

SABA SOFTWARE INC
Form 10-Q
October 07, 2009
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended August 31, 2009

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

For the transition period from to .

001-34372

(Commission File number)

SABA SOFTWARE, INC.

(Exact Name of Registrant as Specified in Its Charter)

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Delaware (State or other jurisdiction of incorporation or organization)	94-3267638 (I.R.S. Employer Identification No.)
2400 Bridge Parkway Redwood Shores, California (Address of principal executive offices)	94065-1166 (Zip Code)
(650) 581-2500 (Registrant's telephone number, including area code)	

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T 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 smaller reporting company. See the definition 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
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

On September 30, 2009, 27,857,090 shares of the registrant's Common Stock, \$.001 par value, were outstanding.

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QUARTER ENDED AUGUST 31, 2009

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Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****SABA SOFTWARE, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS**

(in thousands, except share and per share data)

	August 31, 2009 (Unaudited)	May 31, 2009*
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 21,588	\$ 25,978
Restricted cash	100	100
Accounts receivable, net	18,634	20,010
Prepaid expenses and other current assets	2,494	2,245
Total current assets	42,816	48,333
Property and equipment, net	4,319	4,755
Goodwill	36,095	36,095
Purchased intangible assets, net	7,814	8,743
Restricted cash	260	260
Other assets	1,480	1,537
Total assets	\$ 92,784	\$ 99,723
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 3,727	\$ 2,620
Accrued compensation and related expenses	6,036	5,867
Accrued expenses	3,126	3,137
Deferred revenue	28,136	32,611
Current portion of debt and lease obligations	530	630
Total current liabilities	41,555	44,865
Deferred revenue	2,716	2,728
Other long term liabilities	1,376	1,354
Accrued rent	2,110	2,211
Total liabilities	47,757	51,158
Commitments and contingencies		
Stockholders equity:		
Preferred stock, issuable in series: \$0.001 par value: 5,000,000 authorized shares at August 31, 2009 and May 31, 2009; none issued or outstanding		
Common stock, \$0.001 par value: 50,000,000 authorized; 27,949,621 shares issued at August 31, 2009 and 29,300,148 shares issued May 31, 2009	28	30
Additional paid-in capital	253,592	258,128

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Treasury stock: 102,997 shares at August 31, 2009 and May 31, 2009, at cost	(232)	(232)
Accumulated deficit	(208,210)	(209,230)
Accumulated other comprehensive income	(151)	(131)
Total stockholders' equity	45,027	48,565
Total liabilities and stockholders' equity	\$ 92,784	\$ 99,723

* Derived from audited financial statements included in the Company's Annual Report on Form 10-K for the year ended May 31, 2009 filed with the United States Securities and Exchange Commission.

See Accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents**SABA SOFTWARE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(in thousands, except per share data)****(Unaudited)**

	Three months ended	
	August 31, 2009	August 31, 2008
Revenues:		
License	\$ 5,712	\$ 2,958
License updates and product support	8,756	8,641
OnDemand	5,245	4,918
Professional services	6,098	8,782
Total revenues	25,811	25,299
Cost of revenues:		
Cost of license	210	213
Cost of license updates and product support	2,037	2,207
Cost of OnDemand	2,008	2,426
Cost of professional services	4,552	5,916
Amortization of acquired developed technology	295	295
Total cost of revenues	9,102	11,057
Gross profit	16,709	14,242
Operating expenses:		
Research and development	4,222	4,286
Sales and marketing	6,788	7,107
General and administrative	3,843	4,341
Restructuring	(37)	
Amortization of purchased intangible assets	634	634
Total operating expenses	15,450	16,368
Income (loss) from operations	1,259	(2,126)
Interest income and other (expense), net	(22)	81
Interest expense	(3)	(10)
Income (loss) before provision for income taxes	1,234	(2,055)
Provision for income taxes	(214)	(159)
Net income (loss)	\$ 1,020	\$ (2,214)
Basic net income (loss) per share	\$ 0.03	\$ (0.08)
Diluted net income (loss) per share	\$ 0.03	\$ (0.08)
Shares used in computing basic net income (loss) per share	29,220	29,151

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Shares used in computing diluted net income (loss) per share	29,833	29,151
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See Accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents**SABA SOFTWARE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(in thousands)****(Unaudited)**

	Three months ended	
	August 31, 2009	August 31, 2008
Operating activities:		
Net income (loss)	\$ 1,020	\$ (2,214)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	622	576
Amortization of purchased intangible assets	929	929
Share-based compensation expense	264	590
Changes in operating assets and liabilities:		
Accounts receivable	1,406	330
Prepaid expenses and other current assets	(258)	167
Other assets	51	19
Accounts payable	1,102	1,492
Accrued compensation and related expenses	177	(165)
Accrued expenses	175	(63)
Accrued rent	(264)	184
Deferred revenue	(4,511)	(1,208)
Net cash provided by operating activities	713	637
Investing activities:		
Purchases of property and equipment	(183)	(1,194)
Net cash used in investing activities	(183)	(1,194)
Financing activities:		
Proceeds from issuance of common stock under employee stock plans	45	107
Repurchase of common stock	(4,847)	
Repayments on borrowings under credit facility	(99)	(100)
Repayments on note payable	(22)	(26)
Net cash used in financing activities	(4,923)	(19)
Effect of exchange rate changes on cash	3	(502)
Decrease in cash and cash equivalents	(4,390)	(1,078)
Cash and cash equivalents, beginning of period	25,978	16,624
Cash and cash equivalents, end of period	\$ 21,588	\$ 15,546
Supplemental disclosure of other cash flow information:		
Cash paid out for income taxes, net of refunds	\$ 230	\$ 196
Cash paid for interest	\$ 3	\$ 9

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See Accompanying Notes to Condensed Consolidated Financial Statements.

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SABA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Basis of Presentation

The condensed consolidated financial statements include the accounts of Saba Software, Inc. and its wholly owned subsidiaries (Saba or the Company). All intercompany balances and transactions have been eliminated.

The accompanying condensed consolidated balance sheet as of August 31, 2009, the condensed consolidated statements of operations for the three months ended August 31, 2009 and 2008 and the condensed consolidated statements of cash flows for the three months ended August 31, 2009 and 2008 are unaudited. These unaudited interim condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (US GAAP). In the opinion of management, the unaudited interim condensed consolidated financial statements include all adjustments of a normal recurring nature necessary for the fair presentation of the Company s financial position as of August 31, 2009, and the Company s results of operations for the three months ended August 31, 2009 and 2008 and cash flows for the three months ended August 31, 2009 and 2008.

These unaudited condensed consolidated financial statements should be read in conjunction with Saba s audited condensed consolidated financial statements included in Saba s Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC) on August 12, 2009. The results of operations for the three months ended August 31, 2009 are not necessarily indicative of results for the entire fiscal year ending May 31, 2010 or for any future period.

The condensed consolidated balance sheet at May 31, 2009 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by US GAAP for complete financial statements.

The Company has evaluated subsequent events for recognition or disclosure through the time of filing these consolidated financial statements on Form 10-Q with the U.S. Securities and Exchange Commission on October 7, 2009

2. Summary of Significant Accounting Policies

Revenue Recognition

Saba recognizes license revenues in accordance with the provisions of American Institute of Certified Public Accountants (AICPA) Statement of Position (SOP) 97-2, *Software Revenue Recognition*, as amended by SOP 98-9, *Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions*. Under SOP 97-2, as amended, Saba recognizes license revenues when all of the following conditions are met:

persuasive evidence of an agreement exists;

delivery has occurred;

the fee is fixed or determinable; and

collection is probable.

SOP 97-2, as amended, permits revenue earned on software arrangements involving multiple elements to be allocated to each element based on the residual method, under which revenue is allocated to undelivered elements based on vendor-specific objective evidence of fair value of such undelivered elements and the residual amounts of revenue are allocated to delivered elements. Saba has analyzed each element in its multiple-element arrangements and determined that it has sufficient vendor-specific objective evidence

Table of Contents**SABA SOFTWARE, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)**

(VSOE) to allocate revenues to certain OnDemand offerings, license updates and product support and professional services. Accordingly, assuming all other revenue recognition criteria are met, revenues from perpetual licenses are recognized upon delivery using the residual method in accordance with SOP 98-9. Saba limits its assessment of VSOE for each element to either the price charged when the same element is sold separately or the price established by management, having the relevant authority to do so, for an element not yet sold separately.

License revenues from licenses with a term of three years or more are generally recognized on delivery if the other conditions of SOP 97-2 are satisfied. Saba does not grant its resellers the right of return and does not recognize revenue from resellers until an end-user has been identified and the other conditions of SOP 97-2 are satisfied. License revenues from licenses with a term of less than three years are generally recognized ratably over the term of the arrangement. License updates and product support revenue is recognized ratably over the term of the arrangement, typically 12 months. In arrangements where term licenses are bundled with license updates and product support and such revenue is recognized ratably over the term of the arrangement, Saba allocates the revenue to license revenue and to license updates and product support revenue based on the VSOE of fair value for license updates and product support revenue on perpetual licenses of similar products.

Revenue related to professional services is generally recognized as the services are performed. Although Saba provides professional services on a time and materials basis, a portion of these services is provided on a fixed-fee basis. For services performed on a fixed fee basis, revenues are generally recognized on the proportional performance of the project, with performance measured based on hours of work performed. For contracts that involve significant customization and implementation or consulting services that are essential to the functionality of the software, the license and services revenues are recognized using the percentage-of-completion method or, if Saba is unable to reliably estimate the costs to complete the services, Saba uses the completed contract method of accounting in accordance with SOP 97-2 and relevant guidance of SOP 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*. A contract is considered complete when all significant costs have been incurred or the item has been accepted by the customer.

Revenue from Saba's OnDemand offerings is recognized as a service arrangement whereby the revenue is recognized ratably over the term of the arrangement or on an as-used basis if defined in the contract. Certain of its OnDemand offerings are integrated offerings pursuant to which the customer's ability to access the Company's software is not separable from the services necessary to operate the software and customers are not allowed to take possession of the Company's software, in which case revenue is recognized under the SEC's Staff Accounting Bulletin (SAB) No. 104, *Revenue Recognition*. Saba's OnDemand offerings also include arrangements with customers that have separately licensed and taken possession of the Company's software. When these OnDemand offerings are part of a multiple element arrangement involving licenses, Saba recognizes revenue in accordance with SOP 97-2, when the Emerging Issues Task Force (EITF) *Issue No. 00-3 Application of AICPA Statement of Position 97-2, Software Revenue Recognition, to Arrangements That Include the Right to Use Software Stored on Another Entity's Hardware*, criteria is met.

If the requirements of SOP 97-2 are not met when Saba bills a customer or a customer pays Saba, the billed or paid amount is recorded as deferred revenue, a liability account. As the revenue recognition criterias of SOP 97-2 are satisfied, the requisite amounts are recognized as revenue.

In arrangements that include professional services and OnDemand offerings, but not a license of the Company's software, the Company recognizes revenue for professional services as the services are performed if these professional services qualify as a separate element of the arrangement. If the professional services do not qualify as a separate element of the arrangement, the related revenue is combined with the subscription revenue and recognized ratably over the subscription service period. Additionally, the Company defers the direct costs related to the professional services and recognizes them ratably over the applicable service period. The Company classifies deferred revenue and deferred costs on its consolidated balance sheet as current if the Company expects to recognize such revenue or cost within the following twelve months. When the revenue from professional services is recognized ratably over the subscription service period, the Company allocates the revenue to professional services revenue and to OnDemand revenue based on the VSOE of fair value for similar professional services that qualify as a separate element of the arrangement. The Company's judgment as to whether the consulting services qualify as a separate unit of accounting may materially affect the timing of the Company's revenue recognition and results of operations.

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SFAS No. 157 establishes three levels of inputs that may be used to measure fair value:

Level 1: quoted prices in active markets for identical assets and liabilities;

Level 2: inputs other than Level 1 that are observable, either directly and indirectly, such as quoted prices in active markets for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; or

Level 3: unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Financial Assets and Liabilities Measured at Fair Value on a Recurring Basis

Financial assets and liabilities measured at fair value on a recurring basis, excluding accrued interest components consisted of the following types of instruments as of August 31, 2009 (Level 1 input is defined above):

(in thousands)	Fair Value Measurements Using Input Type Level 1
Assets:	
Money market funds (included in cash equivalents)	\$ 8,618
Total financial assets	\$ 8,618

The Company's valuation techniques used to measure the fair values of the Company's money market funds were derived from quoted market prices.

3. Share-Based Compensation

The Company accounts for share-based payments to employees, including grants of employee stock options, Restricted Stock Units (RSUs) and purchases under employee stock purchase plans, in accordance with Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), *Share-Based Payment*, which requires that these awards (to the extent they are compensatory) be recognized in the Company's consolidated statements of operations based on their fair values.

The Company currently uses the Black-Scholes-Merton option pricing model to determine the fair value of stock options and employee stock purchase plan shares. The determination of the fair value of share-based payment awards on the date of grant using an option-pricing model is affected by the Company's stock price as well as assumptions regarding a number of complex and subjective variables. These variables include

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the expected term of the awards; the Company's expected stock price volatility over the term of the awards, actual and projected employee stock option exercise behaviors, risk-free interest rate and expected dividends. The Company estimates the expected term of share-based awards granted based, in part, on the Company's historical option term experience and, prior to December 31, 2007, by applying the simplified method in accordance with the SEC's SAB No. 107 *Share-Based Payment*, which provides supplemental implementation guidance for SFAS 123R. The Company estimates the volatility of its common stock based upon the Company's historical stock price volatility over the length of the expected term of the options. The Company bases the risk-free interest rate that it uses in the option valuation model on U.S. Treasury zero-coupon issues with remaining maturities

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similar to the expected term of the options. The Company does not anticipate paying any cash dividends in the foreseeable future and therefore uses an expected dividend yield of zero in the option valuation model. The Company is required to estimate forfeitures at the time of grant and revise those estimates in subsequent periods if actual forfeitures differ from those estimates. The Company uses historical data to estimate pre-vesting option forfeitures and records share-based compensation expense only for those awards that are expected to vest. The Company also considers, each quarter, whether there have been any significant changes in facts and circumstances that would affect its forfeiture rate. The expected term of the employee stock purchase plan shares is the average of the remaining purchase periods under each offering period. For RSUs, stock compensation is calculated based on the fair market value of the stock on the award date.

The following assumptions have been used to value the options and awards granted during the three months ended August 31, 2009 and 2008, respectively, under the Company's stock incentive plans and stock purchased under the Company's employee stock purchase plan:

	Three months ended	
	August 31, 2009	August 31, 2008
Stock Options:		
Expected volatility	59%	49%
Risk-free interest rates	0.80%	2.9%
Expected term (years)	4.1	3.8
Expected dividend yield	0%	0%
Employee Stock Purchase Plan:		
Expected volatility	78%	50%
Risk-free interest rates	0.53%	2.3%
Expected term (years)	0.5 2.0	0.5 2.0
Expected dividend yield	0%	0%

The following table summarizes the stock-based compensation expense for stock options and the Company's employee stock purchase plan shares that was recorded in the Company's results of operations in accordance with SFAS 123R for the three months ended August 31, 2009 and, 2008, respectively.

	Three months ended	
(in thousands)	August 31, 2009	August 31, 2008
Cost of revenues	\$ 46	\$ 103
Research and development	56	107
Sales and marketing	71	196
General and administrative	91	184
Share-based compensation expense included in net income (loss)	\$ 264	\$ 590

Prior to the fiscal third quarter ended February 28, 2009, the Board of Directors of the Company granted only stock options. The Board of Directors commenced granting RSUs in addition to stock options during the fiscal third quarter ended February 28, 2009.

RSUs granted by the Board of Directors have been awarded under the Company's 2000 Stock Incentive Plan. The RSUs vest in four annual installments commencing on the one year anniversary of the date of the award. The stock-based compensation expense for RSUs that was recorded in the Company's results of operations in accordance with SFAS 123R for the three months ended August 31, 2009 was \$30,000. As of

August 31, 2009, none of the RSUs were vested.

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The weighted average estimated fair value of options granted was \$1.89 per share for the three months ended August 31, 2009 and \$1.19 per share for the three months ended August 31, 2008. The weighted average estimated fair value of RSUs granted was \$1.30 per share for the three months ended August 31, 2009 and none for the three months ended August 31, 2008.

4. Basic and Diluted Net Income (Loss) Per Share

Basic and diluted net income (loss) per share information for all periods is presented under the requirements of SFAS No. 128, *Earnings per Share*. Basic earnings per share have been computed using the weighted-average number of shares of common stock outstanding during the period. Basic earnings per share excludes the dilutive effects of options as well as any contingently issuable shares in escrow for which specific conditions have not yet been met. Dilutive potential common shares consist of the shares issuable upon the exercise of stock options and the restricted stock unit awards under the treasury stock method. Potentially dilutive issuances have been excluded from the computation of diluted net loss per share as their inclusion would be anti-dilutive, which consist of common stock options, restricted stock units awards and common stock subject to repurchase. The calculations of basic and diluted net income (loss) per share are as follows:

(in thousands, except per share data)	Three months ended	
	August 31, 2009	August 31, 2008
Net income (loss)	\$ 1,020	\$ (2,214)
Weighted-average shares of common stock used in computing diluted net income (loss) per share	29,220	29,151
Effect of dilutive employee stock options and RSUs	613	
Weighted-average shares of common stock used in computing diluted net income (loss) per share	29,833	29,151
Basic net income (loss) per share	\$ 0.03	\$ (0.08)
Diluted net income (loss) per share	\$ 0.03	\$ (0.08)

5. Comprehensive Income (Loss)

Saba reports comprehensive income (loss) in accordance with SFAS No. 130, *Reporting Comprehensive Income*. The following table sets forth the calculation of comprehensive income (loss) for all periods presented:

(in thousands)	Three months ended	
	August 31, 2009	August 31, 2008
Net income (loss)	\$ 1,020	\$ (2,214)
Foreign currency translation loss	(20)	(345)
Comprehensive income (loss)	\$ 1,000	\$ (2,559)

6. Goodwill and Purchased Intangible Assets

Purchased intangible assets consist of acquired developed technology, customer relationships, trade names and customer backlog acquired as part of a purchase business combination. The intangible assets are stated at cost less accumulated amortization and are being amortized on a straight-line basis over their estimated useful lives of two to seven years.

Table of Contents**SABA SOFTWARE, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)**

There were no additions to intangible assets during the three months ended August 31, 2009. The following tables provide a summary of the carrying amounts of purchased intangible assets that continue to be amortized:

(in thousands)	August 31, 2009			Weighted
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Average Useful Life
Customer relationships	\$ 14,920	\$ (9,007)	\$ 5,913	6.3 Years
Tradenames	820	(588)	232	5.0 Years
Acquired developed technology	5,890	(4,221)	1,669	5.0 Years
Total	\$ 21,630	\$ (13,816)	\$ 7,814	

(in thousands)	May 31, 2009			Weighted
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Average Useful Life
Customer relationships	\$ 14,920	\$ (8,413)	\$ 6,507	6.3 Years
Tradenames	820	(547)	273	5.0 Years
Acquired developed technology	5,890	(3,927)	1,963	5.0 Years
Total	\$ 21,630	\$ (12,887)	\$ 8,743	

The total expected future amortization related to purchased intangible assets will be approximately \$2.8 million for the remainder of fiscal 2010 and \$3.3 million and \$1.8 million in fiscal years 2011 through 2012, respectively. All tangible assets will be fully amortized by May 31, 2012.

Goodwill is reviewed annually for impairment (or more frequently if indicators of impairment arise or circumstances otherwise dictate). The Company completed its annual impairment assessment in fiscal 2009 and concluded that goodwill was not impaired. Through the three month period ended August 31, 2009, there were no indicators of impairment of goodwill. Intangible assets are reviewed for impairment whenever events indicate that their carrying amount may not be recoverable. Through the three month period ended August 31, 2009, there were no indicators of impairment of intangible assets.

7. Debt and Other Obligations**Credit Facility**

On January 31, 2006, the Company entered into a credit facility with a bank that provided for (i) a term loan in a principal amount of \$6.5 million, (ii) a receivables borrowing base revolving credit line in an aggregate principal amount of up to \$7.5 million at any time outstanding, which included a sub-limit of up to \$5.0 million for letters of credit, cash management and foreign exchange services and (iii) an equipment facility up to a principal amount of \$3.0 million. All amounts borrowed under the term loan and the credit line were repaid in full on or prior to

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January 31, 2009, in accordance with the terms of the credit facility. The Company obtained advances on November 30, 2006 and February 28, 2007 with respect to the equipment facility, and those advances mature on November 30, 2009 and February 28, 2010, respectively. The Company is not entitled to obtain any additional advances under the equipment facility. The equipment facility is required to be repaid in 36 equal monthly installments of principal, plus interest. The interest rate applicable to the loans under the equipment facility is the bank's prime rate plus 0.25%.

On July 29, 2009, the Company entered into a new credit facility with a bank with no amount drawn down on the line as of August 31, 2009. The new facility provides for a new revolving line of credit with a maturity date of July 28, 2010. An aggregate principal amount of up to \$9.0 million may be outstanding at any time under the revolving line. With respect to borrowings in excess of \$4.0 million, the revolving line is a receivables borrowing base credit facility. The revolving line also includes a sublimit of up to \$4.0 million for letters of credit, cash management and foreign exchange services. The interest rate applicable to the revolving line is,

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at the Company's option, equal to either (i) the sum of the Prime Rate (as defined in the facility) plus 0.25%, or (ii) the sum of the LIBOR Rate (as defined in the facility) plus 3.25%. The new credit facility also incorporates under its terms the outstanding balance owed under the prior equipment facility, but the repayment terms of the prior equipment facility otherwise remain unchanged. The outstanding balance under the equipment facility was \$0.1 million as of August 31, 2009.

The equipment facility and the new credit facility are secured by all of the Company's personal property other than its intellectual property. The facilities includes certain negative covenants restricting or limiting the ability of the Company and its subsidiaries to, among other things: encumber its intellectual property; incur additional indebtedness; create liens on its property; make certain investments and acquisitions; merge or consolidate with any other entity; convey, sell, lease, transfer or otherwise dispose of assets; change its business; experience a change of control; pay dividends, distributions or make other specified restricted payments or repurchases; and enter into certain transactions with affiliates. Such restrictions and limitations are subject to usual and customary exceptions contained in credit agreements of this nature. In addition, the facilities require the Company to satisfy a minimum consolidated EBITDA covenant on a quarterly basis and a minimum liquidity covenant on a monthly basis. If the Company violates any of these restrictive covenants or otherwise breaches the credit facility agreement, the Company may be required to repay the obligations under the facilities prior to their stated maturity date, and the bank may be able to foreclose on any collateral provided by the Company. The Company was in compliance with these covenants as of August 31, 2009.

8. Restructuring

During fiscal year 2009, management approved and initiated a plan to decrease costs during the third and fourth quarters by eliminating approximately 5% of the workforce across all functions (the 2009 Plan). The restructuring eliminated 23 positions during the third quarter, 19 positions in the fourth quarter and charges for the workforce reduction consisted primarily of severance and fringe benefits. The restructuring charges are classified as Restructuring on the statement of operations and totaled approximately \$0.5 million during the six months ended May 31, 2009 of which approximately \$0.4 million had been paid as of May 31, 2009.

During fiscal 2010, the components of accrued restructuring charges and movements within these components through August 31, 2009 for the 2009 Plan were as follows

	Workforce Reduction Charges (in thousands)
Activities for the Year Ended May 31, 2009:	
Fiscal 2009 restructuring plan	\$ 539
Deductions - cash payments	(402)
Impact of exchange rates	9
Accrual as of May 31, 2009	146
Deductions - cash payments	(37)
Adjustments	(37)
Impact of exchange rates	1
Accrual as of August 31, 2009	\$ 73

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SABA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

9. Shareholder Rights Plan

On June 2, 2009, the Company entered into a Rights Agreement (the "Rights Agreement") with Mellon Investor Services LLC, as rights agent. In connection with the Rights Agreement the Board of Directors of the Company authorized and declared a dividend of one right for each outstanding share of the Company common stock to stockholders of record at the close of business on June 15, 2009. Each right entitles the registered holder, subject to the terms of the Rights Agreement, to purchase from the Company one one-thousandth of a share (a "Unit") of Series A Preferred Stock, par value \$0.001 per share at a purchase price of \$12.50 per Unit, subject to adjustment. The rights will expire at the close of business June 2, 2012 unless earlier redeemed or exchanged. Until a right is exercised, the holder thereof, as such, will have no rights as one of the Company's stockholders, including the right to vote or to receive dividends. The rights are not immediately exercisable. Subject to the terms and conditions of the Rights Agreement, they will become exercisable ten business days after a person or group acquires, or commences a tender or exchange offer which would lead to the acquisition of, beneficial ownership of 15% or more of the Company's outstanding common stock. Once a person or group acquires beneficial ownership of 15% or more of the Company's outstanding common stock, subject to the terms of the rights agreement, each right not owned by that person or group or certain related parties will entitle its holder to purchase, at the right's then-current purchase price, units of Series A Preferred Stock or, at the Company's option, shares of common stock or cash, property or other securities of the Company having a market value equal to twice the then-current purchase price.

10. Guarantees

Saba enters into license agreements that generally provide indemnification for its customers against intellectual property claims. To date, Saba has not incurred any costs as a result of such indemnifications and has not accrued any liabilities related to such obligations in its consolidated financial statements.

Saba's license agreements also generally include a warranty that its software products will substantially operate as described in the applicable program documentation for a period of generally 90 days after delivery. To date, Saba has not incurred or accrued any material costs associated with these warranties.

11. Income Taxes

Income tax expense for the three months ended August 31, 2009 and 2008, respectively, was \$214,000, and \$159,000, respectively. Income tax during both of these periods consists primarily of federal alternative minimum tax and state taxes as well as foreign tax expense incurred as a result of local country profits.

As of August 31, 2009 and May 31, 2009, respectively, the Company has established a valuation allowance against the full amount of any U.S. net deferred tax assets. The Company currently provides a valuation allowance against deferred tax assets when it is more likely than not that some portion, or all of its deferred tax assets, will not be realized.

12. Segment Information

Saba operates in a single operating segment, providing software and services that drive organizational excellence by bringing a disciplined approach to aligning, developing, and managing people across the entire organization. The United Kingdom operations represented 13% of total revenues by country for the three months ended August 31, 2009 and 12% for the three months ended August 31, 2008.

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SABA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

13. Litigation

Litigation Relating to Initial Public Offering of Saba

In November 2001, a complaint was filed in the United States District Court for the Southern District of New York (the District Court) against the Company, certain of its officers and directors, and certain underwriters of the Company's initial public offering. The complaint was purportedly filed on behalf of a class of certain persons who purchased the Company's common stock between April 6, 2000 and December 6, 2000. The complaint alleges violations by the Company and its officers and directors of Section 11 of the Securities Act of 1933, as amended (the Securities Act), Section 10(b) of the Securities Exchange Act of 1934, as amended (the Exchange Act), and other related provisions in connection with certain alleged compensation arrangements entered into by the underwriters in connection with the initial public offering. An amended complaint was filed in April 2002. Similar complaints have been filed against hundreds of other issuers that have had initial public offerings since 1998. The complaints allege that the prospectus and the registration statement for the initial public offering failed to disclose that the underwriters allegedly solicited and received excessive commissions from investors and that some investors in the initial public offering agreed with the underwriters to buy additional shares in the aftermarket in order to inflate the price of the Company's stock. The complaints were later consolidated into a single action. The complaint seeks unspecified damages, attorney and expert fees, and other unspecified litigation costs.

On July 1, 2002, the underwriter defendants in the consolidated actions moved to dismiss all of the actions, including the action involving the Company. On July 15, 2002, the Company, along with other non-underwriter defendants in the coordinated cases, moved to dismiss the litigation. On February 19, 2003, the District Court ruled on the motions. The District Court granted the Company's motion to dismiss the claims against the Company under Rule 10b-5, due to the insufficiency of the allegations against the Company. The District Court also granted the motion of the individual defendants, Bobby Yazdani and Terry Carlitz, the Company's Chief Executive Officer and Chairman of the Board and former Chief Financial Officer and a member of the Company's Board of Directors, to dismiss the claims against them under Rule 10b-5 and Section 20 of the Exchange Act. The motions to dismiss the claims under Section 11 of the Securities Act were denied as to virtually all of the defendants in the consolidated cases, including the Company.

In June 2003, a proposed collective partial settlement of this litigation was structured between the plaintiffs, the issuer defendants in the consolidated actions, the issuer officers and directors named as defendants, and the issuers' insurance companies. In June 2004, an agreement of partial settlement was submitted to the District Court for preliminary approval. The District Court granted the preliminary approval motion on February 15, 2005, subject to certain modifications. On August 31, 2005 the District Court issued a preliminary order further approving the modifications to the settlement and certifying the settlement classes. The District Court also appointed the notice administrator for the settlement and ordered that notice of the settlement be distributed to all settlement class members by January 15, 2006. The settlement fairness hearing occurred on April 24, 2006, and the District Court reserved decision at that time.

While the partial settlement was pending approval, the plaintiffs continued to litigate against the underwriter defendants. The District Court directed that the litigation proceed within a number of focus cases rather than in all of the 310 cases that have been consolidated. The Company's case is not one of these focus cases. On October 13, 2004, the District Court certified the focus cases as class actions. The underwriter defendants appealed that ruling, and on December 5, 2006, the Court of Appeals for the Second Circuit reversed the District Court's class certification decision. On April 6, 2007, the Second Circuit denied plaintiffs' petition for rehearing. In light of the Second Circuit opinion, counsel for the issuer defendants informed the District Court that this settlement could not be approved because the defined settlement class, like the litigation class, could not be certified. On June 25, 2007, the District Court entered an order terminating the settlement agreement. On August 14, 2007, the plaintiffs filed their second consolidated amended class action complaints against the focus cases and on September 27, 2007, again moved for class certification. On November 12, 2007, certain of the defendants in the focus cases moved to dismiss the second consolidated amended class action complaints. On March 26, 2008, the District Court denied the motions to dismiss except as to Section 11 claims raised by those plaintiffs who sold their securities for a price in excess of the initial offering price and those who purchased outside the previously certified class period. Briefing on the class certification motion was completed in May 2008. That motion was withdrawn without prejudice on October 10, 2008.

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SABA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

On April 2, 2009, a stipulation and agreement of settlement among the plaintiffs, issuer defendants and underwriter defendants was submitted to the Court for preliminary approval. The Court granted the plaintiffs' motion for preliminary approval and preliminarily certified the settlement classes on June 10, 2009. The settlement fairness hearing was held on September 10, 2009. On October 5, 2009, the Court entered an opinion granting final approval to the settlement and directing that the Clerk of the Court close these actions. Appeals of the final approval decision must be filed within 30 days of the date judgment is entered. The settlement provides, among other things, a release of Saba and its officers, and Saba's agreement to assign to the plaintiffs certain potential claims Saba may have against its underwriters. Any direct financial impact of the proposed settlement is expected to be borne by Saba's insurers.

We intend to dispute these claims and defend the law suit vigorously. However, due to the inherent uncertainties of litigation and because the time to file an appeal of final approval of the settlement has not run, the ultimate outcome of the litigation is uncertain. An unfavorable outcome in litigation could materially and adversely affect the Company's business, financial condition and results of operations.

Litigation Relating to Centra's Initial Public Offering

Centra, certain of its former officers and directors and the managing underwriters of Centra's initial public offering were named as defendants in an action filed in the District Court. The plaintiffs filed an initial complaint on December 6, 2001 and purported to serve the Centra defendants on or about March 18, 2002. The original complaint has been superseded by an amended complaint filed in April 2002. The action, captioned in re Centra Software, Inc. Initial Public Offering Securities Litigation, No. 01 CV 10988, is purportedly brought on behalf of the class of persons who purchased Centra's common stock between February 3, 2000 and December 6, 2000. The complaint asserts claims under Sections 11 and 15 of the Securities Act and Sections 10(b) and 20(a) of the Exchange Act. The complaint alleges that, in connection with Centra's initial public offering in February 2000, the underwriters received undisclosed commissions from certain investors in exchange for allocating shares to them and also agreed to allocate shares to certain customers in exchange for the agreement of those customers to purchase additional shares in the aftermarket at pre-determined prices. The complaint asserts that Centra's registration statement and prospectus for the offering were materially false and misleading due to their failure to disclose these alleged arrangements. The complaint seeks damages in an unspecified amount against Centra and the named individuals. Similar complaints have been filed against hundreds of other issuers that have had initial public offerings since 1998; the complaints have been consolidated into an action captioned in re Initial Public Offering Securities Litigation, No. 21 MC 92.

On July 1, 2002, the underwriter defendants in the consolidated actions moved to dismiss all the actions, including the action involving Centra. On July 15, 2002, Centra, along with other non-underwriter defendants in the coordinated cases, moved to dismiss the litigation. On October 9, 2002, the plaintiffs dismissed, without prejudice, the claims against the named Centra officers and directors in the above-referenced action. On February 19, 2003, the District Court issued an order denying the motion to dismiss the claims against Centra under Rule 10b-5. The motions to dismiss the claims under Section 11 of the Securities Act were denied as to virtually all of the defendants in the consolidated cases, including Centra.

In June 2003, a proposed collective partial settlement of this litigation was structured between the plaintiffs, the issuer defendants in the consolidated actions, the issuer officers and directors named as defendants, and the issuers' insurance companies. In June 2004, an agreement of settlement was submitted to the District Court for preliminary approval. The District Court granted the preliminary approval motion on February 15, 2005, subject to certain modifications. On August 31, 2005 the District Court issued a preliminary order further approving the modifications to the settlement and certifying the settlement classes. The District Court also appointed the notice administrator for the settlement and ordered that notice of the settlement be distributed to all settlement class members by January 15, 2006. The settlement fairness hearing occurred on April 24, 2006, and the District Court reserved decision at that time.

While the partial settlement was pending approval, the plaintiffs continued to litigate against the underwriter defendants. The District Court directed that the litigation proceed within a number of "focus cases" rather than in all of the 310 cases that have been consolidated. The Company's case is not one of these focus cases. On October 13, 2004, the District Court certified the focus cases as class actions. The underwriter defendants appealed that ruling, and on December 5, 2006, the Court of Appeals for the Second Circuit reversed the District Court's class certification decision. On April 6, 2007, the Second Circuit denied plaintiffs' petition for rehearing. In light of the Second Circuit opinion, counsel for the issuer defendants informed the District Court that this settlement could not be

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SABA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

approved because the defined settlement class, like the litigation class, could not be certified. On June 25, 2007, the District Court entered an order terminating the settlement agreement. On August 14, 2007, the plaintiffs filed their second consolidated amended class action complaints against the focus cases and on September 27, 2007, again moved for class certification. On November 12, 2007, certain of the defendants in the focus cases moved to dismiss the second consolidated amended class action complaints. On March 26, 2008, the District Court denied the motions to dismiss except as to Section 11 claims raised by those plaintiffs who sold their securities for a price in excess of the initial offering price and those who purchased outside the previously certified class period. Briefing on the class certification motion was completed in May 2008. That motion was withdrawn without prejudice on October 10, 2008.

On April 2, 2009, a stipulation and agreement of settlement among the plaintiffs, issuer defendants and underwriter defendants was submitted to the Court for preliminary approval. The Court granted the plaintiffs' motion for preliminary approval and preliminarily certified the settlement classes on June 10, 2009. The settlement fairness hearing was held on September 10, 2009. On October 5, 2009, the Court entered an opinion granting final approval to the settlement and directing that the Clerk of the Court close these actions. Appeals of the final approval decision must be filed within 30 days of the date judgment is entered. The settlement provides, among other things, a release of Centra and its officers, and Centra's agreement to assign to the plaintiffs certain potential claims Centra may have against its underwriters. Any direct financial impact of the proposed settlement is expected to be borne by Centra's insurers.

We, on behalf of Centra, intend to dispute these claims and defend the law suit vigorously. However, due to the inherent uncertainties of litigation and because the time to file an appeal of final approval of the settlement has not run, the ultimate outcome of the litigation is uncertain. An unfavorable outcome in litigation could materially and adversely affect the Company's business, financial condition and results of operations.

Litigation Relating to Claim of Patent Infringement by Centra

On August 19, 2003, a complaint was filed against Centra and two other defendants by EdiSync Systems, LLC, in the United States District Court for the District of Colorado (No. 03-D-1587 (OES)) (the Colorado District Court). The complaint alleges infringement of two patents for a remote multiple user editing system and method and seeks permanent injunctive relief against continuing infringement, compensatory damages in an unspecified amount, and interest, costs and expenses associated with the litigation. Centra filed an answer to the complaint denying all of the allegations. No amount has been accrued related to this matter and legal costs incurred in the defense of the matter are being expensed as incurred. Centra filed a request for reexamination of the patents at issue with the U.S. Patent and Trademark Office (the Patent Office). The Company's patent counsel is of the opinion that claims of the patents involved in the suit are invalid. The re-examination request was accepted by the Patent Office and the Colorado District Court approved the parties' motion to stay the court proceedings during the re-examination proceedings. A reexamination certificate has issued for one of the patents that canceled all of the patent's claims, thus rendering that patent of no further force or effect. The Patent Office issued a reexamination certificate for the other patent canceling all of the patent's original claims and allowing certain newly-added claims. The Company believes it is free from liability for past actions, as it believes the newly-added claims would be enforceable only prospectively as of the issue date of the reexamination certificate. Centra has since filed a second reexamination request asking the Patent Office to reconsider the patentability of the newly-added claims in view of newly-discovered prior art and the Patent Office has granted that request. Centra filed a motion with the Colorado District Court seeking a further stay of the action pending completion of the second reexamination proceeding but that motion has not yet been decided. The Company believes that it has meritorious defenses with respect to any future claims and intends to vigorously defend this action. However, due to the inherent uncertainties of litigation, the Company cannot accurately predict the ultimate outcome of the litigation. An unfavorable outcome of the litigation could materially and adversely affect the Company's business, financial condition and results of operations.

Table of Contents**SABA SOFTWARE, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)*****Litigation Relating to Claim of Patent Infringement by Saba***

On November 19, 2007, a complaint was filed against the Company and ten other defendants by Gemini IP, LLC, in the United States District Court for the Eastern District of Texas (No. 07-CV-521) (the Texas District Court). The complaint alleges infringement of a patent directed to a method for processing client help requests using a computer network and seeks permanent injunctive relief against continuing infringement, compensatory damages in an unspecified amount, and interest, costs and expenses associated with the litigation. The Company filed an answer to the complaint denying all of the allegations. At the Company's request, the United States Patent and Trademark Office (the Patent Office) has instituted reexamination proceedings against the asserted patent and the Texas District Court has stayed the action pending the outcome of those proceedings. The Company believes that it has meritorious defenses with respect to the asserted patent and intends to vigorously defend this action. However, due to the inherent uncertainties of litigation, the Company cannot accurately predict the ultimate outcome of the litigation. An unfavorable outcome of the litigation could materially and adversely affect the Company's business, financial condition and results of operations.

Other Litigation

The Company is also a party to various legal disputes and proceedings arising from the ordinary course of general business activities. While, in the opinion of management, resolution of these matters is not expected to have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows, the ultimate outcome of any litigation is uncertain. Were an unfavorable outcome to occur, the impact could be material to the Company.

14. Recent Accounting Pronouncements

In August 2009, the FASB issued Accounting Standards Update 2009-05, *Fair Value Measurements and Disclosures (Topic 820) Measuring Liabilities at Fair Value* (Update 2009-05). Update 2009-05 provides clarification that in circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity is required to measure fair value of such liability using one or more of the techniques prescribed by the update. The Company will adopt Update 2009-05 in the second quarter of fiscal 2010 and is currently evaluating the impact of its pending adoption on the Company's consolidated financial statements.

In June 2009, the FASB issued SFAS No. 168, *The FASB Accounting Standards CodificationTM and the Hierarchy of Generally Accepted Accounting Principles, a replacement of FASB Statement No. 162* (the Codification). The Codification, which was launched on July 1, 2009, became the single source of authoritative non-governmental US GAAP superseding various existing authoritative accounting pronouncements. The Codification eliminates the GAAP hierarchy contained in SFAS No. 162 and establishes one level of authoritative GAAP. All other literature is considered non-authoritative. This Codification is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Company will adopt the Codification in the second quarter of fiscal 2010. There will be no change to the Company's consolidated financial statements due to the implementation of the Codification other than changes in reference to various authoritative accounting pronouncements in the Company's consolidated financial statements.

In May 2009, the FASB issued SFAS No. 165, *Subsequent Events*. SFAS No. 165 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before the financial statements are issued or are available to be issued. The Company adopted SFAS No. 165 in the first quarter of fiscal 2010. The adoption of SFAS No. 165 did not have any impact on the Company's consolidated financial statements.

In April 2009, the FASB issued FASB Staff Position No. FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*. This FASB Staff Position (FSP) amends the other-than-temporary impairment accounting guidance for debt securities. This Staff Position requires that other-than-temporary impairment be separated into the amount of the total impairment related to credit losses and the amount of the total impairment related to all other factors. The amount of the total other-than-temporary impairment related to credit losses is recognized in earnings and the amount related to all other factors is recognized in other comprehensive income. This Staff Position is effective for interim and annual reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. The adoption of FSP No. FAS 115-2 and FAS 124-2 in its first quarter of fiscal 2010 did not have a material impact on the Company's consolidated

financial statements.

Table of Contents**SABA SOFTWARE, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)**

In November 2008, the FASB ratified Emerging Issues Task Force Issue No. 08-7, *Accounting for Defensive Intangible Assets*. EITF 08-7 clarifies the accounting for certain separately identifiable intangible assets which an acquirer does not intend to actively use but intends to hold to prevent its competitors from obtaining access to them. EITF 08-7 requires an acquirer in a business combination to account for a defensive intangible asset as a separate unit of accounting which should be amortized to expense over the period the asset diminishes in value. EITF 08-7 is effective for fiscal years beginning after December 15, 2008, with early adoption prohibited. The Company adopted EITF 08-7 in the first quarter of fiscal 2010. The adoption of EITF 08-7 did not have material impact on the Company's consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. In February 2008, the FASB issued FASB Staff Position No. FAS 157-1, *Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13* and FASB Staff Position No. FAS 157-2, *Effective Date of FASB Statement No. 157*. Collectively, the Staff Positions defer the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008 for nonfinancial assets and nonfinancial liabilities except for items that are recognized or disclosed at fair value on a recurring basis at least annually, and amend the scope of SFAS No. 157. The Company adopted SFAS No. 157 in the first quarter of fiscal 2009, except for those items specifically deferred under FSP No. FAS 157-2, which were adopted in the first quarter of fiscal 2010. The adoption of SFAS No. 157 did not have a material impact on the Company's consolidated financial statements.

In April 2008, the FASB issued FSP No. FAS 142-3, *Determination of the Useful Life of Intangible Assets*. This guidance is intended to improve the consistency between the useful life of a recognized intangible asset under SFAS No. 142, *Goodwill and Other Intangible Assets*, and the period of expected cash flows used to measure the fair value of the asset under SFAS No. 141(R) when the underlying arrangement includes renewal or extension of terms that would require substantial costs or result in a material modification to the asset upon renewal or extension. Companies estimating the useful life of a recognized intangible asset must now consider their historical experience in renewing or extending similar arrangements or, in the absence of historical experience, must consider assumptions that market participants would use about renewal or extension as adjusted for SFAS No. 142's entity-specific factors. The adoption of FSP No. FAS 142-3 in the first quarter of fiscal 2010 did not have a material impact on the Company's consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (revised) (SFAS No. 141(R)), *Business Combinations*. SFAS No. 141(R) changes the accounting for business combinations including the measurement of acquirer shares issued in consideration for a business combination, the recognition of contingent consideration, the accounting for preacquisition gain and loss contingencies, the recognition of capitalized in-process research and development, the accounting for acquisition-related restructuring cost accruals, the treatment of acquisition related transaction costs and the recognition of changes in the acquirer's income tax valuation allowance. SFAS No. 141(R) is effective for fiscal years beginning after December 15, 2008, with early adoption prohibited. The Company adopted SFAS No. 141(R) in the first quarter of fiscal year 2010. The adoption of SFAS No. 141(R) did not have material impact on the Company's consolidated financial statements.

15. Related Party Transactions

During the first quarter of 2010 and 2009, Saba licensed software and sold related support and services to Varian Medical Systems, Inc. (Varian) and Masimo Corporation (Masimo). Both an Executive Vice President of Varian and the Chairman and Chief Executive Officer of Masimo serve as directors on Saba's Board of Directors.

Table of Contents**SABA SOFTWARE, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****(Unaudited)**

During first quarter of fiscal 2010 and 2009, the components of related party transactions were as follows:

	Sales to Related Party		Accounts Receivable	
	August 31, 2009	August 31, 2008	August 31, 2009	May 31, 2009
(in thousands)				
Varian Medical Systems, Inc.	\$ 50	\$ 52	\$ 29	\$ 15
Masimo Corporation	4			1
Total	\$ 54	\$ 52	\$ 29	\$ 16

On August 28, 2009, the Company repurchased 1,384,920 shares of its common stock directly from funds managed by FirstMark Capital L.L.C. in a negotiated transaction for an aggregate purchase price of \$4.85 million. Lawrence D. Lenihan, Jr., a member of the Company's Board of Directors until July 17, 2009, is the Chief Executive Officer and Managing Director of FirstMark Capital, LLC.

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ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the consolidated financial statements and related notes contained herein and the information included in our other filings with the Securities and Exchange Commission. This discussion includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). All statements in this Quarterly Report on Form 10-Q other than statements of historical fact are forward-looking statements. These forward-looking statements involve known and unknown risks and uncertainties. Our actual results may differ materially from those projected or assumed in such forward-looking statements. Among the factors that could cause actual results to differ materially are the factors detailed under Part II, Item 1A: Risk Factors of this Quarterly Report on Form 10-Q. All forward-looking statements and risk factors included in this document are made as of the date of this report, based on information available to us as of such date. We assume no obligation to update any forward-looking statement or risk factor.

Forward-looking statements include statements regarding:

(i) in Part I, Item 1,

future amortization related to intangible assets,

our anticipation that we will not pay any cash dividends in the foreseeable future,

the resolution and effect of pending litigation and our belief regarding our defenses to any such litigation, and

the effect of recent accounting pronouncements

(ii) in Part I, Item 2,

our expectation that the Saba Enterprise Suite and Saba Centra product suite will generate substantially all of our license revenues for the foreseeable future,

our belief that OnDemand revenue will continue to grow for the foreseeable future,

our belief that license updates and product support revenue will continue to grow for the foreseeable future due to our expanded customer base,

our anticipation that a substantial majority of our customers will renew their annual contracts,

our expectations relating to future amortization expenses,

our anticipation that we will continue to experience long sales cycles,

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our expectation that recent accounting pronouncements will not impact our consolidated financial statements,

our anticipation that our available cash resources and credit facilities, combined with cash flows generated from revenues, will be sufficient to meet our presently anticipated working capital, capital expense and business expansion requirements, for at least the next 12 months, and

our anticipation that we will not pay any cash dividends in the foreseeable future,
(iii) in Part II, Item 1A,

our expectation that we will derive substantially all of our revenues for the foreseeable future from the licensing of the Saba Enterprise Suite and the Saba Centra product suite and providing related services,

our expectation to continue to incur non-cash expenses relating to the amortization of purchased intangible assets along with any potential goodwill impairment,

our expectation that our operating results will fluctuate significantly in the future,

our success depending on our ability to attract and retain additional personnel,

our expectation that competition and the pace of change will increase in the future,

our intention to expand our international presence in the future,

our expectation to continue to acquire periodically complementary businesses or technologies,

our expectation to regularly release new products and new versions of our existing products,

our beliefs relating to the Edisync Systems litigation,

our belief that our success depends on our proprietary technology, and

our belief that our success depends on third party relationships.

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These forward-looking statements involve known and unknown risks and uncertainties. Our actual results may differ materially from those projected or assumed in such forward-looking statements. Among the factors that could cause actual results to differ materially are among others:

defects and other problems with our products,

unanticipated adverse changes in the international markets,

incorrect estimates or assumptions,

unanticipated adverse results for pending litigation,

contraction of the economy and world markets,

lack of demand for information technologies from our customers,

requirements for increased spending in research and development,

unanticipated need for capital for operations,

lack of demand for our products,

negative effects of amortization rates,

inability to accurately predict the impact of new accounting pronouncements,

unanticipated difficulties integrating and developing products acquired through acquisitions,

*inability to introduce new products, and
the factors detailed under Part II, Item 1A: Risk Factors of this Quarterly Report on Form 10-Q.*

OVERVIEW

General

We help organizations manage their most important asset – their people. We provide the premier software platform for enterprise learning, collaboration, performance, and talent management, as well as license updates and product support, OnDemand, implementation, training, and consulting services. Our people management solutions drive organizational excellence by bringing a disciplined approach to aligning,

developing and managing people across the entire organization.

By using Saba products to manage their extended workforce, our customers achieve demonstrably higher levels of performance through:

Increased productivity, sales and service effectiveness;

Reduced personnel development and training costs; and

Improved organizational agility and execution.

Our solutions help our customers through the implementation of a management system for aligning goals, developing and motivating people and measuring results. By implementing our solutions, organizations are better equipped to: align their workforce around the organization's business objectives; effectively manage growing regulatory requirements; increase sales and channel readiness; accelerate the productivity of new people joining the extended enterprise of employees, customers, partners, and suppliers; increase both the speed of customer acquisition and long-term customer loyalty; shorten time-to-market of new products; and improve visibility into organizational performance.

Background

We commenced operations in April 1997 and, through March 1998, focused substantially all of our efforts on research activities, developing our products and building our business infrastructure. We shipped our first Saba Enterprise Learning products and began to generate revenues from software license fees, implementation and consulting services fees and support fees in April 1998.

Our corporate headquarters are located in Redwood Shores, California. We have an international presence in Australia, Canada, France, Germany, India, Japan and the United Kingdom through which we conduct various operating activities related to our business. In each of the non-U.S. jurisdictions in which we have subsidiaries, other than India, we have employees or consultants engaged in sales and services activities. In the case of our India subsidiary, our employees primarily engage in software development and quality assurance testing activities.

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Sources of Revenue

We generate revenues from the sale of software licenses, OnDemand services, license updates and product support and professional services.

Software Licenses

We license our software solutions in multi-element arrangements that include a combination of our software, license updates and product support and/or professional services. A significant amount of our license sales are for perpetual licenses. To date, a substantial majority of our software license revenue has been derived from the Saba Learning product suite. For the foreseeable future, we expect the Saba Enterprise Suite and Saba Centra product suite to generate substantially all of our software license revenue. Our license revenue is affected by the strength of general economic and business conditions, as well as customers' budgetary cycles and the competitive position of our software products. In addition, the sales cycle for our products is long, typically six to twelve months. The timing of a few large software license transactions can substantially affect our quarterly license revenue.

OnDemand

OnDemand revenue includes revenue derived from term-based managed application services. These services are provided pursuant to customer agreements with terms typically ranging from one to three years. The associated OnDemand revenue is recognized ratably over the term of the agreement. We believe that OnDemand revenue will continue to grow for the foreseeable future as we anticipate that a substantial majority of our customers will renew their contracts on expiration and that we will continue to add new OnDemand customers.

Licenses Updates and Product Support

License updates and product support includes the right to receive future unspecified updates for the applicable software product and technical support. We typically sell license updates and product support for an initial period of one year concurrently with the sale of the related software license. After the initial period, license updates and product support is renewable on an annual basis at the option of the customer. Our license updates and product support revenue depends upon both our sales of additional software licenses and annual renewals of existing license updates and product support agreements. We believe that license updates and product support revenue will grow steadily for the foreseeable future as we anticipate that a substantial majority of our customers will renew their annual contracts and the sale of new software licenses will increase the number of customers that purchase license updates and product support.

Professional Services

Our professional services business consists of consulting, education and strategic services. Consulting and education services are typically provided to customers that license software directly from us. These consulting and education services are generally provided over a period of three to nine months after licensing the software. Generally, consulting services related to software implementation are not considered essential to the functionality of the software. Our consulting and education services revenue varies directly with the levels of license revenue generated from our direct sales organization in the preceding three to nine month period. In addition, our consulting and education services revenue varies following our commercial release of significant software updates as our customers generally engage our services to assist with the implementation of their software update. We provide consulting services on a time and materials basis and on a fixed fee basis. Strategic services are less dependent than consulting and education services on the sale of our licenses. Strategic services present additional opportunities that arise at different times throughout a customer life cycle. In arrangements that include professional services and OnDemand offerings, but not a license of our software, we recognize revenue for professional services as the services are performed if these professional services qualify as a separate element of the arrangement. If the professional services do not qualify as a separate element of the arrangement, the related revenue is combined with the subscription revenue and recognized ratably over the subscription service period.

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Cost of Revenue

Our cost of revenue primarily consists of compensation, employee benefits and out-of-pocket travel-related expenses for our employees, and the fees of third-party subcontractors, who provide professional services, OnDemand services and license update and product support to our clients. Cost of revenue also includes external hosting fees and depreciation and amortization charges related to the OnDemand infrastructure, third-party license royalty costs, overhead allocated based on headcount and reimbursed expenses. The amortization of acquired developed technology, comprised of the ratable amortization of technological assets acquired in an acquisition in 2006, is also included in the cost of revenue. Many factors affect our cost of revenue, including changes in the mix of products and services, pricing trends and changes in the amount of reimbursed expenses. Because cost as a percentage of revenues is higher for services than for software licenses, an increase in services, including OnDemand services, as a percentage of our total revenue would reduce gross profit as a percentage of total revenue.

Additionally, when our professional services revenue is combined with our OnDemand subscription revenue, we also defer the direct costs related to the professional services and recognize them ratably over the applicable service period. We classify deferred revenue and deferred costs on our consolidated balance sheet as current if we expect to recognize such revenue or cost within the following twelve months. As of August 31, 2009, the deferred balance of the professional services revenue related to such OnDemand offerings and the related deferred costs was \$1.9 million and \$0.9 million, respectively. When the revenue from professional services is recognized ratably over the subscription service period, we allocate the revenue to professional services revenue and to OnDemand revenue based on the VSOE of fair value for similar professional services that qualify as a separate element of the arrangement. Our judgment as to whether the consulting services qualify as a separate unit of accounting may materially affect the timing of our revenue recognition and our results of operations.

Operating Expenses

We classify all operating expenses, except amortization of purchased intangible assets and restructuring, to the research and development, sales and marketing, and general and administrative expense categories based on the nature of the expenses. Each of these three categories includes commonly recurring expenses such as salaries (including stock-based compensation), employee benefits, travel and entertainment costs, and allocated communication, rent and depreciation costs. We allocate communication, rent and depreciation costs to each of the functional areas that derive a benefit from such costs based upon their respective headcounts. The sales and marketing category of operating expenses also includes sales commissions and expenses related to public relations and advertising, trade shows and marketing collateral materials. The general and administrative category of operating expenses also includes allowances for doubtful accounts, and administrative and professional services fees.

CRITICAL ACCOUNTING POLICIES

Our discussion and analysis of financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with US GAAP. The preparation of financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ materially from those estimates. We base our estimates and judgments on historical experience and on various other assumptions that we believe are reasonable under the circumstances. However, future events are subject to change and the best estimates and judgments routinely require adjustment. While a number of accounting policies, methods and estimates affect our financial statements, areas that are particularly significant include revenue recognition policies, the allowance for doubtful accounts, the assessment of recoverability of goodwill and purchased intangible assets and restructuring costs. We have reviewed the critical accounting policies described in the following paragraphs with the Audit Committee of our Board of Directors.

Revenue recognition. We recognize license revenues addressed below in accordance with the provisions of American Institute of Certified Public Accountants (AICPA) Statement of Position (SOP) 97-2, *Software Revenue Recognition*, as amended by SOP 98-9, *Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions*. Under SOP 97-2, as amended, we recognize revenues when all of the following conditions are met:

persuasive evidence of an arrangement exists;

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delivery has occurred;

the fee is fixed or determinable; and

collection is probable.

SOP 97-2, as amended, permits revenue earned on software arrangements involving multiple elements to be allocated to each element based on the residual method, under which revenue is allocated to undelivered elements based on vendor-specific objective evidence of fair value of such undelivered elements and the residual amounts of revenue are allocated to deliver elements. We have analyzed each element in our multiple element arrangements and determined that we have sufficient vendor-specific objective evidence (VSOE) to allocate revenues to certain OnDemand offerings, license updates and product support and professional services. Accordingly, assuming all other revenue recognition criteria are met, revenues from perpetual licenses are recognized upon delivery using the residual method in accordance with SOP 98-9. We limit our assessment of VSOE for each element to the price charged when the same element is sold separately, price charged upon renewal or the price established by management, having the relevant authority to do so, for an element not yet sold separately.

License revenues from licenses with a term of three years or more are generally recognized on delivery if the other conditions of SOP 97-2 are satisfied. We do not grant our resellers the right of return and we do not recognize revenue from resellers until an end-user has been identified and the other conditions of SOP 97-2 are satisfied. License revenues from licenses with a term of less than three years are generally recognized ratably over the term of the arrangement. License updates and product support revenue is also recognized ratably over the term of the arrangement, typically 12 months. In arrangements where term licenses are bundled with license updates and product support and such revenue is recognized ratably over the term of the arrangement, we allocate the revenue to license revenue and to license updates and product support revenue based on the VSOE of fair value for license updates and product support revenue on perpetual license of similar products.

Revenue related to professional services is generally recognized as the services are performed. Although we provide professional services on a time and materials basis, a portion of these services is provided on a fixed-fee basis. For services performed on a fixed fee basis, revenues are generally recognized on the proportional performance of the project, with performance measured based on hours of work performed. For contracts that involve significant customization and implementation or consulting services that are essential to the functionality of the software, the license and services revenues are recognized over the service delivery period using the percentage-of-completion method or, if we are unable to reliably estimate the costs to complete the services, we use the completed contract method of accounting in accordance with SOP 97-2 and relevant guidance of SOP 81-1, *Accounting for Performance of Construction-Type and Certain Production Type Contracts*. A contract is considered complete when all significant costs have been incurred and the item has been accepted by the customer.

Revenue from our OnDemand offerings is recognized as a service arrangement whereby the revenue is recognized ratably over the term of the arrangement or on an as-used basis if defined in the contract. Certain of our OnDemand offerings are integrated offerings pursuant to which the customers' ability to access our software is not separable from the services necessary to operate the software and customers are not allowed to take possession of our software, in which case revenue is recognized under SAB No. 104, *Revenue Recognition*. Our OnDemand offerings also include arrangements with customers that have separately licensed and taken possession of our software. When these OnDemand offerings are part of a multiple element arrangement involving licenses, we recognize revenue in accordance with SOP 97-2, when the EITF Issue No. 00-3 *Application of AICPA Statement of Position 97-2, Software Revenue Recognition, to Arrangements That Include the Right to Use Software Stored on Another Entity's Hardware*, criteria is met.

If the requirements of SOP 97-2 are not met when we bill a customer or a customer pays us, the billed or paid amount is recorded as deferred revenue, a liability account. As the revenue recognition criteria of SOP 97-2 are satisfied, the requisite amounts are recognized as revenue.

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In arrangements that include professional services and OnDemand offerings, but not a license of our software, we recognize revenue for professional services as the services are performed if these professional services qualify as a separate element of the arrangement. If the professional services do not qualify as a separate element of the arrangement, the professional services revenue is combined with the OnDemand subscription revenue and recognized ratably over the OnDemand subscription service period. Additionally, we defer the direct costs related to the professional services and recognize them ratably over the applicable OnDemand service period. We classify deferred revenue and deferred costs on our consolidated balance sheet as current if we expect to recognize such revenue or cost within the following twelve months. When the revenue from professional services is recognized ratably over the subscription service period, we allocate the revenue to professional services revenue and to OnDemand revenue based on the VSOE of fair value for similar professional services that qualify as a separate element of the arrangement. Our judgment as to whether the consulting services qualify as a separate unit of accounting may materially affect the timing of our revenue recognition and our results of operations.

Allowance for doubtful accounts. Accounts receivable are recorded net of allowance for doubtful accounts and totaled \$18.6 million as of August 31, 2009. The allowance for doubtful accounts, which totaled \$0.1 million as of August 31, 2009, is based on our assessment of the amount of probable credit losses in the existing accounts receivable. We determine the allowance based on the aging of the accounts receivable, the financial condition of our customers and their payment history, our historical write-off experience and other assumptions. Past due balances based on order terms and other specific accounts as necessary are reviewed monthly. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. If there is a deterioration of a major customer's credit worthiness or actual defaults are higher than our historical experience, we may be required to increase the allowance for doubtful accounts.

Impairment of goodwill and purchased intangible assets. We account for goodwill under SFAS No. 142, *Goodwill and Other Intangible Assets*. Our goodwill balance at August 31, 2009 was \$36.1 million, including \$21.3 million and \$9.5 million recorded as a result of our acquisitions of Centra and THINQ, respectively. Our goodwill balance at May 31, 2009 was \$36.1 million including \$21.3 million and \$9.5 million recorded as a result of our acquisitions of Centra and THINQ, respectively. We account for purchased intangible assets under SFAS No. 144. As of August 31, 2009, our purchased intangible assets balance was \$7.8 million, net of accumulated amortization. The total expected future amortization related to purchased intangible assets will be approximately \$2.8 million for the remainder of fiscal 2010 and \$3.3 million and \$1.8 million in fiscal years 2011 through 2012, respectively.

SFAS No. 142 prescribes a two-phase process for impairment testing of goodwill. The first phase screens for impairment; while the second phase, if necessary, measures the impairment. We consider Saba to be a single reporting unit. Accordingly, all of our goodwill is associated with the entire company. We perform the required impairment analysis of goodwill annually or on a more frequent basis if indicators of impairment arise or circumstances otherwise dictate. A significant and extended reduction in our enterprise fair value to below the recorded amount of our stockholders' equity could indicate a change in our business climate and under SFAS 142, we could be required to write down the carrying value of our goodwill and record an expense for an impairment loss.

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, we review our long-lived asset groups, including property and equipment and other intangibles, for impairment whenever events indicate that their carrying amount may not be recoverable.

Share-based compensation. Upon our adoption of SFAS 123R, we were required to estimate the awards that we ultimately expect to vest and to reduce share-based compensation expense for the effects of estimated forfeitures of awards over the expense recognition period. Although we estimate forfeitures based on historical experience, forfeitures in the future may differ. Under SFAS 123R, the forfeiture rate must be revised if actual forfeitures differ from our original estimates. Also in connection with our adoption of SFAS 123R, we elected to recognize awards granted after our adoption date under the straight-line amortization method.

We estimate the fair value of employee stock options using the Black-Scholes-Merton (BSM) pricing model. The fair value of an award is affected by our stock price on the date of grant as well as other assumptions including the estimated volatility of our stock price over the term of the awards and the estimated period of time that we expect employees to hold their stock options. For RSUs, stock compensation is calculated based on the fair market value of the stock on the award date. The risk-free interest rate assumption is based upon United States treasury interest rates appropriate for the expected life of the awards. We estimate the volatility of our common stock based upon our historical stock price volatility over the length of the expected term of the stock option. We use

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historical data to estimate pre-vesting option forfeitures and record share-based compensation expense only for those awards that are expected to vest. Our expected dividend rate is zero since we do not currently pay cash dividends on our common stock and do not anticipate doing so in the foreseeable future.

Recent Accounting Pronouncements

In August 2009, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2009-05, *Fair Value Measurements and Disclosures (Topic 820) Measuring Liabilities at Fair Value* (Update 2009-05). Update 2009-05 provides clarification that in circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity is required to measure fair value of such liability using one or more of the techniques prescribed by the update. We will adopt Update 2009-05 in the second quarter of fiscal 2010 and are currently evaluating the impact of its pending adoption on our consolidated financial statements.

In June 2009, the FASB issued Statement No. 168, *The FASB Accounting Standards CodificationTM and the Hierarchy of Generally Accepted Accounting Principles, a replacement of FASB Statement No. 162* (the Codification). The Codification, which was launched on July 1, 2009, became the single source of authoritative non-governmental U.S. generally accepted accounting principles (GAAP), superseding various existing authoritative accounting pronouncements. The Codification eliminates the GAAP hierarchy contained in Statement 162 and establishes one level of authoritative GAAP. All other literature is considered non-authoritative. This Codification is effective for financial statements issued for interim and annual periods ending after September 15, 2009. We will adopt the Codification in the second quarter of fiscal 2010. There will be no change to our consolidated financial statements due to the implementation of the Codification other than changes in reference to various authoritative accounting pronouncements in our consolidated financial statements.

In May 2009, the FASB issued SFAS No. 165, *Subsequent Events*. SFAS No.165 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before the financial statements are issued or are available to be issued. We adopted SFAS No.165 in the first quarter of fiscal 2010. The adoption of SFAS No. 165 did not have any impact on our consolidated financial statements.

In April 2009, the FASB issued FASB Staff Position No. FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*. This FASB Staff Position (FSP) amends the other-than-temporary impairment accounting guidance for debt securities. This Staff Position requires that other-than-temporary impairment be separated into the amount of the total impairment related to credit losses and the amount of the total impairment related to all other factors. The amount of the total other-than-temporary impairment related to credit losses is recognized in earnings and the amount related to all other factors is recognized in other comprehensive income. This Staff Position is effective for interim and annual reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. We adopted FSP No. FAS 115-2 and FAS 124-2 in our first quarter of fiscal 2010 and it did not have a material impact on our consolidated financial statements.

In November 2008, the FASB ratified Emerging Issues Task Force Issue No. 08-7, *Accounting for Defensive Intangible Assets*. EITF 08-7 clarifies the accounting for certain separately identifiable intangible assets which an acquirer does not intend to actively use but intends to hold to prevent its competitors from obtaining access to them. EITF 08-7 requires an acquirer in a business combination to account for a defensive intangible asset as a separate unit of accounting which should be amortized to expense over the period the asset diminishes in value. EITF 08-7 is effective for fiscal years beginning after December 15, 2008, with early adoption prohibited. We adopted EITF 08-7 in the first quarter of fiscal 2010. The adoption of EITF 08-7 did not have material impact on our consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. In February 2008, the FASB issued FASB Staff Position No. FAS 157-1, *Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements*

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That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13 and FASB Staff Position No. FAS 157-2, Effective Date of FASB Statement No. 157. Collectively, the Staff Positions defer the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008 for nonfinancial assets and nonfinancial liabilities except for items that are recognized or disclosed at fair value on a recurring basis at least annually, and amend the scope of SFAS No. 157. We adopted SFAS No. 157 in the first quarter of fiscal year 2009, except for those items specifically deferred under FSP No. FAS 157-2, which were adopted in the first quarter of fiscal 2010. The full adoption of SFAS No. 157 did not have a material impact on our consolidated financial statements.

In April 2008, the FASB issued FSP No. FAS 142-3, *Determination of the Useful Life of Intangible Assets*. This guidance is intended to improve the consistency between the useful life of a recognized intangible asset under SFAS No. 142, *Goodwill and Other Intangible Assets*, and the period of expected cash flows used to measure the fair value of the asset under SFAS No. 141(R) when the underlying arrangement includes renewal or extension of terms that would require substantial costs or result in a material modification to the asset upon renewal or extension. Companies estimating the useful life of a recognized intangible asset must now consider their historical experience in renewing or extending similar arrangements or, in the absence of historical experience, must consider assumptions that market participants would use about renewal or extension as adjusted for SFAS No. 142's entity-specific factors. We adopted FSP No. FAS 142-3 in the first quarter fiscal 2010. The adoption of FSP No. FAS 142-3 did not have a material impact on our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (revised) (SFAS No. 141(R)), *Business Combinations*. SFAS No. 141(R) changes the accounting for business combinations including the measurement of acquirer shares issued in consideration for a business combination, the recognition of contingent consideration, the accounting for preacquisition gain and loss contingencies, the recognition of capitalized in-process research and development, the accounting for acquisition-related restructuring cost accruals, the treatment of acquisition related transaction costs and the recognition of changes in the acquirer's income tax valuation allowance. SFAS No. 141(R) is effective for fiscal years beginning after December 15, 2008, with early adoption prohibited. We adopted SFAS No. 141(R) in the first quarter of fiscal year 2010. We completed the assessment of adopting SFAS No. 141(R) and it did not have impact on the our consolidated financial statements.

Table of Contents**RESULTS OF OPERATIONS****THREE MONTHS ENDED AUGUST 31, 2009 AND 2008***Revenues*

(dollars in thousands)	Three months ended			
	August 31, 2009	Percent of Total Revenues	August 31, 2008	Percent of Total Revenues
Revenues:				
License	\$ 5,712	22%	\$ 2,958	12%
License updates and product support	8,756	34%	8,641	34%
OnDemand	5,245	20%	4,918	19%
Professional services	6,098	24%	8,782	35%
Total revenues	\$ 25,811	100%	\$ 25,299	100%

Total Revenues. Total revenues increased by \$0.5 million, or 2%, during the three months ended August 31, 2009 compared to the three months ended August 31, 2008. As a percentage of total revenues, revenues from customers outside the United States represented 25% for the three months ended August 31, 2009 and 27% for the three months ended August 31, 2008. The only foreign country that consisted of more than 10% of total revenue was the United Kingdom, which represented 13% for the three months ended August 31, 2009 and 12% for the three months ended August 31, 2008.

License Revenue. License revenue increased by \$2.8 million, or 93%, during the three months ended August 31, 2009 compared to the three months ended August 31, 2008. The increase in license revenue is due to strong customer demand and a benefit of approximately \$0.7 million due to net license revenue recognized for prior quarter deferrals.

License Updates and Product Support Revenue. License updates and product support revenue increased slightly by \$0.1 million during the three months ended August 31, 2009 compared to the three months ended August 31, 2008. The slight increase reflects the lower license revenue level in fiscal year 2009.

OnDemand Revenue. OnDemand revenue increased by \$0.3 million, or 7%, during the three months ended August 31, 2009 compared to the three months ended August 31, 2008. The increase is primarily attributable to a high rate of OnDemand renewals and increased demand for Saba Enterprise OnDemand offerings.

Professional Services Revenue. Professional services revenue decreased by \$2.7 million or 31%, during the three months ended August 31, 2009 compared to the three months ended August 31, 2008. The three month decrease is primarily attributable to customers, deferral or reduction in size of service projects during the summer months.

Cost of Revenues

(dollars in thousands)	Three months ended			
	August 31, 2009	Percent of Total Revenues	August 31, 2008	Percent of Total Revenues
Cost of revenues:				
Cost of license	\$ 210	1%	\$ 213	1%
Cost of license updates and product support	2,037	8%	2,207	9%
Cost of OnDemand	2,008	8%	2,426	10%

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Cost of professional services	4,552	18%	5,916	23%
Amortization of acquired developed technology	295	1%	295	1%
Total cost of revenues	\$ 9,102	35%	\$ 11,057	44%

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The following table is a summary of gross margin:

(dollars in thousands)	Three months ended	
	August 31, 2009	August 31, 2008
Gross margin:		
License (including amortization of acquired developed technology)	\$ 5,207	\$ 2,450
<i>Percentage of license revenue</i>	<i>91%</i>	<i>83%</i>
License updates and product support	6,719	6,434
<i>Percentage of license updates and product support revenue</i>	<i>77%</i>	<i>75%</i>
OnDemand	3,237	2,492
<i>Percentage of OnDemand revenue</i>	<i>62%</i>	<i>51%</i>
Professional services	1,546	2,866
<i>Percentage of professional services revenue</i>	<i>25%</i>	<i>33%</i>
Total	\$ 16,709	\$ 14,242
<i>Percentage of total revenues</i>	<i>65%</i>	<i>56%</i>

Cost of License Revenue. Cost of license revenue decreased slightly during the three months ended August 31, 2009 as compared to the three months ended August 31, 2008. Gross margin on license revenue increased to 91% during the three months ended August 31, 2009 from 83% during the three months ended August 31, 2008. The increase in gross margin is primarily the result of the increase in license revenues relative to the fixed cost of license revenue, including amortization of acquired technologies.

Cost of License Updates and Product Support Revenue. Cost of license updates and product support revenue decreased \$0.2 million, or 8%, during the three months ended August 31, 2009 as compared to the three months ended August 31, 2008. The decrease was primarily the result of a decrease in consulting of \$0.1 million and a net decrease of \$0.1 million comprised primarily of employee related, third party consulting and facility related expenses. Gross margin on license updates and product support was 77% during the three months ended August 31, 2009 and 75% during the three months ended August 31, 2008. The increases in gross margins are primarily due to the cost reductions.

Cost of OnDemand Revenue. Cost of OnDemand revenue decreased by \$0.4 million, or 17%, during the three months ended August 31, 2009 compared to the three months ended August 31, 2008. The decrease in the cost of OnDemand revenue was due primarily to decreases in salaries and benefits of \$0.2 million, third party consulting of \$0.1 million, and professional service charges of \$0.1 million. The OnDemand gross margin increased to 62% during the three months ended August 31, 2009 from 51% during the three months ended August 31, 2008. The increase in OnDemand gross margins is the result of higher revenue and a decrease in costs associated with providing OnDemand services.

Cost of Professional Services Revenue. For the three months ended August 31, 2009, cost of professional services revenue decreased \$1.4 million, or 23%, compared to the three months ended August 31, 2008. The decrease in cost of professional services revenue was primarily the result of decreases in third party billable labor and expenses of \$0.8 million and salaries and benefits of \$0.5 million. The professional services gross margin decreased to 25% during the three months ended August 31, 2009, from 33% during the three months ended August 31, 2008 due primarily to lower professional services revenue.

Table of Contents*Operating Expenses*

(dollars in thousands)	Three months ended			
	August 31, 2009	Percent of Total Revenue	August 31, 2008	Percent of Total Revenue
Operating expenses:				
Research and development	\$ 4,222	16%	\$ 4,286	17%
Sales and marketing	6,788	26%	7,107	28%
General and administrative	3,843	15%	4,365	17%
Restructuring	(37)	%	(24)	%
Amortization of purchased intangible assets	634	3%	634	3%
Total operating expenses	\$ 15,450	60%	\$ 16,368	65%

Research and development. Research and development expenses decreased by \$0.1 million, or 2%, for the three months ended August 31, 2009 compared to the three months ended August 31, 2008. The decrease was primarily due to a net decrease in salaries and related benefits of \$0.1 million.

Sales and marketing. Sales and marketing expenses decreased by \$0.3 million, or 4%, for the three months ended August 31, 2009 compared to the three months ended August 31, 2008. The decrease was primarily attributable to decreases in salaries and related benefits of \$0.3 million due to lower headcount, facilities related expenses of \$0.2 million and employee travel of \$0.3 million. These decreases were partially offset primarily by an increase in third party consulting fees of \$0.3 million and recruiting fees of \$0.1 million.

General and administrative. General and administrative expenses decreased by \$0.5 million, or 12%, for the three months ended August 31, 2009 compared to the three months ended August 31, 2008. The decrease was due to first quarter of fiscal 2008 non-recurring general and administrative costs of \$0.7 million primarily related to legal and accounting fees associated with the evaluation of strategic transactions, partially offset by an increase in salaries, benefits and employees related expenses of \$0.1 million and bank fees of \$0.1 million, related to the Company's line of credit entered into in the first quarter of fiscal 2010.

Amortization of purchased intangible assets. Amortization of purchased intangible assets was remained unchanged in the three months ended August 31, 2009, as compared to the three months ended August 31, 2008. Future amortization expense over each of the next four years is currently expected to be approximately \$2.8 million for the remainder of fiscal 2010 and range from \$3.3 million in fiscal 2011 to \$1.8 million in fiscal 2012. We review our intangible assets and the estimated remaining useful lives of those intangible assets for impairment when events or changes in circumstances indicate that the carrying amount might not be recoverable. Any impairment or reduction in our estimate of remaining useful lives could result in decreased amortization expense in future periods.

Restructuring. During the third quarter of fiscal year 2009, Saba management approved a plan to decrease headcount across the company by 5% by eliminating positions. During the first quarter ended August 31, 2009, the Company adjusted prior period charges for the workforce reduction, consisting of severance and fringe benefits. The restructuring charges are classified as Restructuring in the statement of operations and totaled a reduction of approximately \$37,000 during the three months ended August 31, 2009. The remaining restructuring balance of approximately \$73,000 is expected to be paid in the second quarter. Any changes to the estimates of executing the 2009 Plan will be reflected in future results of operations.

Other Income and Expenses

Interest income and other, net. Interest income and other, net consists of interest income and other non-operating expenses. Interest income and other expense, net decreased by \$0.1 million for the three months ended August 31, 2009 compared to the three months ended August 31, 2008. This decrease was primarily attributable to realized foreign currency losses of \$0.2 million and a decrease in interest income of \$11,000 partially offset by an increase in unrealized gains of \$0.2 million on certain foreign denominated transactions.

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Interest expense. Interest expense was \$3,000 for the three months ended August 31, 2009 and \$10,000 for the three months ended August 31, 2008. The decrease in interest expense during the three months ended August 31, 2009 compared to the three months ended August 31, 2008 was primarily due to the lower average debt outstanding under our bank credit facility.

Provision for income taxes The provision for income taxes recorded for the three month ended August 31, 2009 was \$0.2 million, as compared to \$0.2 million for the three months ended August 31, 2008. Income tax expense during both of these periods consists primarily of federal alternative minimum tax and state taxes as well as foreign tax expense incurred as a result of local country profits.

As of August 31, 2009 and May 31, 2009, we had established a valuation allowance against the full amount of any U.S. net deferred tax assets. We currently provide a valuation allowance against deferred tax assets when it is more likely than not that some portion, or all of our deferred tax assets, will not be realized.

DEFERRED REVENUES

Deferred revenues consisted of the following:

(in thousands)	August 31, 2009	May 31, 2009
Software license updates and product support	\$ 17,467	\$ 20,011
OnDemand	9,544	10,925
Professional services	3,153	2,998
Software licenses	688	1,405
Total deferred revenues	\$ 30,852	\$ 35,339
Deferred revenues, current	\$ 28,136	\$ 32,611
Deferred revenues, non-current	2,716	2,728
Total deferred revenues	\$ 30,852	\$ 35,339

Deferred software license updates and product support revenues represent support contracts for which cash has been received plus billings for support agreements for which the service has started but cash has not been received. Software license updates and product support contracts are typically billed on a per annum basis in advance and revenues are recognized ratably over the support periods. Deferred OnDemand revenue represents customer billings made in advance and recognized ratably over the OnDemand service term. Deferred professional services revenue includes prepayments for consulting, education, strategic services and professional services, not separable from the OnDemand subscription business. Revenue for these services is recognized as the services are performed. Deferred revenues from new software licenses typically result from undelivered products or specified enhancements, term license agreements that are recognized over the related term, customer specific acceptance provisions, and software license transactions that cannot be segmented from consulting services or certain extended payment term arrangements. Our deferred revenue is generally at its lowest annual level at the end of the first quarter. We have a disproportionately lower level of renewal billings for software license updates and product support in our first fiscal quarter. The three months ended August 31, 2008, deferred revenues were \$29.7 million.

COMMISSIONS

Commissions are generally expensed as they are earned per the terms of the sales compensation plans.

Table of Contents**KEY OPERATING METRICS****Billing**

We track operating metrics for invoicing, which represents our total billings and renewals for enterprise software maintenance and OnDemand services. For the quarter ended August 31, 2009, we invoiced \$23.4 million compared to \$25.2 million for the quarter ending August 31, 2008. Our renewal rate on enterprise software maintenance on a dollar basis, for the first quarter was 93% compared to 95% for the quarter ended August 31, 2008. Our renewal rate for our OnDemand business for the quarter ended August 31, 2009 was 92% compared to 94% for the quarter ended August 31, 2008.

FLUCTUATIONS OF QUARTERLY RESULTS

Our results of operations have in the past and will likely in the future vary significantly from quarter to quarter. If revenues fall below our expectations, we will likely not be able to reduce our spending rapidly in response to the shortfall and operating losses will increase. We anticipate that we will continue to experience long sales cycles. Therefore, the timing of future customer contracts could be difficult to predict, making it difficult to predict revenues between quarters.

Factors that could affect our quarterly operating results are described under Part II, Item: 1A *Risk Factors* of this Quarterly Report on Form 10-Q.

LIQUIDITY AND CAPITAL RESOURCES

(in thousands)	Three months ended	
	August 31, 2009	August 31, 2008
Net cash provided by operating activities	\$ 713	\$ 637
Net cash used in investing activities	\$ (183)	\$ (1,194)
Net cash used in financing activities	\$ (4,923)	\$ (19)

We have funded our operations through financing activities and our operations and our most significant source of operating cash flows stems from customer purchases of our license, license updates and product support, OnDemand and professional services. Our primary uses of cash from operating activities are for personnel and facilities related expenditures. As of August 31, 2009, we had \$21.6 million in available cash and cash equivalents.

Net Cash Provided By Operating Activities

Net cash provided by operating activities during the three months ended August 31, 2009 was \$0.7 million compared to \$0.6 million used in operating activities during the three months ended August 31, 2008. Net cash used by operating activities during the three months ended August 31, 2009 was primarily a result of adjusting our net income of \$1.0 million for non-cash expenses related to share-based compensation of \$0.3 million, depreciation and amortization of \$1.5 million, increases in accounts payable of \$1.1 million, and decreases in accounts receivable of \$1.4 million, prepaids of \$0.3 million and other assets of \$0.1 million and in deferred rent of \$0.3 million. These increases to our cash provided by operating activities were partially offset by a decrease in deferred revenue of \$4.5 million and a decrease in accrued expenses of \$0.4 million.

Net cash provided by operating activities during the three months ended August 31, 2008 was \$0.6 million, primarily a result of adjusting our net loss of \$2.2 million for non-cash expenses related to share-based compensation of \$0.6 million and depreciation and amortization of \$1.5 million, an increase in accounts payable of \$1.5 million, and decreases in accounts receivable of \$0.3 million and in prepaid expenses and other assets of \$0.2 million. These increases to our cash provided by operating activities were partially offset by a decrease in deferred revenue by \$1.2 million, and a decrease in accrued expenses of \$0.2 million.

Total accounts receivable days sales outstanding (DSO), based on a rolling four quarter calculation, was 69 days at August 31, 2009 and 77 days at May 31, 2009. In addition to the DSO calculation, we have an operating metric for accounts receivable which is billing days outstanding (BDO) that was 75 days at August 31, 2009 and 66 days at May 31, 2009. BDO is calculated using the current quarter total billings and calculating an average daily billings per day. The accounts receivable balance at the end of the period is then divided by the average billing amount to determine the BDO at the end of the period. Changes in accounts receivable have a significant impact on our cash flow. Items that can

affect our accounts receivable DSO and BDO include: timing of license revenue

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and the proportion of that license revenue relative to our other types of revenue, timing of billing of our professional services revenue, contractual payment terms, client payment patterns (including approval or processing delays and cash management) and the effectiveness of our collection efforts.

Net Cash Used In Investing Activities

Net cash used in investing activities was \$0.2 million during the three months ended August 31, 2009 compared to net cash used in investing activities of approximately \$1.2 million for the three months ended August 31, 2008. The net cash used in investing activities was wholly attributable to the purchases of property and equipment, primarily to enhance our OnDemand infrastructure.

Net Cash Used In Financing Activities

Net cash used in financing activities of \$4.9 million during the three months ended August 31, 2009 was primarily attributable to a stock buy back of \$4.8 million associated with the repurchase of 1,384,920 shares and repayments on borrowings under our credit facility and notes payable of \$0.1 million. Net cash used in financing activities of \$19,000 during the three months ended August 31, 2008 was primarily attributable to repayment on borrowings under our credit facility and notes payable of \$0.1 million, partially offset by proceeds from stock issuance of \$0.1 million upon the exercise of stock options.

Contractual Obligations and Commitments

On January 31, 2006, we entered into a credit facility with a bank that provided for a term loan, in a principal amount of \$6.5 million and a receivables borrowing base revolving credit line in an aggregate principal amount of up to \$7.5 million. All amounts borrowed under the term loan and the credit line were repaid in full on or prior to January 31, 2009, in accordance with the terms of the credit facility. In addition, we amended this credit facility in November 2006 to add an equipment facility up to a principal amount of \$3.0 million. All amounts borrowed under the term loan and the credit line were repaid in full on or prior to January 31, 2009, in accordance with the terms of the credit facility. We obtained advances on November 30, 2006 and February 28, 2007 with respect to the equipment facility, and those advances mature on November 30, 2009 and February 28, 2010, respectively. We are not entitled under the terms of the facility to obtain any additional advances.

On July 29, 2009, we entered into a new credit facility with a bank with no amount drawn down on the line as of August 31, 2009. The new facility provides for a new revolving line of credit with a maturity date of July 28, 2010. An aggregate principal amount of up to \$9.0 million may be outstanding at any time under the revolving line. With respect to borrowings in excess of \$4.0 million, the revolving line is a receivables borrowing base credit facility. The revolving line also includes a sublimit of up to \$4.0 million for letters of credit, cash management and foreign exchange services. The interest rate applicable to the revolving line is, at our option, equal to either (i) the sum of the Prime Rate (as defined in the facility) plus 0.25%, or (ii) the sum of the LIBOR Rate (as defined in the facility) plus 3.25%. The new credit facility also incorporates under its terms the outstanding balance owed under the prior equipment facility, but the repayment terms of the prior equipment facility otherwise remain unchanged. The outstanding balance under the equipment facility was \$0.1 million as of August 31, 2009.

The equipment facility and new credit facility are secured by all of our personal property other than our intellectual property. The facilities also include certain negative covenants restricting or limiting the ability of us and our subsidiaries to, among other things: incur additional indebtedness; create liens on our property; make certain investments and acquisitions; merge or consolidate with any other entity; convey, sell, lease, transfer or otherwise dispose of assets; change our business; experience a change of control; pay dividends, distributions or make other specified restricted payments or repurchases; and enter into certain transactions with affiliates. Such restrictions and limitations are subject to usual and customary exceptions contained in credit agreements of this nature. In addition, the facilities require that we satisfy (a) a minimum quarterly EBITDA covenant and (b) a minimum monthly adjusted quick ratio covenant (which also includes a requirement that we maintain certain levels of cash and cash equivalents in accounts with the bank or in accounts at other financial institutions with which the bank has an account control agreement. We were in compliance with the covenants as of August 31, 2009.

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The facilities also contain usual and customary events of default (subject to certain threshold amounts and grace periods). If an event of default occurs and is continuing, we may be required to repay the obligations under the credit facility prior to their stated maturity date and the bank may be able to foreclose on any collateral provided by us.

We currently anticipate that our available cash resources, combined with cash flows generated from revenues will be sufficient to meet our presently anticipated working capital, capital expense and business expansion requirements, for at least the next 12 months. However, we may be required, or could choose, to raise additional funds at any time. Our future liquidity and capital requirements will depend on numerous factors, including our future revenues, the timing and extent of spending to support product development efforts and expansion of sales and marketing and general and administrative activities, the success of our existing and new product and service offerings and competing technological and market developments. There can be no assurance that additional funding, if needed, will be available on terms acceptable to us, if at all

During the quarter ended February 28, 2009, we entered into a non-cancelable three year contract for software services of which \$0.9 million remained as of August 31, 2009.

As of August 31, 2009, there were no material changes in capital leases, operating lease obligations, purchase obligations or any other long-term liabilities reflected on our condensed consolidated balance sheets as compared to such obligations and liabilities as of August 31, 2008.

Off-Balance Sheet Arrangements

As of August 31, 2009, we did not have any off-balance sheet arrangements, as defined in Item 303(a) (4) (ii) of SEC Regulation S-K.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk

Our exposure to market risk for changes in interest rates relates primarily to our borrowings and investments. As described above, we previously entered into a credit facility with a bank that provided for a term loan in a principal amount of \$6.5 million and a receivables borrowing base revolving credit line in an aggregate principal amount of up to \$7.5 million, but all amounts borrowed under the term loan and the credit line were repaid in full on or prior to January 31, 2009, in accordance with the terms of the credit facility. In addition, we amended this credit facility in November 2006 to add an equipment facility up to a principal amount of \$3.0 million. We obtained advances on November 30, 2006 and February 28, 2007 with respect to the equipment facility and those advances mature on November 30, 2009 and February 28, 2010, respectively. We are not entitled under the terms of the facility to obtain any additional advances. The interest rate applicable to loans under the equipment facility is the bank's prime rate plus 0.25%. On July 29, 2009, we entered into a new credit facility with a bank. The new facility provides for a new revolving line of credit with a maturity date of July 28, 2010. An aggregate principal amount of up to \$9.0 million may be outstanding at any time under the revolving line. The interest rate applicable to the revolving line is, at our option, equal to either (i) the sum of the Prime Rate (as defined in the facility) plus 0.25%, or (ii) the sum of the LIBOR Rate (as defined in the facility) plus 3.25%. The new credit facility also incorporates under its terms the outstanding \$0.2 million owed under the prior equipment facility, but the repayment terms of the prior equipment facility otherwise remain unchanged.

As of August 31, 2009, we had \$0.1 million outstanding under the equipment facility and no outstanding borrowings under the receivables borrowing base revolving credit line.

At August 31, 2009, we had available cash and cash equivalents totaling \$21.6 million. Of this amount, approximately \$8.6 million was invested in money market accounts bearing variable interest rates between 0.01% and 9.5%. The remainder of our cash and cash equivalents is held in non-interest bearing accounts at several banks. Variable interest rate securities may produce less income than expected if interest rates fall. A 0.5% change in interest rates would not have a material impact on our financial statements.

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Foreign Currency Risk

We provide our products and services to customers in the United States, Europe and elsewhere throughout the world. Sales are primarily made in U.S. dollars, and to a lesser but increasing extent, British pounds and Euros; however, as we continue to expand our operations, more of our contracts may be denominated in Australian dollars, Canadian dollars, Japanese yen or other foreign currencies. A strengthening of the U.S. dollar could make our products less competitive in foreign markets. We do not use derivative instruments to manage risks associated with foreign currency transactions in order to minimize the impact of changes in foreign currency exchange rates on earnings.

Our exposure to foreign exchange rate fluctuations also arises in part from inter-company accounts with our foreign subsidiaries. These inter-company accounts are typically denominated in the functional currency of the foreign subsidiary, and, when translated into U.S. dollars, have an impact on our operating results depending upon the movement in foreign currency rates. During the three months ended August 31, 2009, our total realized and unrealized losses due to movements in foreign currencies, primarily British pounds, Japanese yen and Australian dollars, were \$43,000. As exchange rates vary, these foreign exchange results may vary and adversely or favorably impact operating results. An unfavorable change of 10% in foreign currency rates would not have a material impact on our financial statements.

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of disclosure controls and procedures.

Saba maintains disclosure controls and procedures, as such term is defined under Exchange Act Rule 13a-15(e), that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15 under the Exchange Act as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our chief executive officer and chief financial officer have concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective at the reasonable assurance level.

(b) Changes in internal control over financial reporting.

We regularly review our system of internal control over financial reporting to ensure we maintain an effective internal control environment. As we grow geographically and with new product offerings, we continue to create new processes and controls as well as improve our existing environment to increase efficiencies. Improvements may include such activities as implementing new, more efficient systems, consolidating activities, and migrating processes.

There were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The material set forth in Note 13 of Notes to Condensed Consolidated Financial Statements in Part I, Item 1 of this quarterly report on Form 10-Q incorporated herein by reference.

ITEM 1A. RISK FACTORS

Set forth below and elsewhere in this Quarterly Report on Form 10-Q and in other documents we file with the SEC, are risks and uncertainties that could cause actual results to differ materially from the results expressed or implied by the forward-looking statements contained in this Quarterly Report. The fact that some of the risk factors may be the same or similar to our past filings means only that the risks are present in multiple periods. We believe that many of the risks detailed here and in our other SEC filings are part of doing business in our industry and will likely be present in all periods reported. The fact that certain risks are endemic to our industry does not lessen the significance of the risk. There are no material changes to the risk factors set forth under the title Risk Factors in our Annual Report on Form 10-K for the fiscal year ended May 31, 2009.

The effects of the recent global economic crisis may impact our business, operating results or financial condition.

The recent global economic crisis has caused a tightening in the credit markets, lower levels of liquidity, increases in the rates of default and bankruptcy, public sector deficits and extreme volatility in credit, equity and fixed income markets, which have contributed to diminished expectations for the global economy. In addition, the U.S. economy and other economies around the world have entered into a recessionary environment characterized by slow or negative economic growth. We believe that these macroeconomic factors may influence our customers purchasing decisions, particularly in some customer segments. We believe that we have experienced some slowing of demand for our products and services as a result of these economic factors, and that this economic climate may continue to adversely affect demand for our products and services for future periods.

Fluctuations in our quarterly results could cause our stock price to experience significant fluctuations or declines.

Our operating results have varied significantly in the past and will likely fluctuate significantly in the future. For instance for the first quarter of fiscal year 2010 and fiscal years 2009, 2008 and 2007, our quarterly revenues have fluctuated between approximately \$28.2 million and \$23.2 million and our quarterly results have fluctuated between net income of approximately \$1.3 million and a net loss of approximately \$3.1 million. Our quarterly operating results are particularly affected by the number of customers licensing our products during any quarter and the size of such licensing transactions. We have limited visibility into our future revenue, especially license revenue, which often has been heavily concentrated in the third month of each quarter. As a result, if we were to fail to close a sufficient number of transactions by the end of our quarter, particularly large license transactions, we would miss our revenue projections. In addition, our operating expenses are based in part on future revenue projections and are relatively fixed in the short-term. If we cannot meet our revenue projections, our business will be seriously harmed and net losses in a given quarter will be even larger than expected.

Other factors that could affect our quarterly operating results include:

The demand for our products and professional services and our efficiency in rendering our professional services;

The variability in the mix of our revenues and bookings in any quarter;

The variability in the mix of the type of services delivered in any quarter and the extent to which third party contractors are used to provide such services;

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The size and complexity of our license transactions and potential delays in recognizing revenue from license transactions;

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The amount and timing of our operating expenses and capital expenditures;

The performance of our international business, which accounts for a substantial part of our consolidated revenues; and

Fluctuations in foreign currency exchange rates.

Due to these and other factors, we believe that quarter-to-quarter comparisons of our revenues and operating results are not necessarily meaningful and should not be relied upon as indicators of future performance. It is possible that in some future quarter our operating results may be below the expectations of public market analysts or investors, which could cause the market price of our common stock to fall.

We have a history of losses, expect future losses and cannot assure you that we will achieve profitability on a consistent basis.

We expect to continue to derive substantially all of our revenues for the foreseeable future from sales of licenses and OnDemand services for the Saba Enterprise Suite and the Saba Centra product suite and providing related services, including license updates and product support, implementation, training and consulting services. Except for three previous quarters (including the fiscal quarter ended August 31, 2009), we have not been profitable on a quarterly or annual basis in the past. We cannot be certain that we will realize sufficient revenues to achieve or sustain profitability on a quarterly or annual basis, especially if our recurring OnDemand business grows faster than expected relative to license sales. In addition, in the future, we expect to continue to incur non-cash expenses relating to the amortization of purchased intangible assets that will contribute to our net losses, along with any potential goodwill impairment. As of May 31, 2009, we had \$8.7 million of purchased intangible assets to be amortized as a result of our January 2006 acquisition of Centra Software, Inc. (Centra) and May 2005 acquisition of THINQ Learning Solutions, Inc. (THINQ) and our goodwill balance was \$36.1 million. Further, starting with the first quarter of fiscal 2007, we were required to record as an expense charges related to all current outstanding and future grants of stock options in our reported results from operations in accordance with SFAS No.123 (revised 2004), which was issued by the FASB in December 2004. These non-cash expenses have made it and will continue to make it significantly more difficult for us to achieve profitability. If we achieve GAAP profitability, we may not be able to sustain it on a consistent basis.

Our OnDemand business depends substantially on customers renewing their agreements and purchasing additional products or users from us. Any decline in our customer renewals would harm our future operating results.

In order for us to improve our operating results, it is important that our OnDemand customers renew their agreements with us when the initial contract term expires and also purchase additional products or additional users. Our OnDemand customers have no obligation to renew their subscriptions after the initial subscription period, and we cannot assure you that customers will renew subscriptions at the same or higher level of service, if at all. During our first quarter of fiscal year 2010, 8 % of our OnDemand customers elected not to renew their agreements with us. Our customers' renewal rates may decline or fluctuate as a result of a number of factors, including their satisfaction or dissatisfaction with our product offerings, pricing, the prices of competing products or services, completion of customer initiatives, mergers and acquisitions affecting our customer base, or reductions in our customers' spending levels. If our OnDemand customers do not renew their subscriptions, renew on less favorable terms or fail to purchase additional products or users, our revenue may decline, and we may not realize significantly improved operating results from our customer base.

Because we generally recognize revenue from the sale of our OnDemand solutions ratably over the term of the subscription period, a significant downturn in our OnDemand business may not be immediately reflected in our operating results.

We generally recognize OnDemand revenue over the terms of our customer agreements, which typically range from one to three years. As a result, most of our quarterly OnDemand revenue results from agreements entered into during previous quarters. A decline in new or renewed subscriptions in any one quarter may not impact our financial performance in that quarter, but will negatively affect our revenue in future quarters. If a number of contracts expire and are not renewed in the same quarter, our revenue could decline significantly in that quarter and in subsequent quarters. Accordingly, the effect of significant declines in sales and market acceptance of our solutions may not be reflected in our short-term results of operations, making our results less indicative of our future prospects. It is also difficult for us to rapidly increase our OnDemand revenue through additional sales in any period, as revenue from new customers must be recognized over the applicable subscription term.

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A decline in the price of, or demand for, our products or our related services offerings, would seriously harm our revenues and operating margins.

To date, Saba Enterprise Learning and related services have accounted for a substantial majority of our revenues. We anticipate that revenues from the Saba Enterprise suite and the Saba Centra product suite, as well as related services, will constitute substantially all of our revenue for the foreseeable future. Consequently, a decline in the price of, or demand for, the Saba Enterprise suite or the Saba Centra product suite or failure to achieve broad market acceptance would seriously harm our business.

Our products have a long sales cycle, which increases the cost of completing sales and renders completion of sales less predictable.

The period between our initial contact with a potential customer and the purchase of our products and services is often long. A customer's decision to purchase our products and services requires the commitment to increase performance through human capital management, involves a significant allocation of resources, and is influenced by a customer's budgetary cycles. To successfully sell our products and services, we generally must educate our potential customers regarding the use and benefits of our products and services. We may commit a substantial amount of time and resources to potential customers without assurance that any sales will be completed or revenues generated. Many of our potential customers are large enterprises that generally take longer to make significant business decisions. Our public sector customers, in particular, are subject to extensive procurement procedures that require many reviews and approvals. Our typical sales cycle has been approximately six to 12 months, making it difficult to predict the quarter in which we may recognize revenue. The delay or failure to complete sales in a particular quarter could reduce our revenues in that quarter. If our sales cycle were to unexpectedly lengthen in general or for one or more large orders, it would adversely affect the timing of our revenues. If we were to experience a delay on a large order, it could harm our ability to meet our forecasts for a given quarter.

Our performance depends on a new market: human capital management.

The market for software solutions that automate human capital management is at an early stage of development and rapidly evolving. Substantially all of our revenues are attributable to the suite of products and services in this market. If this market fails to develop or develops more slowly than we expect, our business would be harmed. If the market grows, the prices of our products may decline rapidly as alternative products are introduced into the market. In addition, our products may become obsolete if we fail to anticipate or adapt to evolving technology standards, or if we fail to identify the challenges and risks in this new market or successfully address these risks.

We experience seasonality in our sales and expense, which could cause our quarterly operating results to fluctuate from quarter to quarter.

We experience quarterly seasonality in the demand for our products and services. For example, revenue has historically been lower in our first fiscal quarter while expenses have been higher than in the immediately preceding fourth fiscal quarter. Contributing to this seasonality is the timing of our first fiscal quarter that occurs during the summer months when general business activities slow down in a number of territories where we conduct our operations, particularly Europe. Our commission structure and other sales incentives also tend to result in fewer sales in the first fiscal quarter than in the fourth fiscal quarter. These seasonal variations in our revenue are likely to lead to fluctuations in our quarterly operating results.

Reductions in information technology spending could limit our ability to grow our business.

Our operating results may vary based on changes in the information technology spending of our clients. The revenue growth and profitability of our business depend on the overall demand for enterprise applications and services. We sell our solutions primarily to large organizations whose businesses fluctuate with general economic and business conditions. As a result, decreased demand for enterprise applications and services, and in particular human capital management solutions, caused by a weakening global economy may cause a decline in our revenue. Historically, economic downturns have resulted in overall reductions in corporate information

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technology spending. In particular, human capital management software may be viewed by some of our existing and potential clients as a lower priority and may be among the first expenditures reduced as a result of unfavorable economic conditions. In the future, potential clients may decide to reduce their information technology budgets by deferring or reconsidering product purchases, which would negatively impact our operating results.

Implementation of accounting regulations and related interpretations and policies, particularly those related to revenue recognition, could cause us to defer recognition of revenue or recognize lower revenue or to report lower earnings per share.

While we believe that we are in compliance with Statement of Position 97-2, *Software Revenue Recognition*, as amended, the accounting professionals continue to discuss a wide range of potential interpretations. Additional implementation guidelines, and changes in interpretations of such guidelines, could lead to unanticipated changes in our current revenue accounting practices that could cause us to defer the recognition of revenue to future periods or to recognize lower revenue. In addition, policies, guidelines and interpretations related to accounting for acquisitions, income taxes, facilities consolidation charges, allowance for doubtful accounts and other financial reporting matters require different judgments on complex matters that are often subject to multiple sources of authoritative guidance. To the extent that management's judgment is incorrect, it could result in an adverse impact on our financial statements. Further, the factual complexities of applying these policies, guidelines and interpretations to specific transactions can lead to unanticipated changes in revenue recognition with respect to such transactions, which may affect our revenue and results of operations.

Standards for compliance with Sarbanes-Oxley Section 404 are burdensome, and if we fail to comply in a timely manner, our business could be harmed and our stock price could decline.

Pursuant to Sarbanes-Oxley Section 404, our management is required to report on and our independent registered public accounting firm to attest to, the effectiveness of our internal controls over financial reporting, at least annually. The rules governing the standards that must be met for management to assess our internal controls over financial reporting are complex. Currently, the rules require significant documentation, testing and possible remediation of our internal controls over financial reporting. The process of reviewing, documenting and testing our internal controls over financial reporting will likely continue to result in increased expenses and the devotion of significant management and other internal resources. During this process, if our management identifies one or more material weaknesses in our internal control over financial reporting, we will be unable to assert such internal control is effective and the price of our stock may suffer. In addition, a control system, no matter how well conceived or operated, can provide only reasonable, not absolute assurance that the objectives of the control system are met. Our management does not expect that our internal controls and procedures will prevent all errors and all fraud, if any, because, in addition to resource constraints, there are inherent limitations in all control systems, including the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple errors or mistakes. If our management is unable to assert that our internal control over financial reporting is effective (or if our independent registered public accounting firm is unable to attest that our management report is fairly stated or they are unable to express an opinion on the effectiveness of our internal controls) we may not be able to timely file, or file at all, our periodic financial reports and thus we will be subject to delisting. Even if we are able to file such reports, investor confidence in the accuracy and completeness of our financial reports may be lost, leading to an adverse effect on the price of our stock.

The loss of our senior executives and key personnel would likely cause our business to suffer.

Our ability to implement a successful long-term strategy, strengthen our competitive position, expand our customer base, and develop and support our products depends to a significant degree on the performance of the senior management team and other key employees, including Bobby Yazdani, our CEO. The loss of any of these individuals could harm our business. Our success will depend in part on our ability to attract and retain additional personnel with the highly specialized expertise necessary to generate revenue and to engineer, design and support our products and services. Like other software companies, we face intense competition for qualified personnel. We may not be able to attract or retain such personnel.

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Intense competition in our target market could impair our ability to grow and achieve profitability on a consistent basis.

The market for our products and services is intensely competitive, dynamic and subject to rapid technological change. The intensity of the competition and the pace of change are expected to increase in the future. Increased competition is likely to result in price reductions, reduced gross margins and loss of market share, any one of which could seriously harm our business. Competitors vary in size and in the scope and breadth of the products and services offered. We encounter competition with respect to different aspects of our solution from a variety of sources including:

Companies that offer human capital management solutions that provide one or more applications within the HCM market, such as learning management, performance management, talent management, competition and recruiting, including Sum Total and Success Factors;

Companies that offer collaboration solutions, such as Microsoft, Adobe and Cisco;

Enterprise software vendors that offer human resources information systems and employee relationship management systems with training and performance modules, such as SAP and Oracle;

Potential customers' internal development efforts; and

Companies that operate Internet-based marketplaces for the sale of on-line learning.

We expect competition from a variety of companies.

Many of our competitors have longer operating histories, substantially greater financial, technical, marketing or other resources, or greater name recognition than we do, enabling them to respond more quickly than we can to new or emerging technologies and changes in customer requirements. Such resources also enable our competitors to withstand prolonged periods of negative cash flows and unfavorable economic, political and market conditions. Competition could seriously impede our ability to sell additional products and services on terms favorable to us. Our current and potential competitors may develop and market new technologies that render our existing or future products and services obsolete, unmarketable or less competitive. Our current and potential competitors may make strategic acquisitions or establish cooperative relationships among themselves or with other partners, thereby increasing the availability of their services to address the needs of our current and prospective customers. We may not be able to compete successfully against our current and future competitors, and competitive pressures that we encounter may seriously harm our business.

If we are unable to manage the complexity of conducting business globally, our international revenues may suffer.

International revenues accounted for 25% and 27% of our revenues for first three months of our fiscal 2010 and 2009, respectively. Although we intend to continue to expand our international presence, in the future we may not be able to successfully market, sell or distribute our products and services in foreign markets. Factors that could materially adversely affect our international operations, and our business and future growth include:

Difficulties in staffing and managing foreign operations, including language barriers;

Seasonal fluctuations in purchasing patterns in other countries, particularly depressed sales during July and August in European markets;

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Difficulties in collecting accounts receivable in foreign countries, particularly European countries in which collections take considerably more time than the United States and collections are more difficult to effect;

Currency exchange rate fluctuations, particularly in countries where we sell our products in denominations other than U.S. dollars, such as in the United Kingdom, the Euro zone, Australia and Japan, or have exposures in inter-company accounts denominated in foreign currencies;

Exposure to tax regimes of multiple countries and potential increased tax exposure relating to in-country profits as well as audits and assessments relating to transfer pricing matters;

Costs attributable to development of internationalized versions of our products and marketing and sales materials;

The burdens of complying with a wide variety of foreign laws and reduced protection for intellectual property rights in some countries;

Tariffs, export controls and other trade barriers; and

Exposure to geopolitical instability, natural disasters and acts of war or terrorism.

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In addition, the reallocation of certain design, development and testing functions from the United States to our lower-cost development centers in India intensifies our exposure to international uncertainties. In recent years, increased growth and development of the technology market in general, and in India specifically, has made it more difficult for us to hire and retain qualified technical employees and other personnel. In addition to the risks inherent in conducting international operations, certain risks are particularly acute in India, such as employee turnover, increasing salaries and less reliable infrastructure.

The enactment of legislation implementing changes in U.S. taxation of international business activities or the adoption of other tax reform policies could materially impact our financial position and results of operations.

Recently several tax bills have been introduced to reform U.S. taxation of international business activities. The current Administration has made public statements indicating that it has made the issue a priority and key members of the U.S. Congress have conducted hearings and proposed legislation. Accordingly, depending on the final form of legislation enacted, if any, these consequences may be significant for us due to the large scale of our international business activities. If any of these proposals are enacted into legislation, they could have material adverse consequences on the amount of tax we pay and thereby on our financial position and results of operations.

Currency exchange rate fluctuations could lower our revenue and net income.

During the first quarter of fiscal 2010, we recognized approximately 25% percent of our revenue in markets outside the United States in each market's respective local currency. We provide our products and services to customers in the United States, Europe and elsewhere through the world. Sales are primarily made in U.S. dollars, and to an increasing extent, British pounds and Euros. As we continue to expand our operations, more of our contracts may be denominated in Australian dollars, Canadian dollars, Japanese yen and other foreign currencies. In preparing our financial statements, we translate revenues and expenses in foreign countries from their local currencies into U.S. dollars using average exchange rates. Because an increasing portion of our sales is in foreign countries, exchange rate fluctuations may have a significant effect on our sales and earnings. Our reported net earnings may be significantly affected by fluctuations in currency exchange rates, with earnings generally increasing with a weaker U.S. dollar and decreasing with a strengthening U.S. dollar. As sales expand in countries where foreign currency transactions may be made, our operating results will increasingly be subject to the risks of exchange rate fluctuations and we may not be able to accurately estimate the impact that these changes may have on our future results of operations or financial condition.

Future acquisitions may result in disruptions to our business if we fail to adequately integrate acquired businesses.

As part of our overall business strategy, we expect to continue periodically to acquire complementary businesses or technologies that will provide additional products or services offerings, additional industry expertise or an expanded geographic presence. We acquired Centra Software, Inc. in January 2006 and THINQ Learning Solutions, Inc. in May 2005. The consideration and negotiation of potential acquisitions, regardless of whether they are completed, could require us to incur substantial expense and divert management's attention from other business concerns.

The pursuit of acquisitions involves a number of uncertainties, including selecting the appropriate products, technologies or companies to acquire and successfully complete the targeted transaction. Completed acquisitions could further result in the use of significant amounts of cash, the incurrence of debt or potentially dilutive issuances of equity securities which may reduce earnings per share. Further, acquisitions that we complete expose us to numerous risks, including:

Difficulties in the assimilation of the operations, technologies, products and personnel of the acquired company;

The diversion of management's attention from other business concerns;

Risks of entering markets in which we have no or limited prior experience;

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The potential loss of key employees, significant customers and strategic partners of the acquired company; and

Exposure to claims by terminated employees, stockholders of the acquired company or other third parties related to the acquisition. Although we generally obtain indemnification and other contractual protection against such claims, we cannot assure that they will be enforceable or sufficient to protect us.

We may incur impairments to goodwill or long-lived assets.

We are required to test goodwill for impairment annually or if a triggering event occurs in accordance with the provisions of SFAS No. 142

Goodwill and Other Intangible Assets. We are also required to test long-lived assets for impairment if a triggering event occurs in accordance with the provisions of SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. Such impairment could be caused by internal factors as well as external factors beyond our control.

Significant negative industry or economic trends, reduced estimates of future cash flows, disruptions to our business, slower growth rates or lack of growth in the areas in which we generate revenues could lead to an impairment charge for any of our intangible assets or goodwill. If, in any period, our stock price decreases to the point where the fair value of the Company, as determined by our market capitalization, is less than our book value, this too could indicate a potential impairment and we may be required to record an impairment charge in our statement of operations in that period which would cause our profits to decline.

We operate in highly competitive environments and projections of future operating results and cash flows may vary significantly from actual results. Additionally, if a significant decline in our stock price and/or market capitalization result in impairment to our goodwill, we may be required to record a charge to earnings in our financial statements during a period in which such impairment is determined to exist, which may negatively impact our results of operations. Our valuation methodology for assessing impairment requires management to make judgments and assumptions based on historical experience and to rely heavily on projections of future operating performance.

Delays in releasing new products or enhanced versions of our existing products could adversely affect our competitive position.

As part of our strategy, we expect to regularly release new products and new versions of our existing products. Even if our new products or new versions of our existing products contain the features and functionality our customers want, in the event we are unable to timely introduce these new products or product releases, our competitive position may be harmed. We cannot assure you that we will be able to successfully complete the development of currently planned or future products or product releases in a timely and efficient manner. Due to the complexity of our products, internal quality assurance testing and customer testing of pre-commercial releases may reveal product performance issues or desirable feature enhancements that could lead us to postpone the release of these products. In addition, the reallocation of resources associated with any postponement would likely cause delays in the development and release of other future products or enhancements to our currently available products. The reallocation of certain design, development and testing functions to our lower-cost development center heightens risks relating to product design, development, testing and introduction. Any delay in releasing future products or enhancements of our products could harm our business.

If we release products containing defects, we may need to halt further shipments, service levels may be reduced and our business and reputation would be harmed.

Products as complex as ours often contain unknown and undetected errors or performance problems. Although our products are subject to rigorous testing and quality control processes, serious defects are frequently found during the period immediately following introduction and initial shipment of new products or enhancements to existing products. Although we attempt to resolve all errors that we believe would be considered serious by our customers before shipment to them, our products are not error-free. These errors or performance problems could result in lost revenues, reduced service levels, delays in customer acceptance on professional services products and would be detrimental to our business and reputation. As is typical in the software industry, with each release we have discovered errors in our products after introduction. We will not be able to detect and correct all errors before releasing our products commercially and these undetected errors could be significant. We cannot assure you that undetected errors or performance problems

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in our existing or future products will not be discovered in the future or that known errors considered minor by us will not be considered serious by our customers, resulting in cancellation of orders, loss of customers, difficulties in achieving our sales goals, increased demands on our support services, a decrease in our revenues and service credits or refunds. To correct such errors, we may expend considerable time and resources to develop and release modifications to our software.

As a result of such errors, we may be subject to warranty and product liability claims that are costly or difficult to settle. Our products and services enable customers to manage critical business information. If product errors are alleged to cause or contribute to security and privacy breaches or misappropriation of confidential information, we may also be subject to significant liability. Although our license agreements contain provisions intended to limit our exposure to liability, we cannot assure you that these limits will be adequate, that they will be enforceable or, if enforceable, that they will be interpreted favorably by a court.

We face risks related to claims third parties that we infringe their intellectual property rights and other litigation.

In recent years, there has been significant litigation in the United States involving patents and other intellectual property rights, particularly in the software and Internet-related industries. We have in the past been and are presently subject to intellectual property actions. For example, on August 19, 2003, EdiSync Systems, LLC filed a complaint against Centra in federal court in Denver, Colorado, alleging infringement of two patents for a remote multiple user editing system and method and seeking to enjoin us from continuing to sell our products, as well as unspecified compensatory damages. Centra filed an answer to the complaint denying all of the allegations, and instituted reexamination proceedings for the patents at issue with the Patent Office. Centra filed a request for reexamination of the patents at issue with the Patent Office. Our patent counsel is of the opinion that claims of the patents involved in the suit are invalid. The re-examination request was accepted by the Patent Office and the Colorado District Court approved the parties' motion to stay the court proceedings during the re-examination proceedings. A reexamination certificate has issued for one of the patents that canceled all of the patent's claims, thus rendering that patent of no further force or effect. The Patent Office issued a reexamination certificate for the other patent canceling all of the patent's original claims and allowing certain newly-added claims. We believe we are free from liability for past actions, as we believe the newly-added claims would be enforceable only prospectively as of the issue date of the reexamination certificate. Centra has since filed a second reexamination request asking the Patent Office to reconsider the patentability of the newly-added claims in view of newly-discovered prior art and the Patent Office has granted that request. Centra filed a motion with the Colorado District Court seeking a further stay of the action pending completion of the second reexamination proceeding but that motion has not yet been decided. Although we believe that we have meritorious defenses and intend to vigorously defend this action, we can give no assurance that we will be able to achieve a satisfactory outcome. We could become subject to additional intellectual property infringement claims as the number of our competitors grows and our products and services overlap with competitive offerings. Any of these claims, even if not meritorious, could be expensive to defend and could divert management's attention from operating our company. If we become liable to third parties for infringing their intellectual property rights, we could be required to pay a substantial award of damages and to develop non-infringing technology, obtain a license or cease selling the products that contain the infringing intellectual property. We may be unable to develop non-infringing technology or obtain a license on commercially reasonable terms, if at all. We also may face other forms of litigation or claims as part of our business, which may expose us to additional costs and risks.

Our products include third party technology, the loss of which could materially harm our business.

We use licensed third party technology components in our products. Future licenses to this technology may not be available to us on commercially reasonable terms, or at all. The loss of or inability to obtain or maintain any of these technology licenses could result in delays in the introduction of new products or could force us to discontinue offering portions of our solutions until equivalent technology, if available, is identified, licensed and integrated.

Our use of open source technology could impose limitations on our ability to commercialize our products.

We use open source software in our application suite. Although we monitor our use of open source software closely, the terms of many open source licenses have not been interpreted by United States courts, and there is risk that such licenses could be construed

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in a manner that imposes unanticipated conditions or restrictions on our ability to commercialize our products. In such event, we could be required to re-engineer our technology or to discontinue offering all or a portion of our products in the event re-engineering cannot be accomplished on a timely basis, any of which could adversely affect our business, operating results and financial condition.

We may not be able to adequately protect our proprietary technology, and our competitors may be able to offer similar products and services that would harm our competitive position.

Our success depends upon our proprietary technology. We rely primarily on copyright, trademark and trade secret laws, confidentiality procedures and contractual provisions to establish and protect our proprietary rights. As part of our confidentiality procedures, we enter into non-disclosure agreements with our employees. Despite these precautions, third parties could copy or otherwise obtain and use our technology without authorization, which may represent potential sales and revenue losses that are difficult to quantify. Policing unauthorized use of our technology is difficult, time-consuming and costly. Were we to discover instances of unauthorized use, there can be no assurance that we would be able to enforce our proprietary rights or obtain adequate recovery for our losses. In addition, we have seven patents issued in the United States and seven patent applications pending in the United States. We cannot assure you that any patents will be issued for any of the pending patent applications. Even for the issued patents, or any patent issued to us in the future, there can be no assurance that such patent will protect our intellectual property, or will not be challenged by third parties. Furthermore, effective protection of intellectual property rights is unavailable or limited in certain foreign countries. We cannot assure you that the protection of our proprietary rights will be adequate or that our competitors will not independently develop similar technology, duplicate our products and services or design around any patents or other intellectual property rights we hold.

Our disaster recovery plan does not include redundant systems, and a disaster could severely damage our operations.

Our disaster recovery plan does not include fully redundant systems for our services at an alternate site. A disaster could severely harm our business because our services could be interrupted for an indeterminate length of time. Our operations depend upon our ability to maintain and protect the computer systems needed for the day-to-day operation of the Saba OnDemand business. A number of these computer systems are located on or near known earthquake fault zones. Although these systems are designed to be fault-tolerant, the systems are vulnerable to damage from fire, floods, earthquakes, power loss, telecommunications failures and other events. Additionally, we do not carry sufficient business insurance to compensate us for all potential losses that could occur.

We outsource the management and maintenance of our OnDemand business to third parties and will depend upon them to provide adequate management and maintenance services.

We rely on third parties to provide key components of our networks and systems. For instance, we rely on third-party Internet service providers to host our products for our OnDemand customers. We also rely on third-party communications service providers for the high-speed connections that link our networks and our Internet service providers' Web servers and office systems to the Internet. Our reliance on third party providers limits our ability to control critical customer service functions and communications systems. Any Internet or communications systems failure or interruption could result in disruption of our service or loss or compromise of customer orders and data. These failures, especially if they are prolonged or repeated, would make our services less attractive to customers and tarnish our reputation.

If our security measures are breached and unauthorized access is obtained to client data, clients may curtail or stop their use of our OnDemand solutions, which would harm our business, operating results and financial condition.

Our OnDemand solutions involve the storage and transmission of confidential information of clients and their existing and potential employees, and security breaches could expose us to a risk of loss of, or unauthorized access to, this information, resulting in possible litigation and possible liability. Although we have never sustained such a breach, if our security measures were ever breached as a result of third party action, employee error, malfeasance or otherwise, and, as a result, an unauthorized party obtained access to this confidential data, our reputation could be damaged, our business may suffer and we could incur significant liability. Techniques used to obtain unauthorized access or to sabotage systems change frequently and generally are not discovered until launched against a target. As a result, we may be unable to anticipate these techniques or to implement adequate preventative measures. If an actual or perceived breach of our security occurs, the market perception of our security measures could be harmed and we could lose sales and clients.

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We depend in part on the success of our relationships with third-party resellers and integrators.

Our success depends on various third-party relationships. The relationships include third party resellers as well as system integrators that assist with implementations of our products. Identifying partners, negotiating and documenting relationships with them and maintaining their relationships require significant time and resources from us. In addition, our agreements with our resellers and integrators are typically non-exclusive and do not prohibit them from working with our competitors or from offering competing products or services. Our competitors may be effective in providing incentives to third parties to favor their products or services. If we are unsuccessful in establishing or maintaining our relationships with these third parties, our ability to compete in the marketplace or to maintain or grow our revenue could be impaired and our operating results would suffer.

Our stock price may fluctuate substantially.

For example, from the beginning of fiscal 2008 through August 31, 2009, the market price for our common stock has fluctuated between \$6.15 per share and \$0.91 per share. The market price for our common stock may be affected by a number of factors, including those described above and the following:

The announcement of new products and services or product and service enhancements by us or our competitors;

Actual or anticipated quarterly variations in our results of operations or those of our competitors;

Changes in earnings estimates or recommendations by securities analysts that may follow our stock;

Developments in our industry, including announcements of significant acquisitions or strategic partnerships; and

General market conditions and other factors, including factors unrelated to our operating performance or the operating performance of our competitors.

In addition, the stock market in general, and the Nasdaq Global Market technology companies in particular, have experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of particular companies. Broad market and industry trends may also materially and adversely affect the market price of our common stock, regardless of our actual operating performance. Volatility in the market price and trading volume of our common stock may prevent our stockholders from selling their shares at a favorable price. In the past, following periods of volatility in the market price of a company's securities, securities class-action litigation has often been initiated against that company. Class-action litigation could result in substantial costs and a diversion of management's attention and resources.

The anti-takeover provisions in our charter documents and our rights plan could delay or prevent a change in control.

Our Amended and Restated Certificate of Incorporation and Amended and Restated Bylaws contain provisions that could make it harder for a third party to acquire us without the consent of our board of directors.

For example, if a potential acquirer were to make a hostile bid for us, the acquirer would not be able to call a special meeting of stockholders to remove our board of directors or act by written consent without a meeting. In addition, our board of directors has staggered terms that make it difficult to remove all directors at once. The acquirer would also be required to provide advance notice of its proposal to remove directors at an annual meeting. The acquirer will not be able to cumulate votes at a meeting, which will require the acquirer to hold more shares to gain representation on the board of directors than if cumulative voting were permitted.

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Our board of directors also has the ability to issue preferred stock that would significantly dilute the ownership of a hostile acquirer. In addition, Section 203 of the Delaware General Corporation Law limits business combination transactions with 15% stockholders that have not been approved by the board of directors. These provisions and other similar provisions make it more difficult for a third party to acquire us without negotiation. These provisions may apply even if the offer may be considered beneficial by some stockholders.

In addition, on June 2, 2009, our board of directors authorized and declared a dividend of one right for each outstanding share of our common stock to stockholders of record at the close of business on June 15, 2009. Each right entitles the registered holder, subject to the terms of the rights agreement between us and the rights agent, to purchase from us one one-thousandth of a share (a unit) of Series A Preferred Stock, par value \$0.001 per share, at a purchase price of \$12.50 per unit, under circumstances described in the rights agreement. The purchase price, the number of units of preferred stock and the type of securities issuable upon exercise of the rights are subject to adjustment. The rights will expire at the close of business June 2, 2012 unless earlier redeemed or exchanged. Until a right is exercised, the holder thereof, as such, will have no rights as one of our stockholders, including the right to vote or to receive dividends. The rights are not immediately exercisable. Subject to the terms and conditions of the rights agreement, they will become exercisable ten business days after a person or group acquires, or commences a tender or exchange offer which would lead to the acquisition of, beneficial ownership of 15% or more of our outstanding common stock. Once a person or group acquires beneficial ownership of 15% or more of our outstanding common stock, subject to the terms of the rights agreement, each right not owned by that person or group or certain related parties will entitle its holder to purchase, at the right's then-current purchase price, units of Series A Preferred Stock or, at our option, shares of common stock or cash, property or other securities of our company having a market value equal to twice the then-current purchase price.

Our anti-takeover provisions as well as our rights agreement could have the effect of discouraging a third party from making a tender offer or otherwise attempting to gain control of us, even though the transactions could be profitable for our stockholders. If the acquirer was discouraged from offering to acquire us or prevented from successfully completing a hostile acquisition by our anti-takeover measures, our stockholders could lose the opportunity to sell their shares at a favorable price.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS
ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares That May Yet Be Purchased Under the Plans or Programs
June 1 30, 2009				
July 1 31, 2009				
August 1 31, 2009	1,384,920	\$ 3.50		
Total	1,384,920	\$ 3.50		

- (1) 1,384,920 shares of common stock were repurchased by the Company directly from funds managed by FirstMark Capital L.L.C. in a single negotiated private transaction and not pursuant to a publicly announced plan or program. Lawrence D. Lenihan, Jr., a member of the Company's Board of Directors until July 17, 2009, is the Chief Executive Officer and Managing Director of FirstMark Capital, LLC

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

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ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

a. Exhibits

See Exhibit Index following the signature page, which is incorporated herein by reference.

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SIGNATURES

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

SABA SOFTWARE, INC.

Dated: October 7, 2009

By: /s/ BOBBY YAZDANI
Bobby Yazdani
Chief Executive Officer and
Chairman of the Board
(Principal Executive Officer)

By: /s/ WILLIAM SLATER
William Slater
Chief Financial Officer
(Principal Financial and Accounting Officer)

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EXHIBIT INDEX

Exhibit	
Number	Document
3.1 ⁽¹⁾	Amended and Restated Certificate of Incorporation of the Company effective as of April 12, 2000.
3.2 ⁽²⁾	Amendment to Amended and Restated Certificate of Incorporation of the Company effective as of May 12, 2003.
3.3 ⁽³⁾	Amendment to Amended and Restated Certificate of Incorporation of the Company effective as of November 19, 2004.
3.3 ⁽⁴⁾	Certificate of Designation of the Series A Preferred Stock, as filed with the Secretary of Delaware on June 2, 2009.
3.4 ⁽⁵⁾	Amended and Restated Bylaws of the Company.
4.1	Reference is made to Exhibits 3.1, 3.2, 3.3, 3.4 and 3.5.
31.1	Certification of Bobby Yazdani, Chief Executive Officer and Chairman of the Board, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated October 7, 2009.
31.2	Certification of William Slater, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated October 7, 2009.
32.1	Certification of Bobby Yazdani, Chief Executive Officer and Chairman of the Board, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated October 7, 2009.
32.2	Certification of William Slater, Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated October 7, 2009.

- (1) Incorporated by reference to Exhibit 3.2 previously filed with the Company's Registration Statement on Form S-1/A (Registration No. 333-95761) filed on March 3, 2000.
- (2) Incorporated by reference to Exhibit 3.3 to the Company's Quarterly Report on Form 10-Q for the quarter ended November 30, 2003.
- (3) Incorporated by reference to Exhibit 3.4 to the Company's Quarterly Report on Form 10-Q for the period ended November 30, 2004.
- (4) Incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K filed on June 2, 2009.
- (5) Incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K filed on September 24, 2009.