additionally, we are involved in various claims arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on our financial position or results of operations.

K. Subsequent Event

On November 15, 2017, our Board of Directors declared a quarterly cash dividend of \$0.11 per share of our Class A and Class B Common Stock. The cash dividend is payable on February 23, 2018 to Class A and Class B shareholders of record at the close of business on February 9, 2018.

Effective November 21, 2017, the Company acquired certain assets of privately held Halo Business Intelligence (Halo), a California corporation and a supplier of advanced analytics and business intelligence solutions, for the supply chain market, pursuant to the terms of an asset purchase agreement, dated as of November 21, 2017 (the Purchase Agreement).

Halo s advanced analytics will be embedded into the Logility Voyager Solutions advanced analytics platform. These enriched analytics will leverage interactive visualization, machine learning algorithms, and artificial intelligence (AI) to transform both structured and unstructured data to accelerate business planning performance and proactively identify new business opportunities or mitigate risks. Customers on the DMI and NGC platforms will be able to add pre-packaged Halo advanced analytics capabilities to their subscriptions to drive quick insights and appropriate actions for their businesses. In addition, Logility will continue to offer Halo standalone to complement other enterprise systems.

Under the terms of the Purchase Agreement, the Company acquired the assets for cash consideration paid of approximately \$9.25 million, which represents a purchase price of approximately \$9.95 million net of a \$700,000 negative working capital adjustment, subject to certain post-closing adjustments.

The Company will include the forward results of Halo in its consolidated financial statements commencing November 21, 2017. The acquired assets consist primarily of accounts receivable, prepaids, other assets, other intangibles assets and are net of certain customer related liabilities. Acquisition related costs were not material for any period presented in the consolidated financial statements. Based upon the timing of the acquisition being subsequent to the end of the Company s second quarter of fiscal 2018, the preliminary accounting for the business combination is incomplete at the time of filing this report. As a result, the Company is unable to provide amounts recognized as of the acquisition date for major classes of assets and liabilities acquired. The Company will include this information in its quarterly report on Form 10-Q for the third quarter of fiscal 2018.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations **FORWARD-LOOKING STATEMENTS**

This report on Form 10-Q contains forward-looking statements relating to our future financial performance, business strategy, financing plans and other future events that involve uncertainties and risks. You can identify these statements by forward-looking words such as anticipate, intend, plan, continue, could, grow, may, potential, predict, seek, estimate, believe, expect, and similar expressions that convey uncertainty of future events or outcomes. Any forward-looking statements we make herein are pursuant to the safe harbor provision of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include statements concerning future:

results of operations;

liquidity, cash flow and capital expenditures;

demand for and pricing of our products and services;

annual contract value (ACV);

viability and effectiveness of strategic alliances;

industry conditions and market conditions;

acquisition activities and the effect of completed acquisitions; and

general economic conditions.

Although we believe that the goals, plans, expectations, and prospects that our forward-looking statements reflect are reasonable in view of the information currently available to us, those statements are not guarantees of performance. There are many factors that could cause our actual results to differ materially from those anticipated by forward-looking statements made herein. These factors include, but are not limited to, continuing U.S. and global economic uncertainty, the timing and degree of business recovery, unpredictability and the irregular pattern of future revenues, dependence on particular market segments or customers, competitive pressures, delays, product liability and warranty claims and other risks associated with new product development, undetected software errors, market acceptance of our products, technological complexity, the challenges and risks associated with integration of acquired product lines, companies and services, as well as a number of other risk factors that could affect our future performance. All forward-looking statements included in this Form 10-Q are based upon information available to us as of the filing date of this Form 10-Q. We undertake no obligation to update any of these forward-looking statements for any reason. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance, or achievements to differ materially from those expressed or implied by these statements. We discuss certain factors in greater detail in "Business Overview" below.

The terms fiscal 2018 and fiscal 2017 refer to our fiscal years ending April 30, 2018 and 2017, respectively.

ECONOMIC OVERVIEW

Corporate capital spending trends and commitments are the primary determinants of the size of the market for business software. Corporate capital spending is, in turn, a function of general economic conditions in the U.S. and abroad and in particular may be affected by conditions in global credit markets.

In October 2017, the International Monetary Fund (IMF) provided an update to the World Economic Outlook (WEO) for the 2017 and 2018 world economic growth forecast. The update noted that, The global upswing in economic activity is strengthening. Global growth, which in 2016 was the weakest since the global financial crisis at 3.2 percent, is projected to rise to 3.6 percent in 2017 and to 3.7 percent in 2018. The growth forecasts for both 2017 and 2018 are 0.1 percentage point stronger compared with the April 2017 World Economic Outlook (WEO) forecast. Broad-based upward revisions in the euro area, Japan, emerging Asia, emerging Europe, and Russia where growth outcomes in the first half of 2017 were better than expected more than offset downward revisions for the United States and the United Kingdom.

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For the remainder of fiscal 2018, we expect the global economy to improve when compared to the prior year, which could result in an improved selling environment. Overall information technology spending seems to be improving. We believe information technology spending will incrementally improve over the long term as increased global competition forces companies to improve productivity by upgrading their technology systems. Although this improvement could slow or regress at any time, due in part to concerns in global capital markets and general economic conditions, we believe that our organizational and financial structure will enable us to take advantage of any sustained economic rebound. Customers continue to take long periods to evaluate discretionary software purchases.

We believe weak economic conditions may be driving some businesses to focus on achieving more process and efficiency enhancements in their operations and to invest in solutions that improve operating margins, rather than make large infrastructure-type technology purchases. If this trend continues, we believe it may tend to favor solutions such as our Logility supply chain solutions, which are designed to provide a more rapid return on investment and are targeted at some of the largest profit drivers in a customer's business. While the current economic crisis has had a particularly adverse impact on the weaker companies in our target markets, we believe a large percentage of our customers are seeking to make investments to strengthen their operations, and some are taking advantage of current economic conditions to gain market share.

BUSINESS OVERVIEW

American Software was incorporated as a Georgia corporation in 1970. We develop, market and support a portfolio of software and services that deliver enterprise management and collaborative supply chain solutions to the global marketplace. We have designed our software and services to bring business value to enterprises by supporting their operations over intranets, extranets, client/servers or the Internet. References to the Company, our products, our software, our services and similar references include the appropriate business unit actually providing the product or service.

We provide our software solutions through three major business segments, which are further broken down into a total of four major product and service groups. The three business segments are (1) Enterprise Resource Planning (ERP), (2) Supply Chain Management (SCM) and (3) Information Technology (IT) Consulting. The ERP segment consists of (i) American Software ERP, which provides purchasing and materials management, customer order processing, financial, e-commerce and traditional manufacturing solutions, and (ii) New Generation Computing (NGC), which provides industry-specific business software to both retailers and manufacturers in the apparel, sewn products and furniture industries. The SCM segment, which consists of Logility, a wholly-owned subsidiary, as well as its subsidiary, Demand Management, Inc. (DMI), provides collaborative supply chain solutions to streamline and optimize the forecasting, inventory, production, supply, allocation, distribution and management of products between trading partners. The IT Consulting segment consists of The Proven Method, an IT staffing and consulting services firm. We also provide support for our software products, such as software enhancements, documentation, updated, customer education, consulting, systems integration services, maintenance and support services.

We derive revenues primarily from four sources: subscriptions, software licenses, services, and maintenance. We generally determine software license and Software as a Service (SaaS) fees based on the depth of functionality, number of production deployments, users and/or sites licensed and/or subscribed. Services and other revenues consist primarily of fees from software implementation, training, consulting services, SaaS, hosting, and managed services. We bill primarily under time and materials arrangements and recognize revenues as we perform services. Subscription and maintenance agreements typically are for a one- to three-year term, commencing at the time of the initial contract. We generally bill these fees annually in advance under agreements with terms of one to three years, and then recognize the resulting revenues ratably over the term of the agreement. Deferred revenues represent advance payments or billings for subscriptions, software licenses, services and maintenance billed in advance of the time we

recognize the related revenues.

Our cost of revenue for licenses includes amortization of capitalized computer software development costs, royalties paid to third-party software vendors, and agent commission expenses related to license revenues generated by the indirect channel, primarily from DMI. Costs for maintenance and services include the cost of personnel to conduct implementations and customer support, consulting, other personnel-related expenses, and agent commission expenses related to maintenance revenues generated by the indirect channel, primarily from DMI. We account for the development costs of software intended for sale in accordance with the Intangibles Goodwill and Other topic of the Financial Accounting Standards Board's (FASB) Accounting Standards Codification. We monitor the net realizable value of our capitalized software on a quarterly basis based on an estimate of future product revenues. We currently expect to fully recover the value of the capitalized software asset recorded on our consolidated balance sheet; however, if future product revenues are less than management's current expectations, we may incur a write-down of capitalized software costs.

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Our selling expenses generally include the salary and commissions paid to our sales professionals, along with marketing, promotional, travel and associated costs. Our general and administrative expenses generally include the salary and benefits paid to executive, corporate and support personnel, as well as facilities-related costs, utilities, communications expenses, and various professional fees.

We currently view the following factors as the primary opportunities and risks associated with our business:

Dependence on Capital Spending Patterns. There is risk associated with our dependence on the capital spending patterns of U.S. and international businesses, which in turn are functions of economic trends and conditions over which we have no control.

Acquisition Opportunities. There are opportunities for selective acquisitions or investments to provide opportunities to expand our sales distribution channels and/or broaden our product offering by providing additional solutions for our target markets.

Acquisition Risks. There are risks associated with acquisitions of complementary companies, products and technologies, including the risks that we will not achieve the financial and strategic goals that we contemplate at the time of the transaction. More specifically, in any acquisition we will face risks and challenges associated with the uncertain value of the acquired business or assets, the difficulty of assimilating operations and personnel, integrating acquired technologies and products and maintaining the loyalty of the customers of the acquired business.

Competitive Technologies. There is a risk that our competitors may develop technologies that are substantially equivalent or superior to our technology.

Competition in General. There are risks inherent in the market for business application software and related services, which has been and continues to be intensely competitive; for example, some of our competitors may become more aggressive with their prices and/or payment terms, which may adversely affect our profit margins.

A discussion of a number of additional risk factors associated with our business is included in our Annual Report on Form 10-K for the fiscal year ended April 30, 2017, which risk factors have been supplemented by the risk factors appearing in Item 1A of Part II of this report on Form 10-Q.

Recent Accounting Pronouncements

In August 2015, the FASB issued Accounting Standards Update No. 2015-14, *Revenue from Contracts with Customers – Deferral of Effective Date*, which defers the implementation of ASU 2014-09, *Revenue from Contracts with Customers*, for one year from the initial effective date. The initial effective date of ASU No. 2014-09 was for annual reporting periods beginning after December 15, 2016, and early adoption was not permitted. ASU No. 2015-14 extends the effective date to annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. Earlier application is permitted only as of reporting periods beginning after December 16, 2016, including interim reporting periods within that reporting period. The Company has performed a

review of the requirements of the new revenue standard and is monitoring the activity of the FASB as it relates to specific interpretive guidance. The Company is reviewing customer contracts and is in the process of applying the five-step model of the new standard to each contract category it has identified and will compare the results to its current accounting practices. The Company plans to adopt ASU 2014-09, as well as other clarifications and technical guidance issued by the FASB related to this new revenue standard, on May 1, 2018. The Company will likely apply the modified retrospective transition method, which would result in an adjustment to retained earnings for the cumulative effect, if any, of applying the standard to contracts in process as of the adoption date. Under this method, the Company would not restate the prior financial statements presented. Therefore, the new standard would require additional disclosures of the amount by which each financial statement line item is affected in the fiscal year 2019 reporting period.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The ASU is effective for annual periods beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption of the update is permitted. The Company is evaluating the impact of the adoption of this update on our consolidated financial statements and related disclosures.

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Three-Month Comparisons. The following table sets forth certain revenue and expense items as a percentage of total revenues and the percentage changes in those items for the three months ended October 31, 2017 and 2016:

| | Three Months Ended October 31, Percentage of Total Revenues | | Pct. Change in Dollars 2017 vs. 2016 |
|---|--|-------------|---|
| | 2017 | 2016 | |
| Revenues: | | | |
| License | 9% | 12% | (22)% |
| Services and other | 50 | 47 | 6 |
| Maintenance | 41 | 41 | 2 |
| Total revenues | 100 | 100 | 1 |
| Cost of revenues: | | | |
| License | 7 | 6 | 30 |
| Services and other | 31 | 35 | (9) |
| Maintenance | 9 | 9 | (8) |
| Total cost of revenues | 47 | 50 | (4) |
| Gross margin | 53 | 50 | 6 |
| Research and development | 10 | 12 | (17) |
| Sales and marketing | 17 | 20 | (15) |
| General and administrative | 14 | 14 | (1) |
| Amortization of acquisition-related intangibles | | 1 | nm |
| Total operating expenses | 41 | 47 | (15) |
| Operating income | 12 | 3 | 358 |
| Other income: | | | |
| Interest income | 1 | 1 | 27 |
| Other, net | 1 | (2) | nm |
| Earnings before income taxes | 14 | 2 | 624 |
| Income tax expense | 5 | | nm |
| Net earnings | 9% | 2% | 502% |

nm not meaningful

Six-Month Comparisons. The following table sets forth certain revenue and expense items as a percentage of total revenues and the percentage changes in those items for the six months ended October 31, 2017 and 2016:

| | Six Months Ended October 31, Percentage of Total Revenues | | Pct. Change in Dollars 2017 vs. 2016 |
|--------------------|--|-------------|---|
| | 2017 | 2016 | |
| Revenues: | | | |
| License | 12% | 14% | (17)% |
| Services and other | 47 | 46 | 2 |
| Maintenance | 41 | 40 | 2 |
| Total revenues | 100 | 100 | (1) |
| Cost of revenues: | | | |
| License | 6 | 6 | 5 |
| Services and other | 30 | 34 | (11) |
| Maintenance | 9 | 10 | (14) |

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| | Six Months Ended October 31, Percentage of Total Revenues | | Pct. Change in Dollars |
|---|---|------|---------------------------|
| | 2017 | 2016 | 2017 vs. 2016 |
| Total cost of revenues | 45 | 50 | (9) |
| Gross margin | 55 | 50 | 8 |
| Research and development | 10 | 12 | (18) |
| Sales and marketing | 18 | 20 | (9) |
| General and administrative | 13 | 13 | (1) |
| Amortization of acquisition-related intangibles | 1 | 1 | (53) |
| Total operating expenses | 42 | 46 | (10) |
| Operating income | 13 | 4 | 191 |
| Other income: | | | |
| Interest income | 1 | 1 | 21 |
| Other, net | 1 | (0) | nm |
| Earnings before income taxes | 15 | 5 | 186 |
| Income tax expense | 6 | 1 | 292 |
| Net earnings | 9% | 4% | 148% |

nm not meaningful

COMPARISON OF RESULTS OF OPERATIONS FOR THE THREE AND SIX MONTHS ENDED OCTOBER 31, 2017 AND 2016**REVENUES**

| | Three Months Ended October 31, % of Total Revenues | | | 2017 | 2016 |
|--------------------|---|-----------|----------|------|------|
| | 2017 | 2016 | % Change | | |
| | (in thousands) | | | | |
| License | \$ 2,449 | \$ 3,140 | (22)% | 9% | 12% |
| Services and other | 13,049 | 12,349 | 6 | 50 | 47 |
| Maintenance | 10,839 | 10,657 | 2 | 41 | 41 |
| Total revenues | \$ 26,337 | \$ 26,146 | 1% | 100% | 100% |

| | Six Months Ended October 31, | | | | |
|--------------------|------------------------------|-----------|----------|------|------|
| | 2017 | 2016 | % Change | 2017 | 2016 |
| | (in thousands) | | | | |
| License | \$ 6,464 | \$ 7,767 | (17)% | 12% | 14% |
| Services and other | 25,091 | 24,570 | 2 | 47 | 46 |
| Maintenance | 21,667 | 21,242 | 2 | 41 | 40 |
| Total revenues | \$ 53,222 | \$ 53,579 | (1)% | 100% | 100% |

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The 1% increase in revenues over the three months ended October 31, 2017 was attributable primarily to a 6% increase in services and other revenues and, to a lesser extent, a 2% increase in maintenance revenues. This was partially offset by a 22% decrease in license fee revenues for the three months ended October 31, 2017 when compared to the same period last year. The decrease in license fee revenues was attributable to a delay in closing several license fee agreements during the quarter in our SCM business unit and increased sales of our products on Logility's Cloud Services platform that require revenue to be deferred over the life of the contracted period, which is typically one to three years. The primary reason for the increase in services and other revenues in the three months ended October 31, 2017 was an increase in Logility's Cloud Services platform partially offset by a decrease in our IT consulting services unit because of the completion of an IT project from one of our larger customers in the prior period.

Due to intense competition in our industry, we do discount license fees from our published list price. Numerous factors contribute to the amount of the discounts provided, such as previous customer purchases, the number of customer sites utilizing the software, the number of modules purchased and the number of users, as well as the overall size of the contract. While all these factors may affect the discount amount of a particular contract, the overall percentage discount has not materially changed in the recent reported fiscal periods.

The change in our revenues from period to period is primarily due to the volume of products and related services sold in any period and the amount of products or modules purchased with each sale.

International revenues represented approximately 20% and 17% of total revenues in the three months ended October 31, 2017 and 2016, respectively. Our revenues, in particular our international revenues, may fluctuate substantially from period to period primarily because we derive most of our license fee revenues from a relatively small number of customers in a given period.

License Revenues

| | Three Months Ended October 31, | | |
|-------------------------------|---|-----------------|-----------------|
| | 2017 | 2016 | % Change |
| | (in thousands) | | |
| Enterprise Resource Planning | \$ 466 | \$ 178 | 162% |
| Supply Chain Management | 1,983 | 2,962 | (33) |
| Total license revenues | \$ 2,449 | \$ 3,140 | (22)% |

| | Six Months Ended October 31, | | |
|-------------------------------|-------------------------------------|-----------------|-----------------|
| | 2017 | 2016 | % Change |
| | (in thousands) | | |
| Enterprise Resource Planning | \$ 602 | \$ 713 | (16)% |
| Supply Chain Management | 5,862 | 7,054 | (17) |
| Total license revenues | \$ 6,464 | \$ 7,767 | (17)% |

For the three and six months ended October 31, 2017, license fee revenues decreased 22% and 17%, respectively, when compared to the same periods in the prior year. In the three and six months ended October 31, 2017, license fee revenues from our SCM business unit decreased 33% and 17%, respectively, when compared to the corresponding periods in the prior year. We believe that the decrease in the first half of fiscal 2017 was partly due to a delay in closing several license fee agreements during the quarter and increased sales of our products on Logility's Cloud Services platform that require revenue to be deferred over the life of the contracted period, which is typically one to three years. Our SCM business unit constituted 81% and 94% of total license fee revenues for the three months ended October 31, 2017 and 2016, respectively. Our SCM business unit constituted 91% of total license fee revenues for both the six months ended October 31, 2017 and 2016 periods. Our ERP business unit license fee revenues increased by 162% the three months ended October 31, 2017 and decreased by 16% for the six months ended October 31, 2017 when compared to the same periods in the prior year. The increase in the current quarter was due to improved sale execution and acceptance of our new product releases to the apparel and retail industries.

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The direct sales channel provided approximately 60% and 76% of license fee revenues for the three and six months ended October 31, 2017, compared to approximately 79% and 81% in the comparable periods last year. The decrease in the proportion of sales by our direct sales channel was due to a larger decrease in license fee revenue from Logility's indirect sales channel. For the three months ended October 31, 2017 and 2016, our margins after commissions on direct sales were approximately 91% and 82%, respectively. For the six months ended October 31, 2017 and 2016, our margins after commissions on direct sales were approximately 81% and 87%, respectively. The margins increased in the current quarter due to the mix of sales commission rates based on each individual salespersons' quotas and related achievement. For the three months ended October 31, 2017 and 2016, our margins after commissions on indirect sales were approximately 43% and 45%, respectively. For the six months ended October 31, 2017 and 2016, our margins after commissions on indirect sales were approximately 37% and 36%, respectively. The indirect channel margins for the current quarter are slightly lower when compared to the same period in the prior year due to the mix of value-added reseller (VAR) commission rates. These margin calculations include only commission expense for comparative purposes and do not include other costs of license fees such as amortization of capitalized software.

Services and Other Revenues

| | Three Months Ended October 31, | | |
|-----------------------------------|---------------------------------------|-------------|-----------------|
| | 2017 | 2016 | % Change |
| | (in thousands) | | |
| Enterprise Resource Planning | \$ 1,198 | \$ 1,205 | (1)% |
| Supply Chain Management | 7,255 | 5,880 | 23 |
| IT Consulting | 4,596 | 5,264 | (13) |
| Total services and other revenues | \$ 13,049 | \$ 12,349 | 6% |

| | Six Months Ended October 31, | | |
|-----------------------------------|-------------------------------------|-------------|-----------------|
| | 2017 | 2016 | % Change |
| | (in thousands) | | |
| Enterprise Resource Planning | \$ 2,427 | \$ 2,299 | 6% |
| Supply Chain Management | 13,699 | 11,993 | 14 |
| IT Consulting | 8,965 | 10,278 | (13) |
| Total services and other revenues | \$ 25,091 | \$ 24,570 | 2% |

For the three and six months ended October 31, 2017, services revenue increased by 6% and 2%, respectively, primarily due to increased services revenues from our SCM business unit which was partially offset by a decrease at our IT consulting business unit. For the three and six months ended October 31, 2017, services and other revenues from our ERP segment decreased by 1% and increased by 6%, respectively, when compared to the same periods in the prior year due to the timing of project work particularly at NGC. For the three and six months ended October 31, 2017, a 23% and 14% increase, respectively, at our SCM business unit was due to services revenue related to our Logility Cloud Services area and an increase in utilization from project implementation services. For both the three and six months ended October 31, 2017, our IT Consulting segment's revenues decreased 13% when compared to the same periods in the prior year due to the completion of an IT project from one of our larger customers in the prior year period. We have observed that there is a tendency for services and other revenues, other than from IT Consulting, to lag changes in license revenues by one to three quarters, as new licenses in one quarter often involve implementation

and consulting services in subsequent quarters, for which we recognize revenues only as we perform those services.

For the three months ended October 31, 2017, Cloud Services Annual Contract Value (ACV) increased approximately 123% to \$9.9 million compared to \$4.4 million in the same period of the prior year. ACV is comprised of SaaS ACV of \$7.2 million compared to approximately \$2.3 million during the same period last year and other cloud services ACV of \$2.7 million compared to \$2.1 million during the same period last year. ACV is a forward-looking operating measure used by management to better understand cloud services (SaaS and other related cloud services) revenue trends within our business, as it reflects our current estimate of revenue to be generated under existing client contracts in the forward 12-month period.

Table of Contents**Maintenance Revenues**

| | Three Months Ended October 31, | | |
|-----------------------------------|---------------------------------------|------------------|-----------------|
| | 2017 | 2016 | % Change |
| | (in thousands) | | |
| Enterprise Resource Planning | \$ 1,424 | \$ 1,376 | 3% |
| Supply Chain Management | 9,415 | 9,281 | 1 |
| Total maintenance revenues | \$ 10,839 | \$ 10,657 | 2% |

| | Six Months Ended October 31, | | |
|-----------------------------------|-------------------------------------|------------------|-----------------|
| | 2017 | 2016 | % Change |
| | (in thousands) | | |
| Enterprise Resource Planning | \$ 2,864 | \$ 2,728 | 5% |
| Supply Chain Management | 18,803 | 18,514 | 2 |
| Total maintenance revenues | \$ 21,667 | \$ 21,242 | 2% |

For both the three and six months ended October 31, 2017, maintenance revenues increased 2% when compared to the same periods in the prior year, due primarily to increased license fees in recent periods. Logility accounted for 87% of total maintenance revenues for the three and six months ended October 31, 2017 and 2016. Typically, our maintenance revenues have had a direct relationship to current and historic license fee revenues, since new licenses are the potential source of new maintenance customers.

GROSS MARGIN

The following table provides both dollar amounts (in thousands) and percentage measures of gross margin:

| | Three months ended October 31, | | | | Six months ended October 31, | | | |
|------------------------------------|---------------------------------------|------------|------------------|------------|-------------------------------------|------------|------------------|------------|
| | 2017 | | 2016 | | 2017 | | 2016 | |
| Gross margin on license fees | \$ 601 | 25% | \$ 1,534 | 49% | \$ 3,109 | 48% | \$ 4,338 | 56% |
| Gross margin on services and other | 4,854 | 37% | 3,305 | 27% | 8,969 | 36% | 6,473 | 26% |
| Gross margin on maintenance | 8,551 | 79% | 8,179 | 77% | 17,152 | 79% | 16,003 | 75% |
| Total gross margin | \$ 14,006 | 53% | \$ 13,018 | 50% | \$ 29,230 | 55% | \$ 26,814 | 50% |

For the three and six months ended October 31, 2017, our total gross margin percentage increased when compared to the same periods in the prior year primarily due to a higher services and other revenue margin from increases in our Logility Cloud Services area and an increase in utilization from project implementation services.

Gross Margin on License Fees

License fee gross margin percentage for the three and six months ended October 31, 2017 decreased when compared to the same periods in the prior year primarily due to lower license fees, an increase in VAR commissions from an increase in indirect sales and higher amortization of acquired software expense from recent acquisitions. License fee gross margin percentage tends to be directly related to the level of license fee revenues due to the relatively fixed cost of computer software amortization expense, amortization of acquired software and the sales mix between our direct and indirect channels.

Gross Margin on Services and Other

For the three and six months ended October 31, 2017, the gross margin percentage on services and other revenue increased by ten percentage points when compared to the same periods in the prior year primarily due to an increase in our Logility Cloud Services area which has higher margin services and related implementation services. Also, the margin increase is due to a decrease in services revenue from our lower margin IT business unit. Services and other gross margin is directly related to the level of services and other revenues. The primary component of cost of services and other revenues is services staffing, which is relatively inelastic in the short term.

Table of Contents**Gross Margin on Maintenance**

Maintenance gross margin percentage for the three and six months ended October 31, 2017 and 2016 increased to 79% from 77% and to 79% from 75%, respectively, primarily due to increased maintenance revenue and cost containment efforts. Maintenance gross margin normally is directly related to the level of maintenance revenues. The primary component of cost of maintenance revenue is maintenance staffing, which is relatively inelastic in the short term.

EXPENSES

| | Three Months Ended | | | | Six Months Ended October 31, | | | |
|---|--------------------|----------|---------------|------|------------------------------|----------|---------------|------|
| | October 31, | | % of Revenues | | October 31, | | % of Revenues | |
| | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| | (in thousands) | | | | (in thousands) | | | |
| Research and development | \$ 2,643 | \$ 3,169 | 10% | 12% | \$ 5,151 | \$ 6,269 | 10% | 12% |
| Sales and marketing | 4,437 | 5,202 | 17 | 20 | 9,670 | 10,672 | 18 | 20 |
| General and administrative | 3,616 | 3,690 | 14 | 14 | 7,155 | 7,201 | 13 | 13 |
| Amortization of acquisition-related intangible assets | 68 | 249 | | 1 | 391 | 317 | 1 | 1 |
| Other income, net | 676 | (167) | 3 | (1) | 1,275 | 493 | 2 | 1 |
| Income tax expense | 1,438 | 129 | 5 | | 2,933 | 748 | 6 | 1 |

Research and Development

Gross product research and development costs include all non-capitalized and capitalized software development costs. A breakdown of the research and development costs is as follows:

| | Three Months Ended | | |
|--|--------------------|----------------|------------------|
| | October 31, 2017 | Percent Change | October 31, 2016 |
| Total capitalized computer software development costs | \$ 1,330 | 37 % | \$ 969 |
| Percentage of gross product research and development costs | 33% | | 23% |
| Total research and development expense | 2,643 | (17)% | 3,169 |
| Percentage of total revenues | 10% | | 12% |
| Total research and development expense and capitalized computer software development costs | \$ 3,973 | (4)% | \$ 4,138 |
| Percentage of total revenues | 15% | | 16% |
| Total amortization of capitalized computer software development costs * | \$ 892 | (10)% | \$ 990 |

| | Six Months Ended (in thousands) | | |
|--|--|---------------------------|-----------------------------|
| | October 31, 2017 | Percent Change | October 31, 2016 |
| Total capitalized computer software development costs | \$ 2,617 | 63 % | \$ 1,606 |
| Percentage of gross product research and development costs | 34% | | 20% |
| Total research and development expense | 5,151 | (18)% | 6,269 |
| Percentage of total revenues | 10% | | 12% |
| Total research and development expense and capitalized computer software development costs | \$ 7,768 | (1)% | \$ 7,875 |
| Percentage of total revenues | 15% | | 15% |
| Total amortization of capitalized computer software development costs * | \$ 1763 | (11)% | \$ 1,980 |

* Included in cost of license fees

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For the three and six months ended October 31, 2017, gross product research and development costs decreased 4% and 1%, respectively when compared to the same periods in the previous year due decreased headcount and related expenses. Capitalized software development costs increased 37% and 63%, respectively, for the three and six months ended October 31, 2017 when compared to the same periods last year due to timing of capitalizable project work. We expect capitalized product development costs to decrease for the remainder of fiscal 2018 as compared to the first half of 2018, and we expect capitalized software amortization expense to be relatively stable in coming quarters. Costs included in gross product development are salaries of product development personnel, hardware lease expense, computer software expense, telephone expense and rent.

Sales and Marketing

For the three and six months ended October 31, 2017, sales and marketing expenses were in the range of 17% to 18% of revenues. The percentage changes were primarily due to decreased headcount and sales commissions as a result of lower license fees. We generally include commissions on indirect sales in cost of sales.

General and Administrative

For the three and six months ended October 31, 2017, general and administrative expenses remained flat when compared to the same periods a year ago.

At October 31, 2017, the total number of employees was 390 compared to 437 at October 31, 2016.

Operating Income/(Loss)

| | Three Months Ended October 31, | | | Six Months Ended | | |
|-------------------------------|---------------------------------------|-------------|-----------------|-------------------------|-------------|-----------------|
| | 2017 | 2016 | % Change | 2017 | 2016 | % Change |
| | (in thousands) | | | October 31, | | |
| | (in thousands) | | | (in thousands) | | |
| Enterprise Resource Planning* | \$ (1,333) | \$ (1,614) | (17)% | \$ (2,849) | \$ (3,029) | (6)% |
| Supply Chain Management | 4,218 | 2,164 | 95% | 9,121 | 5,016 | 82% |
| IT Consulting | 357 | 158 | 126% | 591 | 368 | 61% |
| Total Operating Income | \$ 3,242 | \$ 708 | 358% | \$ 6,863 | \$ 2,355 | 191% |

* includes certain unallocated expenses.

Our ERP segment operating loss decreased 17% and 6% in the three and six months ended October 31, 2017, respectively, compared to the same periods in the prior year primarily due to higher revenues.

Our SCM segment's operating income increased by 95% and 82% for the three and six months ended October 31, 2017, respectively, compared to same periods last year primarily due to higher revenues and decreased headcount and related costs.

Our IT Consulting segment operating income increased 126% and 61% for the three and six months ended October 31, 2017, respectively, when compared to the prior year due to improved margin projects.

Other Income

Other income is comprised of net interest and dividend income, rental income net of related depreciation expenses, exchange rate gains and losses, and realized and unrealized gains and losses from investments.

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For the three months ended October 31, 2017, the increase in other income was due primarily to a higher unrealized gain on investments compared to losses in the prior year period, higher interest income and lower exchange rate losses when compared to the same period last year. This increase was partially offset by lower rental income when compared to the same period last year.

For the six months ended October 31, 2017, the increase in other income was due primarily to a higher unrealized gains on investments when compared to unrealized losses in the same period last year, higher interest income of \$717,000 for the six months ended October 31, 2017 when compared to \$595,000 for the same period in the prior year and \$0 exchange rate impact for the six months ended October 31, 2017 when compared to exchange rate losses of \$180,000 the same period last year. This increase was partially offset by lower rental income of \$170,000 when compared to the same period last year of \$472,000 as a result of our real estate sale in the fourth quarter of fiscal 2017.

We recorded gains of approximately \$268,000 and \$381,000 for the three and six months ended October 31, 2017, respectively, from our trading securities portfolio. We recorded losses of approximately \$610,000 and \$394,000 the three and six months ended October 31, 2016, respectively, from our trading securities portfolio.

For the three and six months ended October 31, 2017, our investments generated an annualized yield of approximately 1.30% and 1.38%, respectively, compared to approximately 1.55% and 1.63% for the three and six months ended October 31, 2016, respectively.

Income Taxes

We recognize deferred tax assets and liabilities based on the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their tax bases. We measure deferred tax assets and liabilities using statutory tax rates in effect in the year in which we expect the differences to reverse. We establish a deferred tax asset for the expected future benefit of net operating loss and credit carry-forwards. Under the Income Tax Topic of the FASB Accounting Standards Codification, we cannot recognize a deferred tax asset for the future benefit of our net operating losses, tax credits and temporary differences unless we can establish that it is more likely than not that the deferred tax asset would be realized. During the three months ended October 31, 2017, our effective tax rate was 36.7% compared to our effective tax rate of 23.8% in the three months ended October 31, 2016. During the six months ended October 31, 2017, our effective rate was 36.0% compared to our effective rate of 26.3% in the six months ended October 31, 2016. The increases in current year effective rates is primarily due to the tax benefit from higher stock option exercises during the same period in the prior year.

Operating Pattern

We experience an irregular pattern of quarterly operating results, caused primarily by fluctuations in both the number and size of software license contracts received and delivered from quarter to quarter and our ability to recognize revenues in that quarter in accordance with our revenue recognition policies. We expect this pattern to continue.

LIQUIDITY, CAPITAL RESOURCES AND FINANCIAL CONDITION

Sources and Uses of Cash

We have historically funded, and continue to fund, our operations and capital expenditures primarily with cash generated from operating activities. The changes in net cash that our operating activities provide generally reflect the changes in net earnings and non-cash operating items plus the effect of changes in operating assets and liabilities, such as investment trading securities, trade accounts receivable, trade accounts payable, accrued expenses and deferred

revenue. We have no debt obligations or off-balance sheet financing arrangements, and therefore, we used no cash for debt service purposes.

The following table shows information about our cash flows and liquidity positions during the six months ended October 31, 2017 and 2016. You should read this table and the discussion that follows in conjunction with our condensed consolidated statements of cash flows contained in Item 1. Financial Statements in Part I of this report and in our Annual Report on Form 10-K for the fiscal year ended April 30, 2017.

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| | Six Months Ended October 31, (in thousands) | |
|---|--|-------------|
| | 2017 | 2016 |
| Net cash provided by operating activities | \$ 520 | \$ 9,635 |
| Net cash used in investing activities | (2,829) | (6,376) |
| Net cash used in financing activities | (2,450) | (4,094) |
| Net change in cash and cash equivalents | \$ (4,759) | \$ (835) |

For the six months ended October 31, 2017, the net cash provided by operating activities decreased when compared to the same period last year was due primarily to: 1) an increase in purchases of trading securities, 2) a decrease in the comparative decrease in customer accounts receivables caused by the timing of closing customer sales and related collections, 3) an increase in the comparative decrease in accounts payable and other accruals due to timing of payments, 4) a decrease in depreciation and amortization and 5) an increase in the comparative increase in prepaid expenses due to the timing of purchases. This decrease was partially offset by: 1) an increase in net earnings, 2) higher proceeds from the maturity and sales of trading securities, 3) a decrease in the comparative decrease in deferred revenues due to timing of revenue recognition, 4) an increase in deferred income tax compared to a decrease in the same period last year, 5) an increase in stock-based compensation expense and 6) a lower gain on investments compared to the same period last year.

The decrease in cash used in investing activities when compared to the same period in the prior year was due primarily to the acquisition of AdapChain, Inc. during the quarter ended October 31, 2016 and a decrease in purchases of property and equipment. That decrease was partially offset by higher capitalized computer software development costs.

The decrease in cash used in financing activities compared to the prior year was due primarily to an increase in proceeds from exercise of stock options and a decrease in the payment for accrued acquisition consideration. This was partially offset by an increase in dividends paid.

The following table shows net changes in total cash, cash equivalents, and investments, which is one measure management uses to view net total cash generated by our activities:

| | As of October 31, (in thousands) | |
|---|---|-------------|
| | 2017 | 2016 |
| Cash and cash equivalents | \$ 61,242 | \$ 48,169 |
| Short and long-term investments | 29,773 | 24,131 |
| Total cash and short and long-term investments | \$ 91,015 | \$ 72,300 |
| Net increase (decrease) in total cash and investments (six months ended October 31) | \$ 1,227 | \$ (5,585) |

Our total activities used less cash and investments during the six months ended October 31, 2017, when compared to the prior year period, due primarily to the improvement in operating results and changes in operating assets and liabilities as noted above.

Days Sales Outstanding in accounts receivable were 57 days as of October 31, 2017, compared to 54 days as of October 31, 2016. This increase is primarily due to timing of cash collections. Our current ratio on October 31, 2017 was 2.7 to 1 and on October 31, 2016 was 2.5 to 1.

Our business in recent periods has generated substantial positive cash flow from operations, excluding purchases and sales of trading securities. For this reason, and because we had \$91.0 million in cash and investments with no debt as of October 31, 2017, we believe that our sources of liquidity and capital resources will be sufficient to satisfy our presently anticipated requirements during at least the next twelve months for working capital, capital expenditures and other corporate needs. However, at some future date we may need to seek additional sources of capital to meet our requirements. If such need arises, we may be required to raise additional funds through equity or debt financing. We do not currently have a bank line of credit. We can provide no assurance that bank lines of credit or other financing will be available on terms acceptable to us. If available, such financing may result in dilution to our shareholders or higher interest expense.

Table of Contents**CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

We have based the following discussion and analysis of financial condition and results of operations on our financial statements, which we have prepared in accordance with U.S. generally accepted accounting principles. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Note 1 in the Notes to the Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended April 30, 2017, describes the significant accounting policies that we have used in preparing our financial statements. On an ongoing basis, we evaluate our estimates, including, but not limited to those related to revenue/collectability, bad debts, capitalized software costs, goodwill, intangible asset impairment, stock-based compensation, income taxes and contingencies. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Our actual results could differ materially from these estimates under different assumptions or conditions.

We believe the critical accounting policies listed below affect significant judgments and estimates used in the preparation of the financial statements.

Revenue Recognition. We recognize revenue predominantly in accordance with the Software Revenue Recognition Topic of the Financial Accounting Standards Board's (FASB) Accounting Standards Codification. We recognize license revenues in connection with license agreements for standard proprietary software upon delivery of the software, provided we deem collection to be probable, the fee is fixed or determinable, there is persuasive evidence of an arrangement, and VSOE exists with respect to any undelivered elements of the arrangement. We generally bill maintenance fees annually in advance and recognize the resulting revenues ratably over the term of the maintenance agreement. We derive revenues from services which primarily include consulting, implementation, training, SaaS, hosting and managed services. We bill for these services primarily under time and materials arrangements and recognize fees as we perform the services. Deferred revenues represent advance payments or billings for software licenses, services, and maintenance billed in advance of the time we recognize revenues. We record revenues from sales of third-party products in accordance with Principal Agent Considerations within the Revenue Recognition Topic of the FASB Accounting Standards Codification. Furthermore, we evaluate sales through our indirect channel on a case-by-case basis to determine whether the transaction should be recorded gross or net, including but not limited to assessing whether or not we (1) act as principal in the transaction, (2) take title to the products, (3) have risks and rewards of ownership, such as the risk of loss for collection, delivery, or returns, and (4) act as an agent or broker with compensation on a commission or fee basis. Accordingly, our sales through the DMI channel are typically recorded on a gross basis.

Generally, our software products do not require significant modification or customization. Installation of the products is routine and is not essential to their functionality. Our sales frequently include maintenance contracts and professional services with the sale of our software licenses. We have established VSOE for our maintenance contracts and professional services. We determine fair value based upon the prices we charge to customers when we sell these elements separately. We defer maintenance revenues, including those sold with the initial license fee, based on VSOE, and recognize the revenue ratably over the maintenance contract period. We recognize consulting and training service revenues, including those sold with license fees, as we perform the services based on their established VSOE. We determine the amount of revenue we allocate to the licenses sold with services or maintenance using the residual method of accounting. Under the residual method, we allocate the total value of the arrangement first to the undelivered elements based on their VSOE and allocate the remainder to license fees. SaaS revenues are recognized ratably over the subscription term as the customer has no ability to take delivery of the software, and the underlying

arrangements typically include a single fee for the service that is billed monthly, quarterly or annually.

Allowance for Doubtful Accounts. We maintain allowances for doubtful accounts for estimated losses resulting from the inability of customers to make required payments. If the financial condition of these customers were to deteriorate, resulting in an impairment of their ability to make payments, we may require additional allowances or we may defer revenue until we determine that collectability is probable. We specifically analyze accounts receivable and historical bad debts, customer creditworthiness, current economic trends and changes in customer payment terms when we evaluate the adequacy of the allowance for doubtful accounts.

Valuation of Long-Lived and Intangible Assets. In accordance with the Intangibles-Goodwill and Other Topic of the FASB's Accounting Standards Codification, we do not amortize goodwill and other intangible assets with indefinite lives. Our goodwill is subject to annual impairment tests, which require us to estimate the fair value of our business compared to the carrying value. The impairment reviews require an analysis of future projections and assumptions about our operating performance. Should such review indicate the assets are impaired, we would record an expense for the impaired assets.

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In accordance with the Property, Plant, and Equipment Topic of the FASB's Accounting Standards Codification, long-lived assets, such as property and equipment and intangible assets, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability would be measured by a comparison of the carrying amount of an asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, we recognize an impairment charge in the amount by which the carrying amount of the asset exceeds the fair value of the asset. The determination of estimated future cash flows, however, requires management to make estimates. Future events and changes in circumstances may require us to record a significant impairment charge in the period in which such events or changes occur. Impairment testing requires considerable analysis and judgment in determining results. If other assumptions and estimates were used in our evaluations, the results could differ significantly.

Annual tests or other future events could cause us to conclude that impairment indicators exist and that our goodwill is impaired. For example, if we had reason to believe that our recorded goodwill and intangible assets had become impaired due to decreases in the fair market value of the underlying business, we would have to take a charge to income for that portion of goodwill or intangible assets that we believed was impaired. Any resulting impairment loss could have a material adverse impact on our financial position and results of operations. At October 31, 2017, our goodwill balance was \$19.5 million and our intangible assets with definite lives balance was approximately \$2.7 million, net of accumulated amortization.

Valuation of Capitalized Software Assets. We capitalize certain computer software development costs in accordance with the Intangibles-Goodwill and Other Topic of the FASB's Accounting Standards Codification. Costs incurred internally to create a computer software product or to develop an enhancement to an existing product are charged to expense when incurred as research and development expense until technological feasibility for the respective product is established. Thereafter, we capitalize all software development costs and report those costs at the lower of unamortized cost or net realizable value. Capitalization ceases when the product or enhancement is available for general release to customers. We make ongoing evaluations of the recoverability of our capitalized software projects by comparing the amount capitalized for each product to the estimated net realizable value of the product. If such evaluations indicate that the unamortized software development costs exceed the net realizable value, we write off the amount by which the unamortized software development costs exceed net realizable value. We amortize capitalized computer software development costs ratably based on the projected revenues associated with the related software or on a straight-line basis over three years, whichever method results in a higher level of amortization. Amortization of capitalized computer software development costs is included in the cost of license revenues in the condensed consolidated statements of operations.

Stock-Based Compensation. We estimate the value of options granted on the date of grant using the Black-Scholes option pricing model. Management's judgments and assumptions related to volatility, the expected term and the forfeiture rate are made in connection with the calculation of stock compensation expense. We periodically review all assumptions used in our stock option pricing model. Changes in these assumptions could have a significant impact on the amount of stock compensation expense.

Income Taxes. We provide for the effect of income taxes on our financial position and results of operations in accordance with the Income Tax Topic of the FASB's Accounting Standards Codification. Under this accounting guidance, income tax expense is recognized for the amount of income taxes payable or refundable for the current year and for the change in net deferred tax assets or liabilities resulting from events that are recorded for financial reporting purposes in a different reporting period than recorded in the tax return. Management must make significant assumptions, judgments and estimates to determine our current provision for income taxes and also our deferred tax assets and liabilities and any valuation allowance to be recorded against our net deferred tax asset. Our judgments, assumptions and estimates relative to the current provision for income tax take into account current tax laws, our

interpretation of current tax laws, allowable deductions, and projected tax credits. Changes in tax law or our interpretation of tax laws could significantly impact the amounts provided for income taxes in our financial position and results of operations. Our assumptions, judgments and estimates relative to the value of our deferred tax assets take into account our expectations of the amount and category of future taxable income. Actual operating results and the underlying amount and category of income in future years, which could significantly increase tax expense, could render inaccurate our current assumptions, judgments and estimates of recoverable net deferred taxes.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Foreign Currency In the three and six months ended October 31, 2017, we generated approximately 20% and 20%, respectively, of our revenues outside the United States. We typically make international sales through our foreign branches or our Logility branch and denominate those sales typically in U.S. dollars, British pounds sterling or euros. However, expenses incurred in connection with these sales are typically denominated in the local currencies. We recorded an exchange rate loss of approximately \$41,000 and a gain of \$400 for the three and six months ended October 31, 2017, respectively, compared to exchange rate losses of approximately

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\$72,000 and \$180,000 for the three months and six months ended October 31, 2016, respectively. We estimate that a 10% movement in foreign currency rates would have had the effect of creating up to a \$317,000 and \$314,000 exchange gain or loss for the three and six months ended October 31, 2017. We have not engaged in any hedging activities.

Interest Rates and Other Market Risks. We have no debt, and therefore limit our discussion of interest rate risk to risk associated with our investment profile. We manage our interest rate risk by maintaining an investment portfolio of trading investments with high credit quality and relatively short average maturities. These instruments include, but are not limited to, money-market instruments, bank time deposits, and taxable and tax-advantaged variable rate and fixed rate obligations of corporations, municipalities, and national, state, and local government agencies, in accordance with an investment policy approved by our Board of Directors. These instruments are denominated in U.S. dollars. The fair market value of these instruments as of October 31, 2017 was approximately \$86.6 million compared to \$69.5 million as of October 31, 2016.

We also hold cash balances in accounts with commercial banks in the United States and foreign countries. These cash balances represent operating balances only and are invested in short-term time deposits of the local bank. Such operating cash balances held at banks outside the United States are denominated in the local currency and are minor.

Many of our investments carry a degree of interest rate risk. When interest rates fall, our income from investments in variable-rate securities declines. When interest rates rise, the fair market value of our investments in fixed-rate securities declines. In addition, our investments in equity securities are subject to stock market volatility. Due in part to these factors, our future investment income may fall short of expectations or we may suffer losses in principal if forced to sell securities, which have seen a decline in market value due to changes in interest rates. We attempt to mitigate risk by holding fixed-rate securities to maturity, but, if our liquidity needs force us to sell fixed-rate securities prior to maturity, we may experience a loss of principal.

Inflation. Although we cannot accurately determine the amounts attributable thereto, we have been affected by inflation through increased costs of employee compensation and other operational expenses. To the extent permitted by the marketplace for our products and services, we attempt to recover increases in costs by periodically increasing prices.

Item 4. Controls and Procedures

Management's Report on Internal Control Over Financial Reporting

Our disclosure controls and procedures (as such term is defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 ("Exchange Act")) are designed to provide reasonable assurance that information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms. Our disclosure controls and procedures are also designed to ensure that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, to allow timely decisions regarding disclosure.

Our principal executive officer and principal financial officer, with the assistance of our Disclosure Committee, have conducted an evaluation of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report. We perform this evaluation on a quarterly basis so that the conclusions concerning the effectiveness of our disclosure controls and procedures can be reported in our Annual Report on Form 10-K and Quarterly Reports on Form 10-Q. Based on this evaluation, our principal executive officer and principal financial

officer have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report.

Changes in Internal Control over Financial Reporting

There have not been any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

We are not currently involved in legal proceedings requiring disclosure under this item.

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Item 1A. Risk Factors

In addition to the other information set forth in this report, you should carefully consider the risk factors disclosed in Item 1A, Risk Factors, of our Annual Report on Form 10-K for the fiscal year ended April 30, 2017. There have been no material changes to the risk factors as previously disclosed in such Annual Report on Form 10-K.

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

None

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

| | |
|-----------------|---|
| Exhibit 3.1 | Amended and Restated Articles of Incorporation, and amendments thereto. (1) |
| Exhibit 3.2 | <u>Amended and Restated By-Laws dated May 18, 2009.</u> (2) |
| Exhibit 31.1 | <u>Rule 13a-14(a)/15d-14(a) Certifications</u> |
| Exhibit 31.2 | <u>Rule 13a-14(a)/15d-14(a) Certifications</u> |
| Exhibit 32.1. | <u>Section 906 Certifications</u> |
| Exhibit 101.INS | XBRL Instance Document. |
| Exhibit 101.SCH | XBRL Taxonomy Extension Schema Document. |
| Exhibit 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document. |
| Exhibit 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document. |
| Exhibit 101.LAB | XBRL Taxonomy Extension Label Linkbase Document. |
| Exhibit 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document. |

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- (1) Incorporated by reference herein. Filed by the Company as an exhibit to its Quarterly Report filed on Form 10-Q for the quarter ended October 31, 1990.
- (2) Incorporated by reference herein. Filed by the Company as an exhibit to its Quarterly Report filed on Form 10-Q for the quarter ended January 31, 2010.

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SIGNATURES

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

AMERICAN SOFTWARE, INC.

Date: December 8, 2017

By: /s/ James C. Edenfield
James C. Edenfield
Executive Chairman, Treasurer and Director

(Principal Executive Officer)

Date: December 8, 2017

By: /s/ Vincent C. Klinges
Vincent C. Klinges
Chief Financial Officer

(Principal Financial Officer)

Date: December 8, 2017

By: /s/ Bryan L. Sell
Bryan L. Sell
Controller and Principal Accounting Officer