

# CORNERSTONES

Compuware Corporation  
Annual Report **2002**



COMPUWARE®

1  
One Company

2  
Process Driven

3  
Customer Facing

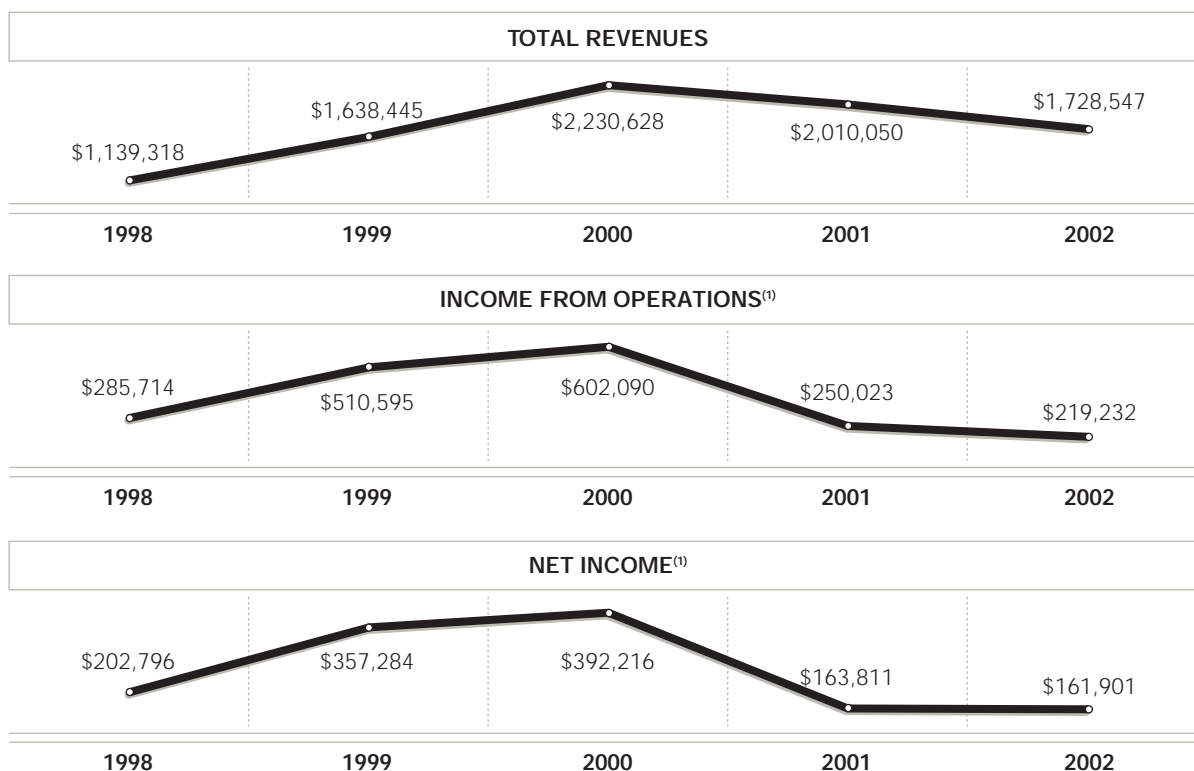
4  
Employees = Assets



## SELECTED CONSOLIDATED FINANCIAL DATA 2002

(In Thousands, Except Per Share Data)

	YEAR ENDED MARCH 31,				
	2002	2001	2000	1999	1998
<b>STATEMENT OF OPERATIONS DATA:</b>					
Total revenues	\$ 1,728,547	\$ 2,010,050	\$ 2,230,628	\$ 1,638,445	\$ 1,139,318
Income from operations <sup>(1)</sup>	219,232	250,023	602,090	510,595	285,714
Net income <sup>(1)</sup>	161,901	163,811	392,216	357,284	202,796
-Diluted earnings per share <sup>(1)</sup>	0.42	0.44	1.02	0.89	0.52
Net income (loss)	(245,255)	119,083	351,976	349,863	193,944
-Diluted earnings (loss) per share	(0.66)	0.32	0.91	0.87	0.50
<b>BALANCE SHEET DATA:</b>					
Working capital	506,692	434,902	391,801	550,586	362,324
Total assets	1,993,938	2,279,374	2,415,907	1,676,683	1,072,640
Long-term debt	—	140,000	450,000	—	6,956
Total shareholders' equity	1,189,851	1,377,372	1,203,872	1,079,522	708,296



(1) Before special charges (restructuring and purchased research and development) and amortization of intangible assets acquired as a result of acquisitions



Peter Harmanos, Jr.



## LETTER *to* SHAREHOLDERS

Fellow Shareholders:

Fiscal 2002 was a difficult year for Compuware Corporation. While our stock price increased 32.4 percent for the fiscal year, we suffered a 14 percent reduction in revenues. Additionally, for the first time in our history, we made the painful decision to significantly reduce Compuware's workforce. These reductions were implemented in areas where our staff was underutilized and our market share could not support business growth. In order to be a successful company, Compuware must grow, and grow profitably. This restructuring, though difficult, will improve Compuware's profitability and better position the company for long-term growth—benefiting our employees and shareholders.

The positive news is that Compuware remains profitable, and our fundamental financial position is very sound. We have outstanding cash flow, no long-term debt and more than \$400 million in cash and cash equivalents. The restructuring announced at the beginning of fiscal 2003 should reduce our annual expenses by approximately \$200 million and considerably improve our professional services margins.

These strong fundamentals mean that Compuware has a good base from which to build. Outstanding employees, excellent technology and the strength of our financial position will help ensure our growth and profitability. But growth and profitability aren't enough. No one on our executive management team is content with Compuware being merely a good



company. We want more than that—and our employees and investors deserve it. But we must increase our revenues and earnings to achieve a better stock price. This is one of my chief responsibilities, and I take it very seriously.

However, increasing revenue growth for a billion-dollar-plus company is a much greater challenge than increasing growth for a smaller organization. This law of large numbers is compounded by the hangover currently affecting our industry. For too many years, companies have poured millions of dollars into packaged applications, dot-coms and overpriced consultants, only to find they needed to spend many times that amount to implement the technology. Decision-makers at these companies are not receiving the return they expect on investments of this magnitude, making them leery of technology investments altogether. Compuware has an advantage here. Our products and services demonstrate some of the most compelling return on investment of any in the industry. Nonetheless, this is the mindset we must overcome in an already difficult economic environment.

“No one on our executive management team is content with Compuware being merely a good company. We want more than that—and our employees and investors deserve it.”

The issues we must address are not only external. In the late 1990s, it was much easier to make money as a technology company than it is today. The business walking in through the door took priority over addressing organizational inefficiencies. Today's economic reality, however, means we must transform our business to succeed: not through a magic pill, or a marketing campaign, but through fundamental change and hard work. Companies the size of Compuware cannot change instantly. But we are committed to changing because we must to meet our goals.

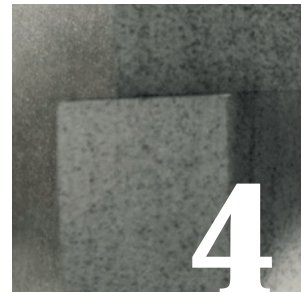
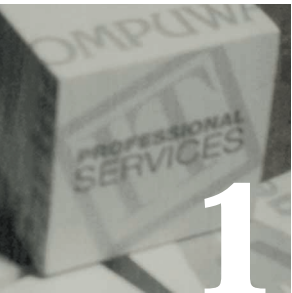
Last year's goals were: to maintain our competitive edge in the mainframe market, to expand our distributed systems market share and to grow our professional services business. How did we do? While the overall business is still profitable and healthy, our results in attaining these goals were largely unimpressive.

Our mainframe business continues to be strong. For the year, our mainframe products' revenue was \$687.3 million. Nearly 30 years in the mainframe products business give Compuware a profitable maintenance base, high margins and longstanding business relationships with Fortune 1,000 companies. Our mainframe business is a competitive advantage that none of



our competitors in the distributed marketplace has, giving us significant cash flow for research and development. Since our mainframe business remains the bedrock upon which we will expand our already formidable family of distributed products, we are aggressively defending our mainframe revenue through continual development efforts.

As a percentage of software revenues, we did not significantly increase distributed systems products' revenue during the fiscal year. Though these results were disappointing, our capacity for growth in this market is enormous, and increasing distributed systems revenue remains a key focus for the company. Compuware distributed products, like our mainframe tools, reduce our customers' expenses, save their time and make their staff more productive. Compuware invests a significant percentage of our research and development (R&D) dollars in our distributed products—an investment dwarfing the percentage of revenue and absolute dollars spent by our competitors in the distributed marketplace. Our R&D efforts are strengthening our award-winning distributed product family, and over the next year we will work toward making every one of our distributed products a "must have."



We were unable to significantly improve our margins or build the critical mass required for growth in our services business this fiscal year. These facts led us to restructure our professional services business beginning in April 2002. While this was a difficult decision, we believe the restructuring will allow Compuware to begin growing its professional services business profitably again. We intend to manage our off-assignment personnel and our hiring practices more effectively, preventing a recurrence of the problems that limited services revenue growth this year. Compuware remains committed to the services business. Our services personnel create new sales opportunities by representing our company to customers around the world, and they continue to provide us with timely, accurate intelligence on customer needs.

As we reviewed our goals from last year, and our plans for the next fiscal year, it became apparent that a fundamental change in the structure and operations of our entire company was necessary. We're profitable and stable, but Compuware is not growing the way it must to be a successful company and a successful investment. To that end, we have implemented a new organizational

structure, based on four cornerstones: One Company, Process Driven, Customer Facing and Employees = Assets. These cornerstones represent an essential change in the way Compuware conducts business every day. I believe in these cornerstones, and I believe in the people who are implementing them. Continue reading this report to learn more about our strategy for change and our plans for products and services in the coming year. These changes are essential and ongoing, and they are the keys to our success.

“The positive news is that Compuware remains profitable, and our fundamental financial position is very sound. We have outstanding cash flow, no long-term debt and more than \$400 million in cash and cash equivalents.”

Thank you for investing in Compuware Corporation. I'm working very hard to make sure your faith in our company is rewarded. I look forward to reporting to you on our progress again next year.

Sincerely,

Peter Karmanos, Jr.  
Chairman and CEO



# ONE COMPANY



Compuware was founded as a professional services company. Our goals: to help people use technology to run their businesses more efficiently and to save them time and money. As the company grew, we added products to our stable of solutions. Compuware products proved extremely successful, delivering value to customers around the world. As Compuware's revenue and workforce increased at a dramatic pace, a separation grew between the services and products groups, resulting in differing practices and policies. Compuware's One-Company cornerstone is our strategy to unite these two sides of our business and use the combined strength of products and services to create new sales opportunities and improved solutions.

Through the One-Company cornerstone, we are creating a unified Compuware, delivering software and services in a coordinated fashion for all of our customers' application life-cycle needs. Customers who use Compuware products often have a need for professional services, whether for assistance in the installation of new products or for help running their IT departments. Additionally, if a company uses Compuware's services, it is likely they could use Compuware products to help improve productivity. By striving to meet our customers' needs through both Compuware products and services, we give our customers a compelling value proposition—a single-source supplier of combined product and service solutions.

The financial arguments for this combination of products and services are compelling. There are significant numbers of our customers who use either Compuware products or services, but not both. By leveraging our existing relationships to sell products or services where none were sold before, Compuware has a significant opportunity to increase revenue.

The One-Company cornerstone promotes the depth and capability of Compuware products and services. For example, customers who currently employ Compuware people to improve application reliability will be made aware of Compuware's products that can augment these services. This is also true for customers who use Compuware products. Are they aware of the services we provide that can increase their productivity? In the past, this was not a sure bet. Now it will be.

We are committed to completing the transformation to One Company over time, through training, education and process-implementation. By forging a unified Compuware, we expect the company to generate more revenue, to be easier for customers to deal with and to present a more clear and compelling value proposition.





# PROCESS

## DRIVEN



In a large and complex business such as Compuware's, a variety of processes exist for tasks ranging from the delivery of services and products to administrative work. Our size and global reach, as well as a history of acquisitions, have left Compuware with a wide variety of processes, some more effective than others. Our Process-Driven cornerstone establishes a commitment to uniformly identify and institutionalize best practices across the company.

Our guidelines for this cornerstone are simple: when a process works effectively, apply it to as many other areas in the company as possible. Such processes can be found inside or outside of Compuware. The key to this cornerstone is our openness to identifying what works and our willingness to implement it. Once such best practices have been identified, they can be applied to other areas. Compuware is placing great emphasis on the documentation of processes, allowing our people to recognize both processes that are outstanding and those that need improvement.

Our efforts to become more uniformly Process Driven are designed to help us meaningfully measure Compuware's success with customers. Using quality measurement techniques, operations staff can identify the primary requirements of customers and break them down until a measurable need is defined. From this point, Compuware can determine what products or services can completely satisfy customer needs. We can then use measures and control plans to monitor how well the process for delivering these products and services is performing.

Additionally, the Process-Driven cornerstone will help Compuware more quickly deliver strong, high-quality technology to our customers. Compuware's product development group has merged with our internal information services team. This new Technology organization is following a strict, defined and unified process for developing technology, both for internal and external use. This common process helps Compuware most directly address the needs of our customers while getting maximum value from the best technology minds in the company.

Underlying this Process-Driven cornerstone is an opportunity to more efficiently bring quality and value to our customers. By improving and institutionalizing efficient processes, Compuware continues to build upon its reputation and strength as a low-cost provider. By employing strategies for universally implementing efficient processes, measuring the efficacy of these processes and identifying areas for improvement, Compuware will deliver its products and services more cost effectively. By driving down our cost of doing business, Compuware can share the benefits of these savings with our customers and investors.



# CUSTOMER *facing*



Compuware's business philosophy has always held that relationships with our customers are primary. No matter the value of the technology or services we provide, if we do not maintain outstanding relationships with our customers, we have failed. Strong relationships allow us to address the inevitable difficulties of working with people and technology. Our Customer-Facing cornerstone builds on this philosophy through an emphasis on frequent personal contact, in-depth product and services knowledge and outstanding service.

In reaffirming our commitment to this Customer-Facing cornerstone, Compuware is encouraging every employee to better determine how to meet and exceed customer needs. This customer-oriented perspective places the power for meeting those needs in the hands of the people who most closely interact with our customers—our sales force. By encouraging our sales staff to fully understand the technologies that support our customers' businesses, we will more easily recognize where Compuware products or services can meet customer needs.

In harmony with the One-Company cornerstone, Compuware recognizes that each customer has needs that often can be met, not with a single product or service engagement, but with a combination of products and services. Communicating the wide scope of Compuware products and services to current and potential clients is a tremendous opportunity for Compuware to increase sales while addressing more of our customers' technology problems. To this end, a comprehensive program is in place to ensure that a fundamental level of knowledge about the spectrum of Compuware solutions exists throughout the company.

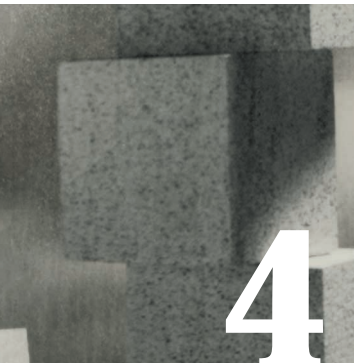
This educational program, combined with the increased commitment to understanding the needs of our customers and prospective customers, presents an opportunity for Compuware to more fully demonstrate the value we can deliver. By understanding our customers better, we create greater momentum for sales, while helping our customers meet their technology needs throughout the entire application life cycle.

In addition to these efforts, we are working hard to remove any hurdles to doing business with Compuware. While such roadblocks exist in any organization, we are focused on eliminating any impediments customers could encounter working with us. By diligently focusing first, foremost and always on the needs of our customers, we expect to provide an even higher level of service, increasing our revenue in the process.





# EMPLOYEES = ASSETS



With more than 11,000 employees throughout the world, Compuware has more than 11,000 potential ambassadors to help customers and potential customers realize the value of using Compuware products and services. Every employee can help Compuware increase revenue. The Employees = Assets cornerstone is based upon our commitment to more effectively utilize our greatest resource—our employees. By helping all employees better understand their contribution to revenue generation, Compuware expects to improve the delivery of products and services to our customers.

As an ambassador for the company, every Compuware employee has the opportunity to help Compuware reach its growth objectives. Increased knowledge of Compuware products and services achieved through the One-Company and Process-Driven cornerstones will help every employee have working knowledge of each Compuware offering. This awareness means that Compuware employees worldwide will be better able to recognize opportunities where Compuware products or services could help customers or potential customers achieve their IT goals.

In addition to training and educating current employees, we are working hard to attract and keep the best people in the industry. By refining our recruiting, retention and mentoring practices, and by hiring those people who agree with Compuware's philosophy and purpose, the company's transition will gain momentum until our strategic goals are more easily achieved. In order to improve our ability to find and retain these employees, Compuware is making increased efforts to recognize employee contributions and help each employee grow in directions that will benefit their careers. Compuware is keeping our worldwide employee base informed and connected through a variety of communications vehicles. These increased and standardized employee communications will keep employees more involved in their career paths and more aware of Compuware's business direction and philosophy.

A major point of emphasis underlying the Employees = Assets cornerstone is improving employee retention. Training new employees is expensive, so increased retention represents an opportunity to significantly reduce costs and improve efficiency. Improved retention will also mean Compuware can spend less time rebuilding lost organizational knowledge and skills. Through the Employees = Assets cornerstone, Compuware can maintain a strong base of committed employees and build on the foundation of a customer-service, value-driven culture.





# PRODUCT *and* SERVICES UPDATE



Since 1973 Compuware's business has been built upon a foundation of value. We give our customers more than they expect for their investment in our people and technology. Our commitment to this mission is unflinching; it guides everything we do. Through our One-Company cornerstone, Compuware delivers value by combining our products and services.

In fiscal year 2003, this integration of products and services will give Compuware considerable opportunities for growth. *Specifically, projects for fiscal 2003 are planned:*

- To increase our Java support by enhancing our OptimalJ and DevPartner product lines.
- To enhance application development support for Microsoft's Visual Studio .NET.
- To expand support for mainframe enterprise products, including the IBM WebSphere MQ environment, as well as continued improvements in support of DB2, IMS and CICS.
- To strengthen our QACenter products through web-based test management, enhanced SAP and Oracle support and .NET/web services application load-testing support.
- To help customers effectively plan for and manage distributed business applications through enhanced Vantage product releases.
- To continually improve software quality and integration.
- To complete the consolidation of all customer-facing and quality assurance organizations, improving our customer focus.
- To focus on our core services business of building, maintaining, enhancing and supporting business systems. These core services include staff supplementation; outsourced application maintenance, development and project management as well as the implementation and use of specific technologies such as Compuware products, wireless offerings and e-business solutions.
- To implement a standard project management methodology using Compuware products, processes and personnel to more effectively deliver all technology projects.
- To expand our alliances and channels, increasing our distribution capabilities.



## Fiscal 2002 Review

During fiscal 2002, Compuware undertook wide-ranging product and services development efforts. With the launch of OptimalJ, Compuware continued to attack the distributed systems market. OptimalJ maximizes developer productivity in the widely used Java 2 Enterprise Edition language through the use of visual models, intelligent design patterns and best practices for infrastructure and coding. OptimalJ reduces the need for experienced developers to conduct repetitive coding tasks while vastly improving the productivity of less-experienced programmers. Also this year, Compuware launched OptimalView, an enterprise portal that provides a unified view of an organization's most important information, applications and processes. OptimalView gives customers an integrated view of the technologies they use most frequently, saving time and money.

The Vantage (formerly EcoSYSTEMS) products were rebranded this fiscal year, and now include VantageView, a web-based reporting console where information from Vantage products is unified for efficient reporting and analysis. Comprised of seven tools, Vantage helps manage the performance of distributed applications. Early in fiscal 2002, Vantage's Application Expert was named Product of the Year in the *Network Computing* 2001 Well-Connected Awards. EcoPREDICTOR, now named Predictor, was also nominated as a finalist for the awards. The Vantage family provides Compuware customers with tools for managing diverse IT environments, including the capability to manage the performance of Microsoft .NET applications.

In further support of our customers' Microsoft investments, DevPartnerDB 4.0 for *Microsoft SQL Server*, released in fiscal 2002, enables the proactive analysis and debugging of SQL stored procedures during application development, increasing the reliability of database applications. Also introduced this fiscal year, DevPartner Studio 6.6 delivers an enhanced version of CodeReview that supports Visual Basic developers migrating applications to Visual Studio .NET.

New features in our QA family of products introduced this fiscal year also support Microsoft .NET technologies. Furthering this support for diverse computing environments, Compuware announced this year that QARun 4.7 supports Siebel eBusiness Applications version 6.0. QARun 4.7 reduces testing labor for Siebel Systems customers, helping them deploy Siebel eBusiness applications more rapidly and with greater confidence. Also this fiscal year, Compuware introduced QACenter Performance Edition 4.8. This version extends Compuware's enterprise-application testing capability by adding support for applications developed using enterprise Java, wireless technology and packaged Oracle applications. QACenter provides organizations with the assurance that their software will perform as expected, before it goes live. QACenter Performance Edition was named "Editor's Choice" this year in the category "QA Tools for the Web" in *Natverk and Kommunikation*, an IDG publication based in Sweden.



Compuware also unveiled QAHiperstation 7.0 during this fiscal year. This latest release provides support for IBM WebSphere for e-business, enabling organizations to test application logic in an automated and cost-effective manner. In additional enterprise product news, Compuware introduced value-based licensing for enterprise products to be deployed on the IBM z/900 series hardware platform. The new licensing model gives customers the capability to define their capacity needs for Compuware product deployment independently of the IBM z/900 "footprint" capacity. Additionally, Compuware announced that its powerful development environment UNIFACE supports DB2 for development purposes on Windows NT and Windows 2000 and for deployment purposes on IBM AIX. This support for DB2, as well as integration with IBM WebSphere, provides added value to Compuware's enterprise customers.

In professional services news this fiscal year, Compuware sold its engineering services business to Kelly Services. This transaction allowed us to place a greater focus on our core services business. Compuware also announced in fiscal 2002 that it had teamed with Microsoft to develop mobile solutions and deploy custom-developed wireless applications to wireless devices. In addition, Compuware professional services staff worked with Microsoft and Washington Publishing Company to deliver services that help healthcare providers, payers and clearinghouses address technology issues related to the Health Insurance Portability and Accountability Act. Late in calendar 2001, Compuware announced that its design and development of the Detroit Medical Center web site, [www.dmc.org](http://www.dmc.org), won two eHealthcare Leadership awards at the Sixth Annual Healthcare Internet and Technology Conference. Additionally this year, Compuware professional services staff developed an XML web services solution for the Colorado Department of Agriculture using Microsoft Visual Studio .NET and the .NET Framework. The application collects and distributes information used by a number of government agencies, allowing the use of a standard web browser to track and disseminate vital information about Colorado's captive elk herds.

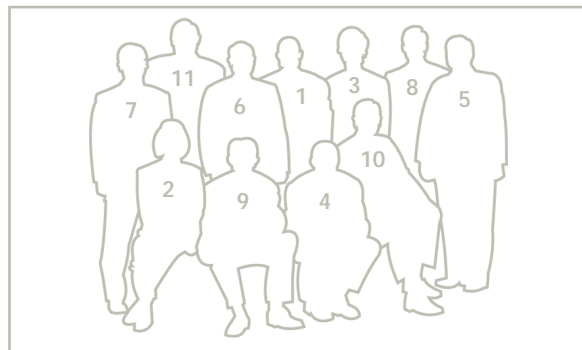
In addition to our significant partnerships with Microsoft, Oracle and others this fiscal year, Compuware announced a strategic relationship with Sun Microsystems to provide technology and services for the Sun ONE architecture. This strategic relationship includes joint product development, marketing and professional services initiatives.

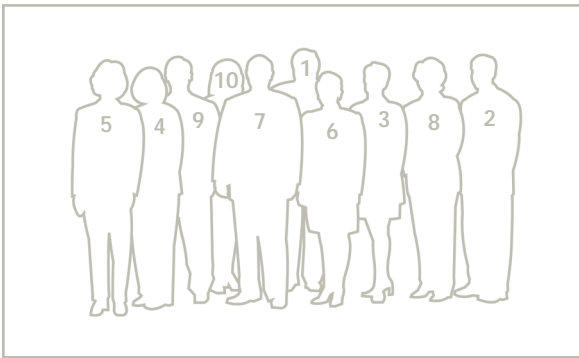
Our product and services development efforts for fiscal 2002 and our plans for fiscal 2003 present Compuware with the arsenal to pursue every opportunity for growth in the coming year. We are confident that our cornerstones strategy will help us pursue these opportunities by transforming the way we do business and improving our operations—ultimately, benefiting our employees and shareholders.

## COMPUWARE CORPORATION BOARD OF DIRECTORS



- |  |  |  |
|--|--|--|
| <p>1. <b>Dennis W. Archer</b><br/>Chairman,<br/>Dickinson Wright</p> <p>2. <b>Elizabeth A. Chappell</b><br/>President, The Economic<br/>Club of Detroit</p> <p>3. <b>Dr. Elaine K. Didier</b><br/>Dean, Oakland University<br/>Library and Professor,<br/>Oakland University</p> <p>4. <b>Bernard M. Goldsmith</b><br/>Managing Director,<br/>Updata Capital, Inc.</p> <p>5. <b>William R. Halling</b><br/>Member of the Board</p> | <p>6. <b>Peter Karmanos, Jr.</b><br/>Chairman of the Board<br/>and Chief Executive Officer,<br/>Compuware Corporation</p> <p>7. <b>Joseph A. Nathan</b><br/>President,<br/>Compuware Corporation</p> <p>8. <b>W. James Prowse</b><br/>Member of the Board</p> <p>9. <b>G. Scott Romney</b><br/>Partner,<br/>Honigman Miller<br/>Schwartz and Cohn</p> <p>10. <b>Thomas Thewes</b><br/>Vice Chairman of the Board</p> | <p>11. <b>Lowell P. Weicker, Jr.</b><br/>Member of the Board</p> <p><b>William O. Grabe</b><br/><i>(not pictured)</i><br/>Managing Member,<br/>General Atlantic Partners</p> |
|--|--|--|





## COMPUWARE CORPORATION STRATEGIC LEADERSHIP

- Chris Bockhausen**  
Senior Vice President and  
Chief Information Officer
- Thomas Costello, Jr.**  
Vice President, General  
Counsel and Secretary
- Donna Debrodt**  
Vice President,  
Marketing, Research  
and Strategy Support
- Lisa Elkin**  
Vice President,  
Communications and  
Investor Relations
- Laura Fournier**  
Senior Vice President,  
Chief Financial Officer  
and Treasurer
- Mary Hepler**  
Vice President,  
Sales Development  
and Support
- Peter Karmanos, Jr.**  
Chairman of the Board  
and Chief Executive  
Officer
- Denise Knoblock**  
Executive Vice President,  
Administration
- Joseph A. Nathan**  
President
- Kathy Rogien**  
Vice President, Human  
Resources



## COMPUWARE CORPORATION OPERATIONS LEADERSHIP

- Irene Dawson**  
Senior Vice President,  
Geographic Sales  
and Delivery,  
Europe, Middle East  
and Africa
- John Debrincat**  
Senior Vice President,  
Geographic Sales and  
Delivery, Asia Pacific
- Henry Jallos**  
Executive Vice President,  
Global Account  
Management
- Paul Johnson**  
Senior Vice President,  
Geographic Sales  
and Delivery,  
North America East
- Toshitaka Nashizawa**  
Senior Vice President,  
Geographic Sales  
and Delivery, Japan
- Alberto Neves**  
Senior Vice President,  
Geographic Sales and  
Delivery, Latin America
- Steve Scheidt**  
Senior Vice President,  
Geographic Sales  
and Delivery,  
North America Central
- Rod Schmitt**  
Senior Vice President,  
Geographic Sales  
and Delivery,  
North America West
- Tommi White**  
Chief Operating Officer

# MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

## FORWARD-LOOKING STATEMENTS

We make forward-looking statements in this report within the meaning of the federal securities laws and may make forward-looking statements on future filings with the Securities and Exchange Commission and in press releases and other communications. Forward-looking statements are identified by the use of the words "believes," "expects," "anticipates," "will," "contemplates," "would" and similar expressions that contemplate future events. Numerous important factors, risks and uncertainties affect the Company's operating results, including without limitation those discussed below. These factors, risks and uncertainties could cause our actual results to differ materially from the results implied by these or any other forward-looking statements made by, or on behalf of, the Company. There can be no assurance that future results will meet expectations. While we believe that our forward-looking statements are reasonable, you should not place undue reliance on any such forward-looking statements, which speak only as of the date made. Except as required by applicable law, we do not undertake any obligation to publicly release any revisions which may be made to any forward-looking statements to reflect events or circumstances occurring after the date of this report.

- Our quarterly financial results vary and may be adversely affected by certain relatively fixed costs. Our product revenues vary from quarter to quarter. Net income may be disproportionately affected by a fluctuation in revenues because only a small portion of our expenses varies with revenues.
- Our success depends in part on our ability to develop product enhancements and new products which keep pace with continuing changes in technology and customer preferences.
- Approximately 24% of our revenue is derived from foreign sources. This exposes us to exchange rate risks on foreign currencies and to other international risks such as the need to comply with foreign and U.S. export laws, and the uncertainty of certain foreign economies.
- While we are expanding our focus on distributed software products, a majority of our revenue from software products is dependent on our customers' continued use of IBM and IBM-compatible mainframe products and on the acceptance

of our pricing structure for software licenses and maintenance. The pricing of our software licenses and maintenance is under constant pressure from customers and competitive vendors.

- We regard our software as proprietary and attempt to protect it with copyrights, trademarks, trade secret laws and restrictions on disclosure, copying and transferring title. Despite these precautions, it may be possible for unauthorized third parties to copy certain portions of our products or to obtain and use information that we regard as proprietary. In addition, the laws of some foreign countries do not protect our proprietary rights to the same extent as the laws of the United States.
- Although we have not received any material claims that our products infringe on the proprietary rights of third parties, there can be no assurance that third parties will not assert infringement claims against us in the future with respect to current and future products or that any such assertion may not require us to enter into royalty arrangements or result in costly litigation.
- We depend on key employees and technical personnel. The loss of certain key employees or our inability to attract and retain other qualified employees could have a material adverse effect on our business.
- Our operating margins may decline. We do not compile margin analysis other than on a segment basis. However, we are aware that operating expenses associated with our distributed systems products are higher than those associated with our traditional mainframe products. Since we believe the best opportunities for revenue growth are in the distributed systems market, products operating margins could experience more pressure. In addition, operating margins in the professional services business are significantly impacted by small fluctuations in revenue since most costs are fixed during any short term period.
- The slowdown in the world economy could continue for an extended period and could cause customers to further delay or forego decisions to license new products or upgrades to their existing environments and this could adversely affect our operating results.



## RESULTS OF OPERATIONS

The following table sets forth, for the periods indicated, certain operational data from the consolidated statements of operations as a percentage of total revenues and the percentage change in such items compared to the prior period:

	PERCENTAGE OF TOTAL REVENUES			PERIOD-TO-PERIOD CHANGE	
	FISCAL YEAR ENDED MARCH 31,			2001 to 2002	2000 to 2001
	2002	2001*	2000*		
Revenues:					
Software license fees	24.2%	24.7%	36.7%	(15.7%)	(39.5%)
Maintenance fees	25.1	22.7	19.4	(5.0)	5.5
Professional services fees	50.7	52.6	43.9	(17.1)	8.1
Total revenues	100.0	100.0	100.0	(14.0)	(9.9)
Operating expenses:					
Cost of software license fees	2.1	2.0	1.4	(8.3)	28.7
Cost of maintenance	2.3	2.6	2.0	(25.3)	17.0
Cost of professional services	50.9	51.7	42.4	(15.3)	9.8
Software product development	5.9	5.1	3.6	(0.3)	26.5
Sales and marketing	22.9	22.5	20.9	(12.3)	(3.3)
Administrative and general	4.3	4.4	3.1	(17.3)	37.5
Goodwill amortization and impairment	24.7	2.1	1.1	**	64.5
Restructuring costs	2.7			**	**
Purchased research and development			0.8		(100.0)
Total operating expenses	115.8	90.4	75.3	10.1	8.2
Income (loss) from operations	(15.8)	9.6	24.7	**	(65.1)
Other income (expense):					
Interest and investment income	1.7	1.5	1.6	(3.9)	(12.1)
Interest expense	(0.4)	(1.6)	(1.1)	76.2	(27.7)
Total other income (expense)	1.3	(0.1)	0.5	**	(105.4)
Income (loss) before income taxes	(14.5)	9.5	25.2	**	(65.8)
Income tax provision (benefit)	(0.3)	3.6	9.4	**	(65.2)
Net income (loss)	(14.2%)	5.9%	15.8%	**	(66.2%)

\* Reclassified to conform to the 2002 presentation.

\*\* Calculation is not meaningful.

The following table sets forth, for the periods indicated, certain operational data after excluding restructuring, purchased research and development and amortization and impairment of intangible assets acquired as a result of acquisitions (excluded charges), (in thousands):

	FISCAL YEAR ENDED MARCH 31,		
	2002	2001	2000
Income (loss) before income taxes	\$ (250,847)	\$ 192,069	\$ 561,776
Amortization and impairment of goodwill <sup>(1)</sup>	426,344	42,092	25,586
Amortization and impairment of purchased software	18,879	15,299	7,271
Restructuring costs <sup>(2)</sup>	46,930		
Purchased research and development			17,900
Income before income taxes and excluded charges	241,306	249,460	612,533
Income tax provision	79,405	85,649	220,317
Net income before excluded charges	\$ 161,901	\$ 163,811	\$ 392,216

<sup>(1)</sup> Before income taxes, amortization and impairment of goodwill during 2002 included \$342.9 million associated with restructuring, \$35.2 million associated with a change in technology related to distributed products and \$9.3 million associated with the transfer of the engineering business discussed in the Professional Services Revenue section below. See note 6 of Notes to Consolidated Financial Statements for more details on the restructuring related charge.

<sup>(2)</sup> See note 6 of Notes to Consolidated Financial Statements for more details on this charge.

We operate in two business segments in the technology industry: products and professional services. We evaluate the performance of our segments based primarily on operating profit or loss before corporate expenses. References to years are to fiscal years ended March 31.

## SOFTWARE PRODUCTS

### Revenue

Our products are designed to support four key activities within the application development process: development and integration, quality assurance, production readiness and performance management of the application to optimize performance in production. Products revenue consists of software license fees and maintenance fees and comprised 49.3%, 47.4% and 56.1% of total revenue during 2002, 2001 and 2000, respectively. OS/390 product revenue (mainframe revenue) decreased \$75.5 million or 9.9% during 2002 and decreased \$268.5 million or 26.0% during 2001. Revenue from distributed software products decreased \$25.2 million or 13.3% during 2002 and decreased \$31.4 million or 14.2% during 2001.

License revenue decreased \$78.0 million or 15.7% during 2002 to \$417.6 million from \$495.6 million during 2001 and decreased \$323.6 million or 39.5% from \$819.2 million during 2000. Maintenance fees decreased \$22.7 million or 5.0% to \$433.8 million during 2002 from \$456.5 million during 2001 and increased \$23.8 million or 5.5% from \$432.7 million in 2000. The decrease in maintenance fees was primarily attributable to lower license fees during both 2002 and 2001 and to market pressure on renewal rates.

The overall decline in product revenue from 2001 to 2002 was primarily attributable to decreases in license fees and maintenance fees associated with decreased customer demand for our products in North America. The overall decline in product revenue from 2000 to 2001 was primarily attributable to a decrease in demand for large enterprise license agreements



(ELAs) and unfavorable changes in foreign currency exchange rates. If foreign exchange rates in 2002 had remained consistent with 2001, products revenue would have been \$870.9 million during 2002 compared to \$952.1 million during 2001. This represents an overall decline in constant U.S. dollars of \$81.2 million, or 8.5%, compared to an actual decline of \$100.7 million, or 10.6%. If foreign exchange rates in 2001 had remained consistent with 2000, product revenue would have been \$984 million in 2001 compared to \$1.252 billion in 2000. This represents an overall decline in constant U.S. dollars of \$268 million or 21.4% compared to the actual decline of \$300 million or 24.0%. Product revenue was further impacted by a decrease in customer demand for large ELAs which are multiyear, and often multipayment contracts. Multiyear contracts greater than \$5 million represented approximately 6.9%, 12.8% and 26.5%, of license revenue in 2002, 2001 and 2000, respectively.

We support clients with product transactions covering multiple years and allowing deferred payment terms. The contract price is allocated between maintenance for the contract term and license revenue. All license revenue associated with these perpetual license agreements is recognized when the customer commits unconditionally to the transaction, the software products and quantities are fixed and the software has been shipped to the customer. License revenue associated with transactions that include an option to exchange or select products in the future has been deferred and is recognized over the contract term. When the license portion is paid over a number of years, the license portion of the payment stream is discounted to its net present value. Interest income is recognized over the payment term. The maintenance associated with all sales has been deferred and is recognized over the applicable maintenance period.

Products revenue by geographic location is presented in the table below (in thousands):

	YEAR ENDED MARCH 31,		
	2002	2001	2000
United States	\$ 532,772	\$ 597,290	\$ 833,365
European subsidiaries	217,800	235,841	285,158
Other international operations	100,810	118,975	133,431
Total products revenue	\$ 851,382	\$ 952,106	\$ 1,251,954

### Operating Profit and Expenses

Financial information for our products segment is as follows (in thousands):

	YEAR ENDED MARCH 31,		
	2002	2001	2000
Revenue	\$ 851,382	\$ 952,106	\$ 1,251,954
Operating expenses	574,573	646,963	624,299
Products operating profit	\$ 276,809	\$ 305,143	\$ 627,655

The products segment generated operating margins of 32.5%, 32.0% and 50.1% during 2002, 2001 and 2000, respectively. Products expenses include cost of software license fees, cost of maintenance, software product development costs, and sales and marketing expenses. The operating margin in 2002 is fairly constant compared to the operating margin in 2001. The decrease in operating margin in 2001 was primarily a result of a decrease in software license revenue while total products costs were fairly constant.

Cost of software license fees includes amortization of capitalized software, the cost of preparing and disseminating products to customers and the cost of author royalties. The decrease in these costs in 2002 was due primarily to decreased author royalties, decreased printing and distribution costs, and decreased salary and benefits associated with lower employee headcount. The increase in these costs in 2001 was due primarily to an increase in amortization of capitalized software products, related to the Programart, CACI and Optimal acquisitions and increased amortization of internally capitalized projects associated with Vantage (formerly EcoSYSTEMS), QALoad, UNIFACE, Abend-AID, File-AID and XPEDITER, which were released for general availability during 2001. As a percentage of software license fees, cost of software license fees were 8.7%, 8.0% and 3.8% in 2002, 2001 and 2000, respectively.

Cost of maintenance consists of the cost of maintenance programmers and product support personnel and the computing, facilities and benefits costs allocated to such personnel. The decrease in cost of maintenance in 2002 was due primarily to decreases in salary and benefits associated with lower employee headcount, reduced travel expenses and reduced costs of corporate systems. The increase in cost of maintenance in 2001 was due, primarily, to a higher average headcount compared to the prior fiscal year. As a percentage of maintenance fees, these costs were 9.1%, 11.6% and 10.5% for 2002, 2001 and 2000, respectively.

Software product development costs consist of the cost of programming personnel, the facilities, computing and benefits costs allocated to such personnel and the costs of preparing user and installation guides for our software products, less the amount of software development costs capitalized during the fiscal year. The decrease in these costs in 2002 was due primarily to decreased salary and benefits associated with lower employee headcount, offset by a charge for leased office space no longer

utilized as a result of the consolidation of development facilities and increased amortization of purchased software due to impairment charges against the purchased software associated with underperforming products acquisitions. The increase in these costs in 2001 was primarily due to an increase in salaries and benefits, including severance costs, associated with a relocation of the software development lab for the Vantage product line and an increase in software development staff related to the Programart and CACI acquisitions during 2000.

Capitalization of internally developed software products begins when technological feasibility of the product is established. Before the capitalization of internally developed software products, total research and development expenditures for 2002 decreased \$0.5 million, or 0.4%, to \$115.6 million from \$116.1 million in 2001. In 2001, total research and development costs increased \$20.5 million, or 21.5%, to \$116.1 million from \$95.6 million in 2000. The major development projects that achieved technological feasibility during 2002 included 3 new interactive analysis and debugging products, 2 new fault management products, 8 new file and data management products, 8 new automated testing products, 18 new systems management products, 10 new application development products, 3 new application performance management products, 2 new license management products, and 9 new Windows development tools.

Sales and marketing costs consist of the sales and marketing expenses associated with the products business, which include costs of direct sales, sales support and marketing staff, the facilities and benefits costs allocated to such personnel and the costs of marketing and sales incentive programs. The decrease in sales and marketing costs from 2001 to 2002 was primarily attributable to decreased salaries and benefits associated with lower average headcount, decreased distributor commissions associated with decreased software license revenue, decreased travel expenses, and decreased advertising expenditures. The decrease in sales and marketing costs from 2000 to 2001 was largely attributable to lower sales commissions associated with decreased product sales and to reduced advertising expenditures, offset, in part, by increased salaries and benefits due, primarily, to a higher average headcount during 2001 compared to the prior year. The direct sales and sales support staff decreased by 508 to 1,951 people at March 31, 2002, as compared to 2,459 at March 31, 2001 and 2,680 at March 31, 2000.



## PROFESSIONAL SERVICES

### Revenue

We offer a broad range of information technology professional services, including business systems analysis, design and programming, software conversion and system planning and consulting. Revenue from professional services decreased \$180.8 million or 17.1% during 2002 and increased \$79.3 million or 8.1% during 2001. The decrease in revenue for 2002 was due, primarily, to a reduction in customer demand for professional services. The increase from 2000 to 2001 was due, primarily, to increased market share associated with the August 1999 acquisition of Data Processing Resources Corporation (DPRC).

On December 1, 2001, we transferred our engineering services business to an unrelated third party. Professional services revenue associated with the engineering business was approximately \$21.0 million in 2002, \$28.6 million in 2001 and \$17.7 million in 2000. Effective January 1, 2002, we assigned our prime contract with a client to a company in which we have a minority equity investment and simultaneously entered into an agreement with this company to become a subcontractor providing services for the client. Professional services revenue associated with this activity was approximately \$36.0 million, \$64.0 million and \$44.0 million during 2002, 2001 and 2000, respectively. These changes, along with the restructuring discussed below, allow us to further focus on our core professional services business.

Professional services revenue by geographic location is presented in the table below (in thousands):

	YEAR ENDED MARCH 31,		
	2002	2001	2000
United States	\$ 783,764	\$ 963,508	\$ 903,146
European subsidiaries	90,031	88,041	66,269
Other international operations	3,370	6,395	9,259
Total professional services revenue	\$ 877,165	\$ 1,057,944	\$ 978,674

### Operating Profit and Expenses

Financial information for our professional services segment is as follows (in thousands):

	YEAR ENDED MARCH 31,		
	2002	2001	2000
Revenue	\$ 877,165	\$ 1,057,944	\$ 978,674
Operating expenses	879,953	1,039,237	946,710
Professional services operating profit	\$ (2,788)	\$ 18,707	\$ 31,964

The professional services segment generated operating margins of negative 0.3%, and positive 1.8% and positive 3.3% during 2002, 2001 and 2000, respectively. The decrease in professional services

operating margin is primarily due to lower utilization, lower billing rates, and reduced customer demand for our services associated with the decline of the economy as a whole and the IT sector specifically.

Cost of professional services includes all costs of our professional services business, including the personnel costs of the professional, management and administrative staff of our services business and the facilities and benefits costs allocated to such personnel. The decrease in these costs from 2001 to 2002 is due, primarily, to reductions in staff, resulting in lower salaries and benefits, reduced travel expenditures and decreased use of subcontractors for special services. The increase in these costs from 2000 to 2001 is due, primarily, to a higher average professional staff headcount during 2001 compared to 2000, and to increased use of subcontractors for special services. The professional billable staff decreased 1,016 people to 7,025 people as of March 31, 2002 from 8,041 people at March 31, 2001. This compares to a decrease of 1,565 professional billable staff, to 8,041 at March 31, 2001 from 9,606 people at March 31, 2000.

#### CORPORATE AND OTHER EXPENSES

Administrative and general expenses decreased 17.3% during 2002 and increased 37.5% during 2001. The decrease in administrative and general expenses during 2002 was primarily attributable to decreased charges against investments in joint ventures. The increase in administrative and general expenses from 2000 to 2001 is primarily attributable to charges against investments in joint ventures, offset, in part, by decreases in legal costs associated with fewer acquisitions, and decreases in outside consulting services.

During 2000, we recognized \$17.9 million of expense for purchased research and development costs associated with the acquisition of in process research and development from Programart Corporation.

Interest and investment income for 2002 was \$29.5 million as compared to \$30.7 million in 2001 and \$34.9 million in 2000.

These decreases were due to lower interest earnings on investments due to reduced interest rates, offset, in part, by increased interest related to customers' deferred installments. Interest expense for 2002 was \$7.4 million as compared to \$31.3 million in 2001 and \$24.5 million in 2000. Interest expense includes amortization of the initial financing fees and ongoing fees associated with the unutilized balance of the Senior Credit Facility (the credit facility) discussed in the Liquidity and Capital Resources section below. The decrease in interest expense from 2001 to 2002 was primarily attributable to the July 2001 payoff of debts previously outstanding under the credit facility. The increase in interest expense from 2000 to 2001 was primarily attributable to interest expense associated with debt outstanding under the credit facility during 2001.

We account for income taxes using the asset and liability approach. Deferred income taxes are provided for the differences between the tax bases of assets or liabilities and their reported amounts in the financial statements. The income tax benefit was \$5.6 million in 2002. This compares to an income tax provision of \$73.0 million in 2001, which represents an effective tax rate of 38.0%, and an income tax provision of \$209.8 million in 2000, which represents an effective tax rate of 37.3%. Our effective tax rate for 2002 differs significantly from the U.S. federal income tax rate of 35.0% primarily as a result of nondeductible goodwill amortization and impairment charges. The 2001 increase in the effective tax rate was due to nondeductible goodwill amortization associated with certain acquisitions and a shift of our state apportionment to states with higher corporate income tax rates.



## RESTRUCTURING AND GOODWILL AMORTIZATION AND IMPAIRMENT CHARGES

In the fourth quarter of 2002, we adopted a restructuring plan which will reorganize our operating divisions, primarily the professional services segment. The plan resulted in total charges of \$389.9 million including \$342.9 million for the impairment of goodwill recognized in the acquisition of certain professional services businesses, primarily DPRC. These changes are designed to increase profitability in the future by better aligning cost structures with current market conditions. We also incurred an impairment charge of \$35.2 million associated with a change in technology related to distributed products and a \$9.3 million charge associated with the transfer of the engineering business.

The restructuring plan includes a reduction of professional services staff at certain locations, the closing of entire professional services offices and a reduction of sales support

personnel, lab technicians and related administrative and financial staff. Approximately 1,600 employees will be terminated as a result of the reorganization. Prior to year-end, we communicated benefits available to employees under the plan. A majority of affected employees are expected to be terminated during the first quarter of 2003. As of May 31, 2002, 1,049 of the affected employees were terminated.

In conjunction with the development of the restructuring plan, we evaluated the carrying value of goodwill and other intangible assets related to the professional services business, and recorded an impairment charge related to our prior services acquisitions. Certain professional services offices acquired as part of those acquisitions have not achieved critical mass or a sustained level of profitability and were closed in April 2002 as part of the restructuring plan. We utilized discounted cash flow analyses to value the remaining business, and recognized goodwill impairment based upon current estimated fair market values.

The following table summarizes the restructuring and impairment charges taken in 2002 (in thousands):

	TOTAL CHARGES	COMPLETED AS OF MARCH 31, 2002	REMAINING ACCRUAL AT MARCH 31, 2002
Employee termination benefits	\$ 19,012	\$ 553	\$ 18,459
Facilities costs (primarily lease abandonments)	26,341	676	25,665
Legal, consulting and outplacement costs	1,299		1,299
Other	278		278
Restructuring charge	46,930	1,229	45,701
Goodwill impairment charge	342,922	342,922	-
Total charges	\$ 389,852	\$ 344,151	\$ 45,701



## LIQUIDITY AND CAPITAL RESOURCES

As of March 31, 2002, cash and investments totaled approximately \$422.4 million. Our primary source of liquidity is cash flow from operations. During 2002 and 2001, we generated \$386.8 million and \$336.6 million, respectively, in operating cash flow. The increased operating cash flow was generated, in part, from the collection of the current portion of prior years' installment receivables as reflected in the decrease in total accounts receivable. During these periods, we had capital expenditures that included property and equipment, capitalized research and software development, and purchased software of \$103.7 million and \$53.7 million, respectively.

As of February 13, 2002, our unsecured credit facility, which expires in August 2003, was reduced to a total of \$500 million available. Interest may be determined on a Euro dollar or base rate (as defined in the credit facility) basis at our option. The credit agreement contains financial ratios and other restrictive covenants and requires commitment fees in accordance with standard banking practice. As of March 31, 2002, we had no long term debt, compared to \$140.0 million as of March 31, 2001. This balance represented borrowings under the credit facility.

We believe available cash resources including the amount available under the credit facility, together with cash flow from operations, will be sufficient to meet our cash needs for the foreseeable future.

Although there were no acquisitions during 2002, we continue to evaluate business acquisition opportunities that fit our strategic plans.

We are building a new corporate headquarters office building with a current estimated cost of \$350 million for the building and an estimated \$50 million for furniture and fixtures. Cash outlays will have no impact on the results of operations until the building is ready for occupancy. When fully occupied, in calendar 2003, the depreciation will result in an annual expense of approximately \$17 million. This will be partially offset by the savings realized by the consolidation of offices. Capital expenditures to date total \$106.8 million. Cash outlays for the next twelve months are expected to be approximately \$218.6 million. Currently, we intend to fund the building using cash flow from operations.

Our cash flow from operations for the coming year is dependent upon the Company's operating divisions meeting their projected levels of sales activity. However, our solid base of accounts receivable installment payments that become due throughout the year provides some level of predictability to cash flow.

For a description of our payment obligations in the future, see note 12 of Notes to Consolidated Financial Statements included in this report.

## RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In July 2001, the FASB issued SFAS No. 141, "Business Combinations." SFAS 141 requires the purchase method of accounting be used for business combinations initiated after June 30, 2001 and eliminates the pooling-of-interests method. We have not done any acquisitions since adopting this standard.

In July 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangible Assets." We are required to adopt this statement for the year ending March 31, 2003. SFAS 142 requires that goodwill no longer be amortized but instead be tested for impairment at least annually and that indefinite lived intangible assets no longer be amortized over their useful lives. We have evaluated our remaining goodwill as of April 1, 2002, and have determined there will be no impairment upon adoption of SFAS No. 142.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This supercedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of." This statement retains the impairment loss recognition and measurement requirements of SFAS No. 121. In addition, it requires that one accounting model be used for long-lived assets to be disposed of by sale, and broadens the presentation of discontinued operations to include more disposal transactions. We adopted this statement on April 1, 2002. It is not expected to have any impact on our financial position or results of operations.



## MANAGEMENT'S DISCUSSION OF CRITICAL ACCOUNTING POLICIES

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The accounting policies discussed below are considered by management to be the most important to an understanding of our financial statements, because their application places the most significant demands on management's judgment and estimates about the effect of matters that are inherently uncertain. Our assumptions and estimates were based on the facts and circumstances known at March 31, 2002, future events rarely develop exactly as forecast, and the best estimates routinely require adjustment. These policies are also discussed in note 1 of the Notes to Consolidated Financial Statements included in this report.

**Revenue Recognition** – A significant portion of license fee revenue is earned in connection with multiyear contracts, for which deferred payments are allowed, with installments collectible over the term of the contract. For most of these contracts, generally accepted accounting principles provide that the license fee portion of the contract should be recognized in income upon shipment of the product, provided that no significant obligations remain and collection of the related receivable is deemed probable. As a result, revenue includes amounts for which the related cash will not be received for an extended period of time. We have significant experience with these types of contracts over a number of years, and believe we have sufficient knowledge of our customers and products to appropriately evaluate the collectibility of the receivables. However, changes in future economic conditions or technological developments could adversely affect our ability to collect these receivables.

**Allowance for Doubtful Accounts** – The collectibility of accounts receivable is regularly evaluated and we believe our allowance for doubtful accounts is appropriate for our accounts receivable balances. In evaluating the allowance, we consider historical loss experience, including the need to adjust for current conditions, and the aging of outstanding receivables. Larger accounts are reviewed on a detail basis, giving consideration to collection experience and any information on the financial viability of the customer. The allowance is reviewed and adjusted each quarter based on the best information available at the time.

**Capitalized Software** – The cost of purchased and internally developed software is capitalized and stated at the lower of unamortized cost or net realizable value. Software is subject to rapid technological obsolescence and estimates of future revenues to be derived from the software could be significantly affected by future developments. The amortization period for capitalized software is generally five years, but adverse developments could result in a shorter life or a write-off based on reduced estimates of net realizable value.

**Impairment of Goodwill** – Goodwill is evaluated at least annually to determine whether events and circumstances have occurred that indicate the remaining estimated useful life may warrant revision or that the remaining balance may not be recoverable. To evaluate the carrying value of goodwill, we utilize a discounted cash flow approach. This analysis requires judgment regarding discount rates, revenue growth and other variables that impact the net realizable value or fair value of the goodwill. Actual future cash flows and other assumed variables could differ from estimates.

## QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

We are exposed primarily to market risks associated with movements in interest rates and foreign currency exchange rates. We believe that we take the necessary steps to appropriately reduce the potential impact of interest rate and foreign exchange exposures on our financial position and operating performance. We do not use derivative financial instruments or forward foreign exchange contracts for investment, speculative or trading purposes. Immediate changes in interest rates and foreign currency rates discussed in the following paragraphs are hypothetical rate scenarios used to calibrate risk and do not currently represent management's view of future market developments. A discussion of our accounting policies for

derivative instruments is included in the Notes to Consolidated Financial Statements.

### Interest Rate Risk

Exposure to market risk for changes in interest rates relates primarily to our cash investments and installment receivables. Derivative financial instruments are not a part of our investment strategy. Investments are placed with high quality issuers to preserve invested funds by limiting default and market risk. In addition, all marketable debt securities and long term debt investments are classified as "held to maturity" which does not expose the consolidated statement of operations or balance sheet to fluctuations in interest rates.

The table below provides information about our investment portfolio, a significant portion of which is in municipal securities or other tax advantaged securities. For investment securities, the table presents principal cash flows and related weighted-average interest rates by expected maturity dates (in thousands, except interest rates):

	FY 2003	FY 2004	FY 2005	TOTAL	FAIR VALUE AT MARCH 31, 2002
Cash Equivalents	\$ 233,305			\$ 233,305	<b>\$ 233,305</b>
Average Interest Rate	1.96%			1.96%	
Average Interest Rate (tax equivalent)	1.97%			1.97%	
Investments	\$ 133,503	\$ 51,057	\$ 4,509	\$ 189,069	<b>\$ 189,110</b>
Average Interest Rate	2.54%	2.64%	2.48%	2.57%	
Average Interest Rate (tax equivalent)	3.87%	3.88%	3.82%	3.87%	



We offer financing arrangements with installment payment terms in connection with our multiyear software sales. Installment accounts are generally receivable over a three to five year period. As of March 31, 2002, non-current receivables amount to \$306.7 million and are due approximately \$190.2 million, \$85.8 million, \$23.6 million, and \$7.1 million in each of the years ended March 31, 2004 through 2007, respectively. The fair value of non-current accounts receivable is estimated by discounting the future cash flows using the current rate at which the Company would finance a similar transaction. At March 31, 2002, the fair value of such receivables is approximately \$304.0 million, compared to \$349.2 million at March 31, 2001. Each 25 basis point increase in interest rates would have an associated \$1.1 million negative impact on the fair value of non-current accounts receivable based on the balance of such receivables at March 31, 2002 compared to a \$1.4 million negative impact at March 31, 2001. A change in interest rates will have no impact on cash flows or net income associated with non-current accounts receivable.

#### Foreign Currency Risk

We have entered into forward foreign exchange contracts primarily to hedge amounts due to or from select subsidiaries

denominated in foreign currencies (mainly in Europe and Asia/Pacific) against fluctuations in exchange rates. Our accounting policies for these contracts are based on our designation of the contracts as hedging transactions. The criteria we use for designating a contract as a hedge include the contract's effectiveness in risk reduction and one-to-one matching of derivative instruments to underlying transactions. Gains and losses on forward foreign exchange contracts are recognized in income in the same period as gains and losses on the underlying transactions. If the underlying hedged transaction is terminated earlier than initially anticipated, the offsetting gain or loss on the related forward foreign exchange contract would be recognized in income in the same period. In addition, since we enter into forward contracts only as a hedge, any change in currency rates would not result in any material net gain or loss, as any gain or loss on the underlying foreign currency denominated balance would be offset by the gain or loss on the forward contract. We operate in certain countries in Latin America and Asia/Pacific where there are limited forward currency exchange markets and thus we have unhedged transaction exposures in these currencies.

The table below provides information about our foreign exchange forward contracts at March 31, 2002. The table presents the value of the contracts in U.S. dollars at the contract maturity date and the fair value of the contracts at March 31, 2002 (in thousands, except contract rates):

	CONTRACT DATE IN 2002	MATURITY DATE IN 2002	CONTRACT RATE	FORWARD POSITION IN U.S. DOLLARS	FAIR VALUE AT MARCH 31, 2002
Forward Sales					
Australian Dollar	March 29	April 30	1.89054	\$ 423	\$ 427
Canadian Dollar	March 29	April 30	1.5962	188	188
Japanese Yen	March 29	April 30	133.028	3,308	3,314
Norwegian Krone	March 29	April 30	8.8873	720	723
Singapore Dollar	March 29	April 30	1.84177	3,149	3,149
Swedish Krona	March 29	April 30	10.3917	77	77
Swiss Franc	March 29	April 30	1.6841	2,138	2,140
British Pound	March 29	April 30	.70488	2,412	2,424
				12,415	12,442
Forward Purchases					
Euro Dollar	March 29	April 30	1.14991	6,896	6,912

Approximately 24% of our revenue is derived from foreign sources. This exposes us to exchange rate risks on foreign currencies related to the fair value of foreign assets and liabilities, net income and cash flows.



## INDEPENDENT AUDITORS' REPORT

To the Shareholders and Board of Directors of Compuware Corporation:

We have audited the accompanying consolidated balance sheets of Compuware Corporation and subsidiaries as of March 31, 2002 and 2001, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three years in the period ended March 31, 2002. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Compuware Corporation and its subsidiaries as of March 31, 2002 and 2001, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 2002 in conformity with accounting principles generally accepted in the United States of America.

*Deloitte + Touche LLP*

Detroit, Michigan  
May 6, 2002



COMPUWARE CORPORATION AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

AS OF MARCH 31, 2002 AND 2001

(In Thousands, Except Share Data)

ASSETS	NOTES	2002	2001
<b>CURRENT ASSETS:</b>			
Cash and cash equivalents		\$ 233,305	\$ 53,340
Investments	3	133,503	185,176
Accounts receivable, less allowance for doubtful accounts of \$23,190 and \$21,267		609,579	705,546
Deferred tax asset, net	10	41,811	32,011
Income taxes refundable, net		27,687	10,028
Prepaid expenses and other current assets		16,954	17,635
<b>Total current assets</b>		<b>1,062,839</b>	<b>1,003,736</b>
<b>INVESTMENTS</b>	3	<b>55,566</b>	<b>16,488</b>
<b>PROPERTY AND EQUIPMENT, LESS ACCUMULATED DEPRECIATION AND AMORTIZATION</b>	4	<b>199,365</b>	<b>125,800</b>
<b>CAPITALIZED SOFTWARE, LESS ACCUMULATED AMORTIZATION OF \$169,611 AND \$137,530</b>		<b>68,998</b>	<b>87,781</b>
<b>OTHER:</b>			
Accounts receivable		306,751	356,431
Goodwill, less accumulated amortization and impairment	2,6	211,792	631,609
Deferred tax asset, net	10	44,884	
Other assets	5	43,743	57,529
<b>Total other assets</b>		<b>607,170</b>	<b>1,045,569</b>
<b>TOTAL ASSETS</b>		<b>\$ 1,993,938</b>	<b>\$ 2,279,374</b>

See notes to consolidated financial statements.



LIABILITIES AND SHAREHOLDERS' EQUITY	NOTES	2002	2001
<b>CURRENT LIABILITIES:</b>			
Accounts payable		\$ 28,646	\$ 39,846
Accrued expenses	6	141,825	127,854
Accrued bonuses and commissions		44,652	50,093
Deferred revenue		341,024	351,041
<b>Total current liabilities</b>		<b>556,147</b>	<b>568,834</b>
<b>LONG TERM DEBT</b>	7		140,000
<b>DEFERRED REVENUE</b>		<b>218,624</b>	172,367
<b>ACCRUED EXPENSES</b>	6	<b>29,316</b>	
<b>DEFERRED TAX LIABILITY, NET</b>	10		20,801
<b>Total liabilities</b>		<b>804,087</b>	<b>902,002</b>
<b>SHAREHOLDERS' EQUITY:</b>			
Preferred stock, no par value - authorized 5,000,000 shares	8		
Common stock, \$.01 par value - authorized 1,600,000,000 shares; issued and outstanding 375,820,254 and 369,816,432 shares in 2002 and 2001, respectively	8,13	3,758	3,698
Additional paid-in capital		676,617	620,743
Retained earnings		528,804	774,059
Accumulated other comprehensive loss		(19,328)	(21,128)
<b>Total shareholders' equity</b>		<b>1,189,851</b>	<b>1,377,372</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b>\$ 1,993,938</b>	<b>\$ 2,279,374</b>



COMPUWARE CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF OPERATIONS

YEARS ENDED MARCH 31, 2002, 2001 and 2000

(In Thousands, Except Per Share Data)

	NOTES	2002	2001	2000
<b>REVENUES:</b>				
Software license fees		\$ 417,631	\$ 495,572	\$ 819,247
Maintenance fees		433,751	456,534	432,707
Professional services fees		877,165	1,057,944	978,674
<b>Total revenues</b>		<b>1,728,547</b>	<b>2,010,050</b>	<b>2,230,628</b>
<b>OPERATING EXPENSES:</b>				
Cost of software license fees		36,255	39,551	30,739
Cost of maintenance		39,662	53,076	45,367
Cost of professional services		879,953	1,039,237	946,710
Software product development		102,332	102,617	81,133
Sales and marketing		396,324	451,719	467,060
Administrative and general	5	73,670	89,126	64,800
Goodwill amortization and impairment	6	426,344	42,092	25,586
Restructuring costs	6	46,930		
Purchased research and development	2			17,900
<b>Total operating expenses</b>		<b>2,001,470</b>	<b>1,817,418</b>	<b>1,679,295</b>
<b>INCOME (LOSS) FROM OPERATIONS</b>		<b>(272,923)</b>	<b>192,632</b>	<b>551,333</b>
<b>OTHER INCOME (EXPENSE):</b>				
Interest and investment income	3	29,504	30,692	34,927
Interest expense		(7,428)	(31,255)	(24,484)
<b>Total other income (expense)</b>		<b>22,076</b>	<b>(563)</b>	<b>10,443</b>
<b>INCOME (LOSS) BEFORE INCOME TAXES</b>		<b>(250,847)</b>	<b>192,069</b>	<b>561,776</b>
<b>INCOME TAX PROVISION (BENEFIT)</b>	10	<b>(5,592)</b>	<b>72,986</b>	<b>209,800</b>
<b>NET INCOME (LOSS)</b>		<b>\$ (245,255)</b>	<b>\$ 119,083</b>	<b>\$ 351,976</b>
Basic earnings (loss) per share	9	\$ (0.66)	\$ 0.33	\$ 0.98
Diluted earnings (loss) per share	9	\$ (0.66)	\$ 0.32	\$ 0.91

See notes to consolidated financial statements.



COMPUWARE CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED MARCH 31, 2002, 2001 and 2000

(In Thousands)

	2002	2001	2000
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net income (loss)	\$ (245,255)	\$ 119,083	\$ 351,976
Adjustments to reconcile net income (loss) to cash provided by operations:			
Purchased research and development			17,900
Goodwill and acquired technology impairment	391,747		
Depreciation and amortization	98,216	103,663	71,510
Tax benefit from exercise of stock options	8,384	10,283	45,962
Issuance of common stock to Employee Stock Ownership Trust	10,657	10,685	6,496
Acquisition tax benefits	6,854	7,454	7,219
Deferred income taxes	(75,485)	105	(5,758)
Gain on sale of marketable securities			(10,918)
Other	3,589	(4,080)	994
Net change in assets and liabilities, net of effects from acquisitions:			
Accounts receivable	145,647	67,799	(385,102)
Prepaid expenses and other current assets	681	8,298	2,962
Other assets	2,595	13,199	(27,716)
Accounts payable and accrued expenses	20,578	(51,012)	(19,222)
Deferred revenue	36,240	39,034	137,954
Income taxes	(17,659)	12,084	(28,858)
<b>Net cash provided by operating activities</b>	<b>386,789</b>	<b>336,595</b>	<b>165,399</b>
<b>CASH USED IN INVESTING ACTIVITIES:</b>			
Purchase of:			
Businesses		(17,576)	(700,266)
Property and equipment:			
Headquarters building	(81,644)	(25,166)	
Other	(8,784)	(14,637)	(34,922)
Capitalized software	(13,300)	(13,881)	(15,698)
Investments:			
Proceeds from maturity	221,716	175,787	339,797
Proceeds from sales of securities			14,194
Purchases	(210,784)	(144,515)	(98,419)
<b>Net cash used in investing activities</b>	<b>(92,796)</b>	<b>(39,988)</b>	<b>(495,314)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Proceeds from long term debt		18,000	533,000
Payment of long term debt	(140,000)	(328,000)	(83,000)
Net proceeds from sale of common stock	6,999	29,673	31,681
Repurchase of common stock			(348,373)
Proceeds from sale of warrant	2,825		
Net proceeds from exercise of stock options	16,148	6,580	33,959
<b>Net cash (used in) provided by financing activities</b>	<b>(114,028)</b>	<b>(273,747)</b>	<b>167,267</b>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>179,965</b>	<b>22,860</b>	<b>(162,648)</b>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	<b>53,340</b>	<b>30,480</b>	<b>193,128</b>
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<b>\$ 233,305</b>	<b>\$ 53,340</b>	<b>\$ 30,480</b>

See notes to consolidated financial statements.



COMPUWARE CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

YEARS ENDED MARCH 31, 2002, 2001 and 2000

(In Thousands, Except Share Data)

	COMMON STOCK		ADDITIONAL PAID-IN CAPITAL
	SHARES	AMOUNT	
<b>BALANCE AT APRIL 1, 1999</b>	367,926,388	\$ 3,679	\$ 304,825
Net income			
Foreign currency translation, net of tax			
Comprehensive income			
Issuance of common stock	1,325,761	13	33,764
Purchase and retirement of common stock	(15,335,259)	(153)	126,098
Acquisition tax benefits			7,219
Exercise of employee stock options and related tax benefit (Note 13)	7,704,344	77	79,844
Other			4,400
<b>BALANCE AT MARCH 31, 2000</b>	361,621,234	3,616	556,150
Net income			
Foreign currency translation, net of tax			
Comprehensive income			
Issuance of common stock	5,735,834	57	40,301
Acquisition tax benefits			7,454
Exercise of employee stock options and related tax benefit (Note 13)	2,459,364	25	16,838
<b>BALANCE AT MARCH 31, 2001</b>	369,816,432	3,698	620,743
<b>Net loss</b>			
<b>Foreign currency translation, net of tax</b>			
<b>Comprehensive loss</b>			
<b>Issuance of common stock</b>	<b>1,981,659</b>	<b>20</b>	<b>17,636</b>
<b>Issuance of warrant (Note 8)</b>			<b>2,825</b>
<b>Acquisition tax benefits</b>			<b>6,854</b>
<b>Exercise of employee stock options and related tax benefit (Note 13)</b>	<b>4,022,163</b>	<b>40</b>	<b>24,492</b>
<b>Other</b>			<b>4,067</b>
<b>BALANCE AT MARCH 31, 2002</b>	<b>375,820,254</b>	<b>\$ 3,758</b>	<b>\$ 676,617</b>

See notes to consolidated financial statements.



RETAINED EARNINGS	ACCUMULATED OTHER COMPREHENSIVE GAIN (LOSS)	TOTAL SHAREHOLDERS' EQUITY	COMPREHENSIVE INCOME (LOSS)
\$ 777,318	\$ (6,300)	\$ 1,079,522	
351,976		351,976	\$ 351,976
	(4,570)	(4,570)	(4,570)
			<u>\$ 347,406</u>
		33,777	
(474,318)		(348,373)	
		7,219	
		79,921	
		4,400	
654,976	(10,870)	1,203,872	
119,083		119,083	\$ 119,083
	(10,258)	(10,258)	(10,258)
			<u>\$ 108,825</u>
		40,358	
		7,454	
		16,863	
774,059	(21,128)	1,377,372	
(245,255)		(245,255)	\$ (245,255)
	1,800	1,800	1,800
			<u>\$ (243,455)</u>
		17,656	
		2,825	
		6,854	
		24,532	
		4,067	
<u>\$ 528,804</u>	<u>\$ (19,328)</u>	<u>\$ 1,189,851</u>	



# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED MARCH 31, 2002, 2001 and 2000

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Business** - Compuware Corporation develops, markets and supports an integrated set of systems software products designed to improve the productivity of data processing professionals in application development, implementation and maintenance. In addition, the Company's professional services include business systems analysis, design, programming and implementation as well as software conversion and systems planning and consulting. The Company's products and services are offered worldwide across a broad spectrum of technologies, including mainframe and distributed systems platforms.

**Basis of Presentation** - The consolidated financial statements include the accounts of Compuware Corporation and its wholly owned subsidiaries after elimination of all significant intercompany balances and transactions. The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America, which require management to make estimates and assumptions that affect the reported amounts of assets, liabilities and the disclosure of contingencies at March 31, 2002 and 2001 and the results of operations for the years ended March 31, 2002, 2001 and 2000. While management has based their assumptions and estimates on the facts and circumstances known at March 31, 2002, final amounts may differ from estimates.

Certain amounts in the fiscal 2001 and 2000 financial statements have been reclassified to conform to the fiscal 2002 presentation.

**Revenue Recognition** - The Company earns revenue from licensing software products, providing maintenance and support for those products and rendering professional services.

**Software license fees** - The Company's software license agreements typically provide for perpetual licenses with maintenance included for terms ranging generally from one to five years. License fee revenue is recognized using the residual method, under which the fair value, based on Compuware-specific objective evidence, of all undelivered elements of the agreement (e.g., maintenance) is deferred. The remaining portion of the fee (the residual) is recognized as license fee revenue upon shipment of the products, provided that no significant obligations remain and collection of the related

receivable is deemed probable. For agreements in which the fair value of the undelivered elements cannot be determined using Compuware-specific objective evidence (e.g., transactions that include an option to exchange or select products in the future), the Company recognizes the license fee revenue on a ratable basis over the term of the license agreement.

The Company offers flexibility to customers purchasing their products and related maintenance. Terms vary, ranging from the standard perpetual license sale, including one year of maintenance, to large multiyear, multiproduct contracts. For fiscal years 2002, 2001 and 2000, multiyear contracts greater than \$5 million represented approximately 6.9%, 12.8% and 26.5%, respectively, of license fee revenue. The Company allows deferred payment terms on multiyear contracts, with installments collectible over the term of the contract. For these contracts, the license fee portion of the receivable is discounted to its net present value. The discount is recognized as interest income over the term of the receivables, and amounted to \$19,562,000, \$18,219,000 and \$9,312,000 for fiscal 2002, 2001 and 2000, respectively. At March 31, 2002, current accounts receivable includes installments on multiyear contracts totaling \$292,105,000 due within the year ending March 31, 2003. Non-current accounts receivable at March 31, 2002 amounted to \$306,751,000, and are due approximately \$190,182,000, \$85,836,000, \$23,619,000 and \$7,114,000 in each of the years ending March 31, 2004 through 2007, respectively.

**Maintenance fees** - The Company's maintenance agreements provide for technical support and advice, including problem resolution services and assistance in product installation, error corrections and any product enhancements released during the maintenance period. Maintenance is included with all mainframe software license agreements for at least one year, and for most distributed product agreements for three months. Maintenance is renewable thereafter for an annual fee. Maintenance fees are deferred and recognized as revenue on a ratable basis over the maintenance period.

**Deferred revenue** - Deferred revenue consists primarily of maintenance fees related to the remaining term of maintenance agreements in effect at those dates. Deferred license fees are also included in deferred revenue for those contracts that are being recognized on a ratable basis.

*Professional services fees* – Revenues from professional services are recognized in the period the services are performed, provided that collection of the related receivable is deemed probable. Professional services fees are generally based on hourly or daily rates; however, for services rendered under fixed-price contracts, revenue is recognized using the percentage of completion method.

**Cash and Cash Equivalents** - For the purpose of the statement of cash flows, the Company considers all investments with an original maturity of three months or less to be cash equivalents.

**Investments** consist of municipal obligations, tax-free zero coupon bonds, U.S. Treasury notes, tax-free and tax advantage auction rate securities. All are classified as held-to-maturity and carried at amortized cost. Those investments that mature within one year from the balance sheet date are classified as current assets. The amortization of bond premiums and discounts is included in interest and investment income.

**Property and Equipment** are stated at cost. Depreciation is provided using the straight-line method over the estimated useful lives of the related assets, which are generally estimated to be 39 years for buildings and three to ten years for furniture and fixtures, computer equipment and software. Leasehold improvements are amortized over the term of the lease, or the estimated life of the improvement, whichever is less. Depreciation and amortization of property and equipment totaled \$26,993,000, \$28,031,000 and \$23,069,000 for the years ended March 31, 2002, 2001 and 2000, respectively.

**Capitalized Software** includes the costs of purchased and internally developed software products and is stated at the lower of unamortized cost or net realizable value. Net purchased software included in capitalized software at March 31, 2002 and 2001 is \$29,723,000 and \$48,353,000, respectively. Capitalization of internally developed software products begins when technological feasibility of the product is established. Software product development includes all expenditures for research and development, net of amounts capitalized. Total software development costs incurred internally by the Company were \$115,626,000, \$116,147,000 and \$95,629,000 in fiscal 2002, 2001 and 2000, respectively, of which \$13,292,000, \$13,530,000 and \$14,496,000, respectively, were capitalized.

The amortization for both internally developed and purchased software products is computed on a product-by-product basis.

The annual amortization is the greater of the amount computed using (a) the ratio that current gross revenues for a product bear to the total of current and anticipated future revenues for that product or (b) the straight-line method over the remaining estimated economic life of the product, including the period being reported on. Amortization begins when the product is available for general release to customers. The amortization period for capitalized software is generally five years. Capitalized software amortization amounted to \$32,081,000, \$28,126,000 and \$20,672,000 in fiscal 2002, 2001 and 2000, respectively. Included in the fiscal 2002 total is additional amortization of \$4,328,000 related to acquired technology that is no longer utilized in the Company's products.

**Goodwill** has been amortized over periods ranging from ten to twenty years using the straight-line method. Goodwill amortization expense was \$38,926,000, \$42,092,000 and \$25,586,000, for the years ended March 31, 2002, 2001 and 2000, respectively. The Company regularly evaluates the remaining goodwill to determine whether later events and circumstances warrant revised estimates of useful lives or impairment charges. To evaluate the carrying value of these assets, the Company utilizes a discounted cash flow approach. This analysis requires judgement regarding discount rates, revenue growth and other variables that impact the net realizable value or fair value of those assets, as applicable. Actual future cash flows and other assumed variables could differ from estimates. During fiscal 2002, the Company recorded an aggregate charge of \$387,418,000 to recognize impairment of goodwill resulting from the restructuring announced on March 31, 2002 (\$342,922,000), the transfer of the professional services engineering division to an unrelated third party in December 2001 (\$9,298,000) and a change in technology related to its distributed products (\$35,198,000).

Effective April 1, 2002, the Company adopted SFAS No. 142, "Goodwill and Other Intangible Assets." Under this pronouncement, goodwill and those intangible assets with indefinite lives will no longer be amortized, but rather will be tested for impairment annually and/or when events or circumstances indicate that their fair value has been reduced below carrying value. The Company has evaluated its remaining goodwill as of April 1, 2002, and has determined there will be no impairment upon adoption of SFAS No. 142.



**Fair Value of Financial Instruments** - The carrying value of cash equivalents, current accounts receivable and accounts payable approximated fair values due to the short-term maturities of these instruments. At March 31, 2002, the fair value of non-current receivables was approximately \$304,043,000 compared to the carrying amount of \$306,751,000. At March 31, 2001, the fair value of non-current receivables was approximately \$349,216,000 compared to the carrying amount of \$356,431,000. Fair value is estimated by discounting the future cash flows using the current rate at which the Company would finance a similar transaction.

**Income Taxes** - The Company accounts for income taxes using the asset and liability approach. Deferred income taxes are provided for the differences between the tax bases of assets or liabilities and their reported amounts in the financial statements.

**Foreign Currency Translation** - The Company's foreign subsidiaries use their respective local currency as their functional currency. Accordingly, assets and liabilities in the consolidated balance sheets have been translated at the rate of exchange at the respective balance sheet dates, and revenues and expenses have been translated at average exchange rates prevailing during the year the transactions occurred. Translation adjustments have been excluded from the results of operations and are reported as accumulated other comprehensive loss.

**Foreign Currency Transactions and Derivatives** - Gains and losses from foreign currency transactions are included in the determination of net income. To offset the risk of future currency fluctuations on balances due to or from foreign subsidiaries, the Company enters into foreign exchange contracts to sell or buy currencies at specified rates on specific dates. Market value gains and losses on these contracts are recognized, offsetting foreign exchange gains or losses on foreign receivables. The Company does not use foreign exchange contracts to hedge anticipated transactions. The net foreign currency transaction loss was \$1,321,000, \$2,487,000 and \$464,000 for the years ended March 31, 2002, 2001 and 2000, respectively. These amounts are included in "sales and marketing" in the consolidated statements of operations.

At March 31, 2002, the Company had contracts maturing through April 2002 to sell \$12,415,000 and purchase \$6,896,000 in foreign currencies. At March 31, 2001, the Company had contracts maturing through April 2001 to sell \$43,115,000 in foreign currencies.

**Earnings Per Share** - Basic EPS is computed by dividing earnings available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS assumes the issuance of common stock for all potentially dilutive equivalent shares outstanding.

**Business Segments** - The Company's two principal operating segments are products and services. The Company provides software products and professional services to the world's largest IT organizations that help information technology professionals efficiently develop, implement and support the applications that run their businesses.

**Recently Issued Accounting Pronouncements** - Statement of Financial Accounting Standards (SFAS) No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," supercedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of" and is effective for all fiscal years beginning after December 15, 2001. This statement retains the impairment loss recognition and measurement requirements of SFAS No. 121. In addition, it requires that one accounting model be used for long-lived assets to be disposed of by sale, and broadens the presentation of discontinued operations to include more disposal transactions. The Company adopted this statement on April 1, 2002; however, it is not expected to have any impact on its financial position or results of operations.

## 2. ACQUISITIONS

### Fiscal 2001 Acquisitions:

During fiscal 2001, the Company completed the acquisitions of Optimal Networks Corporation, a developer of e-business performance measurement tools, for \$5,000,000 in cash and assumed liabilities and Nomex, Inc., a privately-held provider of web design and development services located in Montreal, Canada, for approximately \$8,900,000 in cash. These acquisitions have been accounted for as purchases, and, accordingly, assets and liabilities acquired have been recorded at fair value as of their respective acquisition dates. The aggregate amount by which the acquisition cost exceeded the fair value of the net assets acquired was approximately \$10,500,000.

### Fiscal 2000 Acquisitions:

During fiscal 2000, the Company completed the acquisition of certain professional services companies for a combined total of \$522,500,000, the largest of which was Data Processing Resources Corporation for \$499,500,000. The Company also completed four product-related acquisitions during the year for a combined total of \$180,850,000, the largest of which was Programart Corporation for \$126,100,000. All of the acquisitions were accounted for as purchases and, accordingly, assets and liabilities acquired have been recorded at fair value as of their respective acquisition dates. Of the total purchase price, \$56,500,000 was capitalized as purchased software, \$11,200,000 was allocated to other intangible assets and \$17,900,000 was allocated to in-process research and development and expensed as of the purchase date. The aggregate amount by which the

acquisition cost exceeded the fair value of the net assets acquired was approximately \$600,200,000.

The pro forma unaudited consolidated results of operations, assuming the fiscal 2000 acquisitions had occurred as of the beginning of fiscal 2000, would include revenues of \$2,394,000,000, net income of \$342,000,000 and diluted earnings per share of \$0.89. The pro forma results include the amortization of the goodwill and interest expense on debt assumed to finance these purchases. These amounts do not reflect any benefit from the reduction in costs for certain corporate functions from combined operations. The pro forma results are not necessarily indicative of what actually would have occurred if the acquisitions had been completed as of the beginning of fiscal 2000, nor are they necessarily indicative of future consolidated results.

### 3. INVESTMENTS

A summary of securities classified as held to maturity at March 31, 2002 and 2001 is set forth below (in thousands):

	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	FAIR VALUE
<b>MARCH 31, 2002:</b>				
Municipal Obligations	\$ 94,987	\$ 286	\$ 207	\$ 95,066
Tax Advantage Auction				
Rate Securities	13,200			13,200
Tax Free Auction				
Rate Securities	71,176		1	71,175
US Treasury Notes	4,956		17	4,939
Zero Coupon Bonds	4,750		20	4,730
Securities classified as held to maturity	<u>\$ 189,069</u>	<u>\$ 286</u>	<u>\$ 245</u>	<u>\$ 189,110</u>
<b>MARCH 31, 2001:</b>				
Municipal Obligations	\$ 160,899	\$ 831	\$ 8	\$ 161,722
Tax Advantage Auction				
Rate Securities	16,000			16,000
Tax Free Auction				
Rate Securities	23,602		2	23,600
Zero Coupon Bonds	1,163	12		1,175
Securities classified as held to maturity	<u>\$ 201,664</u>	<u>\$ 843</u>	<u>\$ 10</u>	<u>\$ 202,497</u>



Scheduled maturities of securities classified as held to maturity at March 31, 2002 were as follows (in thousands):

	AMORTIZED COST	FAIR VALUE
Due in:		
2003	\$ 133,503	\$ 133,645
2004	51,057	51,014
2005	4,509	4,451
Total	\$ 189,069	\$ 189,110

**Marketable Securities** - During fiscal 2000, the Company sold securities that had been classified as available-for-sale for approximately \$14.2 million and realized a gain of approximately \$10.9 million. There were no such transactions during fiscal 2001 or 2002. The Company uses the specific identification method as a basis for determining cost and calculating realized gains.

#### 4. PROPERTY AND EQUIPMENT

Property and equipment, summarized by major classification, is as follows (in thousands):

	MARCH 31,	
	2002	2001
Land	\$ 1,776	\$ 1,776
Construction in progress	117,160	25,166
Buildings	28,788	28,780
Leasehold improvements	26,099	24,226
Furniture and fixtures	52,621	52,780
Computer equipment and software	86,438	101,105
	312,882	233,833
Less accumulated depreciation and amortization	113,517	108,033
Total	\$ 199,365	\$ 125,800

On October 23, 2000, the Company entered into a Restated Development Agreement with the city of Detroit and the City of Detroit Downtown Development Authority to construct an office building with retail and related amenities for a current estimated cost of \$350 million. All amounts included in construction in progress relate to this building.

#### 5. INVESTMENTS IN PARTIALLY OWNED COMPANIES

At March 31, 2002, the Company held a 33.3% interest in CareTech Solutions, Inc. (CareTech) and a 49% interest in Foresee Results, Inc. (Foresee). For the years ended March 31, 2001 and 2000, the Company held investments in two other companies in similar lines of business. These two companies were closed in fiscal 2001. The investments in these companies are accounted for under the equity method. The Company records its share of income or loss against its net investment in the company. The net investment balance is included in other

assets. At March 31, 2002, the net investment balance in partially owned companies was \$1,280,000. At March 31, 2001, the net amount was a credit of \$1,232,000. For the years ended March 31, 2002, 2001 and 2000, the Company recognized a net loss of \$819,000, \$21,693,000 and \$764,000, respectively, from these investments, which is included in general and administrative expenses.

At March 31, 2002, CareTech owes the Company \$18,800,000 resulting from the transfer of a contract to provide professional services to a large hospital complex from the Company to CareTech. The note, which equaled the Company's investment

in the contract, is included in other assets and is payable over ten years, the term of the transferred contract. Interest is payable quarterly at 5.25%. Prior to this transfer, CareTech was providing services under this agreement as a sub-contractor to the Company. As of January 1, 2002, CareTech bills these services directly to the hospital.

Foresee was incorporated in October 2001. The Company has pledged \$4,000,000 in equity funding and \$6,000,000 in additional loans, provided that Foresee meets certain milestones in their development process. As of March 31, 2002, \$3,000,000 was paid against the equity pledge, with the balance of \$1,000,000 paid in April 2002.

## 6. RESTRUCTURING AND IMPAIRMENT CHARGES

In the fourth quarter of fiscal 2002, the Company adopted a restructuring plan which will reorganize its operating divisions, primarily the professional services segment. The plan resulted in total charges of \$389,852,000, including \$342,922,000 for the impairment of goodwill recognized in the acquisition of certain professional services businesses, principally Data Processing Resources Corporation. These changes are designed to increase

profitability in the future by better aligning cost structures with current market conditions.

The restructuring plan includes a reduction of professional services staff at certain locations, the closing of entire professional services offices and a reduction of sales support personnel, lab technicians and related administrative and financial staff. Approximately 1,600 employees will be terminated as a result of the reorganization. Prior to year end, the Company communicated benefits available to employees under the plan. A majority of affected employees are expected to be terminated during the first quarter of fiscal 2003. As of March 31, 2002, 74 employees have been terminated.

In conjunction with the development of the restructuring plan, the Company evaluated the carrying value of goodwill and other intangible assets related to the professional services business, and recorded an impairment charge related to the Company's prior services acquisitions. Certain professional services offices acquired as part of those acquisitions have not achieved critical mass or a sustained level of profitability and were closed in April 2002 as part of the restructuring plan. The Company utilized discounted cash flow analyses to value the remaining business, and recognized goodwill impairment based upon current estimated fair market values.

The following table summarizes the restructuring and impairment charges taken in fiscal 2002 (in thousands):

	TOTAL CHARGES	COMPLETED AS OF MARCH 31, 2002	REMAINING ACCRUAL AT MARCH 31, 2002
Employee termination benefits	\$ 19,012	\$ 553	\$ 18,459
Facilities costs (primarily lease abandonments)	26,341	676	25,665
Legal, consulting and outplacement costs	1,299		1,299
Other	278		278
Restructuring charge	46,930	1,229	45,701
Goodwill impairment charge	342,922	342,922	-
Total charges	\$ 389,852	\$ 344,151	\$ 45,701



## 7. LONG TERM DEBT

**Senior Credit Facility** - In August 1999, the Company entered into a \$900 million unsecured Senior Credit Facility (credit facility) maturing in August 2003. Interest may be determined on a Eurodollar or base rate (as defined in the credit facility) basis at the Company's option. The Company currently pays a commitment fee of .3% per annum for any unused portion of the credit facility. During fiscal 2002, the maximum borrowings under the credit facility were \$140 million; average borrowings were \$16.7 million at a weighted average interest rate of 7.97%. At March 31, 2002, there was no amount outstanding under this facility.

The total commitment under the credit facility was permanently reduced to \$500 million on February 13, 2002.

The terms of the credit facility contain, among other provisions, certain financial covenants including minimum interest coverage and minimum net worth requirements, and specific limitations on additional indebtedness, liens and merger activity.

Cash paid for interest totaled approximately \$3,622,000, \$28,627,000 and \$21,861,000 for the years ended March 31, 2002, 2001 and 2000, respectively.

## 8. CAPITAL STOCK

**Preferred Stock Purchase Rights** - Under the Company's shareholder rights plan, each shareholder receives one right to purchase one two-thousandth of a share of Series A Junior Participating Preferred Stock (a right) for each share of common stock owned by the shareholder. Holders of the rights are entitled to purchase for \$40.00 one two-thousandth of one share of the Company's Series A Junior Participating Preferred Stock in certain limited circumstances involving acquisitions of, or offers for, 15 percent or more of the Company's common stock. After any such acquisition is completed, each right entitles its holder to purchase for \$40.00 an amount of common stock of the Company, or in certain circumstances securities of the acquirer, having a then current market value of two times the exercise price of the right. In connection with the shareholder rights plan, the Company has designated 800,000 shares of its 5,000,000 shares of authorized but unissued Preferred Stock as "Series A Junior Participating Preferred Stock." Each one two-thousandth of each share of Series A Junior Participating Preferred Stock will generally be afforded economic rights similar to one share of the Company's common stock. The rights are redeemable for a specified period at a price of \$0.001 per right and expire on November 9, 2010 unless extended or earlier redeemed by the Board of Directors.

**Common Stock Warrant** - In November 2001, the Company issued a non-transferrable warrant entitling a customer to purchase one million shares of common stock at \$10.51 per share in exchange for approximately \$2,800,000 in cash, which was the warrant's fair value at the date of issue. The warrant expires on November 16, 2004 or on the fifth day after the Company's common stock trades at an average price of \$20.00 per share for five consecutive days.



## 9. EARNINGS (LOSS) PER COMMON SHARE

Earnings (loss) per common share data were computed as follows (in thousands, except for per share data):

	YEAR ENDED MARCH 31,		
	2002	2001	2000
<b>Basic earnings (loss) per share:</b>			
Numerator: Net income (loss)	\$ (245,255)	\$ 119,083	\$ 351,976
Denominator:			
Weighted-average common shares outstanding	371,786	365,192	358,560
Basic earnings (loss) per share	\$ (0.66)	\$ 0.33	\$ 0.98
<b>Diluted earnings (loss) per share:</b>			
Numerator: Net income (loss)	\$ (245,255)	\$ 119,083	\$ 351,976
Denominator:			
Weighted-average common shares outstanding	371,786	365,192	358,560
Dilutive effect of stock options and warrants	-	7,617	26,131
Total shares	371,786	372,809	384,691
Diluted earnings (loss) per share	\$ (0.66)	\$ 0.32	\$ 0.91



## 10. INCOME TAXES

Temporary differences and carryforwards which give rise to a significant portion of deferred tax assets and liabilities are as follows (in thousands):

	MARCH 31,	
	2002	2001
Deferred tax assets:		
Deferred maintenance	\$ 11,915	\$ 374
Amortization of intangible assets	69,774	17,388
Restructuring accrual	15,702	
Allowance for doubtful accounts	5,307	5,743
Net operating loss carryforwards	24,201	29,670
Other	34,399	35,874
	161,298	89,049
Less valuation allowance	1,686	5,551
Net deferred tax assets	159,612	83,498
Current portion	41,995	32,358
Long term portion	\$ 117,617	\$ 51,140
Deferred tax liabilities:		
Capitalized research and development costs	\$ 13,746	\$ 13,800
Depreciation	10,892	5,059
Other	48,279	53,429
Total deferred tax liabilities	72,917	72,288
Current portion	184	347
Long term portion	\$ 72,733	\$ 71,941

The income tax provision (benefit) includes the following (in thousands):

	YEAR ENDED MARCH 31,		
	2002	2001	2000
Current:			
Federal	\$ 56,794	\$ 50,711	\$ 181,664
Foreign	8,673	16,370	9,268
State	4,426	5,800	24,626
Total current tax provision	69,893	72,881	215,558
Deferred:			
Federal	(71,435)	(3,297)	(1,638)
Foreign	1,081	3,402	(4,120)
State	(5,131)		
Total deferred tax expense (benefit)	(75,485)	105	(5,758)
Total income tax provision (benefit)	\$ (5,592)	\$ 72,986	\$ 209,800

The Company's income tax expense (benefit) differed from the amount computed on pre-tax income (loss) at the U.S. federal income tax rate of 35% for the following reasons (in thousands):

	YEAR ENDED MARCH 31,		
	2002	2001	2000
Federal income tax (benefit) at statutory rates	\$ (87,796)	\$ 67,224	\$ 196,622
Increase (decrease) in taxes:			
Export sales benefit	(4,290)	(8,024)	(9,537)
State income taxes, net	(458)	3,770	16,007
Goodwill amortization and impairment	88,600	8,831	5,291
Other, net	(1,648)	1,185	1,417
Provision (benefit) for income taxes	\$ (5,592)	\$ 72,986	\$ 209,800

At March 31, 2002 the Company has net operating loss carryforwards for income tax purposes of approximately \$84,196,000 which expire as follows (in thousands):

Year ending March 31:	
2003	\$ 5,101
2004	3,979
2005	5,879
2006	6,046
2008	832
2009	18
2010	2,077
2011	3,835
2014	899
Unlimited carryforward	55,530

Of this amount, approximately \$2,229,000 is available to offset U.S. federal income taxes and approximately \$81,967,000 relates to various foreign jurisdictions.

Cash paid for income taxes totaled approximately \$65,935,000, \$41,538,000 and \$136,838,000 for the years ended March 31, 2002, 2001 and 2000, respectively.



## 11. SEGMENT INFORMATION

Compuware operates in two business segments in the software industry: products and services. The Company provides software products and professional services to the world's largest IT organizations that help IT professionals efficiently develop, implement and support the applications that run their businesses.

The Company's products are designed to support three key activities within the application development process: building, testing and managing the application to optimize performance in production. The Company also offers a broad range of data

processing professional services including business systems analysis, design and programming, software conversion and system planning and consulting.

No single customer provides more than 10% of the Company's revenue.

The Company evaluates the performance of its segments based primarily on operating profit (loss) before corporate expenses, and other income (expense) including restructuring charges, goodwill impairment, purchased research and development and net interest income (expense). The allocation of income taxes is not evaluated at the segment level. Financial information for the Company's business segments is as follows (in thousands):

	YEAR ENDED MARCH 31,		
	2002	2001	2000
Revenues:			
Products:			
Mainframe	\$ 687,286	\$ 762,778	\$ 1,031,273
Distributed systems	164,096	189,328	220,681
Total products revenue	851,382	952,106	1,251,954
Services	877,165	1,057,944	978,674
Total revenues	\$ 1,728,547	\$ 2,010,050	\$ 2,230,628
Income (loss) from operations:			
Products	\$ 276,809	\$ 305,143	\$ 627,655
Services	(2,788)	18,707	31,964
Corporate staff	(73,670)	(89,126)	(64,800)
Goodwill amortization	(38,926)	(42,092)	(25,586)
Income (loss) from operations before goodwill impairment and other charges	161,425	192,632	569,233
Goodwill impairment charge	(387,418)		
Restructuring charge	(46,930)		
Purchased research and development			(17,900)
Other income (expense)	22,076	(563)	10,443
Income (loss) before income taxes	\$ (250,847)	\$ 192,069	\$ 561,776

Financial information regarding geographic operations are presented in the table below (in thousands):

	YEAR ENDED MARCH 31,		
	2002	2001	2000
Revenues:			
United States	\$ 1,316,536	\$ 1,560,798	\$ 1,736,511
Europe	307,831	323,882	351,427
Other international operations	104,180	125,370	142,690
Total revenue	\$ 1,728,547	\$ 2,010,050	\$ 2,230,628

The Company does not evaluate assets and capital expenditures on a segment basis, and accordingly such information is not provided. Less than 10% of the Company's long-lived assets, other than financial instruments, are located outside of the United States.

## 12. COMMITMENTS AND CONTINGENCIES

**Leases** - The Company leases building and office space and computer, office and transportation equipment under various operating lease agreements extending through fiscal 2016. Certain of these leases contain provisions for renewal options and escalation clauses. The following is a schedule of future minimum rental payments for the next five years (in thousands):

YEAR ENDING MARCH 31:	TOTAL COMMITMENT	ACCRUED AS OF MARCH 31, 2002	REMAINING COMMITMENT
2003	\$ 38,948	\$ 7,330	\$ 31,618
2004	31,791	6,755	25,036
2005	23,295	5,133	18,162
2006	17,421	4,505	12,916
2007	15,030	4,519	10,511
Thereafter	21,904	10,507	11,397
Total	\$ 148,389	\$ 38,749	\$ 109,640

Accrued amounts at March 31, 2002 represent the remaining commitments on abandoned leases. Lease expense for the years ended March 31, 2002, 2001 and 2000 under all operating leases amounted to approximately \$54,960,000, \$39,652,000 and \$34,180,000, respectively.



### 13. BENEFIT PLANS

**Employee Stock Ownership Plan** - In July 1986, the Company established an Employee Stock Ownership Plan (ESOP) and Trust. Under the terms of the ESOP, the Company makes annual contributions to the Plan for the benefit of substantially all employees of the Company. The contribution may be in the form of cash or common shares of the Company. The Board of Directors may authorize contributions between a maximum of 25% of eligible compensation and a minimum sufficient to cover current obligations of the Plan. The Company made contributions of \$10,657,000, \$10,685,000 and \$6,496,000 in fiscal 2002, 2001 and 2000, respectively. This is a non-leveraged ESOP plan.

**Employee Stock Purchase Plan** - During fiscal 1996, the Company adopted and the shareholders approved the Global Employee Stock Purchase Plan (GESPP) under which the Company was authorized to issue up to eight million shares of common stock to eligible employees, all of which were distributed as of March 2001. During fiscal 2002, the shareholders approved international and domestic employee stock purchase plans authorizing 15 million shares for issuance to eligible employees. Currently, the offering periods commence on April 1 and October 1 each year. Under the terms of the plan, employees can elect to have up to 10% of their compensation withheld to purchase Company stock at the close of the offering period. The value of the stock purchased in any calendar year cannot exceed \$25,000. The purchase price is 85% of the first or last day's average high and low price for each offering period, whichever is lower. During fiscal 2002, 2001 and 2000, the Company sold approximately 1,007,000, 4,515,000 and 1,009,000 shares, respectively, to eligible employees under the plan.

**Employee Stock Option Plans** - The Company adopted five employee stock option plans dating back to 1991. These plans provide for grants of options to purchase up to 91,000,000 shares of the Company's common stock to employees and directors of the Company, of which approximately 39,613,000 options were outstanding at March 31, 2002. Under the terms of the plans, the Company may grant nonqualified options at the fair market value of the stock on the date of grant. During fiscal 2002, the Company granted approximately 4,375,000 options under the five different Employee Stock Option Plans. Options granted

under these plans vest in cumulative annual installments over a three to five year period. All options were granted at fair market value and expire ten years from the date of grant.

In March 2001, the Company adopted the 2001 Broad Based Stock Option Plan. The plan was approved by the Board of Directors, but was not submitted to the shareholders for approval. The plan provides for grants of options to purchase up to 50,000,000 shares of the Company's common stock to employees or directors of the Company. Under the terms of the plan, the Company may grant nonqualified stock options at the fair market value of the stock on the date of grant. During fiscal 2002, the Company granted approximately 26,997,000 options under the Broad Based Stock Option Plan. Approximately 24,667,000 options were outstanding at March 31, 2002. Options granted under the Broad Based Stock Option Plan vest every six months over a four year period. All options were granted at fair market value and expire ten years from the date of grant.

**Non-Employee Director Stock Option Plan** - In July 1992, the Company adopted the Stock Option Plan for Non-Employee Directors. Under this plan, 2,400,000 shares of common stock are reserved for issuance to non-employee directors of the Company who have not been employees of the Company, any subsidiary of the Company or any entity which controls more than 10% of the total combined voting power of the Company's capital stock for at least one year prior to becoming director. During fiscal 2002, approximately 8,600 options were granted under the Non-Employee Director Stock Option Plan. Approximately 1,491,000 options were outstanding at March 31, 2002.

Each non-employee director receives an annual grant of 20,000 options with additional grants for board and committee meeting attendance. In addition, each non-employee director may receive an additional grant of 10,000 or 20,000 options if pre-established earnings targets are achieved by the Company. Non-employee directors are granted stock options out of the Non-Employee Director Stock Option Plan or the Fiscal 1999 Stock Option Plan.

At March 31, 2002, approximately 93,000 options were outstanding under plans that were terminated by the Company, of which virtually all are fully vested. All outstanding options under the terminated plans remain in effect in accordance with the terms under which they were granted.

During fiscal 1999, the Company implemented a Replacement Stock Option Award program. The program allows selected participants to pay the option exercise price with shares of currently owned Company stock. The Company grants a new stock option award to replace the shares exchanged in the transaction. During fiscal 2002, approximately 1,072,000 options were exercised under the Replacement Stock Option Award program for which approximately 878,000 replacement options were granted.

The Company applies APB Opinion No. 25 and related Interpretations in accounting for its plans. Stock options are

granted at current market prices at the date of grant, therefore, no compensation cost has been recognized for its fixed stock option plans and its stock purchase plan.

If compensation cost for the Company's stock-based compensation plans had been determined based on the fair value at the grant dates for fiscal 2002, 2001 and 2000 consistent with the method prescribed by SFAS No. 123, "Accounting for Stock-Based Compensation," Compuware's net income (loss) and earnings (loss) per share would have been adjusted to the pro forma amounts indicated below:

	YEAR ENDED MARCH 31,		
	2002	2001	2000
Net income (loss):			
As reported	<b>\$(245,255)</b>	\$ 119,083	\$ 351,976
Pro forma	<b>(307,170)</b>	62,154	286,403
Earnings (loss) per share:			
As reported:			
Basic earnings (loss) per share	<b>(0.66)</b>	0.33	0.98
Diluted earnings (loss) per share	<b>(0.66)</b>	0.32	0.91
Pro forma:			
Basic earnings (loss) per share	<b>(0.83)</b>	0.17	0.80
Diluted earnings (loss) per share	<b>(0.83)</b>	0.17	0.74

The pro forma amounts for compensation cost may not be indicative of the effects on net income and earnings per share for future years.

Under SFAS No. 123, the fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions for grants in fiscal 2002, 2001 and 2000, respectively: expected volatility of 64.55%, 95.55% and 85.85%; risk-free interest rates of 4.7%, 4.6% and 6.4%; and expected lives at date of grant of 4.1, 5.0 and 4.8 years. Dividend yields were not a factor as the Company has not issued cash dividends since 1986, and has no plans to do so in the future.

Under SFAS No. 123, the fair value of the employees' stock purchase rights acquired by participation in the GESPP were estimated using the Black-Scholes model with assumptions comparable to the stock option plans above. The weighted-average fair value of the purchase rights granted in fiscal 2002, 2001 and 2000 were \$2.13, \$3.12 and \$12.00, respectively.



A summary of the status of fixed stock option grants under Compuware's stock-based compensation plans as of March 31, 2002, 2001 and 2000, and changes during the years ending on those dates is as follows (shares in thousands):

	2002		2001		2000	
	SHARES UNDER OPTION	WEIGHTED-AVG. EXERCISE PRICE	SHARES UNDER OPTION	WEIGHTED-AVG. EXERCISE PRICE	SHARES UNDER OPTION	WEIGHTED-AVG. EXERCISE PRICE
Outstanding at beginning of year	46,272	\$ 13.53	44,965	\$ 13.93	48,801	\$ 11.21
Granted	31,380	9.46	11,482	9.80	8,392	20.90
Exercised	(4,022)	5.02	(2,459)	5.52	(7,704)	4.77
Exchanged	(878)	12.07	(1,973)	11.43	(1,703)	22.58
Forfeited	(6,888)	12.62	(5,743)	15.45	(2,821)	17.20
Outstanding at year end	<u>65,864</u>	<u>\$ 12.30</u>	<u>46,272</u>	<u>\$ 13.53</u>	<u>44,965</u>	<u>\$ 13.93</u>
Options exercisable at year end	<u>27,581</u>	<u>\$ 12.42</u>	<u>20,140</u>	<u>\$ 9.77</u>	<u>14,769</u>	<u>\$ 8.79</u>
Weighted-average fair value of options granted during the year	<u>\$ 5.09</u>		<u>\$ 7.30</u>		<u>\$ 15.52</u>	

The following tables summarize information about stock options outstanding at March 31, 2002 (shares in thousands):

	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
	SHARES UNDER OPTION	WEIGHTED-AVG. REMAINING LIFE	WEIGHTED-AVG. EXERCISE PRICE	SHARES UNDER OPTION	WEIGHTED-AVG. EXERCISE PRICE
Range of Exercise Prices					
\$ 0.01 to \$10.00	42,440	7.68	\$ 8.38	15,148	\$ 6.85
10.01 to 20.00	13,210	6.24	14.96	6,663	13.80
20.01 to 30.00	9,356	5.53	24.55	5,344	24.58
30.01 to 42.00	858	6.35	32.14	426	32.65
	<u>65,864</u>	<u>7.07</u>	<u>12.30</u>	<u>27,581</u>	<u>12.42</u>

	NUMBER OF SECURITIES TO BE ISSUED UPON EXERCISE OF OUTSTANDING OPTIONS	WEIGHTED-AVERAGE EXERCISE PRICE OF OUTSTANDING OPTIONS	NUMBER OF SECURITIES REMAINING AVAILABLE FOR FUTURE ISSUANCE UNDER EQUITY COMPENSATION PLANS
Equity compensation plans approved by security holders	41,197	\$ 14.05	7,257
Equity compensation plans not approved by security holders	24,667	9.39	24,801

The maximum number of shares for which additional options may be granted was 32,058,441 at March 31, 2002, 55,672,142 at March 31, 2001 and 9,437,993 at March 31, 2000. At March 31, 2002, a total of 98,921,972 shares of the Company's common stock are reserved for issuance under the warrant and all option plans. Income tax benefits associated with the exercise of stock options are reflected as adjustments to additional paid-in capital.

#### 14. QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

Quarterly financial information for the years ended March 31, 2002 and 2001 is as follows (in thousands, except for per share data):

	FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FOURTH QUARTER	YEAR
<b>Fiscal 2002:</b>					
Revenues	\$ 446,748	\$ 424,028	\$ 450,553	\$ 407,218	\$ 1,728,547
Operating income (loss)	51,026	36,961	42,049	(402,959)	(272,923)
Pre-tax income (loss)	55,413	42,750	48,047	(397,057)	(250,847)
Net income (loss)	34,356	26,505	29,789	(335,905)	(245,255)
Basic earnings (loss) per share	0.09	0.07	0.08	(0.90)	(0.66)
Diluted earnings (loss) per share	0.09	0.07	0.08	(0.90)	(0.66)

<b>Fiscal 2001:</b>					
Revenues	\$ 513,874	\$ 486,323	\$ 495,356	\$ 514,497	\$ 2,010,050
Operating income	40,932	21,890	57,450	72,360	192,632
Pre-tax income	38,116	20,792	58,000	75,161	192,069
Net income	23,632	12,891	35,960	46,600	119,083
Basic earnings per share	0.07	0.04	0.10	0.13	0.33
Diluted earnings per share	0.06	0.03	0.10	0.12	0.32

The fourth quarter of fiscal 2002 was impacted by an impairment charge of \$35.2 million associated with a change in technology related to distributed products, restructuring costs of \$46.9 million and an impairment of goodwill related to the restructuring of \$342.9 million.



## SHAREHOLDER INFORMATION

### General Office:

31440 Northwestern Highway  
Farmington Hills, Michigan 48334-2564  
248.737.7300

### Transfer Agent:

EquiServe Trust Company, N.A.  
P.O. Box 43023  
Providence, Rhode Island 02940-3023  
877.282.1169  
www.equiserve.com

### Auditor:

Deloitte & Touche LLP  
600 Renaissance Center, Suite 900  
Detroit, Michigan 48243-1704  
313.396.3000

### Annual Meeting:

The Annual Meeting of Shareholders will be held at 3 p.m. Eastern time on August 27, 2002 in Farmington Hills, Michigan. Notice of place of meeting with proxy form accompanies the Annual Report to Shareholders.

### Form 10-K:

A copy of the Annual Report on Form 10-K, filed with the Securities and Exchange Commission for fiscal 2002, is available without charge by writing to:

**Lisa Elkin**  
**Vice President, Communications and Investor Relations**  
**Compuware Corporation**  
**31440 Northwestern Highway**  
**Farmington Hills, Michigan 48334-2564**

### Investor Resources:

Compuware maintains and updates a web site and a phone line specifically for our investors. To access our investor web site, go to [www.compuware.com](http://www.compuware.com) and click on the Investor Relations link. The Compuware toll-free investor hot line is 877.779.CPWR.

### Common Stock Listing:

The Company's Common Stock is traded on The Nasdaq Stock Market. The Company's symbol is CPWR.

The following table sets forth the high and low trading prices for the company's common stock for the periods indicated, as reported by Nasdaq:

FISCAL YEAR ENDED MARCH 31, 2002	HIGH	LOW	FISCAL YEAR ENDED MARCH 31, 2001	HIGH	LOW
Fourth Quarter	\$ 14.00	\$ 10.68	Fourth Quarter	\$ 14.38	\$ 6.25
Third Quarter	13.68	7.46	Third Quarter	9.25	5.63
Second Quarter	14.50	7.68	Second Quarter	11.25	7.50
First Quarter	\$ 14.00	8.50	First Quarter	22.00	9.25

# COMPUWARE WORLDWIDE OFFICE LOCATIONS

COMPUWARE MARKETS ITS PRODUCTS AND SERVICES THROUGH OFFICES IN THE FOLLOWING NORTH AMERICAN AND INTERNATIONAL LOCALES:

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## North America

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Atlanta, GA	Denver, CO	Milwaukee, WI	Saint Louis, MO
Austin, TX	Farmington Hills, MI	Minneapolis, MN	San Diego, CA
Baltimore, MD	Grand Rapids, MI	Montreal, QC	San Francisco, CA
Boston, MA	Houston, TX	Nashua, NH	Seattle, WA
Charlotte, NC	Irvine, CA	Nashville, TN	Tampa, FL
Chicago, IL	Kansas City, MO	New York, NY	Toronto, ON
Cincinnati, OH	Lansing, MI	Panama City, Panama	Washington, D.C.
Cleveland, OH	Los Angeles, CA	Philadelphia, PA	Woodland Hills, CA
Columbus, OH	Madison, WI	Phoenix, AZ	
Dallas, TX	Mexico City, Mexico	Raleigh, NC	

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## International

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Amsterdam, The Netherlands	Düsseldorf, Germany	Milan, Italy	Seoul, South Korea
Baden-Dättwil, Switzerland	Frankfurt, Germany	Munich, Germany	Singapore, Singapore
Brasilia, Brazil	Hamburg, Germany	Nagoya, Japan	Slough, United Kingdom
Brisbane, Australia	Helsinki, Finland	Osaka, Japan	Stockholm, Sweden
Brussels, Belgium	Hong Kong, China	Oslo, Norway	Sydney, Australia
Canberra, Australia	Johannesburg, South Africa	Paris, France	Tokyo, Japan
Cape Town, South Africa	Lisbon, Portugal	Rio de Janeiro, Brazil	Vienna, Austria
Copenhagen, Denmark	Madrid, Spain	Rome, Italy	
Dortmund, Germany	Melbourne, Australia	São Paulo, Brazil	

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In addition, the company's distributors and resellers have offices that directly serve:

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Argentina	Dominican Republic	Malaysia	Singapore
Australia	Greece	Mauritius	South Korea
Bahrain	India	Panama	Taiwan R.O.C.
Brazil	Indonesia	Peru	Thailand
Chile	Israel	Philippines	Turkey
China	Japan	Puerto Rico	United Arab Emirates
Colombia	Kuwait	Saudi Arabia	Venezuela



**COMPUWARE®**

### Compuware Corporation

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