

SERENA SOFTWARE INC
Form S-4/A
April 05, 2004
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As filed with the Securities and Exchange Commission on April 5, 2004

Registration No. 333-113405

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

PRE-EFFECTIVE AMENDMENT NO. 2

TO

FORM S-4

REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933

SERENA SOFTWARE, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

7372
(Primary Standard Industrial
Classification Code Number)

94-2669809
(I.R.S. Employer
Identification Number)

2755 Campus Drive, 3rd Floor

San Mateo, California 94403-2538

(650) 522-6600

(Address, including ZIP code, and telephone number, including area code, of registrant's principal executive offices)

Mark Woodward

President and Chief Executive Officer

SERENA Software, Inc.

2755 Campus Drive, 3rd Floor

San Mateo, California 94403-2538

(650) 522-6600

(Name, address, including ZIP code, and telephone number, including area code, of agent for service)

Copies to:

Kenneth R. Lamb

Stewart L. McDowell

Gibson, Dunn & Crutcher LLP

One Montgomery Street

San Francisco, CA 94104-4505

(415) 393-8200

Approximate date of commencement of proposed sale to the public: As soon as practicable after this registration statement becomes effective and upon consummation of the transactions described in the enclosed prospectus.

If the securities being registered on this Form are being offered in connection with the formation of a holding company and there is compliance with General Instruction G, check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. _____

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. _____

The Registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act or until the registration statement shall become effective on such date as the United States Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

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The information contained in this document may change. We may not complete the exchange offer and issue these securities until the registration statement filed with the United States Securities and Exchange Commission is effective. This document is not an offer to sell securities, and it is not soliciting an offer to buy securities, in any jurisdiction where the offer or sale is not permitted.

This document is important and requires your immediate attention. If you are in any doubt about the offer or what action you should take, you are recommended immediately to seek your own financial advice from your stockbroker, bank manager, solicitor, accountant or other independent financial advisor authorised under the Financial Services and Markets Act 2000 or another appropriately authorised independent financial advisor.

If you have sold or otherwise transferred your Merant securities, please send this document and the accompanying documents as soon as possible to the purchaser or transferee or to the stockbroker or other agent through whom the sale or transfer was made, for delivery to the purchaser or transferee. We are not making the offer directly or indirectly in or into Canada, Australia or Japan. You should not forward or transmit these documents in or into Canada, Australia or Japan.

OFFER DOCUMENT DATED 18 MARCH 2004

RECOMMENDED CASH AND SHARE OFFER

BY

SERENA SOFTWARE, INC.

(AND BY

LEHMAN BROTHERS

ON ITS BEHALF

OUTSIDE THE UNITED STATES)

FOR

THE ENTIRE ISSUED AND TO BE ISSUED SHARE CAPITAL OF

MERANT PLC

SERENA Software, Inc., referred to as we or SERENA, (and Lehman Brothers on behalf of SERENA outside the United States) is offering to acquire, on the conditions and the further terms set out in this document and in the accompanying acceptance form or letter of transmittal, all of the issued and to be issued and unconditionally allotted ordinary shares of Merant plc, referred to as Merant shares, and Merant American Depositary Shares, referred to as Merant ADSs, represented by American Depositary Receipts, referred to as Merant ADRs, on the following basis:

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for every 1 Merant share	136.5 pence in cash and 0.04966 share of SERENA common stock, US\$0.001 par value per share
for every 1 Merant ADS (each Merant ADS representing 5 Merant shares)	682.5 pence in cash and 0.2483 share of SERENA common stock, US\$0.001 par value per share

If you accept this offer, you may request to vary the proportion of shares of SERENA common stock, par value \$0.001 per share, referred to as SERENA shares, and cash you will receive pursuant to a mix and match election, including by electing to receive only cash or only new SERENA shares. However, your mix and match election will only be satisfied to the extent that other Merant securityholders make opposite elections.

The offer is based on a valuation of 195 pence for each Merant share. On this basis, the offer values the entire issued share capital of Merant at approximately £206 million (US\$380 million). Our offer to pay for and exchange SERENA shares for Merant shares and Merant ADSs is subject to the conditions set forth in Appendix 1 of this document.

SERENA shares are traded on the Nasdaq National Market, referred to as Nasdaq, under the symbol `SRNA`. Merant shares are listed on the Official List and traded on the London Stock Exchange under the symbol `MRN` and on Nasdaq in the form of Merant ADSs under the symbol `MRNT`.

A LETTER OF RECOMMENDATION FROM THE CHAIRMAN OF MERANT BEGINS ON PAGE 30 OF THIS DOCUMENT.

We Are Not Asking You For A Proxy and You Are Requested Not to Send Us a Proxy.

The initial offer period will expire at 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004, unless we specify a later closing date.

At the conclusion of the initial offer period, if all the conditions have been satisfied, fulfilled and/or, to the extent permitted, waived, we will extend the offer for a subsequent offer period of at least 14 calendar days. Merant securityholders will have withdrawal rights during the initial offer period, including any extension thereof, but not during the subsequent offer period, except in limited circumstances.

To accept the offer, you must complete the appropriate acceptance procedures by no later than 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004. The procedures for acceptance of the offer are described beginning on page I-21 of Appendix 1 and in the accompanying acceptance form or letter of transmittal.

In connection with the offer, you should consider the matters discussed under Risk Factors beginning on page 21 of this document.

Neither the SEC nor any securities commission of any state of the United States has approved or disapproved of the securities offered by or on behalf of SERENA or determined if this offer document is truthful or complete. Any representation to the contrary is a criminal offence.

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REFERENCES TO ADDITIONAL INFORMATION

This document incorporates important business and financial information about SERENA and Merant from other documents that are not included in or delivered with this document. This information is available to you without charge upon your written or oral request. You may read and copy any reports, statements or information that the companies file at the SEC's public reference room at 450 Fifth Street, N.W., Washington, D.C. 20549. Please call the SEC at 1 (800) 732-0330 for further information on the public reference room. The SEC filings of SERENA and Merant are also available to the public from commercial document retrieval services and at the internet website maintained by the SEC at www.sec.gov. See the section entitled "Where You Can Find Additional Information." In addition, Merant files annual reports with the Registrar of Companies at Companies House in England and Wales. This information is available through the Companies House website at www.companieshouse.gov.uk upon payment of a minimal fee.

You may also request copies of these documents from us, without charge, excluding all exhibits, unless we have specifically incorporated by reference an exhibit in this document. Merant securityholders may obtain documents incorporated by reference in this document by requesting them in writing or by telephone from our Information Agent at the address set forth below. You can also contact our Information Agent for answers to your questions regarding the offer. In order to receive timely delivery of the documents, you must make your request no later than 8 April 2004.

D.F. KING & CO., INC.

North America

48 Wall Street

New York, NY 10005

Toll Free: 1 (800) 859-8509

Banks and Brokers: 1 (212) 269-5550

Europe

No. 2 London Wall Buildings
London Wall, London EC2M 5PP
Toll Free, UK: 0 800 917 8414
Call Collect: +44 20 7920 9700

SERENA is a registered trademark and the SERENA logo, StarTool and SAFE are trademarks of SERENA. Merant is a registered trademark of Merant. All other products and service names used are trademarks or registered trademarks of their respective owners.

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IMPORTANT INFORMATION

DEFINITIONS

Some words and terms used in this document are defined in Appendix 8 to this document.

APPLICABLE DISCLOSURE REQUIREMENTS

We are making an exchange offer for securities of an English company. Because the offer is subject to English and US securities laws, regulations and disclosure requirements, US and UK investors should be aware that this document consists of a combination of both US and UK format and style. In particular, although material information is summarised in the section entitled Summary of the Material Terms of the offer and the letter from Lehman Brothers contained in this document, the Appendices to this document contain material information concerning the offer which is required by US or UK securities law and may be of interest to you.

FORWARD-LOOKING STATEMENTS

This document and other documents to which we refer you contain forward-looking statements concerning non-historical facts or matters that are subject to risks and uncertainties. These forward-looking statements may be preceded by, followed by or include the words believes, expects, anticipates, intends, plans, projections, estimates, may, will, should, could or similar expressions. These forward-looking statements are based on our expectations or beliefs concerning future events, many of which are outside of our control. Many possible events or factors could affect the actual financial results and performance of SERENA and Merant before the completion of the transaction and of the combined company after the completion of the transaction, and these factors or events could cause those results or performance to differ significantly from those expressed in our forward-looking statements, including but not limited to:

the possibility that the offer may not be completed;

difficulties we may encounter when integrating the SERENA and Merant businesses, along with other recent acquisitions, if the offer is successful;

the percentage of licence revenue typically closed at the end of each quarter making estimation of operating results prior to the end of the quarter extremely uncertain;

weak economic conditions worldwide which may continue to adversely affect the overall demand for software and services, which have resulted in and could continue to result in decreased revenues or lower revenue growth rates;

our reliance on our mainframe products for revenue;

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changes in revenue mix and seasonality;

our ability to deliver our products on the distributed systems platform;

dependence on revenues from our installed base;

continued demand for additional mainframe Million Instructions Per Second, or MIPS, capacity;

expansion of our international organisations; and

our ability to manage our growth.

The safe harbour protection afforded by the US Private Securities Litigation Reform Act of 1995 does not apply to forward-looking statements made in connection with exchange offers.

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FINANCIAL INFORMATION

The extracts from the consolidated financial statements of, and other information about, SERENA appearing in this document are presented in US dollars (US\$) and have been prepared in accordance with accounting principles generally accepted in the United States of America, referred to as US GAAP. The extracts from the consolidated financial statements of, and other information about, Merant appearing in this document are presented in both US dollars (US\$) and pounds sterling (£) or pence (p) and have been prepared in accordance with accounting practices and principles generally accepted in the United Kingdom, referred to as UK GAAP, except that the Merant revenues have been recognised in accordance with both UK and US GAAP. The headers and captions to the Merant financial information will indicate the basis of accounting and the utilised currency. US GAAP and UK GAAP differ in some significant respects. Financial information relating to SERENA is contained in Appendix 2 and is incorporated by reference in this document. Financial information relating to Merant is contained in Appendix 3 and is incorporated by reference in this document. A reconciliation between UK GAAP and US GAAP in respect of certain information set forth in this document is contained in documents of the Merant group incorporated by reference in this document. Certain unaudited pro forma financial information relating to the combined company is contained in Appendix 4. The unaudited pro forma financial information relating to the combined SERENA group has been prepared in accordance with US GAAP.

ABSENCE OF APPRAISAL RIGHTS

Merant securityholders generally do not have appraisal rights under English law. See the section entitled *Appraisal Rights* in Appendix 6 of this document.

RULE 8 NOTICES

Rule 8.3 of The City Code on Takeovers and Mergers, referred to as the City Code, requires public disclosure of dealings during the initial offer period by persons who own or control or pursuant to an agreement or understanding (whether formal or informal) own or control, or who would as a result of any transaction own or control, 1 per cent. or more of any class of relevant securities of Merant and/or SERENA. Relevant securities include Merant securities, SERENA shares, and instruments convertible into either Merant securities or SERENA shares. In the case of the offer, this requirement will apply until the end of the initial offer period.

ADVISORS

Lehman Brothers Europe Limited, referred to as Lehman Brothers, which is regulated in the United Kingdom by The Financial Services Authority, is acting for SERENA and no one else in connection with the offer and will not be responsible to anyone other than SERENA for providing the protections afforded to customers of Lehman Brothers nor for giving advice in relation to the offer. SERENA is making the offer in the United States on its own behalf.

UBS is acting as financial advisor to Merant in connection with the offer and no one else and will not be responsible to anyone other than Merant for providing the protections afforded to clients of UBS nor for providing advice in relation to the offer.

SALES RESTRICTIONS IN CERTAIN COUNTRIES

We are not making the offer directly or indirectly in or into Canada, Australia or Japan. You should not forward or transmit these documents in or into Canada, Australia or Japan.

NO INTERNET SITE IS PART OF THIS DOCUMENT

Each of SERENA and Merant maintains an internet site. The SERENA internet site is at *www.serena.com*. The Merant internet site is at *www.merant.com*. Information contained in or otherwise accessible through these internet sites is not part of this document. All references in this document to these internet sites are inactive textual references to these sites and are for your information only.

Table of Contents**QUESTIONS AND ANSWERS AND SUMMARY OF THE MATERIAL TERMS OF THE OFFER**

This question and answer section highlights selected information from this document but does not contain all of the information that may be important to you. To better understand our offer to holders of Merant shares and Merant ADSs, you should read this entire document carefully, as well as those additional documents to which we refer you. You may obtain the information incorporated by reference into this document by following the instructions in the section captioned "Where You Can Find Additional Information." In particular, you should read the Appendices attached to this document. References in this document to SERENA, we, us and our are references to SERENA and its consolidated subsidiaries, unless the context otherwise requires. References to Merant securityholders are references to holders of Merant shares or Merant ADSs. References to Merant shareholders are references to holders of Merant shares. Terms used in the Appendices to this document are defined in Appendix 8 to this document.

WHO IS OFFERING TO BUY MY MERANT SHARES AND MERANT ADSs?

SERENA is an industry leader in Enterprise Change Management, or ECM, solutions focused on the mainframe platform. For over twenty years we have focused exclusively on providing solutions that help companies automate change to the applications that run their businesses. Today our products are in use at over 3,600 customer sites including 46 of the Fortune 50. We believe our SERENA Application Framework for Enterprises (SAFE) is the next step in ECM, providing cross-platform, cross-process and cross-organisational support across application life cycle processes. With headquarters in San Mateo, California, we serve customers worldwide through local offices and an international network of distributors.

We are listed on Nasdaq under the symbol SRNA. We have a current market capitalisation of approximately US\$755 million based on the closing price of SERENA shares on 15 March 2004, the latest practicable date prior to the posting of this document. In the years ended 31 January 2004 and 2003, we reported the following results (in millions of US Dollars, except per share data):

	Year ended	Year ended
	<u>31 January 2004</u>	<u>31 January 2003</u>
Revenues	105.6	95.8
Profit before tax	33.7	37.3
Charge for tax	12.3	14.1
Net profit after tax	21.4	23.2
Earnings per share	0.53	0.57

In the quarters ended 31 January 2004 and 2003, we reported the following results (in millions of US Dollars, except per share data):

	Quarter ended	Quarter ended
	<u>31 January 2004</u>	<u>31 January 2003</u>
Revenues	29.6	26.1
Profit before tax	9.3	10.8
Charge for tax	3.4	4.0

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Net profit after tax	6.0	6.8
Earnings per share	0.15	0.17

As at 31 January 2004, we had total cash and cash equivalents of US\$377 million.

We were incorporated in California in 1980 and reincorporated in Delaware in 1998. The address of our principal executive offices is 2755 Campus Drive, 3rd Floor, San Mateo, California 94403-2538 and our telephone number is 1 (650) 522-6600.

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WHY ARE YOU MAKING THIS OFFER?

The acquisition of Merant by SERENA will create the second largest provider of ECM software solutions, serving the complex change management needs of at least 46 of the Fortune 50 largest companies worldwide, with a resulting combined installed base of over 15,000 customers. We believe this installed base will provide the combined company with distribution leverage to cross sell products, expand into new geographies, create new opportunities in channel development and generate a profitable and steady maintenance revenue stream.

The combination brings together two leaders in ECM with the complementary strengths of SERENA on mainframe platforms and Merant on distributed systems platforms and similar visions for future market share expansion.

The boards of directors of SERENA and Merant believe the combination should deliver significant strategic benefits and provide opportunities to reduce expenses and that the combined company would:

create the leading ECM vendor with integrated software solutions running on all major operating systems, from the mainframe to UNIX, LINUX and NT distributed systems environments all the way to the worldwide web;

combine SERENA's market leading mainframe Software Configuration Management, or SCM, product with Merant's market leading enterprise distributed SCM product;

deepen and strengthen the customer base by combining SERENA's more than 3,600 customers with Merant's more than 15,000 customer accounts;

accelerate SERENA's ability to offer customers its vision of application life cycle management solutions branded as SERENA's Application Framework for Enterprises (SAFE), thereby accessing larger markets and enabling the combined company to compete more effectively; and

offer significant potential cost savings in the areas of overlap such as dual exchange listing, dual public company compliance obligations and dual administrative infrastructures as well as a number of other duplicative areas and initiatives.

Both SERENA and Merant have been pursuing similar strategies and strategic investments to enable the application of change management technology beyond SCM to broader applications within information technology.

WHAT ARE THE SECURITIES SOUGHT IN THE OFFER?

We are seeking to acquire all of the issued and to be issued Merant shares and Merant ADSs. See paragraph 2 of the letter from Lehman Brothers contained in this document.

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Merant is a leading provider of software and services for managing code, content and other business-critical assets. Merant designs, develops and markets software products and services for ECM, SCM and web content management, under the Merant brand (formerly the PVCS® brand). Merant solutions help companies improve their ability to manage change of software applications, code and web content. In the year ended 30 April 2003, Merant generated approximately 50 per cent. of its revenue from maintenance fees, approximately 38 per cent. from the sale of licences and the remainder of its revenue from consulting and training. Merant has approximately 535 employees worldwide.

Merant shares are listed on the Official List and publicly traded on the London Stock Exchange under the symbol MRN , and (in ADS form) on Nasdaq under the symbol MRNT . Merant has a current market capitalisation of approximately £201 million based on the closing price of Merant shares on 15 March 2004, the latest practicable date prior to the posting of this document.

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Merant released its unaudited third quarter results on 3 March 2004. For the unaudited nine months ended 31 January 2004 and 2003, under UK GAAP, Merant reported the following results (in millions of US Dollars, except per share data):

	Nine Months ended	Nine Months ended
	31 January 2004	31 January 2003
Turnover	91.7	89.1
Profit (loss) before tax	2.0	(19.6)
Charge for (recovery of) tax	(0.2)	
Net profit (loss) after tax	2.2	(19.6)
Earnings (loss) per share	0.02	(0.19)

As at 31 January 2004, Merant had net cash of US\$70.7 million. This is based on an exchange rate of US\$1.8202 : £1.00 on 31 January 2004.

The principal executive offices of Merant are located at Abbey View Everard Close, St. Albans, Herts, AL12PS United Kingdom and the telephone number is +44 (0) 1727 812812.

WHAT WOULD I RECEIVE IN EXCHANGE FOR MY MERANT SECURITIES?

We are offering to pay:

for every 1 Merant share	136.5 pence in cash and 0.04966 of a new SERENA share
for every 1 Merant ADS (each Merant ADS representing 5 Merant shares)	682.5 pence in cash and 0.2483 of a new SERENA share

The offer is based on a valuation of each Merant share at 195 pence. On this basis, the offer values the entire amount of issued share capital of Merant at approximately £206 million (US\$380 million). This is based on an exchange rate of US\$1.8488 : £1.00, calculated as the average of the US dollar / pound sterling exchange rate derived from the noon buying rate in New York City for cable transfers in pounds sterling as certified for customs purposes by the Federal Reserve Bank of New York, referred to as the noon buying rate, for the five trading days ended 3 March 2004 and the price per SERENA share of US\$21.78, calculated as the average of the closing prices of one SERENA share as reported on Nasdaq for the twenty United States trading days ended 1 March 2004.

SERENA is offering a mix and match election under which Merant securityholders who validly accept the offer may request to vary the proportions in which they receive SERENA shares and cash in respect of their Merant shares and Merant ADSs.

HOW DOES THE OFFER COMPARE WITH RECENT PRICES OF MERANT SHARES?

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At 195 pence for each Merant share, the offer represented a premium of approximately:

25 per cent. to the middle market closing price of 155.5 pence per Merant share on 2 March 2004, the last dealing day prior to the announcement of the offer; and

34 per cent. to the average daily middle market closing price of 145.8 pence per Merant share for the three months ended 2 March 2004.

On 2 March 2004, the last dealing day before we announced the offer, the middle market closing price of Merant shares reported on the London Stock Exchange was 155.5 pence per share and the last sale price of Merant ADSs reported on Nasdaq was US\$14.79 per Merant ADS. Between 2 March 2003 and 2 March 2004, the price of Merant shares ranged between 118.50 pence and 183.50 pence per share and the price of Merant

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ADSs ranged from US\$9.07 and US\$15.35 per Merant ADS. We advise you to obtain a recent quotation for Merant shares and Merant ADSs in deciding whether to accept the offer. See paragraph 3 of Appendix 5 of this document.

On 15 March 2004 (the latest practicable date prior to the posting of this document), at the then prevailing noon buying rate of US\$1.7993: £1.00 and a SERENA share price of \$19.68, the offer values each Merant share at 190.8 pence, representing a premium of approximately 23 per cent. to the middle market closing price of 155.5 pence per Merant share on 2 March 2004, the last dealing day prior to the announcement of the offer.

Merant securityholders should bear in mind that fluctuations in the dollar to pound sterling exchange rate from time to time will affect the pound sterling value of any investment in SERENA shares and any dividend income from that investment (payable in US dollars and subject to US withholding tax). Merant securityholders should also bear in mind that the value of the SERENA shares payable in the offer may fluctuate both before and after any consummation of the offer.

A comparison of the rights of holders of SERENA shares and those of holders of Merant shares is contained in Appendix 6 of this document.

MAY I ELECT TO RECEIVE A GREATER PROPORTION OF CASH OR A GREATER PROPORTION OF SERENA SHARES THAN THE STANDARD ENTITLEMENT DESCRIBED ABOVE?

Merant securityholders who validly accept the offer will be able to request under the mix and match election to vary the proportions in which they receive SERENA shares and cash in respect of their Merant securities.

The maximum number of new SERENA shares to be issued under the offer and the maximum amount of cash to be paid under the offer will not be varied as a result of the mix and match election. Accordingly, a Merant securityholder's mix and match election will be satisfied only to the extent that other Merant securityholders make opposite elections. To the extent that elections cannot be satisfied in full, they will be scaled down on a pro rata basis. To the extent that elections can be satisfied, electing Merant securityholders will receive new SERENA shares instead of cash, and vice versa.

Accordingly, Merant securityholders who make mix and match elections will not know the exact number of new SERENA shares or the amount of cash they will receive until settlement of the consideration under the offer, although an announcement of the approximate extent to which mix and match elections will be satisfied will be made two days after the mix and match election ceases to be open for acceptance.

All adjustments to the amount of cash or SERENA shares received by any Merant securityholder in the mix and match election will be calculated based on a value per Merant share of 195 pence and a value per SERENA share of £11.78. The value of a SERENA share for these purposes is based on an exchange rate of US\$1.8488 : £1.00, which is calculated as the average of the US dollar/pound sterling noon buying rate for the five trading days ended 3 March 2004 and price per SERENA share of US\$21.78, which is calculated as the average of the closing prices of one SERENA share as reported on Nasdaq for the 20 US trading days ended 1 March 2004.

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Although the offer will remain open for a subsequent offer period of at least 14 calendar days after the date on which the offer becomes or is declared unconditional in all respects, the mix and match election will remain open until, but not beyond, 3.00 pm (London time), 10.00 am (New York City time) on the date falling five calendar days after the offer becomes or is declared unconditional in all respects. Mix and match elections must be made at the same time as the acceptances of the offer to which they relate, on the relevant acceptance form. Merant securityholders who do not make a mix and match election or who do not accept the offer until after the fifth calendar day after the offer becomes or is declared unconditional in all respects will receive the basic entitlement of 136.5 pence in cash and 0.04966 of a new SERENA share for every Merant share held (directly or through Merant ADSs).

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A mix and match election made by a Merant securityholder may not be changed after the time that it is first made on the relevant acceptance form. However, acceptances, including the associated mix and match election, may be withdrawn in accordance with the procedures set forth in this document. See paragraphs 4 and 14 of the letter from Lehman Brothers and paragraphs 4 and 5 of Part B of Appendix 1 of this document.

The mix and match election will be conditional upon the offer becoming or being declared unconditional in all respects.

CAN I CHOOSE THE CURRENCY FOR THE CASH I RECEIVE?

If you accept the offer for Merant shares, you will receive the cash portion of your consideration in pounds sterling, unless you specifically elect to receive it in US dollars.

If you accept the offer for Merant ADSs, you will receive the cash portion of your consideration for your Merant ADSs in US dollars, unless you specifically elect to receive it in pounds sterling.

If you elect or are deemed to have elected to receive the cash portion of your consideration in US dollars, the cash amount payable in pounds sterling to which you would otherwise be entitled pursuant to the terms of the offer will be converted, subject to conversion expenses, from pounds sterling to US dollars at the exchange rate obtainable on the spot market in London on the date the cash consideration is made available by SERENA to the relevant paying agent for delivery in respect of your Merant securities. The actual amount of US dollars received will depend on the exchange rate prevailing on the day on which funds are made available to the relevant payment agent by SERENA. See paragraph 13 of Part B of Appendix 1 of this document.

DOES THE MERANT BOARD OF DIRECTORS SUPPORT THE OFFER?

The board of directors of Merant, referred to as the Merant directors, which has been so advised by UBS, considers the terms of the offer fair from a financial point of view. In providing advice to the Merant board, UBS has taken account of the Merant board's commercial assessments. Accordingly, the Merant directors unanimously recommend that Merant securityholders accept the offer. Merant securityholders are directed to Appendix 9, which contains important information concerning the assumptions in, limitations of and qualifications to UBS' advice to the Merant board.

Each member of the board of directors of Merant has irrevocably undertaken to accept the offer in respect of their own beneficial holdings, comprising 381,389 Merant shares in aggregate (representing approximately 0.36 per cent. of Merant's existing issued share capital). One Merant director, Gerald Perkel, has also irrevocably undertaken to accept the offer in respect of all Merant shares he receives as a result of the exercise of options during the period while the offer is open for acceptance, representing up to 1,500,000 Merant shares. No other Merant director holds any options over Merant shares. See the letter from the Chairman of Merant in this document.

DO ANY OTHER SHAREHOLDERS SUPPORT THE OFFER?

We have received an additional irrevocable undertaking to accept the offer from Merant Trustees Limited, the trustees for Merant's employee benefit trusts, representing approximately 7.0 per cent. of Merant's existing issued share capital. We have also received confirmations of intent to accept the offer, representing in aggregate approximately 27.3 per cent. of Merant's existing issued share capital. See paragraph 5 of the letter from Lehman Brothers. The Merant securityholders from whom we have received undertakings and confirmations of intent (including a confirmation of intent from Schroder Investment Management Limited), hold an aggregate of 34.61 per cent. of the issued share capital of Merant as at 15 March 2004.

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DO YOU HAVE THE FINANCIAL RESOURCES TO MAKE PAYMENT?

We will fund the cash component of the offer from our existing cash resources. The offer is not conditional upon any financing arrangements other than the effectiveness of the registration statement filed by SERENA with respect to the SERENA shares to be issued in the offer. See paragraph 9 of the letter from Lehman Brothers and paragraph 7 of Appendix 5 of this document.

IS YOUR FINANCIAL CONDITION RELEVANT TO MY DECISION TO ACCEPT THE OFFER?

Yes. If you accept the offer, part of your consideration will be in the form of SERENA shares, and you should consider our financial condition and results of operations before you decide to become one of our stockholders through the offer.

You should also review the information set forth in the section entitled "Risk Factors" beginning on page 21 and Appendix 2 and the documents incorporated by reference in this document which contain detailed business, financial and other information about us.

HOW LONG DO I HAVE TO ACCEPT THE OFFER?

You will have until 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004, to accept the offer, unless the offer is extended. However, if you are a Merant ADS holder and you cannot deliver everything that is required in order to make a valid tender of Merant ADSs by that time, you may gain some time by following the procedures for guaranteed delivery, which are described later in this document. See paragraphs 10, 11 and 12 of Part B of Appendix 1 of this document.

WHAT IS THE DIFFERENCE BETWEEN THE INITIAL OFFER PERIOD AND THE SUBSEQUENT OFFER PERIOD?

The initial offer period is the time during which withdrawal rights apply. The initial offer period is the period from the date of this document until the time and date (not being before 3.00 pm (London time), 10.00 am (New York City time) on 15 April 2004) on which all the conditions are satisfied, fulfilled or, to the extent permitted, waived or, if earlier, the time and date on which the offer lapses. SERENA may declare the offer wholly unconditional at any time after 3.00 pm (London time), 10.00 am (New York City time) on 15 April 2004 (or such later time as the offer is required to be extended pursuant to the City Code or US law).

The subsequent offer period will start as soon as the initial offer period terminates as a result of the offer being declared or becoming wholly unconditional. The subsequent offer period must remain open for at least 14 calendar days but we may extend it beyond that time until a further specified date or until further notice. During the subsequent offer period no withdrawal rights apply, except in limited circumstances. See paragraph 4 of Part B of Appendix 1 of this document.

CAN THE OFFER BE EXTENDED AND UNDER WHAT CIRCUMSTANCES?

Yes. If all of the conditions to the offer have not been either satisfied, fulfilled or, to the extent permitted, waived by SERENA by 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004, SERENA may choose, but shall not be obliged to, extend the initial offer period. We may also be required to extend the initial offer period under applicable UK and US securities laws and regulations if there is a material change in the offer or this offer document. Once all the conditions have been either satisfied, fulfilled or, to the extent permitted, waived by SERENA, the offer will remain open for a subsequent offer period of at least 14 calendar days. See paragraph 1 of Part B of Appendix 1 of this document.

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HOW WILL I BE NOTIFIED IF THE OFFER IS EXTENDED?

If we extend the offer, we will make a public announcement of the extension, not later than 8.00 am (London time), and 8.00 am (New York City time), on the next business day after the day on which the offer was scheduled to expire. See paragraph 3 of Part B of Appendix 1.

We will also announce by 8.00 am (London time), and 8.00 am (New York City time), on the day following the end of the initial offer period that there will be a subsequent offer period. The subsequent offer period will remain open for at least 14 calendar days but we may extend it beyond that time until a further specified date or until further notice.

WHAT ARE THE MOST SIGNIFICANT CONDITIONS TO THE OFFER?

We are not obliged to purchase any Merant shares and/or Merant ADSs unless we have received valid acceptances (which have not been properly withdrawn) in respect of at least 90 per cent. of the Merant shares (including Merant shares represented by Merant ADSs) to which the offer relates, referred to as the Acceptance Condition. We may reduce this percentage, but not below 50 per cent. At least five US business days prior to any reduction, we will announce that we may do this through a press release and/or a newspaper advertisement of general circulation in the US and the UK.

We are not obliged to purchase any Merant shares and/or Merant ADSs unless the new SERENA shares to be issued pursuant to the offer have been authorised for listing on Nasdaq and the registration statement that we have filed with the SEC has been declared effective.

We are not obliged to purchase any Merant shares and/or Merant ADSs if, among other things, the offer has been referred to the United Kingdom Competition Commission by the Secretary of State for Trade and Industry or the applicable waiting period under the United States Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, referred to as the HSR Act, has not expired or been waived.

Subject to the consent of the UK Panel on Takeovers and Mergers, referred to as the Panel, we are not obliged to purchase any Merant shares and/or Merant ADSs if, among other things, certain adverse events material in the context of Merant and its affiliates, taken as a whole, material in the context of SERENA and its subsidiaries, taken as a whole, and/or material in the context of the offer, have occurred.

See Part A and Part B of Appendix 1 of this document.

CAN THE OFFER BE TERMINATED OR AMENDED?

Subject to applicable UK law, the SEC's rules and regulations and the conditions of our offer, which, among other things, limit our ability to amend or terminate our offer, we also reserve the right, at any time or from time to time:

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to extend, for any reason, the period of time during which our offer is open;

to terminate the offer upon the failure of any of the conditions of our offer to be satisfied, in which case all acceptances received prior to the date of termination will cease to be effective; and

to waive any condition or otherwise amend our offer in any respect.

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HOW DO I ACCEPT THE OFFER?

To accept the offer, you must deliver a completed form of acceptance in the case of Merant shares, or a completed letter of transmittal in the case of Merant ADSs, to the UK Receiving Agent or the US Depository, respectively, by not later than the time the offer expires. If your Merant shares are held in uncertificated form (that is, you do not have a share certificate because your Merant shares are held in CREST), you should read carefully paragraph 10 of Part B of Appendix 1 to this document, which sets out the acceptance procedures for holders of Merant shares in uncertificated form. If your Merant ADSs are held in street name in the US, they can be tendered by your nominee through the applicable book entry transfer system. In the case of Merant ADSs, if you cannot get any document or instrument that is required to be delivered by the expiration of the offer, you may gain some time by following the procedures for guaranteed delivery. Receipt of a notice of guaranteed delivery will not be treated as a valid acceptance for the purpose of satisfying the Acceptance Condition. See paragraphs 10, 11 and 12 of Part B of Appendix 1 of this document.

UNTIL WHAT TIME CAN I WITHDRAW MY ACCEPTANCE?

A Merant securityholder who accepts the offer will be entitled to withdraw the acceptance at any time until the end of the initial offer period. Thereafter, withdrawals will not be possible except in very limited circumstances (for example, if we have failed to make certain announcements required by the City Code or if we withdraw an announcement that the offer will not be increased or further extended after a particular date). See paragraph 14 of the letter from Lehman Brothers and paragraph 4 of Part B of Appendix 1 of this document.

HOW DO I WITHDRAW MY ACCEPTANCE?

In order to withdraw Merant shares or Merant ADSs once you have accepted the offer, you must deliver a written notice of withdrawal with the required information to the UK Receiving Agent or the US Depository, respectively, while you still have the right to withdraw the Merant shares or Merant ADSs. See paragraph 4 of Part B of Appendix 1 of this document.

WHEN WILL I BE PAID FOR MY MERANT SECURITIES IF I ACCEPT THE OFFER?

The settlement with respect to the offer will be consistent with UK practice, which differs from US domestic tender offer procedures in certain material respects, particularly with regard to the date of payment. Subject to either the satisfaction, fulfillment or, to the extent permitted, waiver of all the conditions to the offer, settlement of consideration to accepting Merant securityholders will be effected within 14 calendar days after the end of the initial offer period (i.e., the date on which the offer is declared or becomes wholly unconditional), in the case of acceptances received complete in all respects by the end of the initial offer period. In the case of acceptances received complete in all respects during the subsequent offer period (i.e., after the date on which the offer is declared or becomes wholly unconditional) while the offer remains open for acceptance, settlement of consideration will be made within 14 calendar days after such receipt. See paragraph 15 of the letter from Lehman Brothers.

WILL THE OFFER BE FOLLOWED BY A COMPULSORY ACQUISITION?

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Yes. If all of the conditions to the offer are either satisfied, fulfilled or, to the extent permitted, waived and we have acquired 90 per cent. in nominal value of Merant shares (including Merant shares represented by Merant ADSs) to which the offer relates then we will be entitled to and intend to acquire all remaining Merant shares and Merant ADSs pursuant to the Companies Act 1985 of England and Wales, as amended, referred to as the Companies Act, and Merant securityholders may require SERENA to purchase such holder's Merant securities in accordance with the procedures and time limits set forth in the Companies Act. Holders of Merant shares and Merant ADSs subject to the compulsory acquisition would receive the same consideration as those holders of Merant shares and Merant ADSs who accept the offer. If you do not accept the offer at all, and are subject to the

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compulsory acquisition provisions, there will be a limited reintroduction of the mix and match election among the Merant securityholders subject to the compulsory acquisition. This means that Merant securityholders subject to the compulsory acquisition will be able to request to vary the proportions in which they receive SERENA shares and cash in respect of their Merant securities, but that request will be satisfied only to the extent that other Merant securityholders that are also subject to the compulsory acquisition make opposite elections. To the extent that elections made during the compulsory acquisition cannot be satisfied, they will be scaled down on a pro rata basis. See paragraph 11 of Appendix 5 and Appendix 7 of this document.

IF I DECIDE NOT TO ACCEPT, HOW WILL THE OFFER AFFECT MY SECURITIES?

If we are able to, we will acquire all Merant shares and Merant ADSs for which we have not received acceptances pursuant to the compulsory acquisition provisions of the Companies Act and you will become one of our stockholders even if you have not accepted the offer and you will receive the same consideration per Merant share or Merant ADS as those Merant securityholders who have accepted the offer. If the offer becomes wholly unconditional, but we are not able to acquire your Merant securities under the compulsory acquisition procedures, you will remain a Merant securityholder and will, therefore, become a minority stockholder in a subsidiary of SERENA. If the offer is not completed for any reason, your status as a Merant securityholder will not be affected.

We also intend to apply, or request that Merant apply, to Nasdaq, the London Stock Exchange and the UK Listing Authority to have the Merant ADSs and Merant shares delisted, terminate the deposit agreement through which the Merant ADS programme is operated and seek to have the registration of the Merant ADSs and Merant shares under the Securities Exchange Act of 1934, as amended, or the Exchange Act, terminated. Termination of registration under the Exchange Act would substantially reduce the information required to be furnished to holders of the Merant ADSs and Merant shares and would make certain other provisions of the Exchange Act inapplicable to Merant. Such delistings and cancellation would significantly reduce the liquidity and marketability of any Merant shares in respect of which the offer has not been accepted. See paragraph 13 of Appendix 5 of this document.

WILL I HAVE APPRAISAL RIGHTS IN CONNECTION WITH THE OFFER?

Merant securityholders generally do not have appraisal rights under English law. See the section entitled **Appraisal Rights** in Appendix 6 of this document.

WILL I HAVE TO PAY ANY FEES OR COMMISSIONS?

If you are the record owner of your Merant shares and/or Merant ADSs and you accept the offer, you will not have to pay brokerage fees or similar expenses. If you own your Merant shares and/or Merant ADSs through a broker or other nominee, and your broker accepts the offer on your behalf, your broker or nominee may charge you a fee for doing so. You should consult your broker or nominee to determine whether any charges will apply.

WILL I RECEIVE CASH INSTEAD OF FRACTIONAL SERENA SHARES?

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We will not issue fractions of SERENA shares in exchange for Merant shares and Merant ADSs. To the extent that Merant securityholders are entitled to fractional shares, those fractional entitlements will be aggregated and sold in the market and the net proceeds of sale distributed pro rata to the holders of Merant shares and Merant ADSs entitled to them. In the case of holders of Merant ADSs, such payment will be made in US dollars, and in the case of holders of Merant shares, such payment will be made in pounds sterling, the applicable proceeds having been converted from US dollars at a prevailing exchange rate selected by SERENA at the relevant time. Individual entitlements to amounts of less than £2.50 (US \$4.50 based on a noon buying rate of US\$1.7993 : £1.00 as at 15 March 2004, the latest practicable date prior to the posting of this document) will not be paid to Merant securityholders, but will be retained for the benefit of the combined company.

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WILL I BE TAXED ON THE SERENA SHARES AND CASH THAT I RECEIVE?

The following paragraphs, which are intended as a general guide only and are based on current legislation and United Kingdom Inland Revenue practice (which may change) summarise the United Kingdom tax implications of acceptance of the offer for Merant securityholders who are resident or ordinarily resident in the United Kingdom for tax purposes and who hold their Merant shares as investments.

Liability to United Kingdom taxation in respect of chargeable gains will depend upon the individual circumstances of the Merant securityholder and on the form of the consideration received. To the extent that a Merant securityholder receives cash under the basic terms of the offer, this will constitute a disposal of Merant shares for the purposes of United Kingdom taxation of chargeable gains. Such a disposal may, depending upon the individual circumstances of the Merant securityholder, give rise to a liability to United Kingdom tax on chargeable gains.

A Merant securityholder will not be treated as disposing of such securityholder's Merant shares for the purposes of United Kingdom taxation of chargeable gains to the extent that, as a result of acceptance of the offer, the securityholder exchanges those shares for new SERENA shares. Instead the new SERENA shares will be treated as the same asset as the Merant shares acquired when the Merant shares were acquired. The base cost of the new SERENA shares will depend upon the proportion of SERENA shares received as compared to the proportion of cash received under the offer, but in all cases will be a proportion of the relevant shareholder's base cost for the Merant shares. Merant securityholders should note that an application for clearance has been successfully obtained from the Board of Inland Revenue under section 138 Taxation of Chargeable Gains Act 1992.

A subsequent disposal of all or any of the SERENA shares may, depending on individual circumstances, give rise to a liability to United Kingdom tax on chargeable gains.

Merant securityholders who acquire or acquired their Merant shares by exercising rights under Merant share schemes are reminded that special tax provisions may apply to them on the exercise of options or on any disposal of Merant shares acquired under a Merant share scheme, including provisions imposing a charge to United Kingdom income tax.

Any Merant securityholder or participant in a Merant share scheme who is in any doubt about such securityholder's tax position should consult such securityholder's professional advisor immediately.

For US federal income tax purposes, a US holder generally will recognise gain or loss upon the receipt of SERENA shares and cash in exchange for such holder's Merant shares or Merant ADSs pursuant to the offer in an amount equal to the difference between: (a) the sum of (i) the fair market value of such SERENA shares received, (ii) in the case of a US holder who elects to receive the cash consideration payable pursuant to the offer in the form of US dollars, the US dollar amount, and (iii) in the case of a US holder who elects to receive the cash consideration payable pursuant to the offer in the form of pounds sterling, the US dollar value on the date of receipt of the pounds sterling received, determined based on a spot rate on the date the payment is received (it is unclear whether the date of receipt for this purpose is the date that cash is made available by SERENA to the relevant payment agent or the date that cash is received by a US holder), and (b) the US holder's adjusted tax basis in the Merant shares or Merant ADSs, as the case may be.

A non-US holder generally will not recognise any gain or loss for US federal income tax purposes upon the receipt of cash and SERENA shares pursuant to the offer unless the non-US holder has certain connections to the US.

Further information regarding the application of both US and UK tax laws to Merant securityholders who accept the offer is set out in paragraphs 14 and 15 of Appendix 5 of this document.

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WHAT WILL HAPPEN TO MY MERANT SHARE OPTIONS IF THE OFFER IS COMPLETED?

The offer will extend, subject to the terms and conditions set forth in this document and acceptance form(s), to all Merant shares unconditionally allotted or issued fully paid (or credited as fully paid) upon exercise of options under the Merant share schemes while the offer remains open for acceptance (or until such earlier date as SERENA may, subject to the provisions of the City Code, determine). Further details of the proposals to be made to the holders of options under the Merant share schemes are set out in paragraph 11 of the letter from Lehman Brothers.

IF I CHOOSE TO ACCEPT THE OFFER, HOW WILL MY RIGHTS AS A SERENA STOCKHOLDER DIFFER FROM MY RIGHTS AS A MERANT SECURITYHOLDER?

An explanation of the material differences between the rights of Merant securityholders and SERENA stockholders is contained in Appendix 6 of this document.

HOW WILL THIS TRANSACTION BE TREATED FOR ACCOUNTING PURPOSES?

SERENA expects that the transaction will be accounted for using the purchase method of accounting for business combinations. Under the purchase method, the consummation of the offer will be treated as an acquisition of Merant by SERENA, and SERENA will allocate the total purchase price among the assets acquired and liabilities assumed based on their estimated fair values at the closing of the transaction.

WHERE CAN I FIND MORE INFORMATION ABOUT SERENA AND MERANT?

You can find more information about SERENA and Merant from various sources described in the section of this document entitled "Where You Can Find Additional Information."

DO I NEED TO SUBMIT A PROXY?

No. A vote of the Merant securityholders to approve the transaction is not required. **We are not asking you for a proxy and we request that you not send us a proxy.**

WHO CAN ANSWER QUESTIONS I MIGHT HAVE ABOUT THE OFFER?

If you have any questions about the offer, you should contact the Information Agent, D. F. King & Co., Inc. in the UK on 0800 917 8414 (toll free) or +44 20 7920 9700 (call collect) and in the US on 1 (800) 859-8509 (Toll-Free). If you have any questions about procedures for

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acceptance of the offer in the UK, you should contact the UK Receiving Agent, Capita IRG Plc, on 0870 162 3100 or if calling from outside the UK on +44 20 8639 2157.

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The following selected financial information for the five fiscal years ended 31 January 2003, which is presented in accordance with US GAAP, has been derived from our audited annual consolidated financial statements and should be read in conjunction with the audited annual consolidated financial statements and notes thereto in Appendix 2 and incorporated herein by reference. The following selected interim financial information for the nine month periods ended 31 October 2003 and 2002 has been derived from our unaudited interim consolidated financial statements, and should be read in conjunction with the unaudited interim financial statements and notes therein in Appendix 2 and incorporated herein by reference. The unaudited interim financial information presented below for the nine month periods ended 31 October 2003 and 2002 reflects all normal and recurring adjustments which, in the opinion of management, are necessary for a fair presentation of our results of operations and financial position.

SERENA SOFTWARE, INC. (1)

(in thousands of US Dollars, except per share amounts)

	Nine Months Ended		Year Ended 31 January				
	31 October		2003	2002	2001	2000	1999
	2003	2002	2003	2002	2001	2000	1999
Historical Consolidated Statement of Income Data:							
Total revenue	\$ 75,936	\$ 69,677	\$ 95,775	\$ 98,641	\$ 103,609	\$ 75,406	\$ 48,316
Operating income (2) (3)	21,835	22,837	32,524	25,403	35,354	21,913	12,556
Net income (2) (3)	15,384	16,411	23,154	18,509	24,254	14,644	7,330
Net income per share:							
Basic (2) (3) (4)	\$ 0.38	\$ 0.41	\$ 0.57	\$ 0.46	\$ 0.63	\$ 0.40	\$ 0.29
Diluted (2) (3) (4)	\$ 0.38	\$ 0.40	\$ 0.57	\$ 0.46	\$ 0.60	\$ 0.38	\$ 0.27
Weighted average shares used in per share calculations:							
Basic (4)	40,032	40,292	40,367	39,768	38,522	36,751	25,396
Diluted (4)	40,706	40,772	40,854	40,760	40,729	38,819	27,032
Historical Consolidated Balance Sheet Data:							
Cash, cash equivalents and short-term investments	\$ 123,689	\$ 126,529	\$ 143,074	\$ 132,594	\$ 112,658	\$ 101,144	\$ 21,469
Working capital	106,233	113,179	124,151	117,378	105,011	89,631	16,505
Total assets	250,005	250,108	264,523	231,070	203,818	149,059	59,678
Total liabilities	47,833	46,785	51,561	46,294	46,673	34,535	21,573
Total stockholders equity	202,172	203,323	212,962	184,776	157,145	114,524	38,105

(1) The selected historical financial data for all periods presented include the effects of the acquisitions of Optima Software, Inc. from 25 September 1998, Diamond Optimum Systems, Inc. from 14 June 1999, High Power Software, Inc. from 1 May 2000, UltiMIS Corporation from 18 September 2000 and TeamShare, Inc. from 5 June 2003; all of which were accounted for under the purchase method of accounting. The selected historical financial data for all periods presented also include the effects of the StarTool asset purchase from 18 August 2000.

(2)

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For the year ended 31 January 2002, we incurred restructuring costs totaling approximately \$2.5 million pre-tax, all of which were included in operating income. See Note 4(b) to SERENA's Consolidated Financial Statements contained in its Annual Report on Form 10-K for the fiscal year ended 31 January 2002.

- (3) For the years ended 31 January 2001 and 2000, we recorded acquired in-process research and development totaling approximately \$3.0 million and \$1.0 million, respectively, all of which were included in operating income. See Note 10 to SERENA's Consolidated Financial Statements contained in its Annual Report on Form 10-K for the fiscal year ended 31 January 2001.
- (4) All share and per share amounts have been adjusted to reflect the three-for-two stock split in the form of a stock dividend of SERENA's common stock effected 21 March 2000.

Table of Contents**MERANT SELECTED HISTORICAL FINANCIAL INFORMATION**

The following selected financial information for the five fiscal years ended 30 April 2003, which is presented in accordance with US GAAP and in thousands of pounds sterling, has been derived from Merant's audited annual financial statements and should be read in conjunction with the audited annual financial statements and notes thereto included in Appendix 3. The following interim selected financial information for the six month periods ended 31 October 2003 and 2002, which is presented in accordance with US GAAP and in thousands of pounds sterling, has been derived from Merant's unaudited interim financial statements and should be read in conjunction with the unaudited interim financial statements and notes thereto included in Appendix 3. The unaudited interim financial information presented below for the six months periods ended 31 October 2003 and 2002 reflects all normal and recurring adjustments which, in the opinion of management, are necessary for a fair presentation of our results of operations and financial position.

MERANT PLC

(in thousands of pounds sterling, except per share amounts)

	Six Months Ended		Year Ended 30 April				
	31 October		2003	2002	2001	2000	1999
	2003	2002	2003	2002	2001	2000	1999
Historical Consolidated Statement of Income Data:							
Revenue continuing operations	36,764	38,701	78,592	87,068	95,075	80,470	70,035
Operating income (loss)	1,324	(2,012)	2,565	(13,784)	(5,518)	(4,168)	(20,066)
Operating income (loss) from continuing operations	1,324	(2,012)	2,565	(15,185)	(2,960)	(16,445)	(15,049)
Net income (loss) for the period	1,709	(1,511)	1,123	(18,680)	(18,427)	(1,497)	(17,538)
Net income (loss) per share: basic and diluted	0.02p	(0.01)p	1.1p	(14.9)p	(13.7)p	(1.1)p	(12.6)p
Net income (loss) per share from continuing operations	0.02p	(0.01)p	0.5p	(22.9)p	(3.4)p	(9.7)p	(10.8)p
Weighted average number of shares used in computing earnings per share:							
Basic	97,992	103,129	100,739	125,263	134,305	142,163	139,588
Diluted	101,249	103,129	100,739	125,263	134,305	142,163	139,588
Historical Consolidated Balance Sheet Data:							
Cash and cash equivalents	39,226	48,904	45,538	71,620	61,200	79,543	75,394
Total assets	65,590	79,168	74,470	108,053	175,018	209,386	200,484
Shareholders' equity	24,544	24,028	25,131	39,483	72,440	102,977	95,136
Total number of shares in issue	105,269	103,261	103,936	115,027	134,963	149,389	143,673
Share capital	2,105	2,102	2,078	2,300	2,699	2,988	2,873
Historical Consolidated Financial Condition Data:							
Working capital	16,827	21,070	20,226	38,619	19,454	51,867	53,486

Table of Contents**MERANT SELECTED HISTORICAL FINANCIAL INFORMATION**

The following selected financial information for the five fiscal years ended 30 April 2003, which is presented in accordance with UK GAAP and in thousands of pounds sterling, has been derived from Merant's audited annual consolidated financial statements and should be read in conjunction with the audited annual consolidated financial statements and notes thereto included in Appendix 3. The following unaudited interim selected financial information for the six month periods ended 31 October 2003 and 2002, which is presented in accordance with UK GAAP and in thousands of pounds sterling, has been derived from Merant's unaudited interim financial statements and should be read in conjunction with the unaudited interim financial statements and notes thereto included in Appendix 3. The unaudited interim financial information presented below for the six months periods ended 31 October 2003 and 2002 reflects all normal and recurring adjustments which, in the opinion of management, are necessary for a fair presentation of our results of operations and financial position.

MERANT PLC

(in thousands of pounds sterling, except per share amounts)

	Six Months Ended		Year Ended 30 April				
	31 October		2003	2002	2001	2000	1999
	2003	2002					
Historical Consolidated Statement of Income Data:							
Turnover	36,764	38,701	78,592	118,275	215,433	227,283	186,104
Operating profit (loss)	319	(11,330)	(10,692)	(45,398)	(39,762)	(38,132)	(8,511)
Operating profit (loss) from continuing operations	319	(11,330)	(10,692)	(41,953)	(28,798)	(41,456)	(16,036)
Profit (loss) for the period	704	(13,204)	(12,498)	(62,026)	(50,914)	(35,461)	(18,710)
Profit (loss) per share: basic and diluted	0.7p	(12.8)p	(12.4)p	(49.6)p	(37.9)p	(24.9)p	(15.8)p
Weighted average number of shares used in computing earnings per share:							
Basic	97,992	103,129	100,739	125,092	134,305	142,163	114,709
Diluted	101,249	103,129	100,739	125,092	134,305	142,163	114,709
Historical Consolidated Balance Sheet Data:							
Cash and bank deposits	39,226	48,904	45,538	71,620	61,200	79,543	75,394
Total assets	75,088	87,126	82,655	127,785	231,044	304,893	322,457
Total shareholders funds	34,042	31,986	33,316	59,215	128,466	198,484	217,109
Total number of shares in issue	105,269	103,261	103,936	115,027	134,963	149,389	143,673
Share capital	2,105	2,102	2,078	2,300	2,699	2,988	2,873
Historical Consolidated Financial Condition Data:							
Working capital	16,827	21,070	20,226	38,619	19,454	51,867	53,486

Table of Contents**EXCHANGE RATE INFORMATION**

The financial statements of Merant are prepared in pounds sterling. The following table sets forth, for the periods indicated, information concerning the exchange rate as reported in *The Financial Times*, expressed in US dollars per pound sterling. The average rate is calculated by using the closing rates in *The Financial Times* on the last day during a monthly period, and on the last day of each month during an annual period. This is different than the source of the exchange rate used in calculating the value of the transaction. The transaction was valued using the exchange rate derived from the noon buying rate in New York City for cable transfers in pounds sterling as certified for customs purposes by the Federal Reserve Bank of New York.

	<u>HIGH</u>	<u>LOW</u>	<u>END</u>	<u>AVERAGE RATE</u>
NINE MONTHS ENDED 31 OCTOBER 2003	1.70	1.58	1.70	1.62
	<u>HIGH</u>	<u>LOW</u>	<u>END</u>	<u>AVERAGE RATE</u>
YEAR ENDED 30 APRIL				
2003	1.65	1.46	1.60	1.56
2002	1.48	1.41	1.46	1.44
2001	1.52	1.42	1.44	1.47
2000	1.64	1.58	1.58	1.61
1999	1.70	1.60	1.61	1.65

As at 15 March 2004, the latest practicable dealing date prior to the posting of this document, the exchange rate as reported in *The Financial Times* for pounds sterling was \$1.7950. No representation is made that the amounts of sterling presented in this document have been, could have been or could be converted into US dollars at the rates indicated above.

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ILLUSTRATIVE COMPARATIVE PER SHARE DATA

The following table presents historical net income and book value for SERENA and Merant individually. The table also presents unaudited pro forma per share data for SERENA and Merant. The unaudited pro forma earnings and book value per share data give effect to the business combination as if it occurred on 31 October 2003 for balance sheet purposes and 1 February 2002 for income statement purposes and are based on the Unaudited Pro Forma Condensed Combined Financial Information included in Appendix 4 to this document.

The historical stockholders' equity per SERENA share is computed by dividing stockholders' equity by the weighted average number of SERENA shares outstanding at the end of the period. The pro forma combined stockholders' equity per SERENA share is computed by dividing pro forma stockholders' equity by the pro forma weighted average number of SERENA shares outstanding at the end of the period. Neither SERENA nor Merant has declared or paid cash dividends on its common stock.

Historical book value per share for Merant is computed by dividing total stockholders' equity on a US GAAP basis by the weighted average number of shares of Merant common stock outstanding at the end of each period. The equivalent pro forma information was obtained by multiplying the pro forma earnings per common share and pro forma stockholders' equity per common share by the exchange ratio of 0.04966, so that the per share amounts are equated to the respective values for one share of Merant.

The unaudited pro forma data are based on the terms of the business combination in which SERENA will offer cash and new SERENA shares for the Merant shares. The information in the table below should be read in conjunction with the respective audited and unaudited consolidated financial statements of SERENA and Merant, including the notes thereto and the Unaudited Pro Forma Condensed Combined Financial Information included in Appendix 4 to this document.

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	NINE MONTHS ENDED 31 OCTOBER 2003	YEAR ENDED 31 JANUARY 2003
SERENA HISTORICAL		
Earnings per common share:		
Basic	\$ 0.38	\$ 0.57
Diluted	\$ 0.38	\$ 0.57
Stockholders' equity per common share:		
Basic	\$ 5.05	\$ 5.28
Diluted	\$ 4.97	\$ 5.21
MERANT HISTORICAL		
Earnings per common share:		
Basic	\$ 0.05	\$ (0.15)
Diluted	\$ 0.05	\$ (0.15)
Stockholders' equity per common share:		
Basic	\$ 0.42	\$ 0.50
Diluted	\$ 0.41	\$ 0.50
SERENA PRO FORMA COMBINED COMPANY		
Earnings per common share:		
Basic	\$ 0.06	\$ (0.58)
Diluted	\$ 0.06	\$ (0.58)
Stockholders' equity per common share:		
Basic	\$ 6.77	
Diluted	\$ 6.68	
MERANT PRO FORMA EQUIVALENT PER SHARE INFORMATION		
Earnings per common share:		
Basic	\$ 0.00	\$ (0.03)
Diluted	\$ 0.00	\$ (0.03)
Stockholders' equity per common share:		
Basic	\$ 0.34	
Diluted	\$ 0.33	

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RISK FACTORS

By accepting the offer, holders of Merant shares and Merant ADSs will be choosing to invest in SERENA shares. In considering whether to accept the offer, you should consider carefully the following factors, and the other risks and information contained in the documents incorporated by reference, especially the risks described in SERENA's Quarterly Report on Form 10-Q for the period ended 31 October 2003 and the risks described in Merant's Annual Report on Form 20-F for the year ended 30 April 2003. See Where You Can Find Additional Information for where you can find the additional risk factors and other information incorporated by reference in this document.

As used below, we or us refers to SERENA or, after the consummation of our offer as described in this document, SERENA and Merant, as the context requires.

RISKS RELATING TO OUR PROPOSED OFFER

Market fluctuations may reduce the market value of the consideration we are offering to you because the exchange ratio contemplated by our offer is fixed.

The consideration in our offer consists in part of a specified number of SERENA shares, or a fraction of a SERENA share, subject to the mix and match election procedures, rather than a number of SERENA shares, or a fraction of a SERENA share, with a specified value. The value of a SERENA share for these purposes is based on an exchange rate of US\$1.8488 : £1.00, which is calculated as the average of the US dollar /pound sterling noon buying rate for the five trading days ended 3 March 2004 and price per SERENA share of US\$21.78, which is calculated as the average of the closing prices of one SERENA share as reported on Nasdaq for the 20 US trading days ended 1 March 2004. Any fluctuation in the market price of SERENA shares or the pound sterling/dollar exchange rate between now and the closing of our offer will change the value of the SERENA shares that you will receive. Therefore, the value of the SERENA shares that you will receive could be higher or lower than the price on which the determination was based. In addition, SERENA may not trade on a comparable basis to its historical trading performance prior to the consummation of our offer. For information regarding the range of trading prices of SERENA shares on Nasdaq, please refer to Appendix 5.

If you elect the mix and match feature, you may not receive all consideration in the form you have requested.

Our offer contains a mix and match election feature, whereby Merant securityholders who validly accept the offer may request to receive either more SERENA shares or more cash than the standard entitlement. However, elections by Merant securityholders will be satisfied only to the extent that off-setting elections have been made by other Merant securityholders in our offer. In other words, in order for a Merant securityholder to receive a higher proportion of cash, other Merant securityholders will have to elect to receive a higher proportion of SERENA shares, and vice versa. To the extent that elections cannot be satisfied as a result of a lack of such off-setting elections, entitlements to SERENA shares and cash in excess of the standard entitlement will be reduced on a pro rata basis. Once the share allocations have been determined, the cash element of the consideration will be reduced or increased (as the case may be) for each holder of Merant shares or Merant ADSs who has been allocated an increased or reduced number of SERENA shares. All calculations will be made by reference to the number of acceptances and elections as at the fifth calendar day after the offer is declared or becomes wholly unconditional and, for the purposes of these calculations, the assumed value per Merant share will be 195 pence and the assumed value per SERENA share shall be £11.78. We describe our procedures for election and proration in Part B of Appendix 1.

This transaction may adversely affect the liquidity and value of non-tendered Merant shares and Merant ADSs.

In the event that not all of the Merant shares and Merant ADSs are acquired pursuant to the offer, the number of securityholders and the number of Merant shares and Merant ADSs held by individual holders will be

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greatly reduced. As a result, the closing of our offer would adversely affect the liquidity and may adversely affect the market value of the remaining Merant shares and Merant ADSs held by the public. Subject to London Stock Exchange and Nasdaq delisting rules, we may delist the Merant shares on the London Stock Exchange and delist the Merant ADSs on Nasdaq. As a result of the delisting, Merant shares and Merant ADSs not acquired pursuant to our offer may become illiquid and may be of reduced value.

If SERENA encounters difficulties integrating the business operations of SERENA and Merant, it could adversely affect the business of the combined company.

We intend, to the extent possible, to integrate our operations with those of Merant. Our goal in integrating these operations is to increase earnings and achieve cost savings by taking advantage of the significant anticipated synergies of consolidation and enhanced growth opportunities. We anticipate incurring severance payments and other employee related costs, costs for lease terminations, meetings, trainings, rebranding, integration of information technology systems, and other costs in connection with the integration of SERENA and Merant. We cannot be sure that we will not encounter substantial difficulties integrating our operations with Merant's operations, resulting in a delay or the failure to achieve the anticipated synergies and, therefore, the expected increases in earnings and cost savings. The difficulties of combining the operations of the two companies include, among other things:

possible inconsistencies in standards, controls, procedures and policies, business cultures and compensation structures between SERENA and Merant;

coordinating and consolidating ongoing and future research and development efforts;

consolidating corporate and administrative infrastructure, particularly in light of Merant's complex corporate structure;

integrating and managing the technologies and products of the two companies, including consolidating and integrating computer information systems;

consolidating sales and marketing operations;

retaining existing customers and attracting new customers;

retaining strategic partners and attracting new strategic partners;

retaining key employees;

retaining and integrating distributors and key sales representatives;

identifying and eliminating redundant and underperforming operations and assets;

using capital assets efficiently to develop the business of the combined company;

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minimising the diversion of management's attention from ongoing business concerns;

coordinating geographically separate organisations;

possible tax costs or inefficiencies associated with integrating the operations of the combined company;

possible modification of operating control standards in order to comply with the Sarbanes-Oxley Act of 2002 and the rules and regulations promulgated thereunder; and

retaining and attracting new employees to support existing and new products and new technology development.

For these reasons, we may fail to complete successfully the necessary integration of SERENA and Merant, or to realise any of the anticipated benefits of the integration of the two companies. Actual cost savings and synergies may be lower than we currently expect and may take a longer time to achieve than we currently anticipate.

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Whether or not the offer is completed, the announcement of the offer may cause disruptions, including potential loss of customers, suppliers and other business partners, in the business of SERENA or Merant, which could have material adverse effects on each company's or the combined company's business and operations.

Whether or not the offer is completed, SERENA's and Merant's customers, suppliers, distributors, licensors and other business partners, in response to the announcement of the offer, may adversely change or terminate their relationships with either company or the combined company, which could have a material adverse effect on the business of the company concerned. Certain of SERENA's or Merant's current or potential customers may cancel or defer orders for each company's products. In addition, customers of both companies may expect re-negotiated pricing as a result of the offer or the announcement of the offer. The announcement of the offer may also adversely affect the companies' ability to attract new customers.

Some of the contracts with suppliers, distributors, system integrators, customers, licensors, facility owners and other business partners require SERENA or Merant to obtain consent from these other parties in connection with the offer. If their consent cannot be obtained on favourable terms, the combined company may incur higher costs related to replacing suppliers, may suffer a loss of potential future revenue and may lose rights to facilities or intellectual property that are material to the business of the combined company.

Charges to earnings resulting from the acquisition, including the application of the purchase method of accounting, and restructuring and integration costs may materially adversely affect the market value of SERENA shares following the acquisition.

In accordance with US GAAP, the combined company will account for the acquisition using the purchase method of accounting. The combined company will allocate the total estimated purchase price to Merant's net tangible assets, amortisable intangible assets, and in-process research and development based on their fair values as at the date of completion of the acquisition, and record the excess of the purchase price over those fair values as goodwill. The combined company's financial results, including earnings per share, could be adversely affected by a number of financial adjustments required by US GAAP including the following:

The portion of the existing deferred revenues on Merant's balance sheet at the closing of the acquisition which represents maintenance revenue will be adjusted, based on estimated cost to deliver plus an appropriate gross margin.

The portion of the estimated purchase price allocated to in-process research and development will be expensed by the combined company in the quarter in which the acquisition is completed.

The combined company will incur additional amortisation expense over the estimated useful lives of certain of the intangible assets acquired in connection with the acquisition during such estimated useful lives.

To the extent the value of goodwill or intangible assets with indefinite lives becomes impaired, the combined company may be required to incur material charges relating to the impairment of those assets.

We expect to incur costs associated with combining the operations of the two companies, including advisors' fees and other costs related to the offer and the acquisition. These costs may be substantial and may include those related to the severance and stock option acceleration provisions of Merant's employee benefit plans, which could be triggered by the acquisition. We also face potential costs related to employee redeployment or relocation, employee retention which could include salary increases, bonuses or option grants, reorganisation or closure of facilities, relocation and disposal of excess equipment, termination of contracts with third parties that provide redundant or conflicting services and other

integration costs. We have not yet determined the amount of these costs. We expect to account for these costs as purchase related adjustments when the acquisition is completed, which will decrease our net income and impact cash balances for the periods in which those adjustments are made. Each of these charges would negatively impact earnings, which could have a material adverse effect on the price of SERENA shares.

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Upon your receipt of SERENA shares in our offer, you will become a stockholder in a Delaware corporation, which will change certain shareholder rights and privileges you hold as a shareholder of an English company.

SERENA is governed by the laws of the US, the State of Delaware and by its restated certificate of incorporation, as amended, and by-laws. The Delaware General Corporation Law, referred to as the DGCL, extends to stockholders certain rights and privileges that may not exist under UK law and, conversely, does not extend certain rights and privileges that you may have as a shareholder of a company governed by UK law. The directors of a Delaware corporation may elect to adopt certain provisions that have the effect of discouraging a third party from acquiring control of SERENA. Such provisions could limit the price that some investors might be willing to pay in the future for SERENA shares. These Delaware provisions may also have the effect of discouraging or preventing certain types of transactions involving an actual or a threatened change in control of SERENA, including unsolicited takeover attempts, even though such a transaction may offer SERENA stockholders the opportunity to sell their SERENA shares at a price above the prevailing market price. For a detailed discussion of the rights of SERENA stockholders versus the rights of holders of Merant shares or Merant ADSs, see our discussion in the section captioned "Description of SERENA shares and changes in the rights of Merant securityholders" in Appendix 6 of this document.

The market price of SERENA shares may decline as a result of our offer.

The market price of SERENA shares may decline as a result of our offer if:

the integration of Merant's business is unsuccessful;

we do not achieve the expected benefits of our acquisition of Merant as rapidly or to the extent anticipated by financial analysts or investors; or

the effect of our acquisition of Merant on our financial results is not consistent with the expectations of financial analysts or investors.

We estimate that the number of SERENA shares that will be issued on full acceptance of our offer will not be more than 5.9 million, representing approximately 13.3 per cent. of the issued and outstanding SERENA shares, as increased as a result of the offer, calculated as at 15 March 2004. The increase in the number of SERENA shares issued may lead to sales of such shares or the perception that such sales may occur, either of which may adversely affect the market for, and the market price of, SERENA shares.

Full integration of our operations with Merant's operations may not be achieved if we cannot effect the compulsory acquisition of all of the issued and outstanding Merant shares, including shares represented by Merant ADSs, which could adversely affect our ability to realise some or all of the anticipated benefits of the acquisition.

Our offer is subject to a condition that, before the end of our offer period, valid acceptances have been received and not properly withdrawn in respect of at least 90 per cent. of the Merant shares, including shares represented by Merant ADSs, to which the offer relates. To effect the compulsory acquisition of all of the Merant shares to which the offer relates, including shares represented by Merant ADSs to which the offer relates, under UK law, we are required to have acquired at least 90 per cent. of all of the shares of Merant, including shares represented by Merant ADSs. It is possible that, at the end of our offer period, we will not hold a sufficient number of Merant shares, including shares represented by Merant ADSs, to effect a compulsory acquisition of the remaining outstanding Merant shares, including shares represented by Merant ADSs. This could prevent or delay us from realising some or all of the anticipated benefits from the integration of our operations with

Merant's operations.

We expect our offer to trigger certain change of control payments in the employment agreements of certain members of Merant's senior management, which will increase our expenses for the transaction.

The employment agreements of certain members of Merant's senior management contain change of control clauses providing for compensation to be paid in the event the employment agreements of these employees are

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terminated following the consummation of our offer should their respective positions with Merant be materially changed. If successful, our offer would effect such a change of control, thereby giving rise to potential change of control payments.

Antitrust and competition authorities in various jurisdictions may attempt to delay or prevent our acquisition of voting and control rights or may require divestitures, which could adversely affect our ability to consummate the offer.

Under the HSR Act, the transaction may not be consummated unless certain filings have been submitted to the Federal Trade Commission, referred to as the FTC, and the Antitrust Division of the Department of Justice, referred to as the Antitrust Division, and certain waiting period requirements have been satisfied. In addition, the transaction may be subject to review by competition authorities in jurisdictions in which it is not subject to mandatory notification requirements. SERENA and Merant have made these required filings. In addition, completion of the offer is subject to various foreign antitrust laws, though we do not expect to need to make filings except under the HSR Act. We cannot be sure that antitrust enforcers in jurisdictions that have the authority to review the transaction will allow the transaction to proceed without first seeking additional information pursuant to a Request for Additional Information and Documentary Material, referred to as a second request, or similar process or that approvals for the transaction will be obtained at all or without materially adverse restrictions or conditions that would have an adverse effect on the combined company. In addition, it is a condition to the consummation of our offer that we are not required to sell or divest any of our assets or business and that we are not prohibited from owning any portion of the Merant business or assets, to an extent that is material to Merant and its affiliates, taken as a whole, or SERENA and its subsidiaries, taken as a whole.

The FTC and the Antitrust Division frequently scrutinise the legality under the antitrust laws of transactions like the offer. At any time before or after the completion of the offer, the FTC or the Antitrust Division could take any action under the antitrust laws as it deems necessary or desirable in the public interest, including seeking to enjoin the offer or completion of the compulsory acquisition or seeking the divestiture of substantial assets of SERENA or Merant. There can be no assurance that we will receive a favourable result if such a challenge is made. State attorneys general may also bring legal action under the antitrust laws, and private parties may bring such actions under certain circumstances.

The cash portion of the consideration to be paid in our offer to Merant securityholders who accept the offer is based on a fixed amount of pounds sterling and, therefore, SERENA is subject to currency fluctuations through the payment date.

Because SERENA will pay all holders of Merant shares in pounds sterling, SERENA must buy pounds sterling with US dollars at the prevailing exchange rate on the payment date. As a result, the actual amount of US dollars required to buy a sufficient amount of pounds sterling to pay the cash portion of the consideration to such holders will depend upon the exchange rate prevailing on the business day on which the funds are made available by SERENA to the UK Receiving Agent. Additionally, because the cash portion of the consideration payable in the offer is a fixed amount of pounds sterling, the actual amount of US dollars that SERENA will pay with respect to the cash portion of the consideration will depend upon the exchange rate prevailing on the business day on which the funds are made available by SERENA to the US Depository. Therefore, SERENA is subject to the risk of fluctuations in the dollar/pound sterling exchange rate.

Holders of Merant shares who elect to receive cash consideration in US dollars and holders of Merant ADSs who do not elect to receive cash consideration in pounds sterling will be subject to exchange rate risk.

If holders of Merant shares elect to receive cash consideration in US dollars, or holders of Merant ADSs do not elect to receive cash consideration in pounds sterling, the cash amount payable in pounds sterling to which such person would otherwise be entitled pursuant to the terms of the offer will be converted, subject to conversion expenses, from pounds sterling to US dollars at the exchange rate obtainable on the spot market in

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London at approximately noon (London time) on the date the cash consideration is made available by SERENA to the relevant paying agent for delivery in respect of the applicable Merant securities. The actual amount of US dollars received by any Merant securityholder that receives cash consideration in US dollars will depend on the exchange rate prevailing on the day on which funds are made available to the relevant payment agent by SERENA, so such Merant securityholders will be subject to the risk that exchange rate fluctuations could change the amount of US dollars they receive.

Merant executive officers and directors have interests other than as Merant securityholders that may influence them to support the offer.

In considering the recommendation of the Merant directors to accept the offer and tender your Merant shares, you should recognise that Merant directors and officers have interests in the offer that differ from, or are in addition to, their interests as Merant securityholders. These interests include:

current and future employment arrangements;

severance benefits if their employment is terminated after the acquisition;

for the following directors, officers or employees of Merant, full acceleration of their stock options as a result of the acquisition: Gerald Perkel, Scott Hildebrant, Stephen King, Diane Williams, Robert Blaskowsky, Stephen Going, Robert Dunne, Brian Unruh and William Rees Withers; and

the fact that one Merant director, Gerald Perkel, will become a director of SERENA upon completion of the acquisition.

See paragraph 8 of Appendix 5.

Failure to complete the offer could be costly to Merant and its securityholders.

If the offer is not completed for any reason, Merant could suffer a number of consequences that may adversely affect its business, results of operations and stock price, including the following:

the market price of Merant shares may decline, assuming that current market prices reflect a market assumption that the offer will be completed;

the benefits expected from becoming a part of a combined company with SERENA will not be realised;

activities relating to the offer and related uncertainties may divert management's attention from the day-to-day business and cause disruptions among employees and to relationships with customers and business partners, thus detracting from Merant's ability to grow revenue and minimise costs and possibly leading to a loss of revenue and market position that may not be regained if the transaction does not occur;

difficulty continuing Merant's present level of operations, requiring it to scale back the present level of business and consider reductions in force;

disruption of its employee, customer and business partner base; and

an inability to take advantage of alternative business opportunities or effectively respond to competitive pressures.

In addition, under certain circumstances, Merant has agreed to pay us a fee of approximately £2.06 million (US\$3.71 million based on the noon buying rate of US\$1.7993: £1.00 as at 15 March 2004, the latest practicable date prior to the posting of this document). See paragraph 6 of Part B of Appendix 1.

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The acquisition may be completed even though material adverse changes may result from the announcement of the offer, industry-wide changes and other causes, which could adversely affect SERENA's business and financial condition.

Pursuant to the terms of the offer, we may refuse to complete the offer if there is a material adverse change affecting Merant before the closing. However, we will need to obtain the consent of the Panel to invoke certain of our conditions to closing the transaction. The Panel could refuse to permit us to invoke a condition to closing if it feels that SERENA knew or should have known such material adverse change might exist and/or that the change is not material in the context of Merant and its affiliates, taken as a whole, SERENA and its subsidiaries, taken as a whole and/or the offer.

If material adverse changes occur but we must still complete the offer, our stock price may suffer or our business or financial condition may be harmed. This in turn may reduce the value of the consideration paid to Merant securityholders in the offer.

The price of SERENA shares may be affected by factors different from those affecting the price of Merant shares and Merant ADSs.

When the acquisition is completed, Merant securityholders will become holders of SERENA shares. SERENA's business differs from that of Merant, and SERENA's results of operations, as well as the price of SERENA shares may be affected by factors different from those affecting Merant's results of operations and the price of Merant shares and Merant ADSs.

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WHERE YOU CAN FIND ADDITIONAL INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC. Merant files annual and current reports with the SEC and pursuant to the Companies Act. You may read and copy any reports, statements or other information that we and Merant file at the SEC's public reference room at 450 Fifth Street, N.W., Washington, D.C. 20549. Please call the SEC at 1 (800) 732-0330 for further information regarding the public reference room. SERENA's and Merant's public filings also are available to the public from commercial document retrieval services and at the internet website maintained by the SEC at <http://www.sec.gov>.

We have filed a registration statement on Form S-4 to register with the SEC the offering and sale of SERENA shares to be issued to Merant securityholders pursuant to our offer. This document is a part of that registration statement. Upon commencement of the offer, we will file with the SEC a statement on Schedule TO pursuant to Rule 14d-3 under the Exchange Act to furnish certain information about the offer and Merant will file with the SEC a Solicitation/Recommendation Schedule 14D-9 regarding the offer.

As allowed by SEC rules, this document does not contain all of the information that you can find in the registration statement or the exhibits to the registration statement. The SEC allows us to incorporate information into this document by reference, which means that we can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is deemed to be part of this document, except for any information superseded by information contained directly in this document. This document incorporates by reference the documents set forth below that SERENA and Merant have previously filed with the SEC. These documents contain important information about SERENA and Merant and their financial condition.

SERENA Filings (File No. 000-25285):	Period
Annual Report on Form 10-K	Year ended 31 January 2003, as filed on 29 April 2003
Quarterly Reports on Form 10-Q	Quarter ended 30 April 2003, as filed on 13 June 2003; Quarter ended 31 July 2003, as filed on 12 September 2003; and Quarter ended 31 October 2003, as filed on 8 December 2003
Current Reports on Form 8-K	Filed on 20 May 2003; 22 May 2003; 5 August 2003; 21 August 2003; 21 November 2003; 8 December 2003; 10 December 2003; and 20 February 2004
Definitive Proxy Statement on Schedule 14A for 2003 Annual Meeting of Stockholders	Filed on 19 May 2003
Registration Statement on Form 8-A	Filed on 22 January 1999
Merant Filings (File No. 000-19696):	Period
Annual Report on Form 20-F	Year ended 30 April 2003, as filed on 27 October 2003

All additional documents that SERENA or Merant may file with the SEC pursuant to Section 13(a), 13(c), 14 or 15(d) of the Exchange Act after the date of this document and prior to the earliest of the date of the completion of the offer or the earlier termination of the offer, shall also be deemed to be incorporated by reference. These include, but are not limited to, periodic reports, such as annual reports on Form 10-K or 20-F, quarterly reports on Form 10-Q and current reports on Form 8-K, as well as proxy statements; provided, however, that we are not incorporating any information furnished under either Item 9 or Item 12 of any current report on Form 8-K.

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We have supplied all information contained or incorporated by reference in this document relating to us and Merant has supplied all such information relating to Merant.

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You can obtain any of the documents we are incorporating by reference through us, the SEC or the SEC's Internet website as described above. Documents incorporated by reference are available from us without charge, excluding all exhibits unless we have specifically incorporated by reference an exhibit in this document. You may obtain documents incorporated by reference in this document by requesting them in writing or by telephone from us at the following address:

D.F. KING & CO., INC.

North America
48 Wall Street

New York, NY 10005

Toll Free: 1 (800) 859-8509

Banks and Brokers: 1 (212) 269-5550

Europe

No. 2 London Wall Buildings

London Wall, London EC2M 5PP

Toll Free, UK: 0800 917 8414

Call Collect: +44 20 7920 9700

If you request any incorporated documents from us, we will mail them to you by first-class mail, or other equally prompt means, within one business day of receipt of your request.

You should rely only on the information contained or incorporated by reference in this document to decide whether to accept the offer. We have not authorised anyone to provide you with information that is different from what is contained in this document. You should not assume that the information contained in this document is accurate as at any date other than the date on the front of this document unless the information specifically indicates that another date applies, and neither the mailing of this document to the Merant securityholders nor the issuance of SERENA shares pursuant to the offer shall create any implication to the contrary.

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LETTER OF RECOMMENDATION FROM THE CHAIRMAN OF

MERANT plc

(incorporated in England and Wales with registered number 1709998)

Abbey View

Everard Close

St. Albans, Herts, AL12PS

United Kingdom

18 March 2004

To all holders of Merant plc securities and, for information only, to participants in the Merant share schemes

SERENA SOFTWARE, INC.

RECOMMENDED CASH AND SHARE OFFER FOR

THE ENTIRE ISSUED AND TO BE

ISSUED SHARE CAPITAL OF

MERANT PLC

Dear Securityholder,

1. INTRODUCTION

On 3 March 2004, we announced that your board and the board of SERENA had reached agreement on the terms of a recommended cash and share offer for the entire issued and to be issued share capital of Merant. I am writing to explain the background to the transaction and the reasons why the Merant board of directors unanimously recommends that Merant securityholders accept the offer.

Further details of the offer are set out in the letter from Lehman Brothers and in Appendix 1 of this document.

2. TERMS OF THE OFFER

The offer, which is subject to the conditions and further terms set out in the letter from Lehman Brothers, Appendix 1 and the accompanying form of acceptance or letter of transmittal is made on the following basis:

for every 1 Merant share	136.5 pence in cash and 0.04966 of a new SERENA share
for every 1 Merant ADS (each Merant ADS representing 5 Merant shares)	682.5 pence in cash and 0.2483 of a new SERENA share

The offer is based on a valuation of 195 pence for each Merant share. On this basis, the offer values the entire issued share capital of Merant at approximately £206 million (US\$380 million). This is based on an exchange rate of US\$1.8488 : £1.00, calculated at the average of the US dollar / pound sterling noon buying rate for the five trading days ended 3 March 2004 and the price per SERENA share of US\$21.78, calculated as the average of the closing prices of one SERENA share as reported on Nasdaq for the twenty United States trading days ended 1 March 2004. As at 31 January 2004 Merant had net cash and equivalents of £38.8 million (US\$70.7 million based on an exchange rate of US\$1.8202 : £1.00).

SERENA is offering a mix and match election under which Merant securityholders who validly accept the offer may request to vary the proportions in which they receive SERENA shares and cash in respect of their Merant shares and Merant ADSs. A shareholder who successfully elects all cash would receive 195 pence in cash for every 1 Merant share. A shareholder who successfully elects to receive all SERENA shares would receive 0.16553 of a new SERENA share for every 1 Merant share.

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At 195 pence for each Merant share, the offer represented a premium of approximately:

25 per cent. to the middle market closing price of 155.5 pence per Merant share on 2 March 2004, the last dealing day prior to the announcement of the offer; and

34 per cent. to the average daily middle market closing price of 145.8 pence per Merant share for the three months ended 2 March 2004.

On 15 March 2004 (the latest practicable date prior to the posting of this document), at the then prevailing noon buying rate of US\$1.7993: £1.00 and a SERENA share price of \$19.68, the offer values each Merant share at 190.8 pence, representing a premium of approximately 23 per cent. to the middle market closing price of 155.5 pence per Merant share on 2 March 2004, the last dealing day prior to the announcement of the offer.

3. BACKGROUND TO AND REASONS FOR RECOMMENDING ACCEPTANCE OF THE OFFER

The acquisition of Merant by SERENA will create the second largest provider of ECM software solutions, serving the complex change management needs of at least 46 of the Fortune 50 largest companies worldwide, with a resulting combined installed base of over 15,000 customers. SERENA believes this installed base will provide the combined company with distribution leverage to cross sell products, expand into new geographies, create new opportunities in channel development and generate a profitable and steady maintenance revenue stream.

The combination brings together two leaders in ECM with the complementary strengths of SERENA on mainframe platforms and Merant on distributed systems and similar visions for future market share expansion.

The boards of directors of SERENA and Merant believe the combination should deliver significant strategic benefits and provide opportunities to reduce expenses and that the combined company would:

create the leading ECM vendor with integrated software solutions running on all major operating systems, from the mainframe to UNIX, LINUX and NT distributed systems environments all the way to the worldwide web;

combine SERENA's market leading mainframe SCM product, with Merant's market leading enterprise distributed SCM product;

deepen and strengthen the customer base by combining SERENA's more than 3,600 customers with Merant's more than 15,000 customer accounts;

accelerate SERENA's ability to offer customers its vision of application life cycle management solutions branded as SERENA's Application Framework for Enterprises (SAFE), thereby accessing larger markets and enabling the combined company to compete more effectively; and

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offer significant potential cost savings in the areas of overlap such as dual exchange listing, dual public company compliance obligations and dual administrative infrastructures as well as a number of other duplicative areas and initiatives.

Both SERENA and Merant have been pursuing similar strategies and strategic investments to enable the application of change management technology beyond SCM to broader applications within information technology.

4. MANAGEMENT AND EMPLOYEES

SERENA recognises the importance to Merant's business of the skills and experience of Merant's management team and employees.

SERENA has given assurances to the Merant board that the existing employment rights, including pension rights, of the management and employees of Merant will be fully honoured.

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Gerald Perkel, president and chief executive officer of Merant, has agreed to join the board of SERENA as a director subject to the offer becoming or being declared unconditional in all respects.

5. CURRENT TRADING

On 3 March 2004, Merant announced its financial results for the third quarter of fiscal 2004. The statement on the business outlook is set out in Appendix 3.

6. TAXATION

Your attention is drawn to paragraphs 16 and 17 of the letter from Lehman Brothers headed *United Kingdom Taxation* and *United States Federal Taxation*. This information is included as guidance only and you should consult an independent professional advisor in light of your particular circumstances.

7. MERANT SHARE SCHEMES

The offer will extend, subject to the terms and conditions set forth in this document and acceptance form(s), to all Merant shares unconditionally allotted or issued fully paid (or credited as fully paid) upon exercise of options under the Merant share schemes while the offer remains open for acceptance (or until such earlier date as SERENA may, subject to the provisions of the City Code, determine). Further details of the proposals to be made to the holders of options under the Merant share schemes are set out in paragraph 11 of the letter from Lehman Brothers.

8. IRREVOCABLE UNDERTAKINGS AND CONFIRMATIONS OF INTENT TO ACCEPT THE OFFER

SERENA has received irrevocable undertakings to accept the offer representing approximately 7.4 per cent. of Merant's existing issued share capital. SERENA has also received confirmations of intent to accept the offer, representing in aggregate approximately 27.3 per cent. of Merant's existing issued share capital. The Merant securityholders from whom SERENA has received undertakings and confirmations of intent (including a confirmation of intent from Schroder Investment Management Limited), hold an aggregate of 34.61 per cent. of the issued share capital of Merant as at 15 March 2004.

Merant directors have irrevocably undertaken to accept the offer in respect of their own beneficial holdings, comprising 381,389 Merant shares in aggregate (representing approximately 0.36 per cent. of Merant's existing issued share capital). Merant Trustees Limited has irrevocably undertaken to accept the offer in respect of its beneficial holdings, comprising 7,415,488 Merant shares (representing approximately 7.0 per cent. of Merant's existing issued share capital).

One Merant director, Gerald Perkel, has also irrevocably undertaken to accept the offer in respect of all Merant shares he receives as a result of the exercise of options during the period whilst the offer is open for acceptance, representing up to 1,500,000 Merant shares. No other Merant

director holds any options over Merant shares.

The undertakings provided by the Merant directors cease to be binding only if the offer lapses or is withdrawn. The undertaking provided by Merant Trustees Limited ceases to be binding in the same circumstances as those provided by the Merant directors but in addition will lapse if a higher offer is made by a third party (i) which is recommended by Merant and SERENA has not increased its offer within 7 days; or (ii) which is declared unconditional in all respects.

The confirmations of intent are non-legally binding statements of current intention. See paragraph 5 to the letter from Lehman Brothers for further details regarding the undertakings.

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9. INDUCEMENT FEE

In consideration of, and as an inducement to, SERENA making the offer, Merant has agreed to pay SERENA a fee of £2.06 million (US\$3.71 million based on a noon buying rate of US\$1.7993 : £1.00 as at 15 March 2004, the latest practicable date prior to the posting of this document) in the circumstances described below. Save in the following limited circumstances: failure to obtain approval for the offer under the HSR Act or other applicable antitrust law, withdrawal of the offer without consent of the Panel or material breach (and failure to cure) by SERENA of the Inducement Agreement, this fee is payable on either of the following events:

- (a) if a higher competing offer or other competing transaction (or an intention to do either) is publicly announced by a third party and the Merant board fails to reaffirm its unanimous recommendation of the offer and subsequently the offer lapses or is withdrawn; or
- (b) if the board of Merant withdraws or modifies its recommendation of the offer by SERENA.

10. ACTION TO BE TAKEN TO ACCEPT THE OFFER

The procedures for acceptance of the offer are described beginning on page I-21 of Appendix 1 and in the accompanying acceptance form. In order to accept the offer, you should ensure that you return your completed acceptance form as soon as possible and, in any event, so as to be received by no later than 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004.

If you are in any doubt about the action you should take, you are recommended immediately to seek your own independent advice from your stockbroker, bank manager, solicitor, accountant or other duly authorised independent professional advisor.

11. RECOMMENDATION

The Merant board, who have been so advised by UBS, its financial advisor, considers the terms of the offer fair from a financial point of view. In providing advice to the directors, UBS has taken account of the directors' commercial assessments. Merant securityholders are directed to Appendix 9, which contains important information concerning the assumptions in, limitations of and qualifications to UBS advice to the Merant board.

Accordingly, the Merant directors unanimously recommend that Merant securityholders accept the offer. The directors of Merant have irrevocably undertaken to accept the offer in respect of their own personal holdings.

Yours sincerely,

/s/ J. Michael Gullard

J. Michael Gullard

Chairman

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18 March 2004

To all holders of Merant securities and, for information only, to participants in the Merant share schemes

Dear Sir or Madam,

SERENA SOFTWARE, INC.
RECOMMENDED CASH AND SHARE OFFER FOR
ALL OF THE ISSUED AND TO BE
ISSUED SHARE CAPITAL OF
MERANT PLC

1. INTRODUCTION

On 3 March 2004, the boards of SERENA Software, Inc. and Merant plc announced that they had reached agreement on the terms of a recommended cash and share offer for the entire issued and to be issued share capital of Merant, including Merant shares represented by Merant ADSs. This letter and Appendix 1 to this document contain the formal terms and conditions of the offer to be made by Lehman Brothers on behalf of SERENA (except in the United States, where SERENA is making the offer on its own behalf) and should be read in conjunction with the accompanying acceptance form.

Your attention is drawn to the letter from the Chairman of Merant beginning on page 30 of this document which states that the directors of Merant, who have been so advised by UBS, their financial advisor, consider the terms of the offer fair from a financial point of view. In providing advice to the directors of Merant, UBS has taken account of the commercial assessments of the directors of Merant. Accordingly, the directors of Merant unanimously recommend that all Merant securityholders accept the offer, as they have irrevocably undertaken to do themselves in respect of their aggregate holdings of 381,389 Merant shares. Merant securityholders are directed to Appendix 9, which contains important information concerning the assumptions in, limitations of and qualifications to UBS' advice to the Merant board.

To accept the offer, Merant securityholders must complete the appropriate acceptance procedures by no later than 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004. The procedures for acceptance of the offer are described in paragraphs 10, 11 and 12 of Part B of Appendix 1 and in the accompanying acceptance form or letter of transmittal.

2. THE OFFER

SERENA (and Lehman Brothers on behalf of SERENA outside the United States) hereby offer to acquire, subject to the conditions and the further terms set out or referred to in this document and in the relevant acceptance form, all of the Merant securities on the following basis:

for every 1 Merant share	136.5 pence in cash and 0.04966 of a new SERENA share
for every 1 Merant ADS (each Merant ADS representing 5 Merant shares)	682.5 pence in cash and 0.2483 of a new SERENA share

The offer is based on a valuation of 195 pence for each Merant share. On this basis, the offer values the entire issued share capital of Merant at approximately £206 million (US\$380 million). This is based on an exchange rate of US\$1.8488 : £1.00, calculated as the average of the US dollar / pound sterling noon buying rate for the five trading days ended 3 March 2004 and the price per SERENA share of US\$21.78, calculated as the average of the closing prices of one SERENA share as reported on Nasdaq for the twenty United States trading days ended 1 March 2004.

LEHMAN BROTHERS EUROPE LIMITED

25 BANK STREET LONDON E14 5LE TELEPHONE +44 (0)20 7102 1000

AUTHORISED AND REGULATED BY THE FINANCIAL SERVICES AUTHORITY.

REGISTERED IN ENGLAND NO 3950078 AT THE ABOVE ADDRESS.

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On 15 March 2004 (the latest practicable date prior to the posting of this document), at the then prevailing noon buying rate of US\$1.7993: £1.00 and a SERENA share price of \$19.68, the offer values each Merant share at 190.8 pence, representing a premium of approximately 23 per cent. to the middle market closing price of 155.5 pence per Merant share on 2 March 2004, the last dealing day prior to the announcement of the offer.

SERENA expects that the number of SERENA shares that will be issued on full acceptance of the offer will not exceed 5.9 million (representing approximately 13.3 per cent. of the issued and outstanding SERENA shares, as increased as a result of the offer, calculated as at 15 March 2004).

The new SERENA shares issued to Merant securityholders who accept the offer will be credited as fully paid, will rank pari passu in all respects with existing SERENA shares and will be entitled to all dividends and other distributions declared, made or paid after 3 March 2004. Appropriate adjustments to the number of SERENA shares paid in the offer will be made if SERENA effects a stock split, stock dividend or reverse stock split. The new SERENA shares are expected to be authorised for listing, subject to official notice of issuance, on Nasdaq. It is not expected that application will be made for the new SERENA shares to be admitted to dealings on any other stock exchange.

The Merant shares will be acquired by SERENA pursuant to the offer fully paid and free from all liens, charges, equitable interests, encumbrances and other third party rights and interests of any nature and together with all rights attaching thereto from 3 March 2004, including the right to receive and retain all dividends and other distributions (if any) declared, made or payable after 3 March 2004, the date of the announcement of the offer.

Fractions of new SERENA shares will not be issued to accepting Merant securityholders. To the extent that Merant securityholders are entitled to fractional shares, those fractional entitlements will be aggregated and sold in the market and the net proceeds of sale distributed pro rata to the holders of Merant shares and Merant ADSs entitled to them. In the case of holders of Merant ADSs, such payment will be made in US dollars, and in the case of holders of Merant shares, such payment will be made in pounds sterling, the applicable proceeds having been converted from US dollars at a prevailing exchange rate selected by SERENA at the relevant time. Individual entitlements to amounts of less than £2.50 (US \$4.50 based on a noon buying rate of US\$1.7993 : £1.00 as at 15 March 2004, the latest practicable date prior to the posting of this document) will not be paid to Merant securityholders, but will be retained for the benefit of the combined companies.

If sufficient acceptances are received and/or sufficient Merant shares and Merant ADSs are otherwise acquired, SERENA intends to apply the provisions of Sections 428 to 430F (inclusive) of the Companies Act to acquire compulsorily any outstanding Merant shares and Merant ADSs to which the offer relates.

When the offer becomes or is declared unconditional in all respects, SERENA intends to procure the making of an application by Merant for the removal of Merant shares from the Official List of the UK Listing Authority and for the cancellation of trading in Merant shares on the London Stock Exchange's market for listed securities. It is anticipated that cancellation of listing and trading will take effect no earlier than 20 business days after the offer becomes or is declared unconditional in all respects. In such circumstances SERENA also intends to apply for delisting of the Merant ADSs from Nasdaq. Such delistings and cancellation would significantly reduce the liquidity and marketability of any Merant securities in respect of which the offer has not been accepted.

3. BACKGROUND TO AND REASONS FOR THE OFFER

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The acquisition of Merant will create the second largest provider of ECM software solutions, serving the complex change management needs of at least 46 of the Fortune 50 largest companies worldwide, with a resulting combined installed base of over 15,000 customers. SERENA believes this installed base will provide the combined company with distribution leverage to cross sell products, expand into new geographies, create new opportunities in channel development and generate a profitable and steady maintenance revenue stream.

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The combination brings together two leaders in ECM with the complementary strengths of SERENA on mainframe platforms and Merant on distributed systems platforms and similar visions for future market share expansion.

The boards of directors of SERENA and Merant believe the combination should deliver significant strategic benefits and provide opportunities to reduce expenses and that the combined company would:

create the leading ECM vendor with integrated software solutions running on all major operating systems, from the mainframe to UNIX, LINUX and NT distributed systems environments all the way to the worldwide web;

combine SERENA's market leading mainframe SCM product, with Merant's market leading enterprise distributed SCM product;

deepen and strengthen the customer base by combining SERENA's more than 3,600 customers with Merant's more than 15,000 customer accounts;

accelerate SERENA's ability to offer customers its vision of application life cycle management solutions branded as SERENA's Application Framework for Enterprises (SAFE), thereby accessing larger markets and enabling the combined company to compete more effectively; and

offer significant potential cost savings in the areas of overlap such as dual exchange listing, dual public company compliance obligations and dual administrative infrastructures as well as a number of other duplicative areas and initiatives.

Both SERENA and Merant have been pursuing similar strategies and strategic investments to enable the application of change management technology beyond SCM to broader applications within information technology.

4. MIX AND MATCH ELECTION

Merant securityholders who validly accept the offer will be able to request under the mix and match election to vary the proportions in which they receive SERENA shares and cash in respect of their Merant securities.

The maximum number of new SERENA shares to be issued under the offer and the maximum amount of cash to be paid under the offer will not be varied as a result of the mix and match election. Accordingly, a Merant securityholder's mix and match election will be satisfied only to the extent that other Merant securityholders make opposite elections. To the extent that elections cannot be satisfied in full, they will be scaled down on a pro rata basis. To the extent that elections can be satisfied, electing Merant securityholders will receive new SERENA shares instead of cash, and vice versa.

Accordingly, Merant securityholders who make mix and match elections will not know the exact number of new SERENA shares or the amount of cash they will receive until settlement of the consideration under the offer, although an announcement of the approximate extent to which mix and match elections will be satisfied will be made two days after the mix and match election ceases to be open for acceptance.

All adjustments to the amount of cash or SERENA shares received by any Merant securityholder in the mix and match election will be calculated based on a value per Merant share of 195 pence and a value per SERENA share of £11.78. This is based on an exchange rate of US \$1.8488 : £1.00, which is calculated as the average of the dollar/pound sterling noon buying rate for the five trading days ended 3 March 2004 and price per SERENA share of US\$21.78, which is calculated as the average of the closing prices of one SERENA share as reported on Nasdaq for the twenty US trading days ended on 1 March 2004.

Although the offer will remain open for a subsequent offer period of at least 14 calendar days after the date on which the offer becomes or is declared unconditional in all respects, the mix and match election will remain

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open until, but not beyond, 3.00 pm (London time), 10.00 am (New York City time), on the date falling five calendar days after the offer becomes or is declared unconditional in all respects. Mix and match elections must be made at the same time as the acceptances of the offer to which they relate, on the relevant acceptance form. Merant securityholders who do not make a mix and match election or who do not accept the offer until after the fifth calendar day after the offer becomes or is declared unconditional in all respects will receive the basic entitlement of 136.5 pence in cash and 0.04966 new SERENA shares for every Merant share held (directly or through Merant ADSs).

A mix and match election made by a Merant securityholder may not be changed after the time that it is first made on the relevant acceptance form. However, acceptances, including the associated mix and match election, may be withdrawn in accordance with the procedures in paragraph 4 of Part B of Appendix 1. This right of withdrawal, except in the limited circumstances set out in paragraphs 4 (b), (c) and (d) of Part B of Appendix 1, terminates at the time that the offer becomes unconditional in all respects (i.e. at the end of the initial offer period). Accordingly, mix and match elections made in the five calendar day period between the end of the initial offer period and the time and date at which the mix and match election ceases to be open for acceptance cannot be changed or withdrawn.

The mix and match election is conditional upon the offer becoming or being declared unconditional in all respects. See paragraph 5 of part B of Appendix 1 of this document which sets out the procedure for making a mix and match election.

5. UNDERTAKINGS AND CONFIRMATIONS OF INTENT TO ACCEPT THE OFFER

SERENA has received undertakings and confirmations of intent to accept the offer from certain Merant securityholders as set out below. The percentage figures are based on the number of Merant shares in issue on 15 March 2004, being the latest practicable date prior to the posting of this document.

<u>Shareholder</u>	<u>Number of Merant shares</u>	<u>Per cent.</u>	<u>Options</u>
<u>Undertakings</u>			
J Michael Gullard	126,774	0.12	
Michel Berty	24,758	0.02	
Harold Hughes	134,758	0.13	
Barry Lynn	24,758	0.02	
Gerald Perkel	45,583	0.04	1,500,000(1)
Don Watters	24,758	0.02	
Merant Trustees Limited	7,415,488	7.00	
Total Undertakings	7,796,877	7.36	
<u>Confirmations of Intent</u>			
Merant Securityholders(2)	28,862,097	27.25	
Total	36,658,974	34.61	

(1) Does not include options to purchase Merant shares outstanding under Merant's employee benefit trusts. The Merant shares that are held by the employee benefit trusts are the subject of a separate irrevocable undertaking of Merant Trustees Limited.

(2) Including Schroder Investment Management Limited who hold 22,135,805 Merant shares (20.9 per cent.)

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In the quarters ended 31 January 2004 and 2003, SERENA reported the following results (in millions of US Dollars, except per share data):

	Quarter ended	Quarter ended
	31 January 2004	31 January 2003
Revenues	29.6	26.1
Profit before tax	9.3	10.8
Charge for tax	3.4	4.0
Net profit after tax	6.0	6.8
Earnings per share	0.15	0.17

As at 31 January 2004, SERENA had total cash and cash equivalents of US\$377 million.

Further information with respect to SERENA is set forth in Appendix 2 to this document.

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SERENA recognises the importance to Merant's business of the skills and experience of Merant's management team and employees.

SERENA has given assurances to the Merant board that the existing employment rights, including pension rights, of the management and employees of Merant will be fully honoured.

Gerald Perkel, President and Chief Executive Officer of Merant, has agreed to join the board of SERENA as a director subject to the offer becoming or being declared unconditional in all respects.

11. MERANT SHARE SCHEMES

The offer extends, subject to the terms and conditions set forth in this document and acceptance form(s), to all Merant shares unconditionally allotted or issued fully paid (or credited as fully paid) upon exercise of options

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under the Merant share schemes while the offer remains open for acceptance (or until such earlier date as SERENA may, subject to the provisions of the Code, determine). Appropriate proposals will be made to holders of options under the Merant share schemes as outlined below. For these purposes, the Merant share schemes can be divided into three categories, namely (a) Employee Benefit Trust, referred to as EBT, options, (b) Employee Stock Purchase Plan, and (c) options granted pursuant to Merant share schemes not associated with the Employee Benefit Trust, or Non-EBT options.

(a) Employee Benefit Trust

There are two trusts established in 1994 and 2003 and in respect of both Merant Trustees Limited is the Trustee.

Merant Trustees Limited has given an irrevocable undertaking to accept the offer in respect of all the Merant shares it holds. Merant Trustees Limited intends to use the cash it receives under the offer to provide cash cancellation of outstanding options based upon the difference between an offer value per Merant share of 195 pence and the exercise price for each option held. Further details of this proposal will be sent to optionholders in due course.

(b) Employee Stock Purchase Plan

In accordance with the terms of the plan, SERENA will assume the obligation to satisfy outstanding participation rights by the issue of an appropriate number of SERENA shares. Merant Trustees Limited will receive SERENA shares under the offer and has agreed to use such SERENA shares to satisfy the participation rights to the maximum extent they can after settlement of their other outstanding obligations and trust expenses.

(c) Non-EBT Options

Optionholders will hold interests which fall into one or more of the following categories:

1. options which are already vested; or
2. options which are not already vested but which vest on a change of control (i.e. when the offer is declared wholly unconditional); or
3. options which are not already vested and which do not vest on a change of control.

All optionholders (both vested and unvested) will be invited to rollover their options over Merant shares into options over SERENA shares on terms which reflect the value of the offer based on a value per Merant share of 195 pence and a value per SERENA share of £11.78. Further details will be sent to optionholders in due course.

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Optionholders whose options are already vested are able to exercise their options at any time during the initial offer period and accept the offer whilst it is open, including participation in the mix and match election at their election while it is still available.

It is intended that optionholders whose options vest when the offer becomes or is declared wholly unconditional will be offered a facility to enable them to accept the offer in time to participate in the mix and match election.

Merant and SERENA have agreed to give effect to optionholders' pre-existing contractual rights to exercise their options on a cashless basis and to work together to try to provide a cashless exercise facility on a similar basis to optionholders who do not have a pre-existing contractual right to do so.

No cash cancellation will be offered by SERENA except that, in the case of employees resident in jurisdictions outside the US and the UK where it is not practicable to allow such optionholders to participate in the above arrangements, cash cancellation of their options, if and to the extent permitted by applicable law or regulations, may be implemented. If such cash cancellation is not possible then alternative arrangements complying with applicable law and approved by Merant and the Panel may be implemented instead.

Further details of these arrangements will be sent to optionholders in due course.

Table of Contents**12. FINANCIAL EFFECTS OF ACCEPTANCE**

The following table sets out, for illustrative purposes only and on the bases and assumptions set out below, the financial effects of acceptance on capital value for an accepting Merant shareholder, if the offer becomes or is declared unconditional in all respects. Since neither SERENA nor Merant has declared or paid dividends, there are no financial effects on income for an accepting Merant shareholder.

CHANGE IN CAPITAL VALUE

	(A)	(B)
	pence	pence
Market value of 0.04966 of a new SERENA share (Note (i))	58.5	58.5
Cash consideration per Merant share	136.5	136.5
Market value of a Merant share (Note (ii))	155.5	189.5
Increase / (decrease) in capital value	39.5	5.5
This represents an increase / (decrease) of	25.4 per cent.	2.9 per cent.

Notes

- (i) This is based on an exchange rate of US\$1.8488 : £1.00 which is calculated as the average of the US dollar/pound sterling noon buying rate for the five trading days ended 3 March 2003 and price per SERENA share of US\$21.78, which is calculated as the average closing price of SERENA shares as reported on Nasdaq for the 20 United States trading days ended on 1 March 2004.
- (ii) Column (A) is based on the closing price of 155.5 pence per Merant share on 2 March 2004 (the last dealing day prior to the announcement of the offer). Column (B) is based on the closing price of 189.5 pence per Merant share on 15 March (the latest practicable date prior to the posting of this document).
- (iii) No account has been taken of any liability for taxation or the treatment of fractions of Merant shares in assessing the financial effects of accepting the offer.

On 15 March 2004 (the latest practicable date prior to the posting of this document), at the then prevailing noon buying rate of US\$1.7993 : £1.00 and a SERENA share price of \$19.68, the offer values each Merant share at 190.8 pence.

SERENA has never declared or paid any cash dividends on its shares and does not anticipate paying cash dividends in the foreseeable future.

13. PROCEDURES FOR ACCEPTANCE OF THE OFFER

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To accept the offer, you must complete the appropriate acceptance procedures by no later than 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004. The procedures for acceptance of the offer are described in detail beginning on page I-21 of Appendix 1 and in the notes and instructions of the accompanying acceptance form or letter of transmittal.

14. RIGHTS OF WITHDRAWAL

Except to the extent of exemptive relief which may be granted by the SEC, the offer is subject to the US tender offer rules applicable to securities registered under the Exchange Act, as well as to the City Code. This has necessitated a number of changes from the procedures which normally apply to offers for companies governed by the City Code, including those applicable to the rights of holders of Merant securities to withdraw their acceptance of the offer.

Under the offer, holders of Merant securities will be able to withdraw their acceptances at any time during the initial offer period but will not have any withdrawal rights during the subsequent offer period, except in certain limited circumstances (see paragraphs 4(c) and (d) of Part B of Appendix 1 to this document).

The offer will be deemed not to have been validly accepted in respect of any Merant securities acceptances in respect of which have been validly withdrawn. However, the offer may be accepted again in respect of any

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withdrawn Merant securities following one of the procedures described in paragraphs 10, 11 or 12 of Part B of Appendix 1 to this document at any time prior to expiry or lapse of the offer.

Further details of these rights of withdrawal and the procedure for effecting withdrawals are set out in paragraph 4 of Part B of Appendix 1 to this document.

15. SETTLEMENT

(a) Date of Payment

The settlement procedure with respect to the offer will be consistent with UK practice, which differs from US domestic tender offer procedures in certain material respects, particularly with regard to the date of payment.

Subject to either the satisfaction, fulfillment or, to the extent permitted, waiver of all of the conditions, settlement of consideration to accepting Merant securityholders, including accepting holders of Merant ADSs, or their designated agents will be effected in the manner set out below:

- (i) in the case of acceptances received complete in all respects by the end of the initial offer period, within 14 calendar days after such date; or
- (ii) in the case of acceptances received complete in all respects after such date but while the offer remains open for acceptance, within 14 calendar days after such receipt, in the manner set out below.

(b) Merant shares in uncertificated form (that is, in CREST)

Where an acceptance relates to Merant shares in uncertificated form:

- (i) the new SERENA shares to which the accepting Merant securityholder is entitled under the offer will be issued to such shareholder in certificated form and share certificates and/or other documents of title will be dispatched by post (or by such other method as may be approved by the Panel); and
- (ii) the cash consideration to which an accepting Merant securityholder is entitled will be paid by means of a CREST payment obligation in favour of the accepting Merant securityholder's payment bank in respect of the cash consideration due, in accordance with the CREST payment arrangements.

SERENA reserves the right to settle all or any part of the cash consideration referred to above, for all or any accepting Merant securityholder(s), in the manner referred to in paragraph (c) below, if, for any reason, it wishes to do so.

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(c) Merant shares in certificated form and Merant ADSs

Where an acceptance relates to Merant shares in certificated form or Merant ADSs evidenced by Merant ADRs, the new SERENA shares to which an accepting Merant securityholder is entitled under the offer will be issued to the Merant securityholder in certificated form. Definitive certificates for the new SERENA shares and cheques for cash due will be dispatched by post (or by such other method as may be approved by the Panel).

(d) Lapsing of the offer

If by the relevant closing date, the conditions are not either satisfied, fulfilled or, to the extent permitted, waived, the offer will lapse unless a later closing date is selected by SERENA and: (i) in respect of Merant shares in certificated form and Merant ADSs, the relevant share certificate(s), Merant ADRs and/or other documents of title will be returned by post (or by such other method as may be approved by the Panel) within 14 calendar days after the offer lapsing to the person or agent whose name and address (outside Canada, Australia or Japan) is set out in Box 2 (or, if applicable, Box 8) of the form of acceptance or to the person or agent whose name and address (outside Canada, Australia or Japan) is set out in the letter of transmittal (as applicable) or, if none is set out, to the name and address of the person who is the first named holder at the holder's registered address; (ii) in

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respect of Merant shares in uncertificated form (that is, in CREST), the UK Receiving Agent will, immediately after the lapsing of the offer (or within such longer period as the Panel may permit, not exceeding 14 calendar days after the lapsing of the offer), give transfer from escrow instructions to CRESTCo to transfer all relevant Merant shares held in escrow balances and in relation to which it is the escrow agent for the purposes of the offer to the original available balances of the holders of Merant shares concerned; and (iii) in respect of Merant ADSs delivered by book-entry transfer into the US Depository's account at a Book-Entry Transfer Facility, Merant ADSs will be credited to an account maintained at the appropriate Book-Entry Transfer Facility.

Further information on the lapsing of the offer is set out in paragraph 8 of Part B of Appendix 1 to this document.

(e) General

All documents and remittances sent by, to or from Merant securityholders or their appointed agents will be sent at their own risk.

All mandates, instructions and other instruments in force immediately before the offer becomes unconditional relating to holdings of Merant securities will, unless and until revoked, continue in force in relation to payments and notices in respect of new SERENA shares issued under the offer in each case insofar as relevant. If a Merant securityholder has existing SERENA shares, the mandates, instructions and instruments in force for the existing SERENA shares will supersede the mandates, instructions and instruments for the Merant securities.

(f) Currency of cash consideration

Instead of receiving cash consideration to which they are entitled in pounds sterling, Merant shareholders who so wish may elect to receive US dollars. If a Merant shareholder so elects, the amount of pounds sterling to which such shareholder is entitled will be converted, subject to conversion expenses, from pounds sterling to US dollars at the exchange rate obtainable by the UK Receiving Agent on the spot market in London at approximately noon (London time) on the date the cash consideration is made available by SERENA to the relevant payment agent for delivery in respect of the relevant Merant shares. A Merant shareholder may receive such amount on the basis set out above only in respect of the whole of the shareholder's holding of Merant shares in respect of which the shareholder accepts the offer. Merant shareholders may not elect to receive both pounds sterling and US dollars.

Holders of Merant ADSs are entitled under the terms of the offer to receive the cash element of the consideration in pounds sterling. The pounds sterling consideration available to holders of Merant ADSs is the same, per Merant share, as that offered to Merant securityholders. To facilitate the settlement of the offer, unless they elect to receive pounds sterling, holders of Merant ADSs will automatically be deemed to have elected to receive consideration converted into US dollars as described above.

Consideration in US dollars may be inappropriate for Merant securityholders other than persons in the United States and holders of Merant ADSs.

If you are a Merant shareholder and you wish to elect to receive cash consideration in US dollars instead of pounds sterling under the offer, you should complete the appropriate box of the form of acceptance in addition to taking the actions described in paragraphs 10 and 11 of Part B of Appendix 1.

If you are a holder of Merant ADSs and you wish to elect to receive cash consideration in pounds sterling instead of US dollars under the offer, you should complete the appropriate box of your letter of transmittal in addition to taking the actions described in paragraph 12 of Part B of Appendix 1.

The actual amount of US dollars received will depend upon the exchange rate prevailing on the business day on which funds are made available to the relevant payment agent by SERENA. Merant securityholders should be aware that the US dollar/pounds sterling exchange rate which is prevailing on

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the date on which an election is made or deemed to be made to receive US dollars and on the dates of dispatch and receipt of payment may be different from that prevailing on the business day on which funds are made available to the relevant payment agent by SERENA. In all cases, fluctuations in the US dollar/pounds sterling exchange rate are at the risk of accepting Merant securityholders who elect or are treated as having elected to receive their consideration in US dollars. Neither SERENA nor any of its advisors or agents shall have any responsibility with respect to the actual amount of cash consideration payable other than in pounds sterling.

16. UNITED KINGDOM TAXATION

Information on the application of current UK tax law and Inland Revenue practice applicable to Merant securityholders who accept the offer is contained in paragraph 14 of Appendix 5 to this document.

17. UNITED STATES FEDERAL TAXATION

Information on the application of current US federal tax law applicable to Merant securityholders who accept the offer is contained in paragraph 15 of Appendix 5 to this document.

The information in paragraphs 16 and 17 above and paragraphs 14 and 15 of Appendix 5 to this document is provided for guidance only and holders of Merant securities are urged to consult their independent professional advisor in light of their particular circumstances as to the US and UK tax consequences, as well as the effect of any state, local or foreign tax laws.

18. OVERSEAS MERANT SECURITYHOLDERS

The availability of the offer to persons who are not resident in the United Kingdom or the United States may be affected by the laws of the relevant jurisdictions. Persons who are not resident in the United Kingdom or the United States should inform themselves about and observe any applicable requirements. The attention of Merant securityholders who are citizens or residents of jurisdictions outside the United Kingdom or the United States is drawn to paragraph 9 of Part B of Appendix 1 of this document and to the relevant provisions of the acceptance form.

The offer is not being made, directly or indirectly, in or into Canada, Australia or Japan. Accordingly, any accepting Merant securityholder who is unable to give the representations and warranties set out in paragraphs 11(b) and 12(i)(ii)(dd) (as applicable) of Part B of Appendix 1 to this document may be deemed not to have accepted the offer.

19. INDUCEMENT FEE

In consideration of, and as an inducement to, SERENA making the offer for Merant, Merant has agreed to pay SERENA a fee of £2.06 million (US \$3.71 million based on a noon buying rate of US\$1.7993 : £1.00 as at 15 March 2004, the latest practicable date prior to the posting of this

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document) in the circumstances described below. Save in the following limited circumstances: failure to obtain approval for the offer under the HSR Act or other applicable antitrust law, withdrawal of the offer without consent of the Panel or material breach (and failure to cure) by SERENA of the Inducement Agreement, this fee is payable on either of the following events:

- (a) if a higher competing offer or other competing transaction (or an intention to do either) is publicly announced by a third party and the Merant board fails to reaffirm its unanimous recommendation of the offer and subsequently the offer lapses or is withdrawn; or
- (b) if the board of Merant withdraws or modifies its recommendation of the offer by SERENA.

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20. FURTHER INFORMATION

Your attention is drawn to the further information contained in the Appendices which form part of this document, and to the accompanying acceptance form, which should be read in conjunction with this document. The Appendices and the acceptance form contain material information which may not be summarised elsewhere.

21. ACTION TO BE TAKEN

You are urged to complete, sign and return the form of acceptance or letter of transmittal (as appropriate), together with all the required documents, as soon as possible and, in any event, so as to be received by the UK Receiving Agent or the US Depositary, as appropriate, by no later than 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004.

Yours sincerely,

/s/ Keith Jue

for and on behalf of

LEHMAN BROTHERS

Keith Jue

Managing Director

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APPENDIX 1

CONDITIONS AND FURTHER TERMS OF THE OFFER

PART A CONDITIONS OF THE OFFER

This offer, which is being made by SERENA on its own behalf in the United States and by Lehman Brothers on behalf of SERENA outside of the United States, is subject to the following conditions:

- (a) valid acceptances being received (and not, where permitted, withdrawn) by not later than 3.00 pm (London time), 10.00 am (New York City time), on the first closing date of the offer (or such later time(s) and/or date(s) as SERENA may, subject to the rules of the City Code or with the consent of the Panel and in accordance with the Exchange Act, decide) in respect of not less than 90 per cent. (or such lower percentage as SERENA may decide) in nominal value of the Merant securities to which the offer relates, provided that this condition will not be satisfied unless SERENA (together with any of its wholly-owned subsidiaries) shall have acquired or agreed to acquire, whether pursuant to the offer or otherwise, Merant securities carrying, in aggregate, more than 50 per cent. of the voting rights then exercisable at general meetings of Merant, including for this purpose (to the extent, if any, required by the Panel) any such voting rights attaching to any Merant securities which are unconditionally allotted or issued before the offer becomes or is declared unconditional as to acceptances, whether pursuant to the exercise of any outstanding conversion or subscription rights or otherwise and; for this purpose:
 - (i) the expression Merant securities to which the offer relates shall be construed in accordance with sections 428 to 430F of the Companies Act; and
 - (ii) Merant securities which have been unconditionally allotted shall be deemed to carry the voting rights which they will carry upon issue;

provided that, unless SERENA otherwise determines, this condition (a) shall be capable of being satisfied only at a time when all of the other conditions (b) to (k) inclusive have been either satisfied, fulfilled or, to the extent permitted, waived;

- (b) the new SERENA shares having been authorised for listing, subject to official notice of issuance, on Nasdaq and the Registration Statement having been declared effective;
- (c) no Third Party having taken, instituted, implemented or threatened in writing any action, proceedings, suit, investigation or enquiry, or made, proposed or enacted, any statute, regulation or order or taken any other steps and there continuing not to be outstanding any statute, regulation, order or other matter which in each case would reasonably be expected to:
 - (i) make the offer, its implementation or the acquisition or proposed acquisition by SERENA or any US or UK subsidiary of SERENA of any or all shares or other securities in (or the equivalent), or control or management of, Merant or any member of the Wider Merant Group void, illegal or unenforceable in or under the laws of any relevant jurisdiction, or otherwise directly or indirectly materially restrain, prevent, prohibit, materially restrict or materially delay the same or impose additional material conditions or obligations with respect to the offer or such acquisition, or otherwise materially impede, challenge or interfere with the offer or such acquisition, or require material amendment to the terms of the offer or the acquisition or proposed acquisition of any Merant

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securities or the acquisition of control of Merant or the Wider Merant Group by SERENA;

- (ii) limit or delay the ability of any member of the SERENA Group or any member of the Wider Merant Group to acquire or to hold or to exercise effectively, directly or indirectly, all or any rights of ownership in respect of shares or other securities (or the equivalent) in, or to exercise voting or management control over, any member of the Wider Merant Group or any member of the SERENA Group to an extent which is material in the context of the offer;

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- (iii) require, prevent or delay the divestiture or alter the terms envisaged for any proposed divestiture by any member of the SERENA Group of any shares or other securities (or the equivalent) in Merant to an extent which is material in the context of the offer;
 - (iv) require, prevent or delay the divestiture or alter the terms envisaged for any proposed divestiture by any member of the SERENA Group or by any member of the Wider Merant Group of all or any portion of their respective businesses, assets or properties or limit the ability of any of them to conduct any of their respective businesses or to own or control any of their respective assets or properties or any part thereof to an extent which is material in the context of the Wider Merant Group taken as a whole or the SERENA Group taken as a whole;
 - (v) except pursuant to Part XIII A of the Companies Act, require any member of the SERENA Group or of the Wider Merant Group to acquire, or to offer to acquire, any shares or other securities (or the equivalent) in any member of either group owned by any third party or to sell or offer to sell any shares or other securities (or the equivalent in), or any asset of any member of the Wider Merant Group to an extent which is material in the context of the Wider Merant Group taken as a whole or the SERENA Group taken as a whole;
 - (vi) limit the ability of any member of the SERENA Group or of the Wider Merant Group to conduct or integrate or coordinate its business, or any part of it, with the businesses or any part of the businesses of any other member of the SERENA Group or of the Wider Merant Group to an extent which is material in the context of the offer;
 - (vii) result in any member of the SERENA Group or the Wider Merant Group ceasing to be able to carry on business under any name under which it presently does so to an extent which is material in the context of the Wider Merant Group taken as a whole or the SERENA Group taken as a whole;
 - (viii) otherwise adversely affect the business, assets, profits, financial or trading position of any member of the Wider Merant Group or of the SERENA Group to an extent which is material in the context of the offer; and
 - (ix) all applicable time periods during which any Third Party could decide to take, institute or threaten any such action, proceeding, suit, investigation, enquiry or reference or otherwise intervene under the laws or regulations of any relevant jurisdiction having expired, lapsed or been terminated;
- (d) without limitation to condition (c) above:
- (i) all filings having been made and all or any applicable waiting periods and other time periods (including any extensions thereof) under the HSR Act and the regulations thereunder having expired, lapsed or been terminated as appropriate in each case in respect of the proposed acquisition of Merant by SERENA, or any matters arising from that proposed acquisition;
 - (ii) insofar as the merger provision of the Enterprise Act 2002 may be applicable, the Office of Fair Trading indicating in terms satisfactory to SERENA, that it does not intend to refer the proposed acquisition of Merant by SERENA, or any matter arising therefrom, to the Competition Commission, or the statutory period for any such referral expiring without such reference having been made, or the Office of Fair Trading accepting undertakings from SERENA in terms satisfactory to SERENA, in lieu of referring the proposed acquisition by SERENA of Merant, or any matter arising therefrom, to the Competition Commission; and
 - (iii) no statute, rule, regulation, executive order, decree, ruling or injunction having been enacted, entered, promulgated or enforced by any court or other governmental or regulatory entity having jurisdiction over the offer, the Wider Merant Group or the SERENA Group that prohibits, restrains or enjoins the consummation of the offer;

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- (e) all necessary notifications and filings having been made, all applicable time periods (including any extensions of such waiting and other time periods) under any applicable legislation or regulation of any relevant jurisdiction having expired, lapsed or been terminated (as appropriate) and all statutory or

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regulatory obligations in any relevant jurisdiction having been complied with in each case in connection with the offer or the acquisition or proposed acquisition of any shares or other securities (or the equivalent) in Merant or control (directly or indirectly) of Merant or any other member of the Wider Merant Group by any member of the SERENA Group or the carrying on by any member of the Wider Merant Group of its business, where the absence thereof would have a material adverse affect in the context of the Wider Merant Group taken as a whole;

- (f) all necessary Authorisations in any jurisdiction for or in respect of the offer or the acquisition or proposed acquisition of any shares or other securities in Merant or control (directly or indirectly) of Merant or any other member of the Wider Merant Group by any member of the SERENA Group or the carrying on by any member of the Wider Merant Group of its business in any jurisdiction having been obtained, in terms and in a form satisfactory to SERENA, from all appropriate Third Parties or from any persons or bodies with whom any member of the Wider Merant Group has entered into contractual arrangements, in each case where the absence of such Authorisation would have a material adverse effect in the context of the offer and all such Authorisations remaining in full force and effect at the time at which the offer becomes otherwise unconditional in all respects and there being no notice of any intention to revoke, suspend, restrict, adversely modify or not to renew any of the same;
- (g) except as fairly disclosed to SERENA by or on behalf of Merant, or disclosed in Merant filings with the SEC, or as disclosed in the Annual Report and Accounts of Merant, or as publicly announced by Merant (by the delivery of an announcement to a Regulatory Information Service), prior to 3 March 2004, the date of the announcement of the offer, there being no provision of any arrangement, agreement, licence, permit, franchise or other instrument to which any member of the Wider Merant Group is a party, or by or to which any such member or any of its assets is or are or may be bound, entitled or subject or any circumstance, which, in each case as a consequence of the offer or the acquisition or proposed acquisition of any shares or other securities in, or control of, Merant or any other member of the Wider Merant Group by any member of the SERENA Group or otherwise, could or might reasonably be expected to result in, (in any case to an extent which is or would be material in the context of the Wider Merant Group taken as a whole):
 - (i) any monies borrowed by or any other indebtedness or liabilities (actual or contingent) of, or any grant available to, any member of the Wider Merant Group being or becoming repayable or capable of being declared repayable immediately or prior to its stated repayment date or the ability of any member of the Wider Merant Group to borrow monies or incur any indebtedness being withdrawn or inhibited or becoming capable of being withdrawn;
 - (ii) the creation or enforcement of any mortgage, charge or other security interest over the whole or any part of the business, property, assets or interests of any member of the Wider Merant Group or any such mortgage, charge or other security interest (wherever created, arising or having arisen) becoming enforceable;
 - (iii) any such arrangement, agreement, licence, permit, franchise or instrument, or the rights, liabilities, obligations or interests of any member of the Wider Merant Group thereunder, being, or becoming capable of being, terminated or adversely modified or affected or any adverse action being taken or any obligation or liability arising thereunder;
 - (iv) any asset or interest of any member of the Wider Merant Group being or falling to be disposed of or ceasing to be available to any member of the Wider Merant Group or any right arising under which any such asset or interest could be required to be disposed of or could cease to be available to any member of the Wider Merant Group, in each case, otherwise than in the ordinary course of business;
 - (v) any member of the Wider Merant Group ceasing to be able to carry on business under any name under which it presently does so;
 - (vi) the creation of liabilities (actual or contingent) by any member of the Wider Merant Group, otherwise than in the ordinary course of business;

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- (vii) the rights, liabilities, obligations or interests of any member of the Wider Merant Group under any such arrangement, agreement, licence, permit, franchise or other instrument or the interests or business of any such member in or with any other person, firm, company or body (or any arrangement or arrangements relating to any such interests or business) being terminated, adversely modified or affected;
 - (viii) the financial or trading position of any member of the Wider Merant Group being prejudiced or adversely affected, or
 - (ix) no event having occurred which, under any provision of any such arrangement, agreement, licence, permit or other instrument, could result in any of the events or circumstances which are referred to in paragraphs (i) to (viii) of this condition (g) in any case to an extent which is or would be material in the context of the Wider Merant Group taken as a whole;
- (h) since 30 April 2003 and except as disclosed in the Annual Report and Accounts of Merant, or in Merant filings with the SEC, or as otherwise publicly announced by Merant (by the delivery of an announcement to a Regulatory Information Service), or as otherwise fairly disclosed to SERENA by or on behalf of Merant prior to 3 March 2004, no member of the Wider Merant Group having:
- (i) issued or agreed to issue, or authorised or proposed the issue of, additional shares or securities of any class, or securities convertible into or exchangeable for, or rights, warrants or options to subscribe for or acquire, any such shares, securities or convertible securities other than as between Merant and wholly-owned subsidiaries of Merant and other than any options granted as disclosed to SERENA prior to 3 March 2004 and any shares, with the consent of SERENA issued upon the exercise of any options granted under any of the Merant share schemes;
 - (ii) purchased or redeemed or repaid any of its own shares or other securities or reduced or made any other change to any part of its share capital (other than with respect to any wholly-owned subsidiary of Merant);
 - (iii) recommended, declared, issued, paid or made or proposed to recommend, declare, pay, issue or make any bonus, dividend or other distribution whether payable in cash or otherwise (other than to Merant or a wholly-owned subsidiary of Merant);
 - (iv) made, committed to make, authorised, proposed or announced an intention to propose any change in its share or loan capital;
 - (v) merged with, demerged or acquired any body corporate, partnership or business, or (other than a transaction between Merant and a wholly-owned subsidiary of Merant) acquired or disposed of or transferred, mortgaged or charged or created any security interest over any assets or any right, title or interest in any assets (including shares in any undertaking and trade investments) or authorised the same (which is material in the context of the Wider Merant Group taken as a whole);
 - (vi) issued, authorised or proposed the issue of, or authorisation of or made any change in or to any debentures or (except in the ordinary course of business) incurred or increased any indebtedness or liability (actual or contingent), including pursuant to any agreements or arrangements existing prior to 3 March 2004, which in any case is material in the context of the Wider Merant Group taken as a whole;
 - (vii) entered into, varied, or authorised any agreement, transaction, arrangement or commitment (whether in respect of capital expenditure or otherwise), and which in any case is reasonably likely to be material in the context of the Wider Merant Group taken as a whole or the SERENA Group taken as a whole, as the case may be, which:
 - (A) is of a long term, onerous or unusual nature or magnitude or which is reasonably likely to involve an obligation of such nature or magnitude; or

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- (B) which is reasonably likely to restrict the business of any member of the Wider Merant Group or any member of the SERENA Group; or
- (C) is other than in the ordinary course of business;
- (viii) entered into or varied or made any offer to enter into or vary the terms of, any contract, agreement or arrangement with any of the directors of Merant or with Stephen King, Scott Hildebrandt, Diane Williams, Robert Blaskowsky, Stephen Going, Robert Dunne, Brian Unruh or Rees Withers;
- (ix) (other than in respect of any member which is or was at this time dormant) taken or proposed any corporate action or had any legal proceedings instituted or threatened in writing against it or petition presented or order made for its winding-up (voluntarily or otherwise), dissolution or reorganisation or for the appointment of a receiver, administrator, administrative receiver, trustee or similar officer of all or any part of its assets and revenues or any analogous proceedings in any jurisdiction or appointed any analogous person in any jurisdiction which in any case is material in the context of the Wider Merant Group taken as a whole;
- (x) been unable, or admitted in writing that it is unable, to pay its debts as they fall due or having stopped or suspended (or threatened to stop or suspend) payment of its debts generally or ceased or threatened to cease carrying on all or a substantial part of its business which in any case is material in the context of the Wider Merant Group taken as a whole;
- (xi) waived or compromised or settled any claim in a manner which is material in the context of the Wider Merant Group taken as a whole;
- (xii) made any alteration to its memorandum or articles of association that is material in the context of the offer;
- (xiii) implemented, effected or authorised, or proposed or announced its intention to implement, effect, authorise or propose any reconstruction, amalgamation, commitment, merger, scheme or other transaction or arrangement except (in the case of members of the Wider Merant Group other than Merant) to an extent which is not material in the context of the Wider Merant Group taken as a whole;
- (xiv) amended the terms (including the terms relating to acceleration or vesting) of any Merant share schemes in a manner that is material in the context of the Wider Merant Group taken as a whole; or
- (xv) entered into any agreement, commitment or arrangement or passed any resolution or made any offer (which remains open for acceptance) or proposed or announced any intention with respect to any of the transactions, matters or events referred to in this Condition (h);
- (i) since 30 April 2003 and except as disclosed in the Annual Report and Accounts of Merant, or in Merant filings with the SEC, or as otherwise publicly announced by Merant (by the delivery of an announcement to a Regulatory Information Service) or as otherwise fairly disclosed to SERENA by or on behalf of Merant prior to 3 March 2004:
 - (i) there having been no adverse change or deterioration in the business, assets, financial or trading positions or profit or prospects of any member of the Wider Merant Group which in any case is material in the context of the Wider Merant Group taken as a whole;
 - (ii) no contingent or other liability of any member of the Wider Merant Group having arisen or become apparent or increased which in any case is material in the context of the Wider Merant Group taken as a whole;

- (iii) no litigation, arbitration proceedings, prosecution or other legal proceedings to which any member of the Wider Merant Group is or is reasonably likely to become a party (whether as plaintiff, defendant or otherwise) having been threatened, announced, implemented or instituted by or against or remaining outstanding against or in respect of any member of the Wider Merant Group which in any case is material in the context of the Wider Merant Group taken as a whole; and

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- (iv) SERENA not having discovered that any member of the Wider Merant Group or any partnership company or other entity in which any member of the Wider Merant Group has a significant economic interest and which is not a subsidiary undertaking of Merant is subject to any liability (actual or contingent) which is not disclosed in the Annual Report and Accounts of Merant and which in any case is material in the context of the Wider Merant Group taken as a whole;

- (j) except as disclosed in the Annual Report and Accounts of Merant, or in Merant filings with the SEC, or as otherwise publicly announced by Merant (by the delivery of an announcement to a Regulatory Information Service) or as otherwise fairly disclosed to SERENA by or on behalf of Merant prior to 3 March 2004, SERENA not having discovered that any financial or business or other information concerning the Wider Merant Group disclosed at any time by or on behalf of any member of the Wider Merant Group, to any member of the SERENA Group, whether publicly or otherwise, is materially misleading or contains any material misrepresentation of fact or omits to state a fact necessary to make any information contained therein not misleading and which was not subsequently corrected before 3 March 2004 by disclosure either publicly or otherwise to SERENA to an extent which in any case is material in the context of the Wider Merant Group taken as a whole; and

- (k) since 30 April 2003 and except as disclosed in the Annual Report and Accounts of Merant, or in Merant filings with the SEC, or as otherwise publicly announced by Merant (by the delivery of an announcement to a Regulatory Information Service) or as otherwise fairly disclosed to SERENA by or on behalf of Merant prior to 3 March 2004:
 - (i) any past or present member of the Wider Merant Group has not complied with any applicable legislation or regulations of any relevant jurisdiction with regard to the use, treatment, handling, storage, transport, release, disposal, discharge, spillage, leak or emission of any waste or hazardous substance or any substance likely to impair the environment or harm human health, or otherwise relating to environmental matters or the health and safety of any person, or that there has otherwise been any such use, treatment, handling, storage, transport, release, disposal, discharge, spillage, leak or emission (whether or not this constituted a non-compliance by any person with any legislation or regulations and wherever the same may have taken place) which, in any case, would be reasonably likely to give rise to any liability (whether actual or contingent) or cost on the part of any member of the Wider Merant Group which in any case is material in the context of the Wider Merant Group taken as a whole;

 - (ii) there is, or is reasonably likely to be, any liability, whether actual or contingent, or requirement to improve or install new plant or equipment or to make good, repair, reinstate or clean up any property now or previously owned, occupied or made use of by any past or present member of the Wider Merant Group or any other property or any controlled waters under any environmental legislation, regulation, notice, circular, order or other lawful requirement of any relevant authority or third party or otherwise which in any case is material in the context of the Wider Merant Group taken as a whole; or

 - (iii) circumstances exist whereby a person or class of persons would be reasonably likely to have a claim in respect of any product or process of manufacture or materials used therein now or previously manufactured, sold or carried out (including without limitation with respect to ownership or infringement of intellectual property) by any past or present member of the Wider Merant Group which is or would be material in the context of the Wider Merant Group taken as a whole.

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For the purpose of these conditions:

- (a) **Third Party** means any government, government department or governmental, quasi-governmental, supranational, statutory, regulatory, administrative or investigative body, authority (including any national antitrust, competition or merger control authorities or similar authorities), court, trade agency, association, institution or professional or environmental body in any relevant and applicable jurisdiction;
- (b) a **Third Party** shall be regarded as having **intervened** if it has decided to take, institute, implement or threaten any action, proceeding, suit, investigation, enquiry or reference or made, proposed or enacted any statute, regulation, decision or order or taken any measures or other steps or required any action to be taken or information to be provided or otherwise having done anything and **intervene** shall be construed accordingly;
- (c) **Authorisations** means authorisations, orders, recognitions, determinations, certificates, consents, permissions, licences, clearances and approvals other than those the need for which has been fairly disclosed prior to 3 March 2003;
- (d) **Wider Merant Group** means the Merant Group and associated undertakings and any other body corporate, partnership joint venture or person in which the Merant Group and such undertakings (aggregating their interests) have an interest of more than 20 per cent. of the voting or equity capital or the equivalent.

Subject to the requirements of the Panel, SERENA reserves the right to waive all or any of the above conditions, in whole or in part, except condition (a).

The offer will lapse unless the offer is extended or the conditions have been determined by SERENA to have been and to remain satisfied, fulfilled or (if capable of waiver) waived by 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004 in accordance with the City Code or with the consent of the Panel and subject to any requirements of the laws of the US.

The Acceptance Condition shall be capable of being satisfied or being treated as satisfied only at the time when all of the other conditions shall have been either satisfied, fulfilled or (to the extent permitted) waived unless SERENA, with the consent of the Panel, shall otherwise decide. SERENA may declare the offer wholly unconditional at any time after 3.00 pm (London time), 10.00 am (New York City time) on 15 April 2004 (or such later time as the offer is required to be extended pursuant to the City Code or US law).

SERENA shall be under no obligation to waive or treat as satisfied any of conditions (a) to (k) inclusive by a date earlier than the latest date for its satisfaction notwithstanding that any other condition of the offer may on or before such date have been waived or fulfilled and/or that there are no circumstances indicating that any such conditions may not be capable of fulfillment; provided that SERENA will waive the conditions set out in paragraphs (c), d(iii) and (e) to and including (k) above not later than the fifth business day after the later of (i) the twentieth US business day after the date the offer is commenced and (ii) the date of satisfaction (or to the extent permitted, waiver by SERENA in its sole discretion) of the last of the conditions set forth in paragraphs (a), (b), d(i) and (d)(ii) to be satisfied, unless in each case SERENA has, on or prior to 5.00 pm (California time), on such fifth business day, notified Merant in writing of its intention to invoke any such condition.

SERENA reserves the right, subject to the consent of the Panel, to extend the time allowed under the rules of the City Code for satisfaction of the Acceptance Condition and accordingly for the satisfaction, fulfillment or, where permitted, waiver of other conditions, and thus, to extend the duration of the initial offer period.

If SERENA is required by the Panel to make an offer for Merant securities under the provisions of Rule 9 of the City Code, SERENA may make such alterations to the conditions, including the Acceptance Condition, as are necessary to comply with the provisions of that Rule.

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The offer will lapse (unless otherwise agreed by the Panel) if the acquisition of Merant is referred to the UK Competition Commission before 15 April 2004, or the date on which the offer becomes or is declared unconditional as to acceptances, whichever is the later.

If the offer lapses it will cease to be capable of further acceptance. Merant securityholders who have accepted the offer and SERENA shall then cease to be bound by acceptances delivered on or before the date on which the offer lapses.

The attention of member firms of Nasdaq is drawn to certain UK dealing disclosure requirements. The announcement on 3 March 2004 commenced an offer period under the City Code which is published and administered by the Panel. Merant has equity securities traded on the London Stock Exchange and Nasdaq. SERENA has equity securities traded on Nasdaq.

The above disclosure requirements are set out in Rule 8 of the Code. In particular, Rule 8.3 requires public disclosure of dealings during an offer period by persons who own or control or pursuant to an agreement or understanding (whether formal or informal), or who would as a result of any transaction own or control, 1 per cent. or more of any class of relevant securities of Merant and/or SERENA. Relevant securities include Merant securities, SERENA shares and instruments convertible into either Merant securities or SERENA shares. This requirement will apply until the end of the initial offer period.

Disclosure should be made on the appropriate form before 12 noon (London time), on the business day following the date of the dealing transaction. These disclosures should be sent to a Regulatory Information Service in the UK and to the Panel (fax number: +44 20 7256 9386).

Member firms should advise those of their clients who wish to deal in the relevant securities of Merant or SERENA, whether in the US or the UK, that they may be affected by these requirements. If there is any doubt as to their application, the Panel should be consulted (telephone number +44 20 7638 0129, fax number +44 20 7256 9386).

PART B FURTHER TERMS OF THE OFFER

The following further terms apply, unless the contrary is expressed or the context requires otherwise, to the offer.

Unless the context otherwise requires, any reference in Part B of this Appendix 1 and in the acceptance form:

- (i) to the offer will mean the offer and will include any revision, variation or renewal thereof or extension thereto and any election in connection therewith;
- (ii) to the offer becoming unconditional as to acceptances means the Acceptance Condition becoming or being determined by SERENA to be satisfied;

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- (iii) to the offer becoming unconditional in all respects means all conditions being fulfilled, satisfied or, to the extent permitted, waived; and
- (iv) to acceptances of the offer shall include deemed acceptances of the offer.

1. ACCEPTANCE PERIOD

- (a) The offer is initially open for acceptance until 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004. SERENA reserves the right (but will not be obliged, other than as may be required by the City Code or the Exchange Act and the rules and regulations thereunder) at any time or from time to time to extend the offer after such time and, in such event, will make a public announcement of such extension in

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the manner described in paragraph 3 below. If all of the conditions are not satisfied, fulfilled or, to the extent permitted, waived by SERENA as at 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004, the offer will lapse and no Merant securities will be purchased under it unless SERENA extends the offer by specifying a later closing date. If all of the conditions have been satisfied, fulfilled or waived by such time (i.e., the end of the initial offer period), the offer will be extended for a subsequent offer period of at least 14 calendar days.

- (b) Although no revision is envisaged, if the offer is revised, the offer will be extended, if necessary, for a period of at least 14 calendar days (or such lesser period as may be permitted by the Panel and in accordance with the Exchange Act) from the date on which written notification of the revised offer is posted to Merant securityholders. Except with the consent of the Panel, no revision of the offer may be made after 3 May 2004 or, if later, the date which is 14 calendar days before the last date on which the offer can become unconditional as to acceptances.

- (c) Except with the consent of the Panel, the offer, whether revised or not, shall not be capable of becoming unconditional as to acceptances (nor, therefore, unconditional in all respects) and, accordingly, the initial offer period is not (except with the consent of the Panel) capable of being extended, after midnight (London time), 7.00 pm (New York City time), on 17 May 2004 (or any other earlier time or date beyond which SERENA has stated that the offer will not be extended and has not withdrawn that statement). If all of the conditions are not satisfied, fulfilled or, to the extent permitted, waived at such time or any later closing date to which the initial offer period has been duly extended, the offer will lapse unless the Panel agrees otherwise. If the offer lapses for any reason, the offer shall cease to be capable of further acceptance and SERENA and Merant securityholders shall cease to be bound by prior acceptances. SERENA reserves the right, with the permission of the Panel and in accordance with the Exchange Act, to extend the final date for acceptance of the offer and for the satisfaction of the Acceptance Condition and all the other conditions and, accordingly, the initial offer period. SERENA may declare the offer wholly unconditional at any time after 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004 (or such later time as the offer is required to be extended pursuant to the City Code or US law).

- (d) SERENA reserves the right (but will not be obliged) at any time and from time to time to extend the subsequent offer period for any period it chooses. The subsequent offer period must remain open for at least 14 calendar days but may be extended beyond that time until a further specified date or until further notice. If SERENA states that the offer will remain open until further notice, SERENA will give not less than 14 calendar days' notice in writing to Merant securityholders who have not accepted the offer before closing the subsequent offer period.

- (e) If a competitive situation arises (as determined by the Panel) after a 'no increase' and/or 'no extension' statement has been made by or on behalf of SERENA in relation to the offer, SERENA may, if it has specifically reserved the right to do so at the time the statement is made (or otherwise with the consent of the Panel), withdraw the statement and be free to increase or, as the case may be, to extend the offer provided that it complies with the requirements of the City Code and the Exchange Act and in particular that:
 - (i) it announces the withdrawal as soon as possible and in any event within four business days after the date of the announcement of the competing offer or other competitive situation;
 - (ii) it notifies Merant securityholders in writing of the withdrawal (or, in the case of Merant securityholders with registered addresses outside the United Kingdom or United States, or whom SERENA reasonably believes to be nominees, custodians or trustees holding Merant securities for such persons, by announcement in the United Kingdom and United States) at the earliest practicable opportunity; and
 - (iii) any Merant securityholders who accepted the offer after the date of the 'no increase' or 'no extension' statement are given a right of withdrawal in accordance with paragraph 4(d) of Part B of this Appendix below. Withdrawal rights will apply in any event during the initial offer period.

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SERENA may, if it has specifically reserved the right to do so at the time the statement is made, choose not to be bound by the terms of a no increase or no extension statement if it would otherwise prevent the posting of an increased or improved offer (either as to the value or nature of the consideration offered or otherwise) which is recommended for acceptance by the board of directors of Merant, or in other circumstances permitted by the Panel.

2. ACCEPTANCE CONDITION

- (a) For the purposes of determining whether the Acceptance Condition has been satisfied, SERENA may, except as otherwise agreed by the Panel, only take into account acceptances received in respect of or purchases of Merant securities made in respect of which all relevant documents are received by the UK Receiving Agent or the US Depositary by 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004 or such later closing date as may be specified but, except with the consent of the Panel, not later than 1.00 pm on 17 May 2004 or, in each case, any earlier closing date beyond which SERENA has stated that the offer will not be extended (unless the conditions are at that closing date satisfied, fulfilled or, to the extent permitted, waived) and has not withdrawn that statement.

If, with the consent of the Panel, the latest time and date at which the offer may become unconditional as to acceptances (and thus the latest time at which it may become unconditional in all respects) is extended beyond midnight (London time), 7.00 pm (New York City time), on 17 May 2004, so that the initial offer period is accordingly extended, acceptances received and purchases made in respect of which the relevant documents are received by the UK Receiving Agent or the US Depositary after 1.00 pm (London time), 8.00 am (New York City time), on or after that later date may only be taken into account with the agreement of the Panel, except where the City Code permits otherwise.

- (b) Except as otherwise agreed by the Panel:

- (i) an acceptance of the offer in respect of Merant securities will only be treated as valid for the purposes of the Acceptance Condition if the requirements of Note 4 and, if applicable, Note 6 to Rule 10 of the City Code are satisfied in respect of it;
- (ii) a purchase of Merant securities by SERENA or its nominee or (if SERENA is required by the Panel to make an offer for Merant securities under Rule 9 of the City Code) by a person acting in concert with SERENA or its nominee, will only be treated as valid for the purposes of the Acceptance Condition if the requirements of Note 5 and, if applicable, Note 6 to Rule 10 of the City Code are satisfied in respect of it; and
- (iii) before the offer may become unconditional as to acceptances the UK Receiving Agent must issue a certificate to SERENA or Lehman Brothers which states the number of Merant securities in respect of which acceptances have been received and not validly withdrawn and the number of Merant securities otherwise acquired, whether before or during the offer period, which comply with the provisions of the City Code referred to in this paragraph 2(b). Copies of such certificate will be sent to the Panel as soon as possible after it is issued.
- (c) For the purpose of determining whether the Acceptance Condition has been satisfied, SERENA shall be entitled to take into account only those Merant securities carrying voting rights which have been unconditionally allotted or issued, whether pursuant to the exercise of conversion or subscription rights or otherwise, before the determination takes place and written notice of the allotment or issue of which, containing all relevant details, has been received before that time by the UK Receiving Agent or the US Depositary on behalf of SERENA from Merant or its agents at one of the addresses set out in the section of this document entitled Further Information. Notification by e-mail, telex or facsimile transmission does not constitute written notice for this purpose.

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- (d) In accordance with applicable SEC rules, at least five business days prior to any reduction in the percentage of Merant shares (including Merant shares represented by Merant ADSs) required to satisfy the Acceptance Condition, SERENA will announce that it has reserved the right to reduce the Acceptance Condition. The announcement will be made through a press release designed to inform Merant securityholders in the United Kingdom and elsewhere and/or by placing an advertisement in a newspaper of national circulation in the United States. Such announcement will state the exact percentage to which the Acceptance Condition may be reduced, will state that such a reduction is possible but that SERENA need not declare its actual intentions until it is required to do so under the City Code and will contain language advising Merant securityholders to withdraw their Merant securities if their willingness to accept the offer would be affected by a reduction of the Acceptance Condition. SERENA will not make such an announcement unless it believes that there is a significant possibility that a sufficient number of acceptances will be received to permit the Acceptance Condition to be satisfied at such reduced level and that the other conditions will be satisfied, fulfilled or, to the extent permitted, waived at such time. Merant securityholders who are not willing to accept the offer if the Acceptance Condition is reduced to a level lower than 90 per cent. should not accept the offer until it becomes or is declared unconditional as to acceptances (which may be at a level lower than 90 per cent.) and/or be prepared to withdraw their acceptances promptly following an announcement by SERENA of its reservation of the right to reduce the Acceptance Condition. Upon any announcement being made that the percentage of Merant shares (including Merant shares represented by Merant ADSs) required to satisfy the Acceptance Condition may be reduced, the offer shall not be capable of becoming or being declared unconditional in all respects until the expiry of at least five business days thereafter. Merant securityholders will be able to accept the offer for at least five business days after a reduction of the Acceptance Condition either during the initial offer period or the subsequent offer period. If SERENA states that the offer will remain open until further notice, SERENA will not give less than 14 calendar days' notice in writing to Merant securityholders who have not accepted the offer before closing.

3. ANNOUNCEMENTS

- (a) Without prejudice to paragraph 4 below, by 8.00 am (London time) in the UK and 8.00 am (New York City time) in the US on the business day after the day on which the offer is due to expire or becomes unconditional in all respects or on which the offer is revised or is extended, as the case may be, or such later time or date as the Panel may agree subject to compliance with US securities laws, referred to as the relevant day, SERENA will make an appropriate announcement and inform the London Stock Exchange and the Dow Jones News Service. In the announcement SERENA will state (unless otherwise permitted by the Panel) the total number of Merant securities and rights over Merant securities (as nearly as practicable):
- (i) for which acceptances of the offer have been received, showing the extent, if any, to which such acceptances have been received from persons acting or deemed to be acting in concert with SERENA for the purposes of the offer;
 - (ii) held by or on behalf of SERENA or any person acting or deemed to be acting in concert with SERENA for the purposes of the offer before the offer period; and
 - (iii) acquired or agreed to be acquired by or on behalf of SERENA or any person acting or deemed to be acting in concert with SERENA for the purposes of the offer during the offer period;

and the announcement will specify the percentage of the Merant securities represented by each of these figures.

- (b) In calculating the number of Merant securities represented by acceptances and purchases, SERENA may only include acceptances and purchases if they could be counted towards fulfilling the Acceptance Condition under Notes 4, 5 and 6 to Rule 10 of the City Code, unless the Panel agrees otherwise. Subject to this, SERENA may include or exclude, for announcement purposes, acceptances and purchases not in all respects in order or which are subject to verification.

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- (c) Any decision to extend the offer may be made at any time up to, and will be announced by, 8.00 am (London time) in the UK and 8.00 am (New York City time) in the US on the relevant day (or such later time and/or date as the Panel may agree). If the offer is not yet unconditional in all respects (so that the initial offer period has not yet expired) the announcement will state the next closing date or, if the offer has become unconditional in all respects (with the result that the initial offer period has ended), the announcement will state that the offer will remain open for a subsequent offer period until further notice or until a further specified date not less than 14 calendar days after the end of the initial offer period.
- (d) In this Appendix, a reference to the making of an announcement or the giving of notice by or on behalf of SERENA includes the release of an announcement by SERENA's public relations consultants or Lehman Brothers, in each case on behalf of SERENA, to the press and the delivery by hand or telephone, e-mail, telex or facsimile or other electronic transmission of an announcement to the London Stock Exchange and the Dow Jones News Service, as the case may be, and the making of an announcement in any other appropriate manner in accordance with the Code and applicable law (including Rules 14d-4(c) and 14d-6(c) under the Exchange Act, which require that any material change in the information published, sent or given to Merant securityholders in connection with the offer be promptly sent to Merant securityholders in a manner reasonably designed to inform them of such change). An announcement made otherwise than to the London Stock Exchange and the Dow Jones News Service will be notified simultaneously to the London Stock Exchange and the Dow Jones News Service.
- (e) Without limiting the manner in which SERENA may choose to make any public announcement and, subject to SERENA's obligations under applicable law (including Rules 14d-4(c) and 14d-6(c) under the Exchange Act relating to SERENA's obligations to disseminate promptly public announcements concerning material changes to the offer), SERENA will have no obligation to publish, advertise or otherwise communicate any such public announcement other than by making a release to the London Stock Exchange and the Dow Jones News Service.

4. RIGHTS OF WITHDRAWAL

- (a) Except as provided by this paragraph 4, acceptances and elections are irrevocable.
- (b) Merant securities in respect of which valid acceptances have been received may be withdrawn pursuant to the procedures set out below at any time during the initial offer period and in certain other circumstances described below. Merant securities in respect of which valid acceptances have been received during the initial offer period and that are not validly withdrawn during the initial offer period and Merant securities in respect of which valid acceptances have been received during the subsequent offer period may not be withdrawn. SERENA may declare the offer wholly unconditional and thereby terminate the initial offer period and Merant securityholders' withdrawal rights at any time after 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004 (or such later time as the offer is required to be extended pursuant to the City Code or US law). Holders of Merant securities will not have withdrawal rights during the subsequent offer period, except in certain limited circumstances described below. The subsequent offer period must remain open for at least 14 calendar days but may be extended beyond that time until a further specified date or until further notice.
- (c) SERENA will only announce that the Acceptance Condition has been satisfied if all the other conditions are also satisfied, fulfilled or, to the extent permitted, waived and the initial offer period will terminate. Withdrawal rights will also terminate at that time, unless SERENA then fails to comply by 3.30 pm (London time), 10.30 am (New York City time), on the relevant day (as defined in paragraph 3(a) of this Part B) (or such later time and/or date as the Panel may agree) with any of the other requirements specified in paragraph 3(a) of Part B of this Appendix, in which case a Merant securityholder who has previously accepted the offer may withdraw such securityholder's acceptance of the offer by written notice in compliance with paragraphs 4(e) and (f) of Part B of this Appendix (if appropriate) given by post or by hand to the UK Receiving Agent or the US Depository at the addresses set forth in the section of this document entitled Further Information.

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Subject to paragraph 1(c) of Part B of this Appendix, this right of withdrawal may be terminated not less than eight calendar days after the relevant day by SERENA confirming that the offer is still unconditional, and complying with the other requirements specified in paragraph 3(a) of Part B of this Appendix. If that confirmation is given, the first period of 14 calendar days referred to in paragraph 1(b) of Part B of this Appendix will start on the date of that confirmation and compliance.

- (d) If a no increase and/or no extension statement is withdrawn in accordance with paragraph 1(e) of Part B of this Appendix, a person who accepts the offer after the date of the statement may withdraw that person's acceptance in the manner set out in paragraph 4(c) of Part B of this Appendix during the period of eight calendar days after the date SERENA posts the notice of the withdrawal of that statement to Merant securityholders.
- (e) To be effective, a written notice of withdrawal must be received, subject to paragraphs 4(c) and (d) of Part B of this Appendix, before the end of the initial offer period by the party (either the UK Receiving Agent or the US Depository) to whom the acceptance form was originally returned by the relevant Merant securityholder and must specify the name of the person from whom the acceptance was received, the number of Merant securities to be withdrawn and (if share certificates or Merant ADRs, as the case may be, have been provided) the name of the registered holder of the relevant Merant securities, if different from the name of the person from whom the acceptance was received.
- (f) In respect of Merant ADSs, if Merant ADRs have been delivered or otherwise identified to the US Depository, then, prior to the physical release of such Merant ADRs, the serial numbers shown on such Merant ADRs must be submitted and, unless the Merant ADSs evidenced by such Merant ADRs have been delivered by an Eligible Institution, the signatures on the notice of withdrawal must be guaranteed by an Eligible Institution. If interests in Merant ADSs evidenced by Merant ADRs have been delivered pursuant to the procedures for book-entry transfer set out in paragraph 12(c) of Part B of this Appendix, any notice of withdrawal must specify the name and number of the account at the appropriate Book-Entry Transfer Facility to be credited with the withdrawn Merant ADSs and must otherwise comply with such Book-Entry Transfer Facility's procedures.
- (g) In this paragraph 4, written notice (including any letter of appointment, direction or authority) means notice in writing bearing the original signature(s) of the relevant accepting Merant securityholder(s) or the securityholder's agent(s) duly appointed in writing (evidence of whose appointment is produced with the notice in a form satisfactory to SERENA). Notification by telex or facsimile or other electronic transmission or copies will not be sufficient to constitute written notice. Any notice which is postmarked in or otherwise appears to SERENA or its agents to have been sent from Canada, Australia or Japan may be treated as not valid.
- (h) Withdrawals of Merant securities in respect of which valid acceptances have been received may not be rescinded (without SERENA's consent) and any Merant securities properly withdrawn and in respect of which valid acceptances have not been received thereafter will thereafter be deemed not to be the subject of a valid acceptance for the purposes of the offer. Withdrawn Merant securities may be subsequently the subject of a valid acceptance, however, by following one of the procedures described in either paragraph 10, 11 or 12 of Part B of this Appendix, as the case may be, at any time whilst the offer remains open.
- (i) All questions as to the validity (including time of receipt) of any notice of withdrawal will be determined by SERENA, whose determination (except as required by the Panel) will be final and binding. None of SERENA, Merant, Lehman Brothers, the US Depository, the Information Agent, the UK Receiving Agent or any other person will be under any duty to give notification of any defects or irregularities in any notice of withdrawal or incur any liability for failure to give such notification or for any determination under this paragraph (i).

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5. MIX AND MATCH ELECTION

- (a) Merant securityholders who validly accept the offer will be able to request under the mix and match election to vary the proportions in which they receive SERENA shares and cash in respect of their Merant securities.

The maximum number of new SERENA shares to be issued under the offer and the maximum amount of cash to be paid under the offer will not be varied as a result of the mix and match election. Accordingly, a Merant securityholder's mix and match election will be satisfied only to the extent that other Merant securityholders make opposite elections. To the extent that elections cannot be satisfied in full, they will be scaled down on a pro rata basis. To the extent that elections can be satisfied, electing Merant securityholders will receive new SERENA shares instead of cash, and vice versa.

- (b) Valid elections for new SERENA shares made by Merant securityholders in excess of their basic entitlement to new SERENA shares will be satisfied in full where sufficient new SERENA shares are available as a result of other accepting Merant securityholders validly making elections for cash in excess of their basic entitlements under the offer, thereby releasing new SERENA shares to which they would otherwise be entitled under the offer.

If, under the mix and match election, the number of new SERENA shares made available as a result of valid elections for cash in excess of the basic entitlement thereto is insufficient to satisfy in full all valid elections for new SERENA shares in excess of Merant securityholders' basic entitlements thereto, then such excess elections will be scaled down on a pro rata basis and the balance of the consideration will be satisfied in cash in accordance with the basic terms of the offer.

- (c) Valid elections for cash made by Merant securityholders in excess of their basic entitlement to cash will be satisfied in full where sufficient cash is available as a result of other accepting Merant securityholders validly making elections for new SERENA shares in excess of their basic entitlement under the offer, thereby releasing cash to which they would otherwise be entitled under the offer.

If, under the mix and match election, the amount of cash made available as a result of valid elections for new SERENA shares in excess of the basic entitlement thereto is insufficient to satisfy in full all valid elections for cash in excess of Merant securityholders' basic entitlements thereto, then such elections will be scaled down on a pro rata basis and the balance of the consideration will be satisfied in accordance with the basic terms of the offer.

- (d) All adjustments to the amount of cash or SERENA shares received by any Merant securityholder in the mix and match election will be calculated based on a value per Merant share of 195 pence and a value per SERENA share of £11.78. The value of SERENA share for these purposes is based on the average of the dollar/pound sterling noon buying rate for the five trading days ended 3 March 2004 and the average of the closing prices of one SERENA share as reported on Nasdaq for the 20 US trading days ended 1 March 2004.
- (e) Although the offer will remain open for a subsequent offer period of at least 14 calendar days after the date on which the offer becomes or is declared unconditional in all respects (at the end of the initial offer period) and may be extended beyond that time until a further specified date, the mix and match election will remain open until but not beyond 3.00 pm (London time), 10.00 am (New York City time), on the date falling five calendar days after the date on which the offer becomes or is declared unconditional in all respects.
- (f) No election for the mix and match election will be valid unless both a valid acceptance of the offer and a valid election for the mix and match election, duly completed in all respects and (i) accompanied by all relevant share certificate(s), Merant ADRs and/or other document(s) of title in respect of Merant securities in certificated form, or, (ii) if the Merant securities to which the acceptance relates are in uncertificated form, a settlement of a transfer to escrow instruction in favour of the UK Receiving Agent as escrow agent in relation to

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Merant shares or an Agent's Message to the US Depository in relation to Merant ADSs in accordance with the procedures set out in this document, are duly received by the time and date on which the mix and match election closes.

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- (g) In the event that a Merant securityholder purports to elect for both additional cash and additional new SERENA shares under the mix and match election, both purported elections shall be deemed to be void, and such Merant securityholder shall be deemed to have accepted the offer on its basic terms in respect of all the Merant securities to which the relevant acceptance form relates or is deemed to relate.
- (h) If any acceptance form which includes an election for the mix and match election is either received after the time and date upon which the mix and match election closes or is received before such time and date but is not, and is not deemed to be, valid or complete in all respects at such time and date, such election shall, for all purposes, be void and the Merant securityholder purporting to make such election shall not, for any purpose, be entitled to receive any variation of consideration under the mix and match election, but such acceptance, if otherwise valid, shall, subject to the provisions of paragraph (j) below, be deemed to be an acceptance of the offer in respect of the number of Merant securities indicated in the relevant acceptance form and the relevant Merant securityholder will, upon the offer becoming unconditional in all respects be entitled to receive the basic consideration due under the offer in respect thereof.
- (i) The mix and match election will lapse if the offer lapses or expires. An election under the mix and match election may only be made in respect of Merant securities for which the offer is validly accepted. Merant securityholders who do not make a mix and match election will receive the basic terms of the offer. Mix and match elections must be made at the same time as the acceptances of the offer to which they relate, on the relevant acceptance form.
- (j) A mix and match election made by a Merant securityholder may not be changed after the time that it is first made on the relevant acceptance form. However, acceptances including the associated mix and match election may be withdrawn in accordance with the procedures in paragraph 4 of Part B of this Appendix. This right of withdrawal, except in the limited circumstances set out in paragraphs 4(b), (c) and (d) of Part B of this Appendix terminates at the time that the offer becomes unconditional in all respects (i.e. at the end of the initial offer period). Accordingly, mix and match elections made in the 5 calendar day period between the end of the initial offer period and the time and date at which the mix and match election ceases to be open for acceptance cannot be changed or withdrawn.

6. INDUCEMENT FEE

In consideration of, and as an inducement to, SERENA making the offer, Merant has agreed to pay SERENA a fee of £2.06 million (US\$3.71 million based on the noon buying rate of US\$1.7993 : £1.00 on 15 March 2004, the latest practicable date prior to the posting of this document) in certain limited circumstances. Save in certain limited circumstances including failure to obtain approval for the offer under the HSR Act or other applicable antitrust law, this fee is payable on either of the following events:

- (a) if a higher competing offer or other competing transaction (or an intention to do either) is publicly announced by a third party and the Merant board fails to reaffirm its unanimous recommendation of the offer and subsequently the offer lapses or is withdrawn; or
- (b) if the board of Merant withdraws or modifies its recommendation of the offer by SERENA.

7. REVISION OF THE OFFER

- (a) Although no revision is envisaged, if the offer (in its original or previously revised form(s)) is revised (either in terms or conditions or in the value or form of the consideration offered or otherwise) and whether or not the mix and match election (in its original or any previously revised form is revised, the benefit of the revised offer will, subject as provided in paragraphs 7(b), 7(c), 7(e) and 9 of Part B of this Appendix, be made available to a Merant securityholder who has validly accepted the offer (in its original or any revised form(s)) and not validly withdrawn such acceptance, referred to as a previous acceptor, if the revised offer represents, on the date on which it is announced (on such basis as Lehman Brothers and SERENA may consider appropriate), an improvement, or no diminution, in the value of the consideration offered (with the cash consideration consisting of an amount no less than set out in this document) compared with the

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consideration or terms previously offered. The acceptance by or on behalf of a previous acceptor of the offer (in its original or any revised form(s)) will, subject as provided in paragraphs 7(b), 7(c), 7(e) and 9 of Part B of this Appendix, be deemed an acceptance of the revised offer and will constitute the appointment of and direction to any director of SERENA or of Lehman Brothers as such previous acceptor's attorney and/or agent with authority, whether or not such previous acceptor shall have elected for the mix and match election:

- (i) to accept the revised offer on the previous acceptor's behalf;
- (ii) if the revised offer includes alternative forms of consideration, to make on the previous acceptor's behalf elections for and/or accept the alternative forms of consideration on the previous acceptor's behalf in the proportions the attorney and/or agent in his absolute discretion thinks fit; and
- (iii) to execute on the previous acceptor's behalf and in the previous acceptor's name any further documents and take such further actions (if any) as may be required to give effect to those elections or acceptances.

In making any election and/or acceptance, the attorney and/or agent will take into account the nature of any previous acceptance or election made by or on behalf of the previous acceptor and such other facts or matters as he may reasonably consider relevant. The attorney and/or agent shall not be liable to any Merant securityholder or any other person in making any such election and/or acceptance or in making any determination in respect thereof. In this paragraph, the expression the offer shall, and shall be deemed to, mean and include the offer and/or the mix and match election and/or all or any alternative forms of consideration to be given under the offer and any combination or choice of the offer and/or the mix and match election and/or all or any alternative forms of consideration.

- (b) The deemed acceptance and/or election referred to in paragraph 7(a) of Part B of this Appendix will not apply and the power of attorney and authorities conferred by that paragraph will not be exercised if, as a result, the previous acceptor would (on such basis as Lehman Brothers and SERENA may consider appropriate) receive less in aggregate in consideration under the offer than the previous acceptor would have received in aggregate in consideration as a result of the previous acceptor's acceptance of the offer in the form originally accepted by the previous acceptor or on the previous acceptor's behalf (unless the previous acceptor has previously agreed in writing to receive less in aggregate consideration).
- (c) The deemed acceptance and/or election referred to in paragraph 7(a) of Part B of this Appendix will not apply and the power of attorney and the authorities conferred by that paragraph will be ineffective in the case of a previous acceptor who lodges, within 14 calendar days of the posting of the document containing the revised offer and/or any revised or other alternative or election, an acceptance form (or any other form issued on behalf of SERENA) in which he validly elects to receive consideration under the revised offer in some other manner than that set out in the previous acceptor's original acceptance.
- (d) SERENA and Lehman Brothers reserve the right to treat an executed acceptance form relating to the offer (in its original or any previously revised form(s)) which is received (or dated) after the announcement of any revised offer as a valid acceptance of the revised offer (and where applicable a valid election for the alternative forms of consideration). That acceptance will constitute an authority in the terms of paragraph 7(a) of Part B of this Appendix on behalf of the relevant Merant securityholder.
- (e) If SERENA makes a material change in the terms of the offer or if it waives a material condition of the offer prior to the end of the initial offer period, SERENA will disseminate additional offer materials and extend the offer to the extent required by Rules 14d-4(d), 14d-6(c) and 14e-1 under the Exchange Act. The minimum period during which an offer must remain open following material changes in the terms of the offer, other than a change in price or a change in the percentage of securities sought, will depend upon the facts and circumstances then existing, including the materiality of the changes. With respect to a change in price or, subject to certain limitations, a change in the percentage of securities sought, a minimum of ten business days is generally required to allow for adequate dissemination to Merant securityholders. Any reduction of the Acceptance Condition will be effected and announced in the manner described in paragraph 2(d) of Part B of this Appendix.

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8. GENERAL

- (a) If the offer lapses or is withdrawn, neither SERENA nor any person acting, or deemed to be acting, in concert with SERENA for the purposes of the offer nor any of their respective affiliates may, pursuant to the City Code, make an offer (whether inside or outside the United Kingdom) for Merant securities for a period of one year following the date of such lapse or withdrawal, except with the permission of the Panel.
- (b) If the offer lapses or is withdrawn, acceptance forms, Merant share certificates, Merant ADRs and other documents of title will be returned by post (or by such other method as the Panel may approve) within 14 calendar days of the offer lapsing or being withdrawn, at the risk of the Merant securityholder in question, to the person or agent whose name and address (outside Canada, Australia or Japan) is set out in the relevant box on the acceptance form or, if none is set out, to the first-named holder at the holder's registered address (outside Canada, Australia or Japan) or, in the case of Merant ADSs delivered by book-entry transfer into the US Depository's account at a Book-Entry Transfer Facility pursuant to the procedures set forth in paragraph 12(c) of Part B of this Appendix, such Merant ADSs will be credited within such period to an account maintained at the appropriate Book-Entry Transfer Facility.
- (c) The UK Receiving Agent will, immediately after the offer lapses (or within such longer period as the Panel may permit, not exceeding 14 calendar days of the offer lapsing) instruct CRESTCo to transfer all Merant shares held in escrow balances and in relation to which it is the escrow agent for the purposes of the offer to the original available balances of the relevant Merant securityholders.
- (d) Except with the consent of the Panel:
- (i) settlement of the consideration to which any Merant securityholder is entitled under the offer will be fully implemented in accordance with the terms of the offer without regard to any lien, right of set-off, counterclaim or other analogous right to which SERENA or Lehman Brothers may otherwise be, or claim to be, entitled against that Merant securityholder; and
- (ii) settlement of the consideration will be effected in the manner prescribed in paragraph 15 of the letter from Lehman Brothers not later than 14 calendar days after the later of the date on which the offer becomes wholly unconditional and the date of receipt of a valid and complete acceptance form from such Merant securityholder.
- (e) The terms, provisions, instructions and authorities contained in the acceptance forms also constitute part of the terms of the offer. A word or expression defined in this document has the same meaning when used in an acceptance form, unless the context requires otherwise. The provisions of this Appendix shall be deemed to be incorporated in the acceptance forms.
- (f) Any omission or failure to dispatch this document, the acceptance forms, any other documents relating to the offer or any notice required to be dispatched under the terms of the offer to, or any failure to receive the same by, any person to whom the offer is, or should be, made will not in any way invalidate the offer or create any implication that the offer has not been made to any such person. Subject to the provisions of paragraph 9 of Part B of this Appendix, the offer is made to any Merant securityholder to whom this document and the acceptance forms or any related document may not have been dispatched or who may not receive such documents, and these persons may collect the relevant documents from the UK Receiving Agent, the US Depository or the Information Agent at the addresses set forth in the section of this document entitled "Further Information".
- (g) Subject to the City Code, SERENA and Lehman Brothers reserve the right to treat as valid in whole or in part any acceptance of the offer if received by the UK Receiving Agent or the US Depository or otherwise on behalf of SERENA which is not entirely in order or in the correct form or which is not accompanied by (as applicable) the relevant transfer to escrow or the relevant share certificates, Merant ADRs and/or other documents of title which are received by them in a form or at a place or places other than as set out in this document or the relevant acceptance form. In that event, no issue of new SERENA shares or payment of cash under the offer will be made until after the acceptance is entirely in order and (as applicable) the relevant transfer to escrow has settled or the relevant share certificate(s), Merant

ADRs and/or other

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document(s) of title or indemnities satisfactory to SERENA have been received by the UK Receiving Agent or the US Depository, as the case may be.

- (h) If all of the conditions have been either satisfied, fulfilled or, to the extent permitted, waived and SERENA has acquired or contracted to acquire, pursuant to the offer or otherwise, at least 90 per cent. in nominal value of the Merant shares (including Merant shares represented by Merant ADSs) to which the offer relates, before the end of the four month period provided by the Companies Act, SERENA will be entitled, and intends, to acquire the remaining Merant securities on the same terms as the offer pursuant to the compulsory acquisition procedure set out in sections 428 to 430E of the Companies Act (see paragraph 11 of Appendix 5 and Appendix 6 to this document). When the offer becomes or is declared unconditional in all respects, SERENA intends to procure the making of an application by Merant for the removal of Merant shares from the Official List of the UK Listing Authority and for the cancellation of trading in Merant shares on the London Stock Exchange market for listed securities and also for the delisting of Merant ADSs and Merant shares from Nasdaq. The Merant shares do not trade in Nasdaq and are listed on Nasdaq only in connection with the Merant ADS programme. It is anticipated that cancellation of listing from the Official List and cancellation of trading on the London Stock Exchange will take effect no earlier than 20 business days after the offer becomes or is declared unconditional in all respects. Delisting would significantly reduce the liquidity and marketability of any Merant securities with respect to which valid acceptances were not received in the offer. SERENA will make an announcement at least 20 business days prior to cancellation of listing from the Official List and the cancellation of trading on the London Stock Exchange specifying the exact date upon which Merant shares will be delisted. While it is anticipated that cancellation of both listings will take place at the same time, cancellation of the listing of the Merant ADSs and Merant shares on Nasdaq could take place earlier than cancellation of the listing and trading of the Merant shares on the Official List of the UK Listing Authority and the London Stock Exchange, respectively.
- (i) All powers of attorney, appointments of agents and authorities on the terms conferred by or referred to in this Appendix or in the acceptance forms are given by way of security for the performance of the obligations of the relevant Merant securityholders and are irrevocable in accordance with section 4 of the Powers of Attorney Act 1971, except in the circumstances where the donor of the power of attorney or authority validly withdraws the donor's acceptance in accordance with paragraph 4 of Part B of this Appendix 1.
- (j) No acknowledgement of receipt of any acceptance form, share certificate, Merant ADR or other document of title will be given. All communications, notices, certificates, Merant ADRs, documents of title and remittances to be delivered by, and sent to or from, Merant securityholders (or their designated agent(s)) will be delivered or sent at their own risk.
- (k) If a Merant securityholder has existing SERENA shares, the mandates, instructions and instruments in force for the existing SERENA shares will continue in force in relation to new SERENA shares received under the offer.
- (l) SERENA and Lehman Brothers reserve the right to notify any matter, including the making of the offer, to all or any Merant securityholders:
 - (i) with a registered address outside the United Kingdom and the United States; or
 - (ii) whom SERENA or Lehman Brothers knows to be a custodian, trustee or nominee holding Merant securities for persons who are citizens, residents or nationals of jurisdictions outside the United Kingdom and the United States,

by announcement in the United Kingdom to the London Stock Exchange and in the United States to the Dow Jones News Service or in any other appropriate manner or by paid advertisement in newspapers published and circulated in the United Kingdom and the United States. Such notice will be deemed to have been sufficiently given, despite any failure by a Merant securityholder to receive or see that notice. A reference in this document to a notice or the provision of information in writing by or on behalf of SERENA is to be construed accordingly. No such document will be sent to an address in Canada, Australia or Japan.

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- (m) The offer is made at 3.00 pm (London time), 10.00 am (New York City time), on 18 March 2004 and is capable of acceptance from and after that time. Acceptance forms and copies of this document may be collected from the UK Receiving Agent, the US Depository or the Information Agent at one of the addresses set forth in the section of this document entitled Further Information. The offer is made in the United States by SERENA on its own behalf. The terms and conditions set forth in the letter from Lehman Brothers apply equally to such offer.
- (n) This offer will be announced by means of a release to the UK Regulatory News Service on 18 March 2004.
- (o) The offer, all acceptances of the offer, all elections in respect of it and the contract to which it gives rise, are governed by and will be construed in accordance with English law. Execution by or on behalf of a Merant securityholder of an acceptance form constitutes the securityholder's irrevocable submission to the jurisdiction of the courts of England in relation to all matters arising in connection with the offer. However, the conduct of the offer is also subject to US federal securities laws and the securities laws of the US states and other jurisdictions in the US in which the offer is being made if, and to the extent, applicable to the offer.
- (p) References in paragraphs 10, 11 and 12(i) of this Part B to a Merant securityholder, a holder of Merant shares and a holder of Merant ADSs will include references to the person or persons executing the acceptance form and in the event of one or more than one such person executing an acceptance form, such provisions shall apply to them jointly.
- (q) In relation to any acceptance of the offer in respect of a holding of Merant shares which are in uncertificated form, SERENA reserves the right to make such alterations, additions or modifications as may be necessary or desirable to give effect to any purported acceptance of the offer, whether in order to comply with the facilities or requirements of CREST or otherwise, provided such alterations, additions or modifications are consistent with the requirements of the City Code or are otherwise made with the consent of the Panel.
- (r) All references in this Appendix to any statute or statutory provision shall include a statute or statutory provision which amends, consolidates or replaces the same (whether before or after the date hereof).
- (s) Fractions of new SERENA shares will not be allotted or issued to accepting Merant securityholders. To the extent that Merant securityholders are entitled to fractional shares, those fractional entitlements will be aggregated and sold in the market and the net proceeds of sale distributed pro rata to the holders of Merant shares and Merant ADSs entitled to them. In the case of holders of Merant ADSs, such payment will be made in US dollars, and in the case of holders of Merant shares, such payment will be made in pounds sterling, the applicable proceeds having been converted from US dollars at a prevailing exchange rate selected by SERENA at the relevant time. Individual entitlements to amounts of less than £2.50 (US \$4.50 based on a noon buying rate of US\$1.7993 : £1.00 as at 15 March 2004, the latest practicable date prior to the posting of this document) will not be paid to Merant securityholders, but will be retained for the benefit of the combined companies.
- (t) The Merant securities will be acquired by SERENA pursuant to the offer fully paid and free from all liens, equities, charges, equitable interests, encumbrances and other third party rights and interests of any nature whatsoever and together with all rights now or hereafter attaching thereto, including the right to receive and retain all dividends and other distributions, if any, declared, made or payable after 3 March 2004.
- (u) The new SERENA shares will be credited as fully paid, will rank pari passu in all respects with existing SERENA shares, dividends and other distributions declared, paid or made by reference to a record date after 3 March 2004. Appropriate adjustments to the number of SERENA shares paid in the offer will be made if SERENA effects a stock split, stock dividend or reverse stock split.

9. OVERSEAS MERANT SECURITYHOLDERS

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- (a) The making of the offer in, or to certain persons resident in, or nationals or citizens of, jurisdictions outside the United Kingdom or the United States or to their nominees or trustees may be prohibited or affected by the laws of the relevant jurisdiction. Merant securityholders who are persons, citizens, residents or nationals of jurisdictions outside the United Kingdom and the United States should inform themselves about and

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observe any applicable legal requirements. It is the responsibility of such Merant securityholders wishing to accept the offer to satisfy themselves as to the full observance of the laws of the relevant jurisdiction in connection with the offer. This includes the obtaining of any governmental, exchange control or other consents which may be required, compliance with other necessary formalities needing to be observed and the payment of any issue, transfer or other taxes due in that jurisdiction by whomsoever payable and SERENA and Lehman Brothers and any persons acting on their behalf will be fully indemnified and held harmless by any Merant securityholder for whom SERENA or Lehman Brothers are required to pay any issue, transfer or other taxes.

- (b) The offer is not being made, directly or indirectly, in or into Canada, Australia or Japan or by use of the mails of, or by any means or instrumentality of interstate or foreign commerce of, or of any facility of a national securities exchange of Canada, Australia or Japan. This includes, but is not limited to, e-mail, facsimile transmission, telex and telephone. Accordingly, copies of this document, the acceptance forms, and any related offering documents are not being, and must not be mailed, forwarded or otherwise distributed or sent in, into or from Canada, Australia or Japan. Persons receiving such documents (including, without limitation, custodians, nominees and trustees) must not distribute, mail or send them in, into or from Canada, Australia or Japan or use the Canadian, Australian or Japanese mails or any such means, instrumentality or facility for any purpose directly or indirectly in connection with the offer, and so doing may invalidate any related purported acceptance of the offer. Envelopes containing acceptance forms in respect of the offer must not be postmarked in Canada, Australia or Japan or otherwise dispatched from those jurisdictions and all acceptors must provide addresses outside Canada, Australia or Japan for the receipt of the consideration to which they are entitled under the offer or for the return of acceptance forms or documents of title.
- (c) Subject as provided below, a Merant securityholder will be deemed not to have accepted the offer if:
- (i) the securityholder puts **NO** in Box 7 of the form of acceptance and thereby cannot give the representations and warranties set out in paragraphs 11(b) and 12(i)(ii)(dd) of Part B of this Appendix;
 - (ii) the securityholder completes the relevant Box of the acceptance form with an address in Canada, Australia or Japan or has a registered address in Canada, Australia or Japan and in either case the securityholder does not insert in the relevant Box of the acceptance form the name and address of a person or agent outside Canada, Australia or Japan to whom the securityholder wishes the consideration to which the securityholder is entitled under the offer to be sent;
 - (iii) the securityholder inserts in the relevant Box of the acceptance form the name and address of a person or agent in Canada, Australia or Japan to whom the securityholder wishes the consideration to which the securityholder is entitled under the offer to be sent; or
 - (iv) the acceptance form received from the securityholder is in an envelope postmarked in, or which otherwise appears to SERENA or its agents to have been sent from, Canada, Australia or Japan.
- (d) If any person, despite the restrictions referred to in paragraph 9(b) of Part B of this Appendix and whether pursuant to a contractual or legal obligation or otherwise, forwards this document, the acceptance form or any related offering document in, into or from Canada, Australia or Japan or uses the mails or any means or instrumentality (including, without limitation, e-mail, facsimile transmission, telex and telephones) of interstate or foreign commerce of, or any facilities of a national securities exchange of Canada, Australia or Japan in connection with that forwarding, that person should:
- (i) inform the recipient of that fact;
 - (ii) explain to the recipient that such action may invalidate any purported acceptance by the recipient; and
 - (iii) draw the attention of the recipient to this paragraph 9.

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- (e) If any written notice from a Merant securityholder withdrawing such securityholder's acceptance in accordance with paragraph 4 of Part B of this Appendix 1 is received in an envelope postmarked in, or which otherwise appears to SERENA or its agents to have been sent from Canada, Australia or Japan, SERENA reserves the right, in its absolute discretion, to treat that notice as invalid.
- (f) The provisions of this paragraph 9 and any other terms of the offer relating to overseas holders of Merant securities may be waived, varied or modified as regards specific Merant securityholders or on a general basis by SERENA in its sole discretion. Subject to this discretion, the provisions of this paragraph 9 supersede any terms of the offer inconsistent with them. A reference in this paragraph 9 to a Merant securityholder includes the person or persons executing the acceptance form and, in the event of more than one person executing an acceptance form, the provisions of this paragraph 9 apply to them jointly and severally.

10. PROCEDURES FOR ACCEPTING THE OFFER IN RESPECT OF MERANT SHARES

- (a) Holders of Merant shares will have received with this document a form of acceptance. This section should be read together with the form of acceptance. The provisions of this section shall be deemed to be incorporated in, and to form a part of, the form of acceptance. The instructions printed on the form of acceptance shall be deemed to form part of the terms of the offer.

If a holder of Merant shares holds Merant shares in both certificated and uncertificated (that is, CREST) form, such holder should complete a separate form of acceptance for each holding. Similarly, such holder should complete a separate form of acceptance for Merant shares held in uncertificated form, but under different member account IDs, and for Merant shares held in certificated form, but under different designations.

- (b) To accept the offer, any Merant shareholder, including any person in the US who holds Merant shares, wishing to accept the offer in respect of all or any portion of such holder's Merant shares, should complete Box 1 and Box 2 and, if applicable, complete Boxes 3A or 3B, 4, 7, or 8 and, if such holder's Merant shares are in CREST, Box 6 on the form of acceptance. In all cases, Merant shareholders should then sign and date Box 5 of the form of acceptance in accordance with the instructions printed on it. All Merant shareholders who are individuals should sign the form of acceptance in the presence of a witness, who should also sign Box 5 in accordance with the instructions printed on it. Unless witnessed, an acceptance will not be valid.
- (c) An accepting Merant shareholder should return the completed, signed and (if you are an individual) witnessed form of acceptance, whether or not such Merant shares are in CREST, to the UK Receiving Agent. The completed form of acceptance, together, if such holder's Merant shares are in certificated form, with such holder's share certificate(s) and/or other document(s) of title, must be lodged with the UK Receiving Agent, as soon as possible, but in any event so as to arrive **NOT LATER THAN 3.00 PM (LONDON TIME), 10.00 AM (NEW YORK CITY TIME) ON 15 APRIL 2004.**

If you have any questions as to how to complete the form of acceptance please contact either (i) the UK Receiving Agent on 0870 162 3100, or if calling from outside the UK +44 20 8639 2157 or (ii) the Information Agent on 1 (800) 859-8509 if from the US, or 0800 917 8414 if from the UK or +44 20 7920 9700 from outside the UK.

- (d) If Merant shares are in uncertificated form, the holder should insert in Box 6 of the form of acceptance the participant ID and member account ID under which such Merant shares are held by him in CREST and otherwise complete and return the form of acceptance as described above. In addition, such holders should take (or procure to be taken) the action set out below to transfer the Merant shares in respect of which he wishes to accept the offer to an escrow balance, specifying the UK Receiving Agent (in its capacity as a CREST participant under the participant ID referred to below) as the escrow agent, as soon as possible but in any event so that the transfer to escrow settles **NOT LATER THAN 3.00 PM (LONDON TIME), 10.00 AM (NEW YORK CITY TIME) ON 15 APRIL 2004.**

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- (e) IF THE MERANT SECURITYHOLDER IS A CREST SPONSORED MEMBER, SUCH HOLDER SHOULD REFER TO THE HOLDER'S CREST SPONSOR BEFORE TAKING ANY ACTION. Such holder's sponsor will be able to confirm details of such holder's participant ID and the member account ID under which such holder's Merant shares are held. In addition, only the holder's CREST sponsor will be able to send the TTE Instruction to CRESTCo in relation to the holder's Merant shares.
- (f) If Merant shares are in uncertificated form, the holder of such Merant shares should send (or, if the holder is a CREST sponsored member, procure that the holder's CREST sponsor sends) a TTE Instruction to CRESTCo which must be properly authenticated in accordance with CRESTCo's specifications and which must contain, in addition to the other information that is required for a TTE Instruction to settle in CREST, the following details:
- (i) the number of Merant shares to be transferred to an escrow balance;
 - (ii) the member account ID of such Merant shareholder. This must be the same member account ID as the member account ID that is inserted in Box 6 of the form of acceptance;
 - (iii) the participant ID of such Merant shareholder. This must be the same participant ID as the participant ID that is inserted in Box 6 of the form of acceptance;
 - (iv) the participant ID of the escrow agent (the UK Receiving Agent in its capacity as a CREST receiving agent). This is RA10;
 - (v) the member account ID of the escrow agent. This is MERANT;
 - (vi) the form of acceptance Reference Number. This is the form of acceptance Reference Number that appears next to Box 6 on page 3 of the form of acceptance. This Reference Number should be inserted in the first eight characters of the shared note field on the TTE Instruction. Such insertion will enable the UK Receiving Agent to match the transfer to escrow to your form of acceptance. The holder of such shares should keep a separate record of this form of acceptance Reference Number for future reference;
 - (vii) the Intended Settlement Date. This should be as soon as possible and in any event not later than 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004;
 - (viii) the Corporate Action Number for the offer. This is allocated by CRESTCo and can be found by viewing the relevant Corporate Action Details in CREST;
 - (ix) the Corporate Action ISIN. This is GB 0002483831; and
 - (x) input with Standard Delivery instruction of 80.
- (g) After settlement of the TTE Instruction, such Merant shareholder will not be able to access the Merant shares concerned in CREST for any transaction or charging purposes. If all of the conditions are either satisfied, fulfilled or, to the extent permitted, waived, the escrow agent will transfer the Merant shares concerned to itself in accordance with paragraph 11(d) of Part B of this Appendix.
- (h) Such Merant shareholder is recommended to refer to the CREST Manual published by CRESTCo for further information on the CREST procedures outlined above. For ease of processing, such holder is requested, wherever possible, to ensure that a form of acceptance relates to only one transfer to escrow.

- (i) If no form of acceptance Reference Number, or an incorrect form of acceptance Reference Number, is included on the TTE Instruction, SERENA may treat any amount of Merant shares transferred to an escrow balance in favour of the escrow agent specified above from the participant ID and member account ID identified in the TTE Instruction as relating to any Form(s) of Acceptance which relate(s) to the same member account ID and participant ID (up to the amount of Merant shares inserted or deemed to be inserted on the Form(s) of Acceptance concerned).

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- (j) Such Merant shareholder should note that CRESTCo does not make available special procedures, in CREST, for any particular corporate action. Normal system timings and limitations will therefore apply in connection with a TTE Instruction and its settlement. Such holder should therefore ensure that all necessary action is taken by him (or by such holder's CREST sponsor) to enable a TTE Instruction relating to such holder's Merant shares to settle prior to 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004. In this connection such holder is referred in particular to those sections of the CREST Manual concerning practical limitations of the CREST system and timings.
- (k) SERENA will make an appropriate announcement if any of the details contained in this paragraph 10 alter for any reason.
- (l) Normal CREST procedures (including timings) apply in relation to any Merant shares that are, or are to be, converted from uncertificated to certificated form, or from certificated to uncertificated form, during the course of the offer (whether any such conversion arises as a result of a transfer of Merant shares or otherwise). Merant shareholders who are proposing so to convert any Merant shares are recommended to ensure that the conversion procedures are implemented in sufficient time to enable the person holding or acquiring the Merant shares as a result of the conversion to take all necessary steps in connection with an acceptance of the offer (in particular, as regards delivery of share certificates or other documents of title or transfers to an escrow balance as described above) prior to 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004.
- (m) If the share certificate(s) and/or other document(s) of title is/are not readily available or is/are lost, the form of acceptance should nevertheless be completed, signed and sent as stated above to the UK Receiving Agent so as to be received as soon as possible, but in any event no later than 3.00 pm (London time), 10.00 am (New York City time), on 15 April 2004, together with any share certificate(s) and/or other document(s) of title that is/are available, accompanied by a letter stating that the balance will follow or that the accepting holder has lost one or more of such holder's share certificate(s) and/or other documents of title. If the share certificate(s) and/or other document(s) of title are lost, the accepting holder should request the registrar of Merant, Lloyds TSB Registrars, The Causeway, Worthing, West Sussex BN99 6DA, United Kingdom, to send him a letter of indemnity for completion in accordance with the instructions given. When completed, the letter of indemnity must be lodged with the UK Receiving Agent in accordance with the instructions given, in support of the form of acceptance. SERENA may treat as invalid, to the extent that it so determines in its absolute discretion, any acceptance which it has reason to believe has been delivered in breach of obligations owed to a third party by the person delivering it, including (if relevant) any obligation of the ADS Depository under the Amended and Restated Deposit Agreement dated as at 16 March 1998 relating to the Merant ADSs.

11. FORM OF ACCEPTANCE FOR MERANT SHAREHOLDERS

Each holder of Merant shares who executes and lodges or has executed and lodged on such holder's behalf a form of acceptance with the UK Receiving Agent, subject to the rights of withdrawal set out in this document, irrevocably undertakes, represents, warrants and agrees to and with SERENA, Lehman Brothers, the UK Receiving Agent (and so as to bind such holder, such holder's heirs, successors and assigns and such holder's personal or legal representatives) to the following effect:

- (a) that the execution of the form of acceptance shall constitute:
 - (i) an acceptance of the offer in respect of the number of Merant shares inserted or deemed to be inserted in Box 1 of the form of acceptance;
 - (ii) an irrevocable authority and request to SERENA and/or its agents to procure the issue to such Merant shareholder of such new SERENA shares to which such Merant shareholder becomes entitled under the offer;

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- (iii) if Box 3A or Box 3B of the form of acceptance is completed, an election under the mix and match election to receive, subject to availability as a result of offsetting elections:
 - (aa) new SERENA shares instead of the cash consideration to which he would otherwise have been entitled to in consequence of the basic terms of the offer in respect of the number of Merant shares inserted, or deemed to be inserted, in Box 3A; or
 - (bb) cash instead of the new SERENA shares to which he would otherwise have been entitled to in consequence of the basic terms of the offer in respect of the number of Merant shares inserted, or deemed to be inserted, in Box 3B;
- (iv) an agreement to execute any further documents and give any further assurances which may be required to enable SERENA to obtain the full benefit of paragraph 10 of Part B of this Appendix and this paragraph 11 and/or to perfect any of the authorities expressed to be given hereunder;

in each case on and subject to the terms and conditions set out or referred to in this document and the form of acceptance;

- (b) unless NO is put in Box 7 of the form of acceptance that such Merant shareholder;
 - (i) has not received or sent copies or originals of this document, the form of acceptance or any related offering document in, into or from Canada, Australia or Japan;
 - (ii) has not used in connection with the offer or the execution or delivery of the form of acceptance, directly or indirectly, the mails of, or any means or instrumentality (including, without limitation, e-mail, facsimile transmission, telex and telephone) of interstate or foreign commerce of, or any facility of a national securities exchange of Canada, Australia or Japan;
 - (iii) has not mailed or otherwise sent the form of acceptance into or from Canada, Australia or Japan or signed in any of those jurisdictions and such Merant shareholder is accepting the offer from outside Canada, Australia or Japan; and
 - (iv) is not an agent or fiduciary acting on a non-discretionary basis for a principal, unless such agent or fiduciary is an authorised employee of such principal or such principal has given any instructions with respect to the offer from outside Canada, Australia or Japan;
- (c) that the execution of the form of acceptance constitutes, subject to the offer becoming unconditional in all respects in accordance with its terms and to an accepting Merant shareholder not having validly withdrawn such shareholder's acceptance, the irrevocable appointment of any director of, or any person authorised by, SERENA or Lehman Brothers as such shareholder's agent and/or attorney with an irrevocable instruction and authorisation to:
 - (i) complete and execute all or any form(s) of transfer, renunciation or other document in relation to the Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix 1 in favour of SERENA or as SERENA or its agents may direct;
 - (ii) deliver any form(s) of transfer, renunciation or other document with any certificate or other document of title for registration within six months of the offer becoming unconditional in all respects; and
 - (iii)

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take any other action as the agent and/or attorney may think necessary or expedient in connection with such shareholder's acceptance of the offer and/or the mix and match election and to vest in SERENA (or as it may direct) the Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix;

- (d) that the execution of the form of acceptance and its delivery to the UK Receiving Agent constitutes an irrevocable appointment of the UK Receiving Agent as such Merant shareholder's attorney and/or agent and an irrevocable instruction and authority to such attorney and/or agent:
 - (i) subject to the offer becoming unconditional in all respects and such shareholder not having validly withdrawn such shareholder's acceptance, to transfer to SERENA (or to such other person or persons as SERENA or its agent may direct) by means of CREST all or any of the Relevant Merant shares (but not exceeding the number of Merant shares in respect of which the offer is accepted or deemed to be accepted); and

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- (ii) if the offer does not become unconditional in all respects, to give instructions to CRESTCo immediately after the offer lapses (or within such longer period as the Panel may permit, not exceeding 14 calendar days of the offer lapsing) to transfer all relevant Merant shares to the original available balance of the accepting Merant shareholder.

In this paragraph, relevant Merant shares means Merant shares in uncertificated form in respect of which a transfer or transfers to escrow has or have been effected in accordance with the procedures described in paragraph 10 of Part B of this Appendix and where the transfer or transfers to escrow was or were made in respect of Merant shares held under the same member account ID and participant ID as the member account ID and participant ID relating to the relevant form of acceptance (but irrespective of whether or not any form of acceptance Reference Number, or a form of acceptance Reference Number corresponding to that appearing on the relevant form of acceptance, was included in the relevant transfer to escrow instruction);

- (e) that the execution of the form of acceptance constitutes, subject to the offer becoming unconditional in all respects and to an accepting Merant shareholder not having validly withdrawn such shareholder's acceptance, an irrevocable authority and request:
 - (i) to Merant or its agents to procure the registration of the transfer of the Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix and, in respect of Merant shares that are in certificated form, the delivery of the share certificate(s) and other document(s) of title in respect of the Merant shares to SERENA or as it may direct;
 - (ii) if the Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix are in certificated form, to SERENA or its agents to procure the dispatch by post (or by such other method as may be approved by the Panel) of a cheque for the cash consideration to which he is entitled under the offer;
 - (iii) if the Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix are in uncertificated form, to SERENA or its agents to ensure that a payment obligation is created in favour of the Merant shareholder's payment bank in accordance with the CREST payment arrangements in respect of any cash consideration to which that shareholder is entitled; and
 - (iv) To SERENA, Merant or their respective agents to record and act on any instructions with regard to payments or notices which have been entered in the records of Merant in respect of such shareholder's holding of Merant shares;
- (f) that the execution of the form of acceptance constitutes such shareholder's agreement that SERENA may decide to dispatch all or part of the consideration payable to a Merant shareholder whose Merant shares are in uncertificated form in accordance with paragraph 11(e)(ii) of Part B of this Appendix;
- (g) that the execution of the form of acceptance gives a separate authority to any director of, or person authorised by, SERENA or Lehman Brothers within the terms of paragraph 7 of Part B of this Appendix;
- (h) that, subject to the offer becoming unconditional in all respects and the holder not having validly withdrawn the holder's acceptance (or if the offer will become unconditional in all respects or lapse on the outcome of the resolution in question or if the Panel gives its consent) and pending registration:
 - (i) SERENA or its agent shall be entitled to direct the exercise of any votes and any other rights and privileges (including the right to requisition the convening of a general or separate class meeting of Merant) attaching to the Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix;
 - (ii)

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the execution of the form of acceptance by the Merant shareholder, in respect of the Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix, constitutes an authority to Merant or its agent to send any notice, circular, warrant or other document or communication which may be required to be sent to him as a member of Merant (including any share certificate(s) or other documents of title used as a result of conversion of such offeree Shares into certificated form) to SERENA, care of the UK Receiving Agent;

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- (iii) the execution of the form of acceptance by the Merant shareholder, in respect of the Merant shares comprised in such acceptance and in respect of which such acceptance has not been validly withdrawn, constitutes an authority to any director of, or person authorised by, SERENA or Lehman Brothers to sign any document and do such things as may in the opinion of that agent and/or attorney seem necessary or desirable in connection with the exercise of any votes or other rights or privileges attaching to the Merant shares held by such shareholder (including, without limitation, signing any consent to short notice of a general or separate class meeting as such shareholder's agent and/or attorney and on such shareholder's behalf and executing a form of proxy appointing any person nominated by SERENA to attend general and separate class meetings of Merant and attending any such meeting and exercising the votes attaching to the Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix on such shareholder's behalf, where relevant, such votes to be cast so far as possible to satisfy any outstanding Condition of the offer); and
- (iv) the execution of the form of acceptance by the Merant shareholder, in respect of the Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix, constitutes an agreement not to exercise any such rights without the consent of SERENA and irrevocably undertakes not to appoint a proxy for or to attend such general or separate class meetings of Merant.

This authority will cease to be valid if the acceptance is validly withdrawn in accordance with paragraph 4 of Part B of this Appendix;

- (i) that the holder will deliver to the UK Receiving Agent, or procure the delivery to the UK Receiving Agent of, the holder's share certificates and/or other document(s) of title in respect of those Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix that are in certificated form, or an indemnity acceptable to SERENA, as soon as possible and in any event within two months of the offer becoming unconditional in all respects;
- (j) that the holder is the sole legal and beneficial owner of the Merant shares in respect of which the offer is accepted or deemed to be accepted or the holder is the legal owner of such Merant shares and has the necessary capacity and authority to execute the form of acceptance;
- (k) that the holder agrees and acknowledges that the holder is not a customer (as defined in the rules of The Financial Services Authority) of Lehman Brothers in connection with the offer;
- (l) that the holder will take (or procure to be taken) the necessary action to transfer all those Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix that are in uncertificated form in respect of which the offer has been accepted and not validly withdrawn to an escrow balance as soon as possible and in any event so that the transfer to escrow settles within two months of the offer becoming unconditional in all respects;
- (m) that if for any reason any Merant shares in respect of which a transfer to an escrow balance has been effected are converted to certificated form, the holder will immediately deliver or ensure the immediate delivery of the share certificates or other documents of title in respect of all those Merant shares that are converted to the UK Receiving Agent at the address specified in the section of this document entitled Further Information ;
- (n) that the creation of a payment obligation in favour of the holder's payment bank in accordance with the CREST payment arrangements as referred to in paragraph 11(e)(iii) of Part B of this Appendix will, to the extent of the obligation so created, discharge fully any obligation of SERENA or Lehman Brothers to pay to him the cash consideration to which the holder is entitled under the offer;
- (o) that the holder will do everything as shall in the opinion of SERENA or its agents be necessary or expedient to vest in SERENA or its nominees the Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix and to enable the UK Receiving Agent to perform its functions as escrow agent for the purposes of the offer;

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- (p) that the holder agrees to ratify everything which may be done or effected by any director of, or person authorised by, SERENA, Lehman Brothers or the UK Receiving Agent in exercise of any of the powers and/or authorities under Part B of this Appendix;
- (q) that, if any provision of Part B of this Appendix will be unenforceable or invalid or will not operate so as to afford SERENA, Lehman Brothers or the UK Receiving Agent or any of their respective directors or persons authorised by them, the benefit of the authority expressed to be given in Part B of this Appendix, the holder will, with all practicable speed, do everything that may be required or desirable to enable SERENA, Lehman Brothers and the UK Receiving Agent and any of their respective directors or persons authorised by them to secure the full benefit of Part B of this Appendix;
- (r) that the holder represents and warrants that the holder is entitled to sell and transfer the beneficial ownership of the Merant shares referred to in paragraph 11(a)(i) of Part B of this Appendix and that such Shares are sold fully paid and free from all liens, equities, charges, encumbrances and other interests and together with all rights attaching to them on or after 15 April 2004 including without limitation, the right to receive and retain all dividends and other distributions declared, made or payable after that date;
- (s) that such holder agrees that the terms and conditions of the offer are deemed to be incorporated in, and form part of, the form of acceptance which shall be read and construed accordingly;
- (t) that such holder agrees that, on execution, the form of acceptance takes effect as a deed; and
- (u) that such holder agrees that the execution of the form of acceptance constitutes such holder's submission to the jurisdiction of the courts of England in relation to all matters arising in connection with the offer and the form of acceptance and that nothing shall limit the right of SERENA and/or Lehman Brothers to bring any action, suit or proceeding arising out of or in connection with the offer and the form of acceptance in any other manner permitted by law or in any court of competent jurisdiction.

A reference in this paragraph 11 to a holder of Merant shares includes a reference to the person or persons executing the form of acceptance and in the event of more than one person executing a form of acceptance, the provisions of this paragraph 11 will apply to them jointly and to each of them.

12. PROCEDURES FOR ACCEPTANCE IN RESPECT OF MERANT ADSs

- (a) Letter of transmittal/Notice of guaranteed delivery

If you are a holder of Merant ADSs evidenced by Merant ADRs, you will have also received a letter of transmittal and a notice of guaranteed delivery for use in connection with the offer. This section should be read together with the instructions on the letter of transmittal. The provisions of this paragraph 12 shall be deemed to be incorporated in, and form a part of, the relevant letter of transmittal. The instructions printed on the relevant letter of transmittal shall be deemed to form part of the terms of the offer.

- (b) Valid tendering

For a holder of Merant ADSs evidenced by Merant ADRs to tender such Merant ADSs validly pursuant to the offer, either:

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- (i) a properly completed and duly executed letter of transmittal, together with any required signature guarantees or, in the case of a book-entry transfer, an Agent's Message, and any other documents required by the letter of transmittal, must be received by the US Depository at one of its addresses set out in the section of this document entitled "Further Information" and either the Merant ADRs evidencing such Merant ADSs must be received by the US Depository at one of such addresses or such Merant

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ADRs evidencing such Merant ADSs must be delivered pursuant to the procedure for book-entry transfer set forth below (and a Book-Entry Confirmation received by the US Depository in accordance with such procedures); or

- (ii) such holder must comply with the guaranteed delivery procedures set out in paragraph 12(h) below.

The offer in respect of Merant ADSs evidenced by Merant ADRs shall be validly accepted by: (i) delivery of a letter of transmittal, the relevant Merant ADRs evidencing Merant ADSs and other required documents to the US Depository by a holder of Merant ADSs (without any further action by the US Depository) subject to the terms and conditions set out in this document and the letter of transmittal; or (ii) completion of the book-entry transfer procedures described below. The acceptance of the offer by a tendering holder of Merant ADSs evidenced by Merant ADRs pursuant to the procedures described above, subject to the withdrawal rights described below, will be deemed to constitute a binding agreement between such tendering holder of Merant ADSs and SERENA upon the terms and subject to the conditions of the offer. Accordingly, references in this document and in the letter of transmittal to a tender of Merant ADS shall be construed to mean an acceptance of the offer in respect of such Merant ADS upon the terms and subject to the conditions of the offer. If a Merant ADR evidencing a Merant ADS has been tendered by a holder of Merant ADSs, the Merant shares represented by such Merant ADSs may not be tendered independently by such holder of Merant shares. A letter of transmittal and other required documents contained in an envelope postmarked in Canada, Australia or Japan or otherwise appearing to SERENA or its agents to have been sent from Canada, Australia or Japan may be rejected as invalid.

- (c) Book-entry transfer

The US Depository will establish an account at each of the Book-Entry Transfer Facilities with respect to interests in Merant ADSs evidenced by Merant ADRs held in book-entry form for the purposes of the offer within two business days from the date of this document. Any financial institution that is a participant in any of the Book-Entry Transfer Facility's systems may make book-entry delivery of interests in Merant ADSs by causing a Book-Entry Transfer Facility to transfer such interests in Merant ADSs into the US Depository's account at such Book-Entry Transfer Facility in accordance with that Book-Entry Transfer Facility's procedures for such transfer.

Although delivery of interests in Merant ADSs evidenced by Merant ADRs may be effected through book-entry transfer into the US Depository's account at a Book-Entry Transfer Facility, either:

- (i) the letter of transmittal, properly completed and duly executed, together with any required signature guarantees; or
- (ii) an Agent's Message,

and, in either case, any other required documents, must in any case be transmitted to, and received by, the US Depository at one of its addresses set out in the section of this document entitled "Further Information" before Merant ADSs evidenced by Merant ADRs will be either counted as a valid acceptance, or purchased, or such holder must comply with the Guaranteed Delivery Procedures described below. Delivery of documents to a Book-Entry Transfer Facility does not constitute delivery to the US Depository.

- (d) Method of delivery

The method of delivery of Merant ADRs, letters of transmittal and all other required documents is at the option and risk of the tendering holder of Merant ADSs. Merant ADSs will be deemed delivered only when the Merant ADRs representing such Merant ADSs are actually received by the US Depository (including in the case of a book-entry transfer, by Book-Entry Confirmation). If delivery is by mail, registered mail with

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return receipt requested, properly insured, is recommended. In all cases, sufficient time should be allowed to ensure timely delivery. No acknowledgement of receipt of documents will be given by, or on behalf of, SERENA.

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(e) Signature guarantees

No signature guarantee is required on the letter of transmittal if:

- (i) the letter of transmittal is signed by the registered holder of the Merant ADSs tendered therewith and such registered holder has not completed either the Box entitled "Special Delivery Instructions" or the Box entitled "Special Payment Instructions" in the letter of transmittal; or
- (ii) such Merant ADSs are tendered for the account of an Eligible Institution.

In all other cases, all signatures on letters of transmittal must be guaranteed by an Eligible Institution. See Instructions 1 and 5 to the letter of transmittal.

(f) Merant ADSs and Merant ADRs

If the Merant ADSs are registered in the name of a person other than the person who signs the letter of transmittal, then the tendered Merant ADRs must be endorsed or accompanied by appropriate stock powers, signed exactly as the name or names of the registered owner or owners appear on the Merant ADRs, with the signatures on the Merant ADRs or stock powers guaranteed as aforesaid. See Instruction 5 to the letter of transmittal.

(g) Partial acceptances (not applicable to book-entry holders of Merant ADSs)

If fewer than all of the Merant ADSs evidenced by any Merant ADRs delivered to the US Depository are to be tendered, the holder thereof should so indicate in the letter of transmittal by filling in the number of Merant ADSs which are tendered in the Box entitled "Number of ADSs Tendered". In such case, a new Merant ADR for the remainder of the Merant ADSs represented by the former Merant ADR will be sent to the person(s) signing such letter of transmittal (or as such person properly indicates thereon) as promptly as practicable following the date the tendered Merant ADSs are purchased. All Merant ADSs delivered to the US Depository will be deemed to have been tendered unless otherwise indicated. See Instruction 4 to the letter of transmittal. In the case of partial tenders, Merant ADSs not tendered will not be reissued to a person other than the registered holder.

(h) Guaranteed delivery procedures

- (i) If a holder of Merant ADSs evidenced by Merant ADRs wishes to tender Merant ADSs pursuant to the offer and the Merant ADRs evidencing such Merant ADSs are not immediately available or the procedures for book-entry transfer cannot be completed on a timely basis, or if time will not permit all required documents to reach the US Depository whilst the offer remains open for acceptance, such holder's tender of Merant ADSs may be effected if all of the following conditions are satisfied, referred to as the Guaranteed Delivery Procedures:

- (aa) such tender is made by or through an Eligible Institution;

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- (bb) a properly completed and duly executed notice of guaranteed delivery substantially in the form provided by SERENA is received by the US Depositary, as provided below, whilst the offer remains open for acceptance; and

 - (cc) the Merant ADRs evidencing all tendered Merant ADSs (or, in the case of Merant ADSs held in book-entry form, timely confirmation of the book-entry transfer of such interests in Merant ADSs into the US Depositary's account at a Book-Entry Transfer Facility as described above) together with a properly completed and duly executed letter of transmittal with any required signature guarantees or, in the case of a book-entry transfer, an Agent's Message and any other documents required by the letter of transmittal, are received by the US Depositary within three Nasdaq business days after the date of execution of such notice of guaranteed delivery.
- (ii) The Notice of Guaranteed Delivery may be delivered by hand, transmitted by facsimile transmission or mailed to the US Depositary and must include a signature guarantee by an Eligible Institution in the form set out in such notice of guaranteed delivery.

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(iii) Receipt of a notice of guaranteed delivery will not be treated as a valid acceptance for the purpose of satisfying the Acceptance Condition. To be counted towards satisfaction of this requirement, the Merant ADRs evidencing Merant ADSs referred to in the notice of guaranteed delivery must be received prior to the relevant closing date by the US Depository (or, in the case of interests in Merant ADSs evidenced by Merant ADRs held in book-entry form, timely confirmation of a book-entry transfer of such interests in Merant ADSs into the US Depository's account at a Book-Entry Transfer Facility pursuant to the procedures set out above) together with a duly executed letter of transmittal with any required signature guarantees (or, in the case of a book-entry transfer an Agent's Message) and any other required documents.

(i) Other requirements

By executing the letter of transmittal as set out above, the tendering holder of Merant ADSs evidenced by Merant ADRs will agree that, effective from and after the date all conditions are either satisfied, fulfilled or, to the extent permitted, waived (unless the tendering holder shall have validly withdrawn such holder's tender prior to that time):

- (i) SERENA or its agents shall be entitled to direct the exercise of any votes attaching to any Merant shares represented by Merant ADSs, in respect of which the offer has been accepted or is deemed to have been accepted, referred to as the accepted ADSs, and any other rights and privileges attaching to such Merant shares, including any right to requisition a general meeting of Merant or any class of its shareholders;
- (ii) the execution of the letter of transmittal (together with any signature guarantees) and its delivery to the US Depository or the completion of the book-entry transfer procedures shall constitute:
 - (aa) an authority to Merant or its agents from the tendering holder of accepted ADSs to send any notice, circular, warrant, document or other communication that may be required to be sent to him as a holder of Merant ADSs, to SERENA at the office of the UK Receiving Agent;
 - (bb) an authority to SERENA or its agent to sign any consent to short notice of a general meeting or separate class meeting on behalf of the tendering holder of accepted ADSs and/or to execute a form of proxy in respect of such accepted ADSs appointing any person nominated by SERENA to attend general meetings and separate class meetings of Merant and any adjournment thereof and to exercise the votes attaching to the Merant shares represented by such accepted ADSs on such tendering holder's behalf;
 - (cc) the agreement of such tendering holder of accepted ADSs not to exercise any of such rights without the consent of SERENA and the irrevocable undertaking of such tendering holder of accepted ADSs not to appoint a proxy for or to attend any such general meetings or separate class meetings;
 - (dd) a representation and warranty that such holder of Merant ADSs; (i) has not received or sent copies or originals of this document or any letter of transmittal or any related documents in, into or from, Canada, Australia or Japan; (ii) has not used in connection with the offer or the execution or delivery of the letter of transmittal, directly or indirectly, the mails of, or any means or instrumentality (including, without limitation, e-mail, facsimile transmission, telex and telephone) of interstate or foreign commerce of, or any facility of a national securities exchange of Canada, Australia or Japan; (iii) is accepting the offer from outside Canada, Australia or Japan; and (iv) is not an agent or fiduciary acting on a non-discretionary basis for a principal, unless such agent or fiduciary is an authorised employee of such principal or such principal has given any instructions with respect to the offer from outside Canada, Australia or Japan;
 - (ee) confirmation that such holder of Merant ADSs is entitled to sell and transfer the beneficial ownership of the accepted ADSs and that such accepted ADSs are sold fully paid and free from all liens, equitable interests, charges, and encumbrances and

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together with all rights attaching thereto including voting rights and the right to all dividends and other distributions declared, paid

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or made on or after 15 April 2004 including, without limitation, the right to receive and retain all dividends and other distributions declared, made or payable after that date; and

- (ff) the execution of the letter of transmittal (together with any signature guarantees) and its delivery to the US Depository (or the completion of the Book-entry transfer procedures) shall constitute an authority to any director of SERENA or Lehman Brothers and to SERENA or Lehman Brothers and/or their respective agents in accordance with the terms of paragraph 7 of Part B of this Appendix.

References in this paragraph 12 to a holder of Merant ADSs shall include references to the person or persons executing a letter of transmittal and in the event of more than one person executing a letter of transmittal the provisions of this Part B shall apply to them jointly and to each of them.

13. CURRENCY OF CASH CONSIDERATION

Instead of receiving cash consideration in pounds sterling, Merant securityholders who so wish may elect to receive US dollars on the basis that the cash amount payable in pounds sterling to which such holder would otherwise be entitled pursuant to the terms of the offer will be converted, subject to conversion expenses, from pounds sterling to US dollars at the exchange rate obtainable by the relevant payment agent (either the UK Receiving Agent or the US Depository) on the spot market in London on the date the cash consideration is made available by SERENA to the relevant payment agent for delivery in respect of the relevant Merant shares. A Merant securityholder may receive such amount on the basis set out above only in respect of the whole of such securityholder's holding of Merant shares in respect of which such securityholder accepts the offer. Merant securityholders may not elect to receive both pounds sterling and US dollars.

Holders of Merant ADSs are entitled under the terms of the offer to receive the cash element of the consideration in pounds sterling. The pounds sterling consideration available to holders of Merant ADSs is the same, per Merant share as that offered to Merant securityholders. To facilitate the settlement of the offer, unless they elect to receive pounds sterling, holders of Merant ADSs will receive consideration converted into US dollars as described above, as if such holders of Merant ADSs had elected to receive dollars.

Consideration in US dollars may be inappropriate for Merant securityholders other than persons in the US and holders of Merant ADSs.

The actual amount of US dollars received will depend upon the exchange rate prevailing on the day on which funds are made available to the relevant payment agent by SERENA. Merant securityholders should be aware that the US dollar/pounds sterling exchange rate which is prevailing at the date on which an election is made to receive dollars and on the dates of dispatch and receipt of payment may be different from that prevailing on the day on which funds are made available to the relevant payment agent by SERENA. In all cases, fluctuations in the US dollar/pounds sterling exchange rate are at the risk of accepting Merant securityholders who elect or are treated as having elected to receive their consideration in US dollars. Neither SERENA nor any of its advisors or agents shall have any responsibility with respect to the actual amount of cash consideration payable other than in pounds sterling.

14. SUBSTITUTE ACCEPTANCE FORMS

Holders of Merant securities have been sent with this document a form of acceptance and/or a letter of transmittal (accompanied by a notice of guaranteed delivery). All holders of Merant shares, including persons in the US who hold Merant shares, have been sent a form of acceptance,

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which they must use to accept the offer. All holders of Merant ADSs have been sent a letter of transmittal and a notice of guaranteed delivery which they must use to accept the offer. Should any holder of Merant securities receive an incorrect form with which to accept the offer or require any additional forms, that person should contact the UK Receiving Agent or the US Depositary at the addresses set out in the section of this document entitled Further Information, who will provide the appropriate forms.

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APPENDIX 2

FURTHER INFORMATION ON SERENA

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Table of Contents**BUSINESS DESCRIPTION**

SERENA is an industry leader in ECM solutions focused on the mainframe platform. For over twenty years we have focused exclusively on providing solutions that help companies automate change to the applications that run their businesses. Today our products are in use at over 3,600 customer sites including 46 of the Fortune 50. We believe our SERENA Application Framework for Enterprises (SAFE) is the next step in ECM, providing cross-platform, cross-process and cross-organizational support across application life cycle processes. With headquarters in San Mateo, California, we serve customers worldwide through local offices and an international network of distributors.

We are listed on Nasdaq under the symbol SRNA. We have a current market capitalization of approximately US\$755 million based on the closing price of SERENA shares on 15 March 2004, the latest practicable date prior to the posting of this document. In the years ended 31 January 2004 and 2003, we reported the following results (in millions of US Dollars, except per share data):

	Year ended	Year ended
	31 January 2004	31 January 2003
Revenues	105.6	95.8
Profit before tax	33.7	37.3
Charge for tax	12.3	14.1
Net profit after tax	21.4	23.2
Earnings per share	0.53	0.57

In the quarters ended 31 January 2004 and 2003, we reported the following results (in millions of US Dollars, except per share data):

	Quarter ended	Quarter ended
	31 January 2004	31 January 2003
Revenues	29.6	26.1
Profit before tax	9.3	10.8
Charge for tax	3.4	4.0
Net profit after tax	6.0	6.8
Earnings per share	0.15	0.17

As at 31 January 2004, we had total cash and cash equivalents of US\$377 million.

Recent Developments

In December 2003, we issued \$220 million of subordinated convertible notes due 2023, referred to as the convertible notes, in a private offering. The convertible notes mature on December 15, 2023, bear interest at a coupon rate of one and one half percent annually, and will be converted into our common stock if our stock price reaches levels specified in the notes. In connection with the issuance of our convertible notes we incurred \$6.7 million of transaction costs, which primarily consisted of investment banker, legal and other professional fees which are being

amortized using the straight-line method over the term of the convertible notes.

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(in thousands, except share data)

	January 31,	
	2002	2003
Assets		
Current assets:		
Cash and cash equivalents	\$ 85,954	\$ 105,402
Short-term investments	46,640	37,672
Accounts receivable, net of allowance of \$846 and \$869 in fiscal 2002 and 2003, respectively	14,111	16,514
Deferred taxes	5,834	6,549
Prepaid expenses and other current assets	838	744
Total current assets	153,377	166,881
Long-term investments	24,321	48,374
Property and equipment, net	3,036	3,078
Deferred taxes		561
Goodwill and other intangible assets, net	50,135	45,360
Other assets	201	269
Total assets	\$ 231,070	\$ 264,523
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	\$ 710	\$ 533
Income taxes payable	1,650	7,921
Accrued expenses	11,762	8,266
Deferred revenue	21,877	26,010
Total current liabilities	35,999	42,730
Deferred revenue, net of current portion	8,886	8,373
Deferred taxes	1,409	458
Total liabilities	46,294	51,561
Commitments and contingencies:		
Stockholders equity:		
Preferred stock, \$0.001 par value; 5,000,000 shares authorized; no shares issued and outstanding		
Common stock, \$0.001 par value; 90,000,000 shares authorized; 40,274,214 and 40,645,508 shares issued and outstanding at January 31, 2002 and 2003, respectively	40	41

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Additional paid-in capital	123,517	126,006
Deferred stock-based compensation	(23)	
Notes receivable from stockholders	(10,350)	(8,519)
Accumulated other comprehensive income	21	709
Retained earnings	71,571	94,725
	<u> </u>	<u> </u>
Total stockholders' equity	184,776	212,962
	<u> </u>	<u> </u>
Total liabilities and stockholders' equity	\$ 231,070	\$ 264,523
	<u> </u>	<u> </u>

See accompanying notes to consolidated financial statements

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Table of Contents**SERENA SOFTWARE, INC.****CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME****(in thousands, except per share data)**

	Fiscal Year Ended January 31,		
	2001	2002	2003
Revenue:			
Software licenses	\$ 58,037	\$ 49,514	\$ 44,250
Maintenance	37,227	41,812	44,476
Professional services	8,345	7,315	7,049
Total revenue	103,609	98,641	95,775
Cost of revenue:			
Software licenses	1,600	931	1,224
Maintenance	5,610	5,448	5,548
Professional services	6,938	6,576	6,519
Total cost of revenue	14,148	12,955	13,291
Gross profit	89,461	85,686	82,484
Operating expenses:			
Sales and marketing	27,154	29,357	26,361
Research and development	10,101	13,308	11,779
General and administrative	8,511	6,618	7,311
Stock-based compensation	223	135	23
Amortization of intangible assets, including goodwill in fiscal 2001 and 2002	5,146	8,336	4,486
Acquired in-process research and development	2,972		
Restructuring charges		2,529	
Total operating expenses	54,107	60,283	49,960
Operating income	35,354	25,403	32,524
Interest and other income, net	7,475	5,968	4,726
Income before income taxes	42,829	31,371	37,250
Income taxes	18,575	12,862	14,096
Net income	\$ 24,254	\$ 18,509	\$ 23,154
Comprehensive income:			
Net income	\$ 24,254	\$ 18,509	\$ 23,154
Other comprehensive (loss) income:			
Foreign currency translation adjustments	(202)	(5)	312

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Unrealized gain on marketable securities	101	167	376
Other comprehensive (loss) income	(101)	162	688
Total comprehensive income	\$ 24,153	\$ 18,671	\$ 23,842
Net income per share:			
Basic	\$ 0.63	\$ 0.46	\$ 0.57
Diluted	\$ 0.60	\$ 0.46	\$ 0.57
Weighted average shares used in per share calculations:			
Basic	38,522	39,768	40,367
Diluted	40,729	40,760	40,854

See accompanying notes to consolidated financial statements

Table of Contents**SERENA SOFTWARE, INC.****CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY**

(in thousands, except share data)

	<u>Common Stock</u>		<u>Additional Paid-in Capital</u>	<u>Deferred Stock-based Compensation</u>	<u>Notes Receivable from Stockholders</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>	<u>Retained Earnings</u>	<u>Total Stockholders Equity</u>
	<u>Shares</u>	<u>Amount</u>						
Balance as of January 31, 2000	38,285,612	\$ 38	\$ 89,281	\$ (380)	\$ (3,182)	\$ (40)	\$ 28,808	\$ 114,525
Issuance of common stock under HPS, StarTool and UltiMIS acquisitions	396,324	1	14,281					14,282
Issuance of common stock under the employee stock purchase plan	183,449		1,484					1,484
Issuance of restricted common stock for notes receivable, net of repurchases	484,500	1	9,293		(9,294)			
Common stock options exercised	338,628		1,049					1,049
Payments of accrued interest and principal on restricted common stock					1,379			1,379
Amortization of stock-based compensation				223				223
Accrued interest on note receivable					(1,017)			(1,017)
Tax benefit from employee stock plans			1,067					1,067
Net income							24,254	24,254
Other comprehensive loss						(101)		(101)
Balance as of January 31, 2001	39,688,513	40	116,455	(157)	(12,114)	(141)	53,062	157,145
Issuance of common stock under the employee stock purchase plan	146,921		1,802					1,802
Repurchase of common stock	(80,000)		(794)					(794)
Common stock options exercised	518,780		3,206					3,206
Payments of accrued interest and principal on restricted common stock					2,474			2,474
Amortization of stock-based compensation				134				134
Accrued interest on note receivable					(710)			(710)
Issuance of stock warrant			129					129
Tax benefit from employee stock plans			2,719					2,719
Net income							18,509	18,509
Other comprehensive income						162		162
Balance as of January 31, 2002	40,274,214	40	123,517	(23)	(10,350)	21	71,571	184,776

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Issuance of common stock under the employee stock purchase plan	123,721		1,489					1,489
Repurchase of common stock	(112,422)		(1,508)		27			(1,481)
Common stock options exercised	359,995	1	2,068					2,069
Payments of accrued interest and principal on restricted common stock					2,470			2,470
Amortization of stock-based compensation				23				23
Accrued interest on note receivable						(666)		(666)
Tax benefit from employee stock plans			440					440
Net income							23,154	23,154
Other comprehensive income						688		688
Balance as of January 31, 2003	40,645,508	\$ 41	\$ 126,006	\$	\$ (8,519)	\$ 709	\$ 94,725	\$ 212,962

See accompanying notes to consolidated financial statements

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

	Fiscal Year Ended		
	January 31,		
	2001	2002	2003
Cash flows from operating activities:			
Net income	\$ 24,254	\$ 18,509	\$ 23,154
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	1,161	1,568	1,384
Deferred income taxes	(4,403)	481	(2,226)
Tax benefit from employee stock plans	1,067	2,719	440
Provision in allowance for bad debts	975	1,108	875
(Gain) loss on disposal of property and equipment	(1)	119	(23)
Accrued interest on notes receivable from stockholders, net of cash received	(853)	(339)	(164)
Amortization of deferred stock-based compensation	223	135	23
Amortization of intangible assets, including goodwill in fiscal 2001 and 2002	5,146	8,336	4,486
Acquired in-process research and development	2,972		
Issuance of stock warrant in exchange for operating services provided		129	
Changes in operating assets and liabilities:			
Accounts receivable	(6,062)	5,595	(2,839)
Prepaid expenses and other assets	(894)	548	(31)
Accounts payable	538	(194)	(213)
Income taxes payable	3,498	(4,837)	6,204
Accrued expenses	545	(1,360)	(1,713)
Deferred revenue	3,842	6,690	2,541
Net cash provided by operating activities	32,008	39,207	31,898
Cash flows used in investing activities:			
Purchases of property and equipment	(2,055)	(1,428)	(1,388)
Purchases of short-term and long-term investments	(4,123)	(43,314)	(14,709)
Cash paid in acquisition of HPS, StarTool and UltiMIS in fiscal 2001, net of cash acquired	(25,128)		
Cash paid for UltiMIS Corporation earn-out			(710)
Net cash used in investing activities	(31,306)	(44,742)	(16,807)
Cash flows from financing activities:			
Common stock repurchased under the stock repurchase plan		(794)	(1,508)
Sale of common stock under the employee stock purchase plan	1,484	1,802	1,489
Exercise of stock options under the employee stock option plan	1,049	3,206	2,069
Payment of principal on notes receivable from stockholders	1,215	2,101	1,995
Net cash provided by financing activities	3,748	6,315	4,045
Effect of exchange rate changes on cash	(202)	(5)	312
Net increase in cash and cash equivalents	4,248	775	19,448

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Cash and cash equivalents at beginning of year	80,931	85,179	85,954
	<u> </u>	<u> </u>	<u> </u>
Cash and cash equivalents at end of year	\$ 85,179	\$ 85,954	\$ 105,402
	<u> </u>	<u> </u>	<u> </u>
Supplemental disclosures of cash flow information:			
Income taxes paid	\$ 18,478	\$ 14,459	\$ 9,814
	<u> </u>	<u> </u>	<u> </u>
Non-cash investing and financing activity:			
Common stock issued in acquisition of HPS, StarTool and UltiMIS in fiscal 2001	\$ 14,283	\$	\$
	<u> </u>	<u> </u>	<u> </u>
Restricted stock issued for notes receivable from stockholders	\$ 9,294	\$	\$
	<u> </u>	<u> </u>	<u> </u>
Unrealized gain on marketable securities	\$ 101	\$ 167	\$ 376
	<u> </u>	<u> </u>	<u> </u>
Contingent consideration accrued for (reversed from) the UltiMIS acquisition, net	\$	\$ 1,000	\$ (290)
	<u> </u>	<u> </u>	<u> </u>
Additional paid-in capital from issuance of stock warrant	\$	\$ (129)	\$
	<u> </u>	<u> </u>	<u> </u>

See accompanying notes to consolidated financial statements

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Fiscal Years Ended January 31, 2001, 2002 and 2003

(1) Description of Business and Summary of Significant Accounting Policies

(a) Description of Business

SERENA Software, Inc. (the Company) is an industry-leading supplier of software that automates change to enterprise code and content. Its principal markets are North America, and to a lesser extent, Europe. Export sales represented approximately 18%, 19%, and 29% of total revenue in fiscal 2001, 2002 and 2003, respectively.

(b) Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

(c) Foreign Currency Translation

The functional currency of the Company's UK subsidiary is the British pound. The functional currency of the Company's German, French and Belgian subsidiaries is the euro. These foreign subsidiaries' financial statements are translated using current exchange rates for balance sheet accounts and average rates for income statement accounts. Translation adjustments are recorded as other comprehensive income or loss in the consolidated statements of income and comprehensive income. Foreign currency transaction gains and losses are included in operating expenses, and have not been material to date.

(d) Cash, Cash Equivalents and Investments

The Company considers all highly liquid investments purchased with original remaining maturities of three months or less to be cash equivalents. As of January 31, 2002 and 2003, cash equivalents consisted of commercial paper and money market funds.

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The Company has classified its investments as available-for-sale. These investments are carried at fair value, based on quoted market prices, and unrealized gains and losses are recorded as other comprehensive income or loss in the consolidated statements of income and comprehensive income. Realized gains and losses upon sale or maturity of these investments are determined using the specific identification method.

Interest and other income, net consists principally of earnings generated from interest-bearing accounts held by the Company and, to a lesser extent, interest accrued from stockholder notes.

Cash equivalents consist of securities with original remaining maturities of three months or less. Investments as of January 31, 2002 consisted of \$46,640,000 of securities which mature in less than one year and \$24,321,000 of securities which mature in one to two years. Investments as of January 31, 2003 consisted of \$37,672,000 of securities which mature in less than one year and \$48,374,000 of securities which mature in one to two years. Cash, cash equivalents and investments consisted of the following as of January 31, 2002 and 2003 (in thousands):

	As of January 31, 2002			As of January 31, 2003		
	Unrealized			Unrealized		
	Cost	Gains	Market	Cost	Gains	Market
Cash and Cash Equivalents:						
Cash	\$ 4,636	\$	\$ 4,636	\$ 7,382	\$	\$ 7,382
CD s/Bonds	5,000		5,000	5,000		5,000
Money Market Funds	65,309		65,309	93,020		93,020
Corporate Notes	10,969	40	11,009			
	<u>\$ 85,914</u>	<u>\$ 40</u>	<u>\$ 85,954</u>	<u>\$ 105,402</u>	<u>\$</u>	<u>\$ 105,402</u>
Investments:						
Corporate Notes	\$ 70,733	\$ 228	\$ 70,961	\$ 85,402	\$ 644	\$ 86,046
	<u>\$ 70,733</u>	<u>\$ 228</u>	<u>\$ 70,961</u>	<u>\$ 85,402</u>	<u>\$ 644</u>	<u>\$ 86,046</u>

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(1) Description of Business and Summary of Significant Accounting Policies (Continued)

(e) Property and Equipment

Property and equipment are stated at cost and are depreciated using the straight-line method over the estimated useful lives of the assets, generally three to five years.

(f) Goodwill and Other Intangible Assets

Goodwill and other intangible assets include work-force-in-place, non-compete agreements, acquired technology and goodwill associated with the acquisitions of Optima Software, Inc., Diamond Optimum Systems, Inc., High Power Software, Inc., the *StarTool FDM* product and UltiMIS Corporation. Non-compete and acquired technology are amortized using the straight-line method over the estimated useful lives of the related assets, from 1 year to 7 years. With the adoption of SFAS No. 142 on February 1, 2002, goodwill and work-force-in-place have ceased to be amortized to income effective with the beginning of fiscal 2003 and is instead reviewed for impairment.

(g) Impairment or Disposal of Long-lived Assets

The Company evaluates its long-lived assets and certain identifiable intangibles, for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets or intangibles may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceed the fair value of the assets. If an asset is to be disposed of, it is reported at the lower of the carrying amount or fair value less costs to sell. To date, there has been no impairment of long-lived assets.

(h) Software Development Costs

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Development costs related to software products are expensed as incurred until technological feasibility of the product has been established. Based on the Company's product development process, technological feasibility is established upon completion of a working model. Costs incurred by the Company between completion of the working model and the point at which the product is ready for general release have not been significant. Accordingly, no costs have been capitalized to date. The Company has, however, capitalized certain costs totaling \$476,000 and \$103,000 in fiscal 2002 and 2003, respectively, associated with computer software it has acquired for internal use. The capitalization and amortization of these costs are in accordance with AICPA Statement of Position (SOP) 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*. Software development costs are being amortized over periods of three to five years.

(i) Income Taxes

Income taxes are recorded using the asset and liability method. Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

(j) Concentrations of Credit Risk

Financial instruments, potentially subjecting the Company to concentrations of credit risk, consist primarily of temporary cash investments. The Company places its temporary cash investments with two major financial institutions. The Company maintains an allowance for potential credit losses on customer trade accounts receivable.

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(1) Description of Business and Summary of Significant Accounting Policies (Continued)

(k) Fair Value of Financial Instruments

The fair value of the Company's cash and cash equivalents, accounts receivable, and accounts payable approximate their respective carrying amounts.

(l) Use of Estimates

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(m) Revenue Recognition

SERENA recognizes revenue in accordance with Statement of Position (SOP) 97-2, *Software Revenue Recognition*, as amended by SOP 98-9, and generally recognizes revenue when all of the following criteria are met as set forth in paragraph 8 of SOP 97-2: (1) persuasive evidence of an arrangement exists, (2) delivery has occurred, (3) the fee is fixed or determinable and (4) collectibility is probable. SERENA defines each of these four criteria as follows:

Persuasive evidence of an arrangement exists. It is SERENA's customary practice to have a written contract, which is signed by both the customer and SERENA, or a purchase order from those customers who have previously negotiated a standard license arrangement with SERENA.

Delivery has occurred. SERENA's software is physically delivered to the customer. If an arrangement includes undelivered products or services that are essential to the functionality of the delivered product, delivery is not considered to have occurred until these products or services are

delivered.

The fee is fixed or determinable. SERENA's policy is to not provide customers the right to a refund of any portion of their license fees paid. SERENA may agree to extended payment terms with a foreign customer based on local customs. Generally, at least 80% of the arrangement fees are due within one year or less. Arrangements with payment terms extending beyond these customary payment terms are considered not to be fixed or determinable, and revenues from such arrangements are recognized as payments become due and payable.

Collectibility is probable. Collectibility is assessed on a customer-by-customer basis. SERENA typically sells to customers for whom there is a history of successful collection. If it is determined from the outset of an arrangement that collectibility is not probable, revenues are recognized as cash is collected.

For contracts with multiple elements (e.g., license and maintenance), revenue is allocated to each component of the contract based on vendor specific objective evidence (VSOE) of its fair value, which is the price charged when the elements are sold separately. Since VSOE has not been established for license transactions, the residual method is used to allocate revenue to the license portion of multiple-element transactions. Therefore, the Company recognizes the difference between the total arrangement fee and the amount deferred for the undelivered items as revenue.

The Company sells its products to its end users and distributors under license agreements. Each new mainframe license includes maintenance, which includes the right to receive telephone support, bug fixes and

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(1) Description of Business and Summary of Significant Accounting Policies (Continued)

unspecified upgrades and enhancements, for a specified duration of time, usually one year. The fee associated with such agreements is allocated between software license revenue and maintenance revenue based on the residual method. Software license revenue from these agreements is recognized upon receipt and acceptance of a signed contract and delivery of the software, provided the related fee is fixed and determinable, collectibility of the revenue is probable and the arrangement does not involve significant customization of the software. If an acceptance period is required, revenue is recognized upon the earlier of customer acceptance or the expiration of the acceptance period, as defined in the applicable software license agreement.

The Company recognizes maintenance revenue ratably over the life of the related maintenance contract. Maintenance contracts on perpetual licenses generally renew annually. The Company typically invoices and collects maintenance fees on an annual basis at the anniversary date of the license. Deferred revenue represents amounts received by the Company in advance of performance of the maintenance obligation. Professional services revenue includes fees derived from the delivery of training, installation, and consulting services. Revenue from training, installation, and consulting services is recognized on a time and materials basis as the related services are performed.

(n) Stock-Based Compensation

The Company uses the intrinsic value method to account for stock-based compensation. The Company amortizes deferred stock-based compensation on an accelerated basis in accordance with Financial Accounting Standards Board (FASB) Interpretation No. 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans*.

The Company accounts for employee stock-based compensation in accordance with Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees* and related interpretations. Since the exercise price of options granted under such plans is generally equal to the market value on the date of grant, no compensation cost has been recognized for grants under its stock option plans and stock purchase plans. In accordance with APB No. 25, the Company does not recognize compensation cost related to its employee stock purchase plan. If compensation cost for the Company's stock-based compensation plans had been determined consistent with SFAS No. 123, *Accounting for Stock-Based Compensation* and SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*, the Company's net income and net income per share would have been reduced to the pro forma amounts indicated below (in thousands, except per share amounts):

Fiscal Year Ended

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	January 31,		
	2001	2002	2003
Net income, as reported	\$ 24,254	\$ 18,509	\$ 23,154
Add: stock-based employee compensation expense included in reported net income, net of tax	126	80	14
Deduct: total stock-based employee compensation expense determined under fair value based method for all awards, net of tax	(5,332)	(9,149)	(11,054)
Pro forma net income	\$ 19,048	\$ 9,440	\$ 12,114
Basic net income per share:			
As reported	\$ 0.63	\$ 0.46	\$ 0.57
Pro forma	\$ 0.49	\$ 0.24	\$ 0.30
Diluted net income per share:			
As reported	\$ 0.60	\$ 0.46	\$ 0.57
Pro forma	\$ 0.47	\$ 0.23	\$ 0.30

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(1) Description of Business and Summary of Significant Accounting Policies (Continued)

For the pro forma amounts determined under SFAS No. 123, as set forth above, the fair value of each stock option grant under the stock option plans is estimated on the date of grant using the Black-Scholes Option-Pricing Model with the following weighted-average assumptions used for grants in fiscal 2001, 2002 and 2003; risk-free interest rates averaging 6.2% in 2001, 6.0% in 2002 and 2.8% in 2003; a dividend yield of 0% for all years; a weighted-average expected life of 4.5 years for all years; and a volatility factor of the expected market price of the Company's common stock of 134% for 2001, 116% for 2002 and 109% for 2003.

The fair value of the employees' purchase rights under the employee purchase plan is estimated on the date of grant using the Black-Scholes Option-Pricing Model with the following weighted-average assumptions for these rights granted in fiscal 2001, 2002 and 2003; risk-free interest rates averaging 6.2% in 2001, 6.0% in 2002 and 1.1% in 2003; a dividend yield of 0% for all years; a weighted-average expected life of 0.5 years for all years; and a volatility factor of the expected market price of the Company's common stock of 134% for 2001, 116% for 2002 and 89% for 2003.

(o) Net Income Per Share

Basic net income per share is computed using the weighted-average number of shares of common stock outstanding. Diluted net income per share is computed using the weighted-average number of shares of common stock outstanding and, when dilutive, potentially dilutive shares from restricted stock, options and warrants to purchase common stock using the treasury stock method.

(p) Accumulated Other Comprehensive (Loss) Income

Accumulated other comprehensive (loss) income consists entirely of cumulative translation adjustments resulting from the Company's application of its foreign currency translation policy and unrealized gains (losses) on marketable securities. The tax effects on the unrealized gains (losses) were not significant during any of the periods presented.

(q) Segment Reporting

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Statement of Financial Accounting Standards (SFAS) No. 131, *Disclosures about Segments of an Enterprise and Related Information* establishes standards for the manner in which public companies report information about operating segments in annual and interim financial statements. It also establishes standards for related disclosures about products and services, geographic areas, and major customers. The method for determining what information to report is based on the way management organizes the operating segments within the Company for making operating decisions and assessing financial performance. The Company's chief operating decision-maker is considered to be the Company's chief executive officer (CEO). The CEO reviews financial information presented on an entity level basis accompanied by disaggregated information about revenues by product type and certain information about geographic regions for purposes of making operating decisions and assessing financial performance. The entity level financial information is identical to the information presented in the accompanying statements of operations. Therefore, the Company has determined that it operates in a single operating segment: enterprise change management software.

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(1) Description of Business and Summary of Significant Accounting Policies (Continued)

Geographic information

	Year Ended January 31,		
	2001	2002	2003
	(In thousands)		
Revenues:			
North America	\$ 84,883	\$ 79,629	\$ 67,954
Europe	18,726	19,012	27,821
Total	\$ 103,609	\$ 98,641	\$ 95,775

The Company operates in North America and Europe. In general, revenues are attributed to the country in which the contract originates.

	January 31,	
	2002	2003
	(In thousands)	
Long-lived assets:		
North America	\$ 77,458	\$ 97,410
Europe	235	232
Total	\$ 77,693	\$ 97,642

Long-lived assets consist primarily of goodwill and other intangible assets, property and equipment and other long-term assets.

Major customers

No customer accounted for 10% or more of consolidated revenues in fiscal 2001 or 2002. In fiscal 2003, due to several large transactions with one international customer, this single customer accounted for 13% of fiscal 2003 consolidated revenues. No other customer accounted for 10% or more of consolidated revenues in fiscal 2003.

(r) Advertising

Advertising costs are expensed as incurred. Advertising expense is included in sales and marketing expense and amounted to \$1.4 million, \$1.4 million and \$1.3 million in fiscal 2001, 2002 and 2003, respectively.

(s) Recently Issued Accounting Standards

In August 2001, the FASB issued SFAS No. 143, *Accounting for Asset Retirement Obligations*. SFAS No. 143 requires an enterprise to record the fair value of an asset retirement obligation as a liability in the period in which it incurs a legal obligation associated with the retirement of a tangible long-lived asset. SFAS No. 143 also requires an enterprise to record a corresponding amount to the liability as an increase in the carrying amount of the related long-lived asset (i.e., the associated asset retirement costs) and to depreciate that cost over the remaining useful life of the asset. The amount of the asset retirement obligation is revised at the end of each period to reflect the passage of time (i.e., accretion expense) and changes in the estimated future cash flows underlying the initial fair value measurement. The Company is required to adopt SFAS No. 143 as of February 1, 2003. The Company does not expect SFAS No. 143 to have a material impact on its financial position or results of operations.

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(1) Description of Business and Summary of Significant Accounting Policies (Continued)

In April 2002, the FASB issued SFAS No. 145, *Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections*. Among other provisions, SFAS 145 rescinds SFAS 4, *Reporting Gains and Losses from Extinguishment of Debt*. Accordingly, gains or losses from extinguishment of debt that do not meet the criteria of APB No. 30 should be reclassified to income from continuing operations in all prior periods presented. SFAS 145 is effective for fiscal years beginning after May 15, 2002. The Company plans to adopt SFAS 145 beginning in its fiscal year 2004. The effect of adopting SFAS 145 is not expected to have a material effect on the Company's consolidated financial position or results of operations.

In July 2002, the FASB issued SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*. SFAS No. 146 eliminates Emerging Issues Task Force, or EITF, Issue No. 94-3 *Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring)*. Under SFAS No. 146, liabilities for costs associated with an exit or disposal activity are recognized when the liabilities are incurred, as opposed to being recognized at the date of entity's commitment to an exit plan under EITF No. 94-3. Furthermore, SFAS No. 146 establishes that fair value is the objective for initial measurement of the liabilities. This Statement will be effective for exit or disposal activities that are initiated after December 31, 2002.

In November 2002, the FASB issued Interpretation No. 45, *Guarantors Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*. Interpretation No. 45 requires a guarantor to include disclosure of certain obligations, and if applicable, at the inception of the guarantee, recognize a liability for the fair value of other certain obligations undertaken in issuing a guarantee. The recognition requirement is effective for guarantees issued or modified after December 31, 2002 and is not expected to have a material impact on the Company. The Company has provided the applicable disclosures of Interpretation No. 45 in these financial statements.

In December 2002, the FASB issued SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*. SFAS No. 148 amends SFAS No. 123, *Accounting for Stock-Based Compensation* to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on the reported results. The disclosure provisions of SFAS No. 148 are effective for financial statements for fiscal years ending after December 15, 2002. The Company has adopted the disclosure provisions of SFAS No. 148.

(2) Property and Equipment

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Property and equipment consisted of the following (in thousands):

	January 31,	
	2002	2003
Computers and equipment	\$ 6,056	\$ 6,592
Furniture and fixtures	1,726	1,888
Automobiles	107	
	<u>7,889</u>	<u>8,480</u>
Less: accumulated depreciation	4,853	5,402
	<u>\$ 3,036</u>	<u>\$ 3,078</u>

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(3) Goodwill and Other Intangible Assets

In July 2001, the FASB approved the issuance of SFAS No. 142, *Goodwill and Other Intangible Assets*. SFAS No. 142 provides guidance on how to account for goodwill and certain intangible assets after an acquisition is completed. The most substantive change is that goodwill and other indefinite life intangible assets can no longer be amortized but instead should be periodically tested for impairment. In the fiscal quarter ended April 30, 2002, the Company reevaluated its intangible asset lives and no adjustment to any of the useful lives was determined to be necessary. In the fiscal quarter ended July 31, 2002 and in accordance with Statement No. 142, the Company completed its initial transitional goodwill impairment test and concluded that there was no impairment of goodwill as of February 1, 2002. The annual impairment test required by SFAS No. 142 will be performed in the fourth fiscal quarter each year and has been performed in the fourth quarter of fiscal 2003. With the annual impairment test in the fourth quarter of fiscal 2003, the Company has concluded that there was no impairment of goodwill as of January 31, 2003. No reclassification of intangible assets apart from goodwill was necessary as a result of the adoption of Statement No. 142. We have also stopped the amortization of approximately \$28.9 million of goodwill beginning February 1, 2002. This reduction in amortization effective February 1, 2002 affected the comparability of current period results of operations with prior periods.

Goodwill and other intangible assets consisted of the following (in thousands):

	January 31,	
	2002	2003
Work-force-in-place	\$ 739	\$ 739
Non-compete agreement	944	944
Acquired technology	27,626	27,626
Goodwill	37,322	37,032
	<u>66,631</u>	<u>66,341</u>
Less: accumulated amortization	16,496	20,981
	<u>\$ 50,135</u>	<u>\$ 45,360</u>

Goodwill and other intangible assets consist of amortized intangible assets and intangible assets no longer subject to amortization under SFAS No. 142 as follows (in thousands):

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As of January 31, 2003

	<u>Gross Carrying Amount</u>	<u>Accumulated Amortization</u>	<u>Net Carrying Amount</u>
Amortized intangible assets:			
Non-compete agreements	\$ 944	\$ (944)	\$
Acquired technology	27,626	(11,141)	16,485
Total	\$ 28,570	\$ (12,085)	\$ 16,485
Unamortized intangible assets:			
Work-force-in-place	\$ 739	\$ (739)	\$
Goodwill	37,032	(8,157)	28,875
Total	\$ 37,771	\$ (8,896)	\$ 28,875

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(3) Goodwill and Other Intangible Assets (Continued)

Aggregate amortization expense:	
For year ended January 31, 2003	\$ 4,486
Estimated amortization expense:	
For year ended January 31, 2004	\$ 4,324
For year ended January 31, 2005	4,085
For year ended January 31, 2006	3,447
For year ended January 31, 2007	3,002
For year ended January 31, 2008	1,627
Thereafter	
Total	\$ 16,485

The changes in the carrying amount of goodwill for the year ended January 31, 2003 are as follows (in thousands):

Balance as of January 31, 2002	\$ 37,322
Activity during the year:	
Goodwill acquired	
Impairment losses recognized	
UltiMIS earnout reversal	(290)
Balance as of January 31, 2003	\$ 37,032

The following table presents the pro forma effects of SFAS No. 142, assuming we had adopted the standard as of February 1, 2000 (in thousands, except per share amounts):

Fiscal Year Ended January 31,

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	<u>2001</u>	<u>2002</u>	<u>2003</u>
Net income:			
Reported net income	\$ 24,254	\$ 18,509	\$ 23,154
Add back: goodwill and work-force-in-place amortization, net of tax	2,682	3,711	
	<u> </u>	<u> </u>	<u> </u>
Adjusted net income	\$ 26,936	\$ 22,220	\$ 23,154
	<u> </u>	<u> </u>	<u> </u>
Basic earnings per share:			
Reported basic earnings per share	\$ 0.63	\$ 0.46	\$ 0.57
Add back: goodwill and work-force-in-place amortization, net of tax	0.07	0.10	
	<u> </u>	<u> </u>	<u> </u>
Adjusted basic earnings per share	\$ 0.70	\$ 0.56	\$ 0.57
	<u> </u>	<u> </u>	<u> </u>
Diluted earnings per share:			
Reported diluted earnings per share	\$ 0.60	\$ 0.46	\$ 0.57
Add back: goodwill and work-force-in-place amortization, net of tax	0.06	0.09	
	<u> </u>	<u> </u>	<u> </u>
Adjusted diluted earnings per share	\$ 0.66	\$ 0.55	\$ 0.57
	<u> </u>	<u> </u>	<u> </u>

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Table of Contents**SERENA SOFTWARE, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Fiscal Years Ended January 31, 2001, 2002 and 2003****(4) Accrued Expenses****(a) Total Accrued Expenses**

Total accrued expenses consisted of the following (in thousands):

	January 31,	
	2002	2003
Management incentive bonuses and commissions	\$ 2,421	\$ 1,824
Payroll-related items	2,644	2,514
Royalties	475	407
Restructuring charges	1,175	422
Other	5,047	3,099
	\$ 11,762	\$ 8,266

(b) Restructuring Charges

On August 6, 2001, in response to the general weakening of the worldwide economy and resulting IT spending slowdown, the Company announced and began to execute its plan to reduce the workforce by approximately 12% or 45 positions affecting all parts of the organization and incur costs associated with the closure of facilities. The Company recorded a restructuring charge in the third quarter of fiscal 2002 consisting principally of severance, payroll taxes and other employee benefits totaling \$1.5 million and facilities closures totaling \$1.0 million. The Company has realized and expects to continue to realize cost savings going forward as a result of this reduction and other cost savings initiatives implemented. The Company's restructuring is substantially complete with these actions. The nature of the restructuring charges and the amounts paid through and accrued as of January 31, 2003 are summarized as follows (in thousands):

As of January 31, 2003

	<u>Total</u>	<u>Paid</u>	<u>Accrued</u>
Severance, payroll taxes and other employee benefits	\$ 1,483	\$ 1,135	\$ 348
Facilities closures	875	806	69
Legal and other miscellaneous	70	65	5
	<u> </u>	<u> </u>	<u> </u>
Total restructuring accrual	\$ 2,428	\$ 2,006	\$ 422
		<u> </u>	<u> </u>
Fixed asset impairment	101		
	<u> </u>		
Total restructuring charges	\$ 2,529		
	<u> </u>		

(5) Stockholders Equity

(a) Repurchase of Common Stock

In connection with the Company's Stock Repurchase Programs, the Company repurchased 80,000 shares of its common stock for cash at an average price of \$9.92 per share in fiscal 2002, and an additional 111,000 shares of its common stock for cash at an average price of \$13.34 per share in fiscal 2003.

(b) Restricted Stock Agreements

In March 1998, the Company issued 84,375 shares of restricted common stock to a director at \$0.96 per share in exchange for a full recourse note. In May 1999, 161,438 shares associated with the original restricted

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(5) Stockholders' Equity (Continued)

common stock issuance in January 1998 were repurchased at the original purchase price. In the fourth quarter of fiscal 2000, two officers early exercised common stock options and received 295,314 shares of restricted stock at an average price of \$3.99 per share. On February 1, 2000, an officer early exercised common stock options and received 4,500 shares of restricted stock at an average price of \$3.11 per share. The early exercise feature was included in the original stock option plan. On February 16, 2000 and under the Company's 1997 Stock Option and Incentive Plan, certain officers early exercised common stock options and the Company issued 817,500 shares of restricted common stock of the Company at \$19.33 per share in exchange for promissory notes. Restrictions lapse over two to four years, depending upon the individual and the earnings per share performance of the Company. In the event an employee is terminated or the director leaves the service of the Board, the Company has the right to repurchase, for a price equal to the individual's original purchase price, any remaining restricted shares held by the individual.

In connection with restricted common stock issued in January 1998, the Company recorded deferred stock-based compensation of \$3,681,000 representing the difference between the issuance price and the fair value of the Company's common stock at the date of issuance. An additional \$158,000 and \$75,000 of deferred stock-based compensation was recorded for the March 1998 issuance and fourth quarter of fiscal 1999 early exercise, respectively. There was no deferred stock-based compensation recorded in connection with the February 2000 issuance. These amounts are being amortized over the restriction period of the individual shares. Amortization of deferred stock-based compensation related to restricted common stock of \$223,000, \$135,000 and \$23,000 was recognized in fiscal 2001, 2002 and 2003, respectively. With the close of fiscal 2003, all deferred stock-based compensation recorded with respect to restricted common stock issuances has now been fully amortized. Beginning in fiscal 2004 and going forward, there will be no amortization of deferred stock-based compensation.

On June 1, 2000 and again on November 1, 2002, in connection with two officers' resignations from the Company, the Company exercised in full its repurchase rights with respect to the restricted common stock originally issued to each officer on February 16, 2000 under the Company's 1997 Stock Option and Incentive Plan. The Company repurchased 337,500 shares and 1,422 shares, respectively, of restricted common stock at the original purchase price of \$19.33 per share. There had been no deferred stock-based compensation recorded in connection with the original restricted common stock issuance.

(c) Net Income Per Share

The following is a reconciliation of the shares used in the computation of basic and diluted net income per share (in thousands):

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	Fiscal Year Ended January 31,		
	2001	2002	2003
Basic net income per share weighted average number of common shares outstanding	38,522	39,768	40,367
Effect of potentially dilutive securities outstanding restricted stock and options	2,207	992	487
Shares used in diluted net income per share computation	40,729	40,760	40,854

Options to purchase shares of common stock at a share price which is greater than the closing market price of the shares at the balance sheet date are not included in the computation of diluted earnings per share, or EPS,

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(5) Stockholders Equity (Continued)

because the effect of their inclusion would have been anti-dilutive. For each of the years ended January 31, 2001, 2002 and 2003, 234,500, 603,039 and 3,075,596, respectively, of options to purchase shares of common stock at an average share price of \$40.735, \$32.734 and \$20.746, respectively, were excluded from the computation of diluted EPS.

(6) Income Taxes

Income taxes are as follows (in thousands):

	Fiscal Year Ended January 31,		
	2001	2002	2003
Current:			
Federal	\$ 16,815	\$ 9,369	\$ 13,393
State	3,741	2,335	2,703
Foreign	242	316	362
	<u>20,798</u>	<u>12,020</u>	<u>16,458</u>
Deferred:			
Federal	(1,941)	1,005	(1,937)
State	(282)	(163)	(425)
	<u>(2,223)</u>	<u>842</u>	<u>(2,362)</u>
Total income taxes	<u>\$ 18,575</u>	<u>\$ 12,862</u>	<u>\$ 14,096</u>

The Company's effective tax rate differs from the statutory federal income tax rate of 35% for fiscal 2001, 2002 and 2003, primarily due to the following (in thousands):

	Fiscal Year Ended January 31,		
	2001	2002	2003
Tax expense at federal statutory rate	\$ 14,990	\$ 10,980	\$ 13,038
Research and experimentation credit	(732)	(1,027)	(882)
State tax, net of federal benefit	2,273	1,412	2,143
Foreign sales corporation benefit	(317)	(310)	(320)
Nondeductible stock-based compensation	78	47	8
Nondeductible intangible asset amortization	866	1,280	
In-process research and development	1,040		
Other	377	480	109
Total income taxes	\$ 18,575	\$ 12,862	\$ 14,096

Undistributed earnings of foreign subsidiaries for which US income taxes have not been provided were immaterial during the periods presented.

Table of Contents**SERENA SOFTWARE, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Fiscal Years Ended January 31, 2001, 2002 and 2003****(6) Income Taxes (Continued)**

The Company's net deferred tax assets are summarized as follows (in thousands):

	January 31,	
	2002	2003
	<u> </u>	<u> </u>
Deferred tax assets:		
Allowance for doubtful accounts	\$ 365	\$ 371
Accrued expenses	1,443	1,277
Deferred revenue	3,837	4,858
Long lived assets acquired in a business combination		471
Property and equipment		90
Other	189	43
	<u> </u>	<u> </u>
Total deferred tax assets	5,834	7,110
	<u> </u>	<u> </u>
Deferred tax liabilities:		
Long lived assets acquired in a business combination	(764)	
Property and equipment	(362)	
State taxes	(283)	(458)
	<u> </u>	<u> </u>
Total deferred tax liabilities	(1,409)	(458)
	<u> </u>	<u> </u>
Net deferred tax assets	\$ 4,425	\$ 6,652
	<u> </u>	<u> </u>

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which temporary differences become deductible. Management believes it is likely that the deferred tax assets will be realized; accordingly, no valuation allowance has been established.

(7) Employee and Director Benefit Plans

(a) Retirement Plan

The Company has a defined contribution retirement plan for all eligible employees. Participants may make contributions to the plan in accordance with provisions of the plan. The Company may make discretionary contributions to the plan. For the years ended January 31, 2001, 2002, and 2003, the Company made contributions of \$711,000, \$916,000 and \$879,000, respectively. Such contributions generally vest over six years.

(b) Stock Option Plans

In October 1997, the Company's Board of Directors approved the Company's 1997 Stock Option and Incentive Plan (the "Plan"). The Plan allows for grants to officers, directors and employees of the Company incentive stock options, nonqualified stock options and restricted stock. Options are generally granted for a 10-year term (5 years if the employee is more than a 10% shareholder) and generally vest over 4 years. Options are generally granted at fair market value (110% of fair market value if optionee is more than a 10% shareholder), as determined by the Board of Directors. Restricted stock may be granted pursuant to the Plan, as evidenced by agreement and determined by the Board of Directors.

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(7) Employee and Director Benefit Plans (Continued)

The Plan automatically terminates in September 2007. Each option and award granted under the Plan will remain in effect until such option or award has been satisfied by the issuance of shares or terminated in accordance with its terms and the terms of the Plan.

In December 2001, the Company's Board of Directors amended the Company's 1999 Director Option Plan (the Director Plan). The Director Plan allows for grants to non-employee directors of the Company incentive stock options, nonqualified stock options and restricted stock. The Director Plan provides that options will be granted to non-employee directors pursuant to an automatic nondiscretionary grant mechanism. Each new non-employee director is automatically granted an option to purchase 37,500 shares of common stock at the time he or she is first elected to the Board of Directors (First Option). Each non-employee director will subsequently be granted an option to purchase 15,000 shares of common stock at the beginning of each fiscal year (Subsequent Option). Each such option will be granted at the fair market value of the common stock on the date of grant. First Options granted to non-employee directors under the 1999 Director Option Plan will become exercisable over four years, with one quarter of the shares subject to the option vesting after one year and the remaining shares vesting ratably in monthly installments thereafter. Subsequent Options vest annually on the first anniversary of the grant date.

Stock option activity under the Plan and the Director Plan are as follows:

	Shares Available For Grant	Options Outstanding	Weighted- Average Exercise Price	Weighted Average Grant Date Fair Value Per Share
Balances as of January 31, 2000	2,080,518	1,847,640	\$ 4.84	
Authorized	937,500			
Restricted stock issued	(822,000)			
Restricted stock repurchased	337,500			
Granted with an exercise price equal to the fair value of common stock	(2,004,100)	2,004,100	\$ 24.05	\$ 24.05
Cancelled	226,519	(226,519)	\$ 15.97	
Exercised		(338,628)	\$ 3.10	
Balance as of January 31, 2001	755,937	3,286,593	\$ 15.98	
Authorized	1,050,000			
Granted with an exercise price equal to the fair value of common stock	(1,119,700)	1,119,700	\$ 20.30	\$ 20.30

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Cancelled	477,516	(477,516)	\$ 20.79	
Exercised		(517,400)	\$ 6.18	
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Balance as of January 31, 2002	1,163,753	3,411,377	\$ 18.04	
Authorized	1,150,000			
Restricted stock repurchased	1,422			
Granted with an exercise price equal to the fair value of common stock	(1,452,000)	1,452,000	\$ 13.74	\$ 13.74
Cancelled	283,757	(283,757)	\$ 24.11	
Exercised		(395,620)	\$ 5.24	
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Balance as of January 31, 2003	1,146,932	4,184,000	\$ 17.33	
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

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Table of Contents**SERENA SOFTWARE, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Fiscal Years Ended January 31, 2001, 2002 and 2003****(7) Employee and Director Benefit Plans (Continued)**

On February 14, 2001, the Company's board of directors approved the addition of 1,400,000 shares of the Company's common stock \$.001 par value per share (the Shares), of which (i) 990,000 Shares were added to the Amended and Restated 1997 Stock Option and Incentive Plan, (ii) 350,000 Shares were added to the 1999 Employee Stock Purchase Plan and (iii) 60,000 Shares were added to the 1999 Director Option Plan.

On June 1, 2001, the Company filed with the Securities and Exchange Commission a Form S-8 Registration Statement Under the Securities Act of 1933 (the Registration Statement). In the Registration Statement, the Company registered a total of 2,562,500 shares of the Company's common stock \$.001 par value per share (the Shares), of which (i) 1,927,500 Shares were registered under the Amended and Restated 1997 Stock Option and Incentive Plan, (ii) 575,000 Shares were registered under the 1999 Employee Stock Purchase Plan and (iii) 60,000 Shares were registered under the 1999 Director Option Plan.

On February 20, 2002, the Company's board of directors approved the addition of 1,400,000 shares of the Company's common stock \$.001 par value per share (the Shares), of which (i) 1,000,000 Shares were added to the Amended and Restated 1997 Stock Option and Incentive Plan, (ii) 250,000 Shares were added to the 1999 Employee Stock Purchase Plan and (iii) 150,000 Shares were added to the 1999 Director Option Plan. In fiscal 2001, 2002 and 2003, there was no deferred stock-based compensation recorded with respect to options issued by the Company. Stock-based compensation expense related to options to purchase common stock of \$143,000, \$122,000 and \$23,000 was recognized in fiscal 2001, 2002 and 2003, respectively.

The following table summarizes information about stock options outstanding at January 31, 2003:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number of Shares	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
\$0.667 - \$ 0.667	16,000	4.93	\$ 0.667	16,000	\$ 0.667
\$0.963 - \$ 4.667	257,782	5.53	\$ 3.456	257,782	\$ 3.456
\$6.000 - \$17.312	1,691,122	8.85	\$ 12.791	210,824	\$ 8.712
\$17.500 - \$17.500	778,762	7.27	\$ 17.500	511,921	\$ 17.500

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\$17.917 - \$29.687	1,078,773	8.06	\$ 22.183	497,433	\$ 22.111
\$30.875 - \$36.437	287,061	7.83	\$ 31.741	160,233	\$ 31.851
\$40.187 - \$47.500	74,500	7.70	\$ 44.448	42,108	\$ 44.359
\$0.667 - \$47.500	4,184,000	8.04	\$ 17.331	1,696,301	\$ 17.489

(c) Employee Stock Purchase Plan

The Employee Stock Purchase Plan allows eligible employee participants to purchase shares of our common stock at a discount through payroll deductions. Commencing with the Company's IPO in February 1999, the plan consisted initially of a twenty-four-month offering period with an initial six-month purchase period followed by an abbreviated purchase period to get purchase periods on a six-month May/November purchase period cycle thereafter. Currently, the plan consists of twelve-month offerings with two six-month purchase periods in each offering period. As of January 31, 2003, all employees participating in the plan have twelve-month offering periods. Employees purchase shares at 85% of market value at either the beginning of the offering period or the

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(7) Employee and Director Benefit Plans (Continued)

end of the purchase period, whichever price is lower. As of January 31, 2003, we had reserved 1,162,500 shares of our common stock for issuance under this plan, and approximately 584,639 shares remain available for future issuance.

(d) Nonemployee Stock Warrant

During fiscal 2002, the Company granted a fully vested stock purchase warrant to acquire 10,000 shares of common stock to a third party, contingent upon obtaining recruiting services. In July 2001, the services were performed. The Company recorded the fair value of the stock warrant of approximately \$129,000 as general and administrative expense in fiscal 2002.

The fair value of stock warrant issued to the third party was estimated at the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions: Expected volatility of 117%; Risk-free interest rate of 5%; Contractual life of the term of the security; and Dividend yield of zero.

(8) Commitments and Contingencies

(a) Leases

The Company has noncancelable operating lease agreements for office space that expire between calendar 2003 and 2008. Minimum lease payments for the five succeeding years as of January 31, 2003, are as follows (in thousands):

Fiscal Year Ending January 31,	
2004	\$ 1,176
2005	1,246

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2006	1,186
2007	807
2008	842
Thereafter	
	<hr/>
	\$ 5,257
	<hr/>

Rent expense was \$1,164,000, \$1,634,000 and \$1,462,000 for the fiscal years ended January 31, 2001, 2002, and 2003, respectively.

(b) Licensing and Other Agreements

The Company has commitments under licensing agreements that provide for payments based on revenues of certain products. For the fiscal years ended January 31, 2001, 2002, and 2003, the Company's fees paid or accrued under these license agreements were \$2,422,000, \$583,000 and \$944,000, respectively.

The Company's acquisition of High Power Software, Inc. in May 2000 (see Note 9(a)) and the *StarTool* Asset Purchase in August 2000 (see Note 11) resulted in the elimination of certain royalty commitments under licensing arrangements.

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(8) Commitments and Contingencies (Continued)

(c) Customer Indemnification

From time to time, the Company agrees to indemnify its customers against liability if the Company's products infringe a third party's intellectual property rights. As of January 31, 2003, the Company was not subject to any pending litigation alleging that the Company's products infringe the intellectual property rights of any third parties.

(9) Acquisitions

(a) High Power Software, Inc.

On May 1, 2000, the Company acquired High Power Software, Inc. (HPS). HPS shared ownership rights in the Company's *ChangeMan SSM* (formerly, *Detect+Resolve Mainframe*) technology. The acquisition was accounted for using the purchase method of accounting, and accordingly, the results of operations of HPS are included in the Company's consolidated financial statements from May 1, 2000. The Company acquired all the assets and assumed all the liabilities of HPS in exchange for cash of approximately \$1.4 million and the issuance of 91,954 shares of the Company's common stock valued at \$19.97 per share. The transaction was valued at approximately \$3.3 million.

Acquired technology, consisting of current completed technologies at the date of acquisition and valued on the premise of fair market value in continued use under the discounted cash flow approach, will be amortized over a five-year period, the period of time the Company estimates as its economic useful life. Acquired in-process research and development, consisting of current technologies under development at the date of acquisition and valued on the premise of fair market value in continued use under the discounted cash flow approach, was expensed immediately in the second fiscal quarter ended July 31, 2000 in accordance with generally accepted accounting principles. See Note 10 for further discussion of acquired in-process research and development. Work-force-in-place, consisting principally of the HPS development team, was valued on a replacement cost basis and was amortized over a six-month period, the period of time the Company estimated would be required to hire, train, and achieve full productivity for a replacement work force. Goodwill represents the excess of the purchase price over the fair value of the net assets acquired and was originally amortized on the basis of a 7 year life, until amortization ceased pursuant to SFAS No. 142, which was adopted on February 1, 2002 (See Footnote 3).

(b) UltiMIS Corporation

On September 18, 2000, the Company acquired UltiMIS Corporation (UltiMIS), a provider of data center performance and programmer productivity software products which provided the Company an integrated suite of products for file and data management, fault diagnostics, application performance monitoring, testing and debugging. The acquisition was accounted for using the purchase method of accounting, and accordingly, the results of operations of UltiMIS are included in the Company's consolidated financial statements from September 18, 2000.

The Company acquired all the assets and assumed all the liabilities of UltiMIS in exchange for cash of approximately \$7.7 million and the issuance of 173,758 shares of the Company's common stock valued at \$43.35 per share. The transaction was originally valued at approximately \$15.3 million. The Company accrued

Table of Contents**SERENA SOFTWARE, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Fiscal Years Ended January 31, 2001, 2002 and 2003****(9) Acquisitions (Continued)**

additional contingent consideration, net of a reversal, totaling \$710,000 in connection with the earnout agreement. This contingent consideration was recorded as goodwill and is in addition to the goodwill and total consideration amounts noted above.

Acquired technology, consisting of current completed technologies at the date of acquisition and valued on the premise of fair market value in continued use under the discounted cash flow approach, is amortized over a five-year period, the period of time the Company estimates as its economic useful life. Acquired in-process research and development, consisting of current technologies under development at the date of acquisition and valued on the premise of fair market value in continued use under the discounted cash flow approach, was expensed immediately in the third fiscal quarter ended October 31, 2000 in accordance with generally accepted accounting principles. See Note 10 for further discussion of acquired in-process research and development. Work-force-in-place, consisting principally of the UltiMIS development team, was valued on a replacement cost basis and was amortized over a six-month period, the period of time the Company estimated would be required to hire, train, and achieve full productivity for a replacement work force. The non-compete agreements were entered into with the two UltiMIS officers and founders. The non-compete agreements were valued based on the estimated amount of business that might be lost if these two principals were competing against the Company over the period of the agreements, and they are being amortized over the two-year term of the agreements. Goodwill represents the excess of the purchase price over the fair value of the net assets acquired and was originally amortized on the basis of a 7 year life, until amortization ceased pursuant to SFAS No. 142, which was adopted on February 1, 2002 (See Footnote 3).

(c) Summary of the Purchase Price Allocation

The allocation of the total consideration made for each acquisition is as follows (in thousands):

	High Power Software	UltiMIS Corporation
	<u> </u>	<u> </u>
Tangible assets	\$ 6	\$ 573
Assumed liabilities	(173)	(1,310)
Acquired technology	1,894	2,800
Acquired in-process research and development	491	2,481
Work-force-in-place	49	211
Non-compete agreements		516
Deferred tax liability	(855)	(1,552)
Goodwill	1,907	12,613

Total consideration	\$ 3,319	\$ 16,332
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With respect to the HPS and UltiMIS acquisitions, pro forma financial information giving effect to each acquisition as if it had occurred at the beginning of the periods presented would not have been materially different than the Company's historical operating results.

(10) Acquired In-process Research and Development

As a result of the Company's acquisitions of HPS on May 1, 2000 and UltiMIS on September 18, 2000, the Company recorded acquired in-process research and development totaling \$491,000 and \$2,481,000, respectively. For both transactions, the premise of value was fair market value in continued use.

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(10) Acquired In-process Research and Development (Continued)

Among the assets that were valued by the Company were the *Change Transfer* and *Softwatch* products from the HPS acquisition, and the *StarProbe* and *StarTest* products from the UltiMIS acquisition, all of which were currently under development at their respective dates of acquisition. These technologies currently under development were valued on the premise of fair market value in continued use employing a version of the income approach referred to as the discounted cash flow approach. This methodology is based on discounting to present value, at an appropriate risk-adjusted discount rate, both the expenditures to be made to complete the development efforts (excluding the efforts to be completed on the development efforts underway) and the operating cash flows which the applications are projected to generate, less a return on the assets necessary to generate the operating cash flows.

From these projected revenues, the Company deducted costs of sales, operating costs (excluding costs associated with the efforts to be completed on the development efforts underway), royalties and taxes to determine net cash flows. The Company estimated the percentage of completion of the development efforts for each application by comparing the estimated costs incurred and portions of the development accomplished through their respective acquisition dates by the total estimated cost and total development effort of developing these same applications. This percentage was calculated for each application and was then applied to the net cash flows for which each application was projected to generate. These net cash flows were then discounted to present values using appropriate risk-adjusted discount rates in order to arrive at discounted fair values for each application.

The percentage complete and the appropriate risk-adjusted discount rate for each application were as follows:

<u>Application Under Development</u>	<u>Percentage Complete</u>	<u>Discount Rate</u>
HPS acquisition		
Change Transfer	80.00%	24.00%
Softwatch	60.00%	26.50%
UltiMIS acquisition		
StarProbe	90.00%	30.00%
StarTest	70.00%	32.50%

The rates used to discount the net cash flows to present value were initially based on the weighted average cost of capital (WACC). With respect to the HPS acquisition, the Company used discount rates of 24.0% and 26.5% for valuing the acquired in-process research and development and 21.5% for the core technologies. With respect to the UltiMIS acquisition, the Company used discount rates of 30.0% and 32.5% for valuing the acquired in-process research and development and 25.0% for the core technologies. In all cases, these discount rates are higher than the implied WACC due to the inherent uncertainties surrounding the successful development of the acquired in-process research and development, the

useful life of such in-process research and development, the profitability levels of such in-process research and development, and the uncertainty of technological advances that were unknown at the time.

(11) StarTool Asset Purchase

On August 18, 2000, the Company acquired the *StarTool* technology from its principal developer, an employee, pursuant to the *Startool* Asset Purchase Agreement dated August 18, 2000. Prior to the acquisition, the

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SERENA SOFTWARE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fiscal Years Ended January 31, 2001, 2002 and 2003

(11) StarTool Asset Purchase (Continued)

developer had granted the Company an exclusive, worldwide and non-transferable license to copy, market and distribute the *StarTool* Program technology and all options thereto. The Company paid an aggregate amount of \$20.9 million in a combination of \$16 million in cash and 130,612 shares of common stock valued at \$37.625 per share to the developer in exchange for all rights, title and interests in and to the *StarTool* technology. The per share value of the common stock was determined based on the closing market price of the common stock on August 18, 2000. The common stock received by the developer was placed in a hold-back escrow account at the closing of the transaction to cover any losses that the developer has agreed to indemnify the Company for in connection with the acquisition. Technology acquired has been capitalized and is being amortized over its estimated useful life of seven years.

Also pursuant to the Agreement, the developer entered into an Employment Agreement, on August 18, 2000, with the Company for a term of five years, to serve as a software architect. In August 2002, the developer tendered his resignation thereby terminating the Employment Agreement and his employment with the Company effective August 9, 2002.

(12) Subsequent Events Stock Repurchase Program and Repurchase of Common Stock (Unaudited)

In February 2003, our Board of Directors authorized the repurchase of up to 1.0 million shares of our Common Stock from time to time in the open market or in privately negotiated block transactions. The Company will utilize any reacquired shares under this program for reissuance in connection with employee stock programs and general corporate purposes. At various times from February 25, 2003 through April 1, 2003, the Company repurchased in aggregate a total of 484,800 shares of its common stock for cash at an average price of \$15.18 per share. The timing and size of any future stock repurchases are subject to market conditions, stock prices, our cash position and other cash requirements going forward.

Table of Contents**SERENA SOFTWARE, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except share data)****(Unaudited)**

	October 31, 2003	January 31, 2003
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 105,297	\$ 105,402
Short-term investments	18,392	37,672
Accounts receivable, net of allowance of \$868 and \$869 at October 31 and January 31, 2003, respectively	15,296	16,514
Deferred taxes, net of liabilities	4,862	6,549
Prepaid expenses and other current assets	965	744
	<u>144,812</u>	<u>166,881</u>
Total current assets	144,812	166,881
Long-term investments	39,753	48,374
Property and equipment, net	3,269	3,078
Deferred taxes, net of liabilities	259	103
Goodwill and other intangible assets, net	61,632	45,360
Other assets	280	269
	<u>250,005</u>	<u>264,065</u>
TOTAL ASSETS	\$ 250,005	\$ 264,065
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 1,251	\$ 533
Income taxes payable	4,014	7,921
Accrued expenses	7,020	8,266
Deferred revenue	26,294	26,010
	<u>38,579</u>	<u>42,730</u>
Total current liabilities	38,579	42,730
Deferred revenue, net of current portion	9,254	8,373
	<u>47,833</u>	<u>51,103</u>
Total liabilities	47,833	51,103
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 5,000,000 shares authorized; no shares issued and outstanding		
Common stock, \$0.001 par value; 90,000,000 shares authorized; 39,162,539 and 40,645,508 shares issued and outstanding at October 31 and January 31, 2003, respectively	39	41
Additional paid-in capital	93,102	126,006
Notes receivable from stockholders	(1,211)	(8,519)
Accumulated other comprehensive income	134	709
Retained earnings	110,108	94,725

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Total stockholders' equity	202,172	212,962
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 250,005	\$ 264,065

See accompanying notes to condensed consolidated financial statements.

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Table of Contents**SERENA SOFTWARE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME****For the Three Months and Nine Months Ended October 31, 2003 and 2002****(In thousands, except per share data)****(Unaudited)**

	Three Months Ended October 31,		Nine Months Ended October 31,	
	2003	2002	2003	2002
Revenue:				
Software licenses	\$ 10,963	\$ 11,502	\$ 31,862	\$ 31,458
Maintenance	13,121	11,165	37,481	32,957
Professional services	2,571	1,966	6,593	5,262
Total revenue	26,655	24,633	75,936	69,677
Cost of revenue:				
Software licenses	129	363	512	946
Maintenance	1,606	1,405	4,715	4,192
Professional services	2,462	1,794	6,506	4,715
Total cost of revenue	4,197	3,562	11,733	9,853
Gross profit	22,458	21,071	64,203	59,824
Operating expenses:				
Sales and marketing	7,341	6,487	21,008	19,487
Research and development	3,671	2,981	10,130	8,873
General and administrative	1,881	1,811	5,349	5,200
Stock-based compensation		5		22
Amortization of intangible assets	2,664	1,113	5,881	3,405
Total operating expenses	15,557	12,397	42,368	36,987
Operating income	6,901	8,674	21,835	22,837
Interest and other income, net	677	1,237	2,495	3,633
Income before income taxes	7,578	9,911	24,330	26,470
Income taxes	2,728	3,766	8,946	10,059

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Net income	\$ 4,850	\$ 6,145	\$ 15,384	\$ 16,411
Comprehensive income:				
Net income	\$ 4,850	\$ 6,145	\$ 15,384	\$ 16,411
Other comprehensive (loss) income:				
Foreign currency translation adjustment	(59)	71	(14)	113
Unrealized (loss) gain on marketable securities	(44)	225	(561)	470
Other comprehensive (loss) income	(103)	296	(575)	583
Total comprehensive income	\$ 4,747	\$ 6,441	\$ 14,809	\$ 16,994
Net income per share:				
Basic	\$ 0.12	\$ 0.15	\$ 0.38	\$ 0.41
Diluted	\$ 0.12	\$ 0.15	\$ 0.38	\$ 0.40
Weighted average shares used in per share calculations:				
Basic	39,545	40,420	40,032	40,292
Diluted	40,173	41,000	40,706	40,772

See accompanying notes to condensed consolidated financial statements.

Table of Contents**SERENA SOFTWARE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****For the Nine Months Ended October 31, 2003 and 2002****(In thousands)****(Unaudited)**

	Nine Months Ended October 31,	
	2003	2002
Cash flows from operating activities:		
Net income	\$ 15,384	\$ 16,411
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	1,170	1,026
Provision in allowance for bad debts	254	775
Gain on disposal of property and equipment	(2)	(30)
Accrued interest on notes receivable from stockholders, net of cash received	1,281	(399)
Amortization of deferred stock-based compensation	22	22
Amortization of intangible assets	5,881	3,405
Changes in operating assets and liabilities:		
Accounts receivable	2,526	(3,925)
Prepaid expenses and other assets	(32)	(305)
Accounts payable	594	(394)
Income taxes payable	(3,935)	3,865
Accrued expenses	(2,244)	(1,718)
Deferred revenue	(1,161)	(504)
Net cash provided by operating activities	19,716	18,229
Cash flows used in investing activities:		
Purchases of property and equipment	(843)	(1,336)
Sales (purchases) of short-term and long-term investments	27,340	(5,010)
Cash paid for UltiMIS Corporation earn-out	(710)	(710)
Cash paid for TeamShare Inc., net of cash received	(19,425)	(19,425)
Net cash provided by (used in) investing activities	7,072	(7,056)
Cash flows from financing activities:		
Exercise of stock options under the employee stock option plan	4,251	1,321
Sale of common stock under the employee stock purchase plan	779	813
Payment of principal on notes receivable from stockholders	6,026	624
Common stock repurchased under the stock repurchase plan	(37,935)	(829)

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Net cash (used in) provided by financing activities	(26,879)	1,929
Effect of exchange rate changes on cash	(14)	113
Net (decrease) increase in cash and cash equivalents	(105)	13,215
Cash and cash equivalents at beginning of period	105,402	85,954
Cash and cash equivalents at end of period	\$ 105,297	\$ 99,169
Supplemental disclosures of cash flow information:		
Income taxes paid	\$ 13,199	\$ 6,395
Non-cash investing and financing activity:		
Unrealized (loss) gain on marketable securities	\$ (561)	\$ 470
Contingent consideration accrued for the UltiMIS acquisition, net	\$	\$ (290)

See accompanying notes to condensed consolidated financial statements.

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

SERENA Software, Inc. (SERENA or the Company) is an Enterprise Change Management (ECM) industry leader providing solutions that help companies automate change to the applications that run their businesses. The Company s solutions take a cross-platform and cross-organizational view of enterprise applications, allowing customers to define, enforce and automate application lifecycle processes. Its principal markets are North America, and to a lesser extent, Europe.

The accompanying unaudited condensed consolidated financial statements have been prepared on substantially the same basis as the audited consolidated financial statements, and in the opinion of management include all adjustments, consisting only of normal recurring adjustments, except as otherwise noted, necessary for their fair presentation. These unaudited condensed consolidated financial statements and the notes thereto have been prepared in accordance with the Instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all disclosures required by accounting principles generally accepted in the United States of America and Regulation S-X for annual financial statements. For these additional disclosures, readers should refer to the Company s annual report on Form 10-K for the fiscal year ended January 31, 2003. The interim results presented are not necessarily indicative of results for any subsequent quarter or for the fiscal year ending January 31, 2004.

Reclassifications

Certain reclassifications have been made to the January 31, 2003 balances in order to conform to the October 31, 2003 presentation.

(1) Stock-Based Compensation

The Company uses the intrinsic value method to account for stock-based compensation. The Company amortizes deferred stock-based compensation on an accelerated basis in accordance with Financial Accounting Standards Board (FASB) Interpretation No. 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans*.

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

The Company accounts for employee stock-based compensation in accordance with Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees* and related interpretations. Since the exercise price of options granted under such plans is generally equal to the market value on the date of grant, no compensation cost has been recognized for grants under its stock option plans and stock purchase plans. In accordance with APB No. 25, the Company does not recognize compensation cost related to its employee stock purchase plan. If compensation cost for the Company's stock-based compensation plans had been determined consistent with SFAS No. 123, *Accounting for Stock-Based Compensation* and SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*, the Company's net income and net income per share would have been reduced to the pro forma amounts indicated below (in thousands, except per share amounts):

	Three Months Ended		Nine Months Ended	
	October 31,		October 31,	
	2003	2002	2003	2002
Net income, as reported	\$ 4,850	\$ 6,145	\$ 15,384	\$ 16,411
Add: stock-based employee compensation expense included in reported net income, net of tax		3		14
Deduct: total stock-based employee compensation expense determined under fair value based method for all awards, net of tax	(2,205)	(2,950)	(7,546)	(8,636)
Pro forma net income	\$ 2,645	\$ 3,198	\$ 7,838	\$ 7,789
Basic net income per share:				
As reported	\$ 0.12	\$ 0.15	\$ 0.38	\$ 0.41
Pro forma	\$ 0.07	\$ 0.08	\$ 0.20	\$ 0.19
Diluted net income per share:				
As reported	\$ 0.12	\$ 0.15	\$ 0.38	\$ 0.40
Pro forma	\$ 0.07	\$ 0.08	\$ 0.19	\$ 0.19

For the pro forma amounts determined under SFAS No. 123, as set forth above, the fair value of each stock option grant under the stock option plans and the fair value of the employees' purchase rights under the employee stock purchase plan (ESPP) are estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants in the three and nine months ended October 31, 2003 and 2002.

	Stock Option Plans		ESPP		Stock Option Plans		ESPP	
	Three Months Ended October 31,				Nine Months Ended October 31,			
	2003	2002	2003	2002	2003	2002	2003	2002
Expected life (in years)	4.5	4.5	0.5	0.5	4.5	4.5	0.5	0.5
Risk-free interest rate	2.9%	2.8%	1.1%	1.1%	2.9%	2.8%	1.1%	1.1%
Volatility	101%	109%	49%	89%	101%	109%	49%	89%
Dividend yield	none	none	none	none	none	none	none	none

The Black-Scholes option-pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option-pricing models require the input of

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

highly subjective assumptions including the expected stock price volatility. We used historical volatility rates. Because our employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of our options.

(2) Net Income Per Share

Basic net income per share is computed using the weighted-average number of shares of common stock outstanding. Diluted net income per share is computed using the weighted-average number of shares of common stock outstanding and, when dilutive, potentially dilutive common shares from restricted stock and options to purchase common stock using the treasury stock method.

The following is a reconciliation of the shares used in the computation of basic and diluted net income per share (in thousands):

	Three Months		Nine Months	
	Ended		Ended	
	October 31,		October 31,	
	2003	2002	2003	2002
Basic net income per share weighted average number of common shares outstanding	39,545	40,420	40,032	40,292
Effect of potentially dilutive securities outstanding stock options	628	580	674	480
Shares used in diluted net income per share computation	40,173	41,000	40,706	40,772

Options to purchase shares of common stock at a share price which is greater than the average closing market price of the shares for the quarter are not included in the computation of diluted earnings per share because the effect of their inclusion would be anti-dilutive. For both the three and nine month periods ended October 31, 2003, 1,724,562 options to purchase shares of common stock at an average share price of \$23.96 were excluded from the computation of diluted EPS. For the same three and nine month periods a year ago, 3,141,666 options to purchase shares of common stock at an average share price of \$20.86 were excluded from the computation of diluted EPS.

(3) Recent Accounting Pronouncements

In August 2001, the FASB issued SFAS No. 143, *Accounting for Asset Retirement Obligations*. SFAS No. 143 requires an enterprise to record the fair value of an asset retirement obligation as a liability in the period in which it incurs a legal obligation associated with the retirement of a tangible long-lived asset. SFAS No. 143 also requires an enterprise to record a corresponding amount to the liability as an increase in the carrying amount of the related long-lived asset (i.e., the associated asset retirement costs) and to depreciate that cost over the remaining useful life of the asset. The amount of the asset retirement obligation is revised at the end of each period to reflect the passage of time (i.e., accretion expense) and changes in the estimated future cash flows underlying the initial fair value measurement. The Company adopted the provisions of SFAS No. 143 as of February 1, 2003, and the adoption did not have a material impact on the Company's consolidated financial position or results of operations.

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

In July 2002, the FASB issued SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*. SFAS No. 146 eliminates Emerging Issues Task Force, or EITF, Issue No. 94-3 *Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring)*. Under SFAS No. 146, liabilities for costs associated with an exit or disposal activity are recognized when the liabilities are incurred, as opposed to being recognized at the date of entity's commitment to an exit plan under EITF No. 94-3. Furthermore, SFAS No. 146 establishes that fair value is the objective for initial measurement of the liabilities. This Statement is effective for exit or disposal activities that are initiated after December 31, 2002.

In November 2002, the FASB issued Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*. Interpretation No. 45 requires a guarantor to include disclosure of certain obligations, and if applicable, at the inception of the guarantee, recognize a liability for the fair value of other certain obligations undertaken in issuing a guarantee. The recognition requirement is effective for guarantees issued or modified after December 31, 2002 and did not have a material impact on the Company.

The following is a summary of our agreements that the Company has determined are within the scope of Interpretation No. 45, or FIN 45, which are separately grandfathered because the guarantees were in effect prior to December 31, 2002. Accordingly, the Company has no liabilities recorded for these agreements as of October 31, 2003.

As permitted under Delaware law and our by-laws and certificate of incorporation, the Company has agreements whereby the Company indemnifies our officers and directors for certain events or occurrences while the officer or director is, or was serving, at our request in such capacity. The term of the indemnification period is for the officer's or director's lifetime. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements is unlimited; however, the Company has a directors' and officers' insurance policy that may enable the Company to recover a portion of any future amounts paid. Assuming the applicability of coverage and the willingness of the insurer to assume coverage and subject to certain retention, loss limits and other policy provisions, the Company believes the estimated fair value of this indemnification obligation is not material. However, no assurances can be given that the insurers will not attempt to dispute the validity, applicability or amount of coverage, which attempts may result in expensive and time-consuming litigation against the insurers.

When, as part of an acquisition, the Company acquires all of the stock or all of the assets and liabilities of a company, the Company assumes the liability for certain events or occurrences that took place prior to the date of acquisition. The maximum potential amount of future payments the Company could be required to make for such obligations is undeterminable at this time. Accordingly, the Company has no liabilities recorded for these types of agreements as of October 31, 2003.

From time to time, the Company engages various professional service firms which require as a condition of their engagement that the Company undertake to indemnify them for all claims and damages arising out of their engagement. In the recent past, the Company has not been subject to

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any significant claims for such losses and has not incurred any material costs in defending or settling claims related to these indemnification obligations. Accordingly, the Company believes the estimated fair value of these obligations is not material.

The Company undertakes indemnification obligations in our ordinary course of business in connection with, among other things, the licensing of our products and the provision by the Company of consulting services.

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

Pursuant to these agreements, the Company may indemnify the other party for certain losses suffered or incurred by the indemnified party, generally our business partners or customers, in connection with various types of claims, which may include, without limitation, claims of intellectual property infringement, certain tax liabilities, negligence and intentional acts in the performance of services and violations of laws. The term of these indemnification obligations is generally perpetual. In general, the Company attempts to limit the maximum potential amount of future payments the Company could be required to make under these indemnification obligations to the purchase price paid, but in some cases the obligation may not be so limited. In addition, the Company may, in certain situations, warrant that, for a certain period of time from the date of delivery, our software products will be free from defects in media or workmanship. From time to time, the Company may also warrant that our professional services will be performed in a good and workmanlike manner. In addition, it is the Company's standard policy to seek to disclaim most warranties, including any implied or statutory warranties such as warranties of merchantability, fitness for a particular purpose, quality and non-infringement, as well as any liability with respect to incidental, consequential, special exemplary, punitive or similar damages. In some states, such disclaimers may not be enforceable. If necessary, the Company would provide for the estimated cost of product and service warranties based on specific warranty claims and claim history. In the recent past, the Company has not been subject to any significant claims for such losses and has not incurred any material costs in defending or settling claims related to these indemnification obligations. Accordingly, the Company believes the estimated fair value of these agreements is not material.

In November 2002, the EITF reached a consensus on EITF No. 00-21, *Revenue Arrangements with Multiple Deliverables*. EITF No. 00-21 addresses certain aspects of the accounting by a vendor for arrangements under which the vendor will perform multiple revenue-generating activities. EITF No. 00-21 became effective for interim periods beginning after June 15, 2003, which is the Company's third quarter of fiscal 2004. The effect of adopting EITF 00-21 this quarter did not have a material impact on the Company's consolidated financial position or results of operations.

In December 2002, the FASB issued SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*. SFAS No. 148 amends SFAS No. 123, *Accounting for Stock-Based Compensation* to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on the reported results. The disclosure provisions of SFAS No. 148 are effective for financial statements for fiscal years ending after December 15, 2002. The Company has adopted the disclosure provisions of SFAS No. 148.

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SERENA SOFTWARE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(Unaudited)

(4) Restructuring Costs

On August 6, 2001, in response to the general weakening of the worldwide economy and resulting IT spending slowdown, the Company announced and began to execute its plan to reduce workforce by approximately 12% or 45 positions affecting all parts of the organization and incur costs associated with the closure of facilities. The Company recorded a restructuring charge in the third quarter of fiscal 2002 consisting principally of severance, payroll taxes and other employee benefits totaling \$1.5 million and facilities closures totaling \$1.0 million. The Company has realized and expects to continue to realize cost savings going forward as a result of this reduction and other cost savings initiatives implemented. The Company's restructuring is substantially complete with these actions. The nature of the restructuring charges and the amounts paid through and accrued as of October 31, 2003 are summarized as follows (in thousands):

		As of October 31, 2003		
	Total	Paid	Adjustments	Accrued
Severance, payroll taxes and other employee benefits	\$ 1,483	\$ 1,135	\$ (195)	\$ 153
Facilities closures	875	989	195	81
Legal and other miscellaneous	70	65		5
Total restructuring accrual	2,428	\$ 2,189	\$	\$ 239
Fixed asset impairment	101			
Total restructuring charges	\$ 2,529			

(5) Goodwill and Other Intangibles

In July 2001, the FASB approved the issuance of SFAS No. 142, *Goodwill and Other Intangible Assets*. SFAS No. 142 provides guidance on how to account for goodwill and certain intangible assets after an acquisition is completed. The most substantive change is that goodwill and other indefinite life intangible assets can no longer be amortized but instead should be periodically tested for impairment. In the fiscal quarter ended April 30, 2002, the Company reevaluated its intangible asset lives and no adjustment to any of the useful lives was determined to be necessary. In the fiscal quarter ended July 31, 2002 and in accordance with Statement No. 142, the Company completed its initial transitional goodwill impairment test and concluded that there was no impairment of goodwill as of February 1, 2002. With the annual impairment test in the fourth quarter of fiscal 2003, the Company concluded that there was no impairment of goodwill as of January 31, 2003.

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

Goodwill and other intangible assets consisted of the following (in thousands):

	As of October 31, 2003	As of January 31, 2003
	<u> </u>	<u> </u>
Goodwill	\$ 35,980	\$ 28,877
Other intangible assets:		
Non-compete agreements	1,634	944
Acquired technology	37,476	27,626
Maintenance service contracts	1,800	
Trademark/Trade name portfolio	200	
Customer relationships	2,510	
	<u> </u>	<u> </u>
	43,620	28,570
Accumulated amortization	(17,968)	(12,087)
	<u> </u>	<u> </u>
	\$ 25,652	\$ 16,483
	<u> </u>	<u> </u>
Aggregate amortization expense:		
Nine Months Ended October 31, 2003		\$ 5,881
		<u> </u>
Estimated intangible amortization expense:		
For the remaining three months of Fiscal 2004		\$ 2,664
For year ended January 31, 2005		9,216
For year ended January 31, 2006		7,748
For year ended January 31, 2007		4,398
For year ended January 31, 2008		1,626
Thereafter		
		<u> </u>
Total		\$ 25,652
		<u> </u>

The weighted average remaining amortization period for acquired technology is 37 months, trademark/trade name portfolio and customer relationships is 31 months, non-compete agreements is 19 months, and maintenance service contracts is 7 months. The total weighted average remaining amortization period for all intangible assets is 35 months. The aggregate amortization expense of intangible assets was \$2.7 million and \$5.9 million for the three and nine months ended October 31, 2003, respectively, and \$1.1 million and \$3.4 million for the same periods a

year ago.

The changes in the net carrying amount of goodwill for the nine months ended October 31, 2003 are as follows (in thousands):

Balance as of January 31, 2003	\$ 28,877
Activity during the first nine months of fiscal 2004:	
Goodwill acquired in TeamShare acquisition	7,103
Impairment losses recognized	
	<hr/>
Balance as of October 31, 2003	\$ 35,980
	<hr/>

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SERENA SOFTWARE, INC.

6.0x	5.5x	6.5x	Junior secured loans	18,572	Discounted cash flow EBITDA				
multiples	7.5x	3.5x	9.5x	Market yields	11.5%	7.0%	13.5%	Junior secured loans	— Enterprise
								value Revenue	multiples
									0.6x
									0.5x
									0.6x
									Equity securities
									8,121
									Discounted cash flow EBITDA
									multiples
									3.8x
									3.5x
									4.0x
									Market yields
									17.0%
									16.0%
									18.0%
									Equity securities
									18,164
									Enterprise
									value EBITDA
									multiples
									4.6x
									3.3x
									13.3x
									Equity securities
									249
									Enterprise value Revenue
									multiples
									0.8x
									0.1x
									3.8x
									Total Level 3 Assets
									\$324,792⁽¹⁾
									Liabilities:
									Secured
									Borrowings
									\$1,314
									Discounted cash flow
									Market yields
									7.7%
									7.1%
									8.2%

(1) Excludes loans of \$88,128 at fair value where valuation (unadjusted) is obtained from a third-party pricing service for which such disclosure is not required.

The significant unobservable inputs used in the market approach of fair value measurement of the Company's investments are the market multiples of EBITDA or revenue of the comparable guideline public companies. The Company selects a population of public companies for each investment with similar operations and attributes of the portfolio company. Using these guideline public companies' data, a range of multiples of enterprise value to EBITDA is calculated. The Company selects percentages from the range of multiples for purposes of determining the portfolio company's estimated enterprise value based on said multiple and generally the latest twelve months EBITDA of the portfolio company (or other meaningful measure). Increases (decreases) in the multiple will result in an increase (decrease) in enterprise value, resulting in an increase (decrease) in the fair value estimate of the investment.

The significant unobservable inputs used in the yield approach of fair value measurement of the Company's investments is the discount rate used to discount the estimated future cash flows expected to be received from the underlying investment, which include both future principal and interest payments. Increases (decreases) in the discount rate would result in a decrease (increase) in the fair value estimate of the investment. Included in the consideration and selection of discount rates are the following factors: risk of default, rating of the investment and comparable investments, and call provisions.

Other Financial Assets and Liabilities

ASC Topic 820 requires disclosure of the fair value of financial instruments for which it is practical to estimate such value. The Company believes that the carrying amounts of its other financial instruments such as cash, receivables and payables approximate the fair value of such items due to the short maturity of such instruments. Fair value of the Company's revolving credit facility is estimated by discounting remaining payments using applicable market rates or market quotes for similar instruments at the measurement date, if applicable. The Company believes that the carrying value of its revolving credit facility approximates fair value. SBA-guaranteed debentures are carried at cost and with their longer maturity dates, fair value is estimated by discounting remaining payments using current market rates for similar instruments and considering such factors as the legal maturity date and the ability of market participants to prepay the debentures. As of June 30, 2017 and December 31, 2016, the fair value of the Company's SBA debentures using Level 3 inputs were estimated at \$85,600 and \$51,500, respectively, which is the same as the Company's carrying value of the SBA debentures.

Note 5. Transactions with Affiliated Companies

An affiliated company is a company in which the Company has ownership of 5% or more of its voting securities. A controlled affiliate company is a company in which the Company has ownership of more than 25% of its voting securities. Transactions related to the Company's investments with affiliates for the six months ended June 30, 2017 and 2016 were as follows:

Portfolio Company	Fair value at December 31, 2016	Purchases (cost)	Sales and paydowns (cost)	PIK interest (cost)	Discount accretion	Net realized gains (losses)	Net unrealized gains (losses)	Fair value at June 30, 2017
Non-controlled affiliate company investments ⁽¹⁾ :								
American Community Homes, Inc.	\$ 13,950	\$ 647	\$ —	\$ 111	\$ 33	\$ —	\$ (166)	\$ 14,575
Rockdale Blackhawk, LLC	27,077	925	(16)	—	96	—	(8,379)	19,703
Rocket Dog Brands, LLC	1,054	—	—	130	(1)	—	(764)	419
SHI Holdings, Inc.	4,297	723	—	—	10	—	110	5,140
Summit Container Corporation	3,663	—	(102)	37	12	—	(157)	3,453
Total non-controlled affiliate company investments	\$ 50,041	\$ 2,295	\$ (118)	\$ 278	\$ 150	\$ —	\$ (9,356)	\$ 43,290
Controlled affiliate company investments ⁽¹⁾ :								
TPP Acquisition, Inc. ⁽²⁾	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
TPP Operating, Inc. ⁽²⁾	8,899	2,807	—	—	—	—	(2,234)	9,472
Total controlled affiliate company investments	\$ 8,899	\$ 2,807	\$ —	\$ —	\$ —	\$ —	\$ (2,234)	\$ 9,472

Portfolio Company	Fair value at December 31, 2015	Purchases (cost)	Sales and paydowns (cost)	PIK interest (cost)	Discount accretion	Net realized gains (losses)	Net unrealized gains (losses)	Fair value at June 30, 2016
Non-controlled affiliate company investments ⁽¹⁾ :								
American Community Homes, Inc.	\$ 11,692	\$ 488	\$ —	\$ 99	\$ 29	\$ —	\$ 997	\$ 13,305
Rockdale Blackhawk, LLC	21,903	—	(1,412)	—	92	—	3,038	23,621
Rocket Dog Brands, LLC	1,752	384	—	168	5	—	(961)	1,348
Summit Container Corporation	3,400	137	(95)	29	13	—	122	3,606
Total non-controlled affiliate company investments	\$ 38,747	\$ 1,009	\$ (1,507)	\$ 296	\$ 139	\$ —	\$ 3,196	\$ 41,880
Controlled affiliate company investments ⁽¹⁾ :								
TPP Acquisition, Inc.	\$ 6,525	\$ 1,900	\$ —	\$ —	\$ —	\$ —	\$ (1,075)	\$ 7,350
Total controlled affiliate company investments	\$ 6,525	\$ 1,900	\$ —	\$ —	\$ —	\$ —	\$ (1,075)	\$ 7,350

Portfolio Company	For the six months ended June 30,					
	2017			2016		
	Interest income	Dividend income	Fee income	Interest income	Dividend income	Fee income
Non-controlled affiliate company investments ⁽¹⁾						
American Community Homes, Inc.	\$744	\$ —	\$ —	\$705	\$ —	\$ —
Rockdale Blackhawk, LLC	889	—	—	925	2,413	—
Rocket Dog Brands, LLC	126	—	—	231	—	—
SHI Holdings, Inc.	232	—	—	—	—	—
Summit Container Corporation	316	—	—	304	—	—
Total non-controlled affiliate company investments	\$2,307	\$ —	\$ —	\$2,165	\$ 2,413	\$ —
Controlled affiliate company investments ⁽¹⁾ :						
TPP Acquisition, Inc.	\$—	\$ —	\$ —	\$10	\$ —	\$ —
TPP Operating, Inc.	394	—	—	—	—	—
Total controlled affiliate company investments	\$394	\$ —	\$ —	\$10	\$ —	\$ —

(1) Includes both loan and equity security investment transactions for these portfolio companies.

On September 2, 2016 TPP Acquisition, Inc. filed for bankruptcy as part of a restructuring process. The existing lenders, including the Company submitted a credit bid to purchase certain assets of TPP Acquisition, Inc., which was approved by the bankruptcy court and the sale closed on November 8, 2016. A new operating company, TPP Operating, Inc., was formed to acquire certain of the assets of TPP Acquisition, Inc. and continue business operations. These new operations are no longer encumbered by significant lease liabilities. The Company owns 40% of the equity interests in both the former operating company, TPP Acquisition, Inc. (which is in wind-down) and the new operating company, TPP Operating, Inc. During the bankruptcy period, the Company and the other existing lenders provided additional financing through a debtor-in-possession financing (“DIP”) facility. Upon the purchase of TPP Acquisition, Inc.’s assets, TPP Operating, Inc. entered into a new credit facility with the existing lenders, including the Company. The principal amount of the new facility with TPP Operating, Inc. represented the amount owed to the lenders under the pre-petition facilities plus the amount funded under the DIP facility, less the amount of the credit bid. The cost basis of the Company’s equity investment in TPP Operating, Inc. represents the credit bid and equates to the reduction of principal outstanding on the debt facilities when the new facility was issued to TPP Operating, Inc. As of June 30, 2017, the Company valued its positions in TPP Operating, Inc. utilizing an enterprise value waterfall model. The key inputs to the model were an estimated 2017 revenue forecast and revenue multiple developed using comparable public and private company data.

Note 6. Transactions with Related Parties

The Company has entered into an Investment Advisory and Management Agreement with MC Advisors, under which MC Advisors, subject to the overall supervision of the Board, provides investment advisory services to the Company. The Company pays MC Advisors a fee for its services under the Investment Advisory and Management Agreement

consisting of two components—a base management fee and an incentive fee. The base management fee is calculated at an annual rate equal to 1.75% of invested assets (calculated as total assets excluding cash) and is payable in arrears. Base management fees for the three and six months ended June 30, 2017 was \$1,903 and \$3,708, respectively. Base management fees for the three and six months ended June 30, 2016 were \$1,504 and \$3,004, respectively.

The incentive fee consists of two parts. The first part is calculated and payable quarterly in arrears and equals 20% of “pre-incentive fee net investment income” for the immediately preceding quarter, subject to a 2% (8% annualized) preferred return, or “hurdle,” and a “catch up” feature. The foregoing incentive fee is subject to a total return requirement, which provides that no incentive fee in respect of preincentive fee net investment income will be payable except to the extent that 20% of the cumulative net increase in net assets resulting from operations over the then current and 11 preceding calendar quarters exceeds the cumulative incentive fees accrued and/or paid for the 11 preceding calendar quarters. Therefore, any ordinary income incentive fee that is payable in a calendar quarter will be limited to the lesser of (1) 20% of the amount by which preincentive fee net investment income for such calendar quarter exceeds the 2% hurdle, subject to the “catch-up” provision, and (2) (x) 20% of the cumulative net increase in net assets resulting from operations for the then current and 11 preceding calendar quarters minus (y) the cumulative incentive fees accrued and/or paid for the 11 preceding calendar quarters. For the foregoing purpose, the “cumulative net increase in net assets resulting from operations” is the sum of preincentive fee net investment income, realized gains and losses and unrealized gains and losses for the then current and 11 preceding calendar quarters. The second part of the incentive fee is determined and payable in arrears as of the end of each fiscal year in an amount equal to 20% of realized capital gains, if any, on a cumulative basis from inception through the end of the year, computed net of all realized capital losses on a cumulative basis and unrealized depreciation, less the aggregate amount of any previously paid capital gain incentive fees.

Incentive fees, excluding the impact of the incentive fee waiver, for the three and six months ended June 30, 2017 were \$1,460 and \$2,750, respectively. Incentive fees for the three months ended June 30, 2017 consisted solely of part one incentive fees (based on net investment income) of \$1,460. Incentive fees for the six months ended June 30, 2017, consisted of part one incentive fees of \$2,925 and part two incentive fees (based upon net realized and unrealized gains and losses, or capital gains) of (\$175). Part two incentive fees reduced total incentive fees for the six months ended June 30, 2017, primarily as a result of net unrealized losses during the period. Incentive fees for the three and six months ended June 30, 2016 were \$1,319 and \$3,059, respectively. Incentive fees for the three months ended June 30, 2016, consisted of part one incentive fees of \$1,416 and part two incentive fees of (\$97). Part two incentive fees reduced the total incentive fees for the three months ended June 30, 2016, primarily as a result of net unrealized losses during the period. Incentive fees for the six months ended June 30, 2016, consisted of part one incentive fees of \$2,921 and part two incentive fees of \$138. The Company accrues, but does not pay, a capital gains incentive fee in connection with any unrealized capital appreciation, as appropriate. If, on a cumulative basis, the sum of net realized gain (loss) plus net unrealized gain (loss) during a period, the Company will reverse any excess capital gains incentive fee previously accrued such that the amount of capital gains incentive fee accrued is no more than 20% of the sum of net realized gain (loss) plus net unrealized gain (loss). For the three and six months ended June 30, 2017, MC Advisors waived part one incentive fees of \$250 and \$250, respectively. For the three and six months ended June 30, 2016 no incentive fees were waived.

The Company has entered into an Administration Agreement with Monroe Capital Management Advisors, LLC (“MC Management”), under which the Company reimburses MC Management (subject to the review and approval of the Board) for its allocable portion of overhead and other expenses, including the costs of furnishing the Company with office facilities and equipment and providing clerical, bookkeeping, record-keeping and other administrative services at such facilities, and the Company’s allocable portion of the cost of the chief financial officer and chief compliance officer and their respective staffs. To the extent that MC Management outsources any of its functions, the Company will pay the fees associated with such functions on a direct basis, without incremental profit to MC Management. For the three and six months ended June 30, 2017, the Company incurred \$846 and \$1,676, respectively, in administrative expenses (included within Professional fees, Administrative service fees and General and administrative expenses on the consolidated statements of operations) under the Administration Agreement, of which \$301 and \$631, respectively, was related to MC Management overhead and salary allocation and paid directly to MC Management. For the three and six months ended June 30, 2016, the Company incurred \$724 and \$1,423, respectively, in administrative expenses (included within Professional fees, Administrative service fees and General and administrative expenses on the consolidated statements of operations) under the Administration Agreement, of which \$304 and \$632, respectively, was related to MC Management overhead and salary allocation and paid directly to MC Management. As of June 30, 2017 and December 31, 2016, \$293 and \$330, respectively, of expenses were due to MC Management under this agreement and are included in accounts payable and accrued expenses on the consolidated statements of assets and liabilities.

The Company has entered into a license agreement with Monroe Capital LLC under which Monroe Capital LLC has agreed to grant the Company a non-exclusive, royalty-free license to use the name “Monroe Capital” for specified purposes in its business. Under this agreement, the Company will have a right to use the “Monroe Capital” name at no cost, subject to certain conditions, for so long as the Advisor or one of its affiliates remains its investment advisor. Other than with respect to this limited license, the Company has no legal right to the “Monroe Capital” name.

As of June 30, 2017 and December 31, 2016, the Company had accounts payable to members of the Board of zero and zero, respectively, representing accrued and unpaid fees for their services.

Note 7. Borrowings

Revolving Credit Facility: As of June 30, 2017, the Company had U.S. dollar borrowings of \$91,500 and non-U.S. dollar borrowings denominated in Great Britain pounds of £1,800 (\$2,345 in U.S. dollars) under its revolving credit facility with ING Capital LLC, as agent, to finance the purchase of the Company's assets. The borrowings denominated in Great Britain pounds are translated into U.S. dollars based on the spot rate at each balance sheet date. The impact resulting from changes in foreign currency borrowings is included in change in unrealized gain (loss) on foreign currency borrowings in the Company's consolidated statements of operations. The borrowings denominated in Great Britain pounds may be positively or negatively affected by movements in the rate of exchange between the U.S. dollar and the Great Britain pound. This movement is beyond the control of the Company and cannot be predicted. As of December 31, 2016, the Company had U.S. dollar borrowings of \$129,000 outstanding under the revolving credit facility. As of June 30, 2017, the maximum amount the Company was able to borrow was \$200,000 and this borrowing can be increased to \$300,000 pursuant to an accordion feature (subject to maintaining 200% asset coverage, as defined by the 1940 Act). On February 22, 2017, the Company closed a \$40,000 upside to the revolving credit facility, bringing the maximum amount the Company is able to borrow from \$160,000 to the now current maximum amount of \$200,000, in accordance with the facility's accordion feature. The maturity date on the facility is December 14, 2020.

The revolving credit facility is secured by a lien on all of the Company's assets, including cash on hand, but excluding the assets of the Company's wholly-owned subsidiary, MRCC SBIC. The Company's ability to borrow under the revolving credit facility is subject to availability under a defined borrowing base, which varies based on portfolio characteristics and certain eligibility criteria and concentration limits, as well as required valuation methodologies. The Company may make draws under the revolving credit facility to make or purchase additional investments through December 2019 and for general working capital purposes until the maturity date of the revolving credit facility. Borrowings under the revolving credit facility bear interest, at the Company's election, at an annual rate of LIBOR (one-month, two-month, three-month or six-month at our discretion based on the term of the borrowing) plus 2.75% or at a daily rate equal to 2.00% per annum plus the greater of the prime interest rate, the federal funds rate plus 0.5% or LIBOR plus 1.0%. The LIBOR rate on the revolving credit facility was reduced to LIBOR plus 2.75% from LIBOR plus 3.00% in conjunction with the Company's capital raise on June 9, 2017, as net worth (excluding investments in MRCC SBIC) exceeded \$225,000. In addition to the stated interest rate on borrowings under the revolving credit facility, the Company is required to pay a fee of 0.5% per annum on any unused portion of the revolving credit facility if the unused portion of the facility is less than 65% of the then available maximum borrowing or a fee of 1.0% per annum on any unused portion of the revolving credit facility if the unused portion of the facility is greater than or equal to 65% of the then available maximum borrowing. As of June 30, 2017 and December 31, 2016, the outstanding borrowings were accruing at a weighted average interest rate of 4.1% and 3.8%, respectively. The weighted average interest rate of the revolving credit facility borrowings (excluding debt issuance costs) for the three and six months ended June 30, 2017 was 4.0% and 4.1%, respectively. The weighted average fee rate on the unused portion of the revolving credit facility for the three and six months ended June 30, 2017 was 0.5% and 0.5%, respectively. The weighted average interest rate of the revolving credit facility borrowings (excluding debt issuance costs) for the three and six months ended June 30, 2016 was 3.6% and 3.5%, respectively. The weighted average fee rate on the unused

portion of the revolving credit facility for the three and six months ended June 30, 2016 was 0.5% and 0.5%, respectively.

The Company's ability to borrow under the revolving credit facility is subject to availability under the borrowing base, which permits the Company to borrow up to 70% of the fair market value of its portfolio company investments depending on the type of the investment the Company holds and whether the investment is quoted. The Company's ability to borrow is also subject to certain concentration limits, and continued compliance with the representations, warranties and covenants given by the Company under the facility. The revolving credit facility contains certain financial and restrictive covenants, including, but not limited to, the Company's maintenance of: (1) a minimum consolidated total net assets at least equal to the greater of (a) 40% of the consolidated total assets on the last day of each quarter or (b) \$120,000 plus 65% of the net proceeds to the Company from sales of its securities after December 14, 2015; (2) a ratio of total assets (less total liabilities other than indebtedness) to total indebtedness of not less than 2.1 times; and (3) a ratio of earnings before interest and taxes to interest expense of at least 2.5 times. The credit facility also requires the Company to undertake customary indemnification obligations with respect to ING Capital LLC and other members of the lending group and to reimburse the lenders for expenses associated with entering into the credit facility. The revolving credit facility also has customary provisions regarding events of default, including events of default for nonpayment, change in control transactions at both Monroe Capital Corporation and MC Advisors, failure to comply with financial and negative covenants, and failure to maintain our relationship with MC Advisors. If the Company incurs an event of default under the revolving credit facility and fails to remedy such default under any applicable grace period, if any, then the entire revolving credit facility could become immediately due and payable, which would materially and adversely affect the Company's liquidity, financial condition, results of operations and cash flows.

The Company's revolving credit facility also imposes certain conditions that may limit the amount of the Company's distributions to stockholders. Distributions payable in the Company's common stock under the DRIP are not limited by the revolving credit facility. Distributions in cash or property other than common stock are generally limited to 115% of the amount of distributions required to maintain the Company's status as a RIC.

SBA Debentures: On February 28, 2014, the Company's wholly-owned subsidiary, MRCC SBIC received a license from the SBA to operate as a SBIC under Section 301(c) of the Small Business Investment Act of 1958, as amended. MRCC SBIC commenced operations on September 16, 2013.

The SBIC license allows MRCC SBIC to obtain leverage by issuing SBA-guaranteed debentures, subject to the issuance of a leverage commitment by the SBA and other customary procedures. SBA-guaranteed debentures are non-recourse, interest only debentures with interest payable semi-annually and have a ten year maturity. The principal amount of SBA-guaranteed debentures is not required to be paid prior to maturity but may be prepaid at any time without penalty. The interest rate of SBA-guaranteed debentures is fixed on a semi-annual basis (pooling date) at a market-driven spread over U.S. Treasury Notes with 10-year maturities. The SBA, as a creditor, has a superior claim to MRCC SBIC's assets over the Company's stockholders in the event the Company liquidates MRCC SBIC or the SBA exercises its remedies upon an event of default.

SBA regulations currently limit the amount that an individual SBIC may borrow to a maximum of \$150,000 when it has at least \$75,000 in regulatory capital, receives a leverage commitment from the SBA and has been through an audit examination by the SBA subsequent to licensing. The SBA also historically limited a related group of SBICs (commonly referred to as a “family of funds”) to a maximum of \$225,000 in total borrowings. On December 18, 2015, this family of funds limitation was raised to \$350,000 in total borrowings. As the Company has other affiliated SBICs already in operation, MRCC SBIC was historically limited to a maximum of \$40,000 in borrowings. Pursuant to the increase in the family of funds limitation, the Company submitted a commitment application to the SBA and on April 13, 2016, MRCC SBIC was approved by the SBA for an additional \$75,000 in SBA-guaranteed debentures, for a total of \$115,000 in available debentures.

As of June 30, 2017, MRCC SBIC had \$57,624 in leverageable capital and \$85,600 in SBA-guaranteed debentures outstanding. As of December 31, 2016, MRCC SBIC had \$41,000 in leverageable capital and \$51,500 in SBA-guaranteed debentures outstanding. As of June 30, 2017, the Company has made all required leverageable capital contributions to MRCC SBIC in order to access the remaining \$29,400 in available SBA-guaranteed debentures.

As of June 30, 2017, MRCC SBIC had the following SBA-guaranteed debentures outstanding (dollars in thousands):

Maturity Date	Interest Rate	Amount
September 2024	3.4 %	\$ 12,920
March 2025	3.3 %	14,800
March 2025	2.9 %	7,080
September 2025	3.6 %	5,200
March 2027	3.5 %	20,000
September 2027	2.2 % ⁽¹⁾	25,600
Total		\$85,600

(1) Represents an interim rate of interest as the SBA-guaranteed debentures had not yet pooled.

As of December 31, 2016, MRCC SBIC had the following SBA-guaranteed debentures outstanding (dollars in thousands):

Maturity Date	Interest Rate		Amount
September 2024	3.4	%	\$12,920
March 2025	3.3	%	14,800
March 2025	2.9	%	7,080
September 2025	3.6	%	5,200
March 2027	2.1	% ⁽¹⁾	9,200
March 2027	2.0	% ⁽¹⁾	2,300
Total			\$51,500

(1) Represents an interim rate of interest as the SBA-guaranteed debentures had not yet pooled.

On October 2, 2014, the Company was granted exemptive relief from the SEC for permission to exclude the debt of MRCC SBIC guaranteed by the SBA from the 200% asset coverage test under the 1940 Act. The receipt of this exemption for this SBA-guaranteed debt increases flexibility under the 200% asset coverage test.

Secured Borrowings: Certain partial loan sales do not qualify for sale accounting under ASC Topic 860 because these sales do not meet the definition of a “participating interest,” as defined in the guidance, in order for sale treatment to be allowed. Participations or other partial loan sales which do not meet the definition of a participating interest remain as an investment on the accompanying consolidated statements of assets and liabilities and the portion sold is recorded as a secured borrowing in the liabilities section of the consolidated statements of assets and liabilities. For these partial loan sales, the interest earned on the entire loan balance is recorded within “interest income” and the interest earned by the buyer in the partial loan sale is recorded within “interest and other debt financing expenses” in the accompanying consolidated statements of operations.

As of June 30, 2017, there were no secured borrowings. As of December 31, 2016, secured borrowings at fair value totaled \$1,314 and the fair value of the loans that are associated with these secured borrowings was \$5,814. These secured borrowings were created as a result of the Company’s completion of partial loan sales of certain unitranche loan assets during the year ended December 31, 2013 that did not meet the definition of a “participating interest.” As a result, sale treatment was not allowed and these partial loan sales were treated as secured borrowings. No such partial loan sales occurred during the year ended December 31, 2016 and the six months ended June 30, 2017. During the three and six months ended June 30, 2017, repayments on secured borrowings totaled \$1,254 and \$1,254, respectively. During the three and six months ended June 30, 2016 repayments on secured borrowings totaled \$77 and \$277, respectively. The weighted average interest rate on the Company’s secured borrowings was approximately zero and

6.3% as of June 30, 2017 and December 31, 2016, respectively.

Components of interest expense: The components of the Company's interest expense and other debt financing expenses are as follows:

	Three months ended June 30,	
	2017	2016
Interest expense – revolving credit facility	\$1,385	\$1,188
Interest expense – SBA debentures	518	326
Amortization of deferred financing costs	255	199
Interest expense – secured borrowings	13	35
Other	13	25
Total interest and other debt financing expenses	\$2,184	\$1,773

	Six months ended June 30,	
	2017	2016
Interest expense – revolving credit facility	\$2,730	\$2,316
Interest expense – SBA debentures	924	652
Amortization of deferred financing costs	486	381
Interest expense – secured borrowings	34	72
Other	20	43
Total interest and other debt financing expenses	\$4,194	\$3,464

Note 8. Distributions

The Company's distributions are recorded on the record date. The following table summarizes distributions declared during the six months ended June 30, 2017 and 2016:

Date Declared	Record Date	Payment Date	Amount Per Share	Cash Distribution	DRIP Shares Issued	DRIP Shares Value	DRIP Shares Repurchased in the Open Market	Cost of DRIP Shares Repurchased
Six months ended June 30, 2017:								
March 7, 2017	March 17, 2017	March 31, 2017	\$ 0.35	\$ 5,549	16,217	\$ 254	—	\$ —
May 31, 2017	June 15, 2017	June 30, 2017	0.35	6,807	17,932	271	—	—
Total distributions declared			\$ 0.70	\$ 12,356	34,149	\$ 525	—	\$ —
Six months ended June 30, 2016:								
March 4, 2016	March 15, 2016	March 31, 2016	\$ 0.35	\$ 4,553	—	\$ —	20,144	\$ 277
June 1, 2016	June 15, 2016	June 30, 2016	0.35	4,553	—	\$ —	18,518	275
Total distributions declared			\$ 0.70	\$ 9,106	—	\$ —	38,662	\$ 552

Note 9. Stock Activity

Stock Issuances: On July 1, 2016, the Company amended the ATM securities offering program with MLV & Co, LLC (“MLV”) and JMP Securities LLC to replace MLV with FBR Capital Markets & Co. (“FBR”), an affiliate of MLV (the “Prior ATM Program”). On May 12, 2017, the Company entered into new equity distribution agreements with each FBR and JMP that reference the Company's current registration statement (the “ATM Program”). All other material terms of the Prior ATM Program remain unchanged under the ATM Program. During the six months ended June 30, 2017, the Company sold 173,939 shares at an average price of \$15.71 per share for gross proceeds of \$2,732 under the Prior ATM Program and no shares were sold under the ATM Program. Aggregate underwriters' discounts and commissions were \$41 and offering costs were \$23, resulting in net proceeds of approximately \$2,668. There were no stock issuances during the six months ended June 30, 2016.

On June 9, 2017, the Company closed a public offering of 3,000,000 shares of its common stock at a public offering price of \$15.00 per share, raising approximately \$45,000 in gross proceeds. On June 14, 2017, pursuant to the underwriters' exercise of the over-allotment option, the Company sold an additional 450,000 shares of its common stock, at a public offering price of \$15.00 per share, and additional \$6,750 in gross proceeds for a total of \$51,750. Aggregate underwriters' discounts and commissions were \$2,070 and offering costs were \$127, resulting in net

proceeds of approximately \$49,553.

Note 10. Commitments and Contingencies

Commitments: As of June 30, 2017 and December 31, 2016, the Company had \$37,419 and \$37,716, respectively, in outstanding commitments to fund investments under undrawn revolvers, capital expenditure loans and delayed draw commitments.

Indemnifications: In the normal course of business, the Company enters into contracts and agreements that contain a variety of representations and warranties that provide general indemnifications. The Company's maximum exposure under these agreements is unknown, as these involve future claims that may be made against the Company but that have not occurred. The Company expects the risk of any future obligations under these indemnifications to be remote.

Concentration of credit and counterparty risk: Credit risk arises primarily from the potential inability of counterparties to perform in accordance with the terms of the contract. In the event that the counterparties do not fulfill their obligations, the Company may be exposed to risk. The risk of default depends on the creditworthiness of the counterparties or issuers of the instruments. It is the Company's policy to review, as necessary, the credit standing of each counterparty.

Market risk: The Company's investments and borrowings are subject to market risk. Market risk is the potential for changes in the value due to market changes. Market risk is directly impacted by the volatility and liquidity in the markets in which the investments and borrowings are traded.

Legal proceedings: In the normal course of business, the Company may be subject to legal and regulatory proceedings that are generally incidental to its ongoing operations. While there can be no assurance of the ultimate disposition of any such proceedings, the Company is not currently aware of any such proceedings or disposition that would have a material adverse effect on the Company's consolidated financial statements.

Note 11. Financial Highlights

The following is a schedule of financial highlights for the six months ended June 30, 2017 and 2016:

	June 30, 2017	June 30, 2016	
Per share data:			
Net asset value at beginning of period	\$ 14.52	\$ 14.19	
Net investment income ⁽¹⁾	0.71	0.89	
Net gain (loss) on investments, secured borrowings and foreign currency borrowings ⁽¹⁾	(0.50))	0.13
Net increase in net assets from operations ⁽¹⁾	0.21	1.02	
Stockholder distributions ⁽²⁾	(0.70))	(0.70)
Effect of share issuances above (below) NAV ⁽³⁾	0.02	(0.01)	
Net asset value at end of period	\$ 14.05	\$ 14.50	
Net assets at end of period	\$ 284,308	\$ 188,650	
Shares outstanding at end of period	20,239,957	13,008,007	
Per share market value at end of period	\$ 15.23	\$ 14.83	
Total return based on market value ⁽⁴⁾	3.58	%	18.92
Total return based on average net asset value ⁽⁵⁾	1.41	%	7.07
Ratio/Supplemental data:			
Ratio of net investment income to average net assets ⁽⁶⁾	10.59	%	14.07
Ratio of total expenses to average net assets ^{(6) (7)}	8.62	%	10.30
Average debt outstanding	\$ 184,799	\$ 164,917	
Average debt outstanding per share	\$ 10.88	\$ 12.68	
Portfolio turnover ⁽⁸⁾	17.73	%	13.41

(1) Calculated using the weighted average shares outstanding during the period.

(2) Management monitors available taxable earnings, including net investment income and realized capital gains, to determine if a tax return of capital may occur for the year. To the extent the Company's taxable earnings fall below the total amount of the Company's distributions for that fiscal year, a portion of those distributions may be deemed a tax return of capital to the Company's stockholders. The tax character of distributions will be determined at the end of the fiscal year. However, if the character of such distributions were determined as of June 30, 2017 and 2016, none of the distributions would have been characterized as a tax return of capital to the Company's stockholders; this tax return of capital may differ from the return of capital calculated with reference to net investment income for financial reporting purposes.

(3) Includes the impact of different share amounts used in calculating per share data as a result of calculating certain per share data based on weighted average shares outstanding during the period and certain per share data based on shares outstanding as of a period end or transaction date.

(4) Total return based on market value is calculated assuming a purchase of common shares at the market value on the first day and a sale at the market value on the last day of the periods reported. Distributions, if any, are assumed for purposes of this calculation to be reinvested at prices obtained under the Company's DRIP. Total return based on market value does not reflect brokerage commissions. Return calculations are not annualized.

(5) Total return based on average net asset value is calculated by dividing the net increase in net assets from operations by the average net asset value. Return calculations are not annualized.

(6) Ratios are annualized. Incentive fees included within the ratio are not annualized.

(7) The following is a schedule of supplemental ratios for the six months ended June 30, 2017 and 2016. These ratios have been annualized unless otherwise noted.

	June 30, 2017		June 30, 2016	
Ratio of interest and other debt financing expenses to average net assets	3.32	%	3.72	%
Ratio of total expenses (without incentive fees) to average net assets	7.64	%	8.66	%
Ratio of incentive fees, net of incentive fee waiver, to average net assets (not annualized) ⁽⁹⁾	0.98	%	1.64	%

(8) Ratios are not annualized.

(9) The ratio of waived incentive fees to average net assets was 0.10% and zero for six months ended June 30, 2017 and 2016, respectively.

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

Except as otherwise specified, references to "we," "us" and "our" refer to Monroe Capital Corporation and its consolidated subsidiaries. The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes appearing in our annual report on Form 10-K (the "Annual Report") for the year ended December 31, 2016, filed with the U.S. Securities and Exchange Commission ("SEC") on March 7, 2017. The information contained in this section should also be read in conjunction with our unaudited consolidated financial statements and related notes and other financial information appearing elsewhere in this quarterly report on Form 10-Q (the "Quarterly Report").

FORWARD-LOOKING STATEMENTS

This Quarterly Report, including Management's Discussion and Analysis of Financial Condition and Results of Operations, contains statements that constitute forward-looking statements, which relate to future events or our future performance or future financial condition. These forward-looking statements are not historical facts, but rather are based on current expectations, estimates and projections about our company, our industry, our beliefs and our assumptions. The forward-looking statements contained in this Quarterly Report involve risks and uncertainties, including statements as to:

- our future operating results;
- our business prospects and the prospects of our prospective portfolio companies;
- the dependence of our future success on the general economy and its impact on the industries in which we invest;
- the impact of a protracted decline in the liquidity of credit markets on our business;
- the impact of increased competition;
- the impact of fluctuations in interest rates on our business and our portfolio companies;
- our contractual arrangements and relationships with third parties;

- the valuation of our investments in portfolio companies, particularly those having no liquid trading market;

- the ability of our prospective portfolio companies to achieve their objectives;

- our expected financings and investments;

- the adequacy of our cash resources and working capital;

- the ability of our Monroe Capital BDC Advisors, LLC (“MC Advisors”) to locate suitable investments for us and to monitor our investments; and

- the impact of future legislation and regulation on our business and our portfolio companies.

We use words such as “anticipates,” “believes,” “expects,” “intends,” “seeks,” “plans,” “estimates,” “targets,” “expects” and similar expressions to identify forward-looking statements. The forward looking statements contained in this Quarterly Report involve risks and uncertainties. Our actual results could differ materially from those implied or expressed in the forward-looking statements for any reason, including the factors set forth in “*Part I—Item 1A. Risk Factors*” in our Annual Report and “*Part II—Item 1A. Risk Factors*” in this Quarterly Report.

Although we believe that the assumptions on which these forward-looking statements are based are reasonable, any of those assumptions could prove to be inaccurate, and as a result, the forward-looking statements based on those assumptions also could be inaccurate. Important assumptions include our ability to originate new loans and investments, certain margins and levels of profitability and the availability of additional capital. In light of these and other uncertainties, the inclusion of a projection or forward-looking statement in this Quarterly Report should not be regarded as a representation by us that our plans and objectives will be achieved.

We have based the forward-looking statements included in this Quarterly Report on information available to us on the date of this Quarterly Report, and we assume no obligation to update any such forward-looking statements. Although we undertake no obligation to revise or update any forward-looking statements in this Quarterly Report, whether as a result of new information, future events or otherwise, you are advised to consult any additional disclosures that we may make directly to you or through reports that we in the future may file with the SEC, including Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and current reports on Form 8-K.

Overview

Monroe Capital Corporation is an externally managed, closed-end, non-diversified management investment company that has elected to be treated as a business development company (“BDC”) under the Investment Company Act of 1940, as amended (the “1940 Act”). In addition, for tax purposes, we have elected to be treated as a regulated investment company (“RIC”) under the subchapter M of the Internal Revenue Code of 1986, as amended (the “Code”). We were incorporated under the Maryland General Corporation Law on February 9, 2011. We are a specialty finance company focused on providing financing solutions primarily to lower middle-market companies in the United States and Canada. We provide customized financing solutions focused primarily on senior secured, junior secured and unitranche (a combination of senior secured and junior secured debt in the same facility in which we syndicate a “first out” portion of the loan to an investor and retain a “last out” portion of the loan) debt and, to a lesser extent, unsecured subordinated debt and equity, including equity co-investments in preferred and common stock, and warrants.

Our shares are currently listed on the NASDAQ Global Select Market under the symbol “MRCC”.

Our investment objective is to maximize the total return to our stockholders in the form of current income and capital appreciation through investment in senior, unitranche and junior secured debt and, to a lesser extent, subordinated debt and equity investments. We seek to use our extensive leveraged finance origination infrastructure and broad expertise in sourcing loans to invest in primarily senior, unitranche and junior secured debt of middle-market companies. Our investments in senior, unitranche, junior secured debt and other investments generally will range between \$2.0 million and \$18.0 million each, although this investment size may vary proportionately with the size of our capital base. As of June 30, 2017, our portfolio included approximately 78.8% senior secured debt, 8.4% unitranche secured debt, 8.5% junior secured debt and 4.3% equity securities, compared to December 31, 2016, when our portfolio included

approximately 66.7% senior secured debt, 12.5% unitranche secured debt, 14.4% junior secured debt and 6.4% equity securities. We expect that the companies in which we invest may be leveraged, often as a result of leveraged buy-outs or other recapitalization transactions, and, in certain cases, will not be rated by national ratings agencies. If such companies were rated, we believe that they would typically receive a rating below investment grade (between BB and CCC under the Standard & Poor's system) from the national rating agencies.

While our primary focus is to maximize current income and capital appreciation through debt investments in thinly traded or private U.S. companies, we may invest a portion of the portfolio in opportunistic investments in order to seek to enhance returns to stockholders. Such investments may include investments in high-yield bonds, distressed debt, private equity or securities of public companies that are not thinly traded and securities of middle-market companies located outside of the United States. We expect that these public companies generally will have debt securities that are non-investment grade.

On February 28, 2014, our wholly-owned subsidiary, Monroe Capital Corporation SBIC, LP ("MRCC SBIC"), a Delaware limited partnership, received a license from the Small Business Administration ("SBA") to operate as a Small Business Investment Company ("SBIC") under Section 301(c) of the Small Business Investment Act of 1958. MRCC SBIC commenced operations on September 16, 2013. As of June 30, 2017, MRCC SBIC had \$57.6 million in leverageable capital and \$85.6 million in SBA-guaranteed debentures outstanding. See "*SBA Debentures*" below for more information.

On June 9, 2017, we closed a public offering of 3,000,000 shares of our common stock at a public offering price of \$15.00 per share, raising approximately \$45.0 million in gross proceeds. On June 14, 2017, pursuant to the underwriters' exercise of the over-allotment option, we sold an additional 450,000 shares of our common stock, at a public offering price of \$15.00 per share, and additional \$6.8 million in gross proceeds for a total of \$51.8 million. Aggregate underwriters' discounts and commissions were \$2.1 and offering costs were \$0.1 million, resulting in net proceeds of approximately \$49.6 million.

Investment income

We generate interest income on the debt investments in portfolio company investments that we originate or acquire. Our debt investments, whether in the form of senior, junior or unitranche secured debt, typically have an initial term of three to seven years and bear interest at a fixed or floating rate. In some instances we receive payments on our debt investment based on scheduled amortization of the outstanding balances. In addition, we receive repayments of some of our debt investments prior to their scheduled maturity date. In some cases, our investments provide for deferred interest of payment-in-kind ("PIK") interest. In addition, we may generate revenue in the form of commitment, origination, amendment, structuring or due diligence fees, fees for providing managerial assistance and consulting fees. Loan origination fees, original issue discount and market discount or premium are capitalized, and we accrete or amortize such amounts as interest income. We record prepayment premiums and prepayment gains (losses) on loans as interest income. As the frequency or volume of the repayments which trigger these prepayment premiums and prepayment gains (losses) may fluctuate significantly from period to period, the associated interest income recorded may also fluctuate significantly from period to period. Interest and fee income is recorded on the accrual basis to the

extent we expect to collect such amounts. In addition, we also generate dividend income on preferred equity securities, common equity securities and LLC interests in accordance with our revenue recognition policies.

Expenses

Our primary operating expenses include the payment of fees to MC Advisors under the Investment Advisory and Management Agreement (management and incentive fees), and the payment of fees to Monroe Capital Management Advisors, LLC (“MC Management”) for our allocable portion of overhead and other expenses under the Administration Agreement and other operating costs. See Note 6 to our consolidated financial statements and “*Related Party Transactions*” below for additional information on our Investment Advisory and Management Agreement and Administration agreement. Our expenses also include interest expense on our revolving credit facility, our SBA-guaranteed debentures and our secured borrowings. We bear all other out-of-pocket costs and expenses of our operations and transactions.

Net gain (loss) on investments, secured borrowings and foreign currency borrowings

We recognize realized gains or losses on investments based on the difference between the net proceeds from the disposition and the cost basis of the investment without regard to unrealized gains or losses previously recognized. We record current period changes in fair value of investments, secured borrowings, and foreign currency borrowings within net change in unrealized gain (loss) on investments, net change in unrealized gain (loss) on secured borrowings, and net change in unrealized gain (loss) on foreign currency borrowings, respectively, in the consolidated statements of operations.

Portfolio and Investment Activity

During the three months ended June 30, 2017, we invested \$62.4 million in eight new portfolio companies and \$11.0 million in 12 existing portfolio companies and had \$41.6 million in aggregate amount of sales and principal repayments, resulting in net investments of \$31.8 million for the period.

During the six months ended June 30, 2017, we invested \$89.7 million in 10 new portfolio companies and \$25.2 million in 18 existing portfolio companies and had \$75.5 million in aggregate amount of sales and principal repayments, resulting in net investments of \$39.4 million for the period.

During the three months ended June 30, 2016, we invested \$11.8 million in three new portfolio companies and \$7.8 million in eight existing portfolio companies and had \$20.6 million in aggregate amount of sales and principal repayments, resulting in net repayments of \$1.0 million for the period.

During the six months ended June 30, 2016, we invested \$16.7 million in four new portfolio companies and \$29.2 million in 15 existing portfolio companies and had \$47.4 million in aggregate amount of sales and principal repayments, resulting in net repayments of \$1.5 million for the period.

The following tables show the composition of the investment portfolio (in thousands) and associated yield data:

	June 30, 2017						
	Fair Value	Percentage		Weighted Average		Weighted Average	
	of			Annualized		Annualized	
	Total Portfolio			Contractual		Effective Yield	
				Coupon Yield	⁽¹⁾		⁽²⁾
Senior secured loans	\$351,491	78.8	%	9.4	%	9.4	%
Unitranche loans	37,302	8.4		10.4		11.5	
Junior secured loans	37,709	8.5		9.0		9.0	
Equity securities	19,047	4.3		10.8		10.8	
Total	\$445,549	100.0	%	9.4	%	9.6	%

	December 31, 2016						
	Fair Value	Percentage		Weighted Average		Weighted Average	
	of			Annualized		Annualized	
	Total Portfolio			Contractual		Effective Yield	
				Coupon Yield	⁽¹⁾		⁽²⁾
Senior secured loans	\$275,253	66.7	%	9.2	%	9.2	%
Unitranche loans	51,638	12.5		10.9		11.4	
Junior secured loans	59,366	14.4		9.7		9.7	
Equity securities	26,663	6.4		10.8		10.8	
Total	\$412,920	100.0	%	9.5	%	9.6	%

(1) The weighted average contractual coupon yield at period end is computed by dividing (a) the interest income on debt investments and preferred equity investments (with a stated coupon rate) at the period end contractual coupon rate for each investment by (b) the par value of our debt investment and the cost basis of our preferred equity investments.

(2) The weighted average annualized effective yield on portfolio investments at period end is computed by dividing (a) interest income on debt investments and preferred equity investments (with a stated coupon rate) at the period end effective rate for each investment by (b) the par value of our debt investments and the cost basis of our preferred equity investments. The weighted average annualized effective yield on portfolio investments is a metric on the investment portfolio alone and does not represent a return to stockholders. This metric is not inclusive of our fees and expenses, the impact of leverage on the portfolio or sales load that may be paid by investors.

The portfolio weighted average contractual coupon yield and weighted average effective yield decreased slightly during the three and six months ended June 30, 2017 as the portfolio mix continued to shift toward senior secured loans.

The following table shows the portfolio composition by industry grouping at fair value (dollars in thousands):

	June 30, 2017		December 31, 2016		
	Investments at Fair Value	Percentage of Total Portfolio	Investments at Fair Value	Percentage of Total Portfolio	
Aerospace & Defense	\$9,995	2.2	% \$ 10,601	2.6	%
Automotive	8,446	1.9	7,514	1.8	
Banking, Finance, Insurance & Real Estate	61,735	13.9	37,130	9.0	
Beverage, Food & Tobacco	17,517	4.0	16,794	4.1	
Chemicals, Plastics & Rubber	9,541	2.1	4,040	1.0	
Construction & Building	18,343	4.1	18,602	4.5	
Consumer Goods: Durable	—	—	3,620	0.9	
Consumer Goods: Non-Durable	19,735	4.4	32,000	7.7	
Containers, Packaging & Glass	3,453	0.8	3,663	0.9	
Energy: Oil & Gas	7,531	1.7	7,803	1.9	
Environmental Industries	3,696	0.8	3,768	0.9	
Healthcare & Pharmaceuticals	56,472	12.7	56,435	13.7	
High Tech Industries	36,888	8.3	18,899	4.6	
Hotels, Gaming & Leisure	36,977	8.3	38,010	9.2	

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Media: Advertising, Printing & Publishing	20,435	4.6	11,742	2.8	
Media: Broadcasting & Subscription	17,165	3.9	18,046	4.4	
Media: Diversified & Production	4,994	1.1	4,938	1.2	
Metals & Mining	5,392	1.2	5,268	1.3	
Retail	37,763	8.5	38,147	9.2	
Services: Business	23,823	5.3	40,164	9.7	
Services: Consumer	21,282	4.8	24,807	6.0	
Telecommunications	3,514	0.8	3,430	0.8	
Utilities: Electric	2,835	0.6	2,999	0.7	
Wholesale	18,017	4.0	4,500	1.1	
Total	\$445,549	100.0	% \$412,920	100.0	%

Portfolio Asset Quality

MC Advisors’ portfolio management staff closely monitors all credits, with senior portfolio managers covering agented and more complex investments. MC Advisors segregates our capital markets investments by industry. The MC Advisors’ monitoring process and projections developed by Monroe Capital both have daily, weekly, monthly and quarterly components and related reports, each to evaluate performance against historical, budget and underwriting expectations. MC Advisors’ analysts will monitor performance using standard industry software tools to provide consistent disclosure of performance. MC Advisors also monitors our investment exposure using a proprietary trend analysis tool. When necessary, MC Advisors will update our internal risk ratings, borrowing base criteria and covenant compliance reports.

As part of the monitoring process, MC Advisors regularly assesses the risk profile of each of our investments and rates each of them based on an internal proprietary system that uses the categories listed below, which we refer to as MC Advisors’ investment performance rating. For any investment rated in grades 3, 4 or 5, MC Advisors will increase its monitoring intensity and prepare regular updates for the investment committee, summarizing current operating results and material impending events and suggesting recommended actions. MC Advisors monitors and, when appropriate, changes the investment ratings assigned to each investment in our portfolio. In connection with our valuation process, MC Advisors reviews these investment ratings on a quarterly basis, and our board of directors (the “Board”) reviews and affirms such ratings. A definition of the rating system follows:

Investment

Performance Summary Description

Risk Rating

Grade 1	Includes investments exhibiting the least amount of risk in our portfolio. The issuer is performing above expectations or the issuer's operating trends and risk factors are generally positive.
Grade 2	Includes investments exhibiting an acceptable level of risk that is similar to the risk at the time of origination. The issuer is generally performing as expected or the risk factors are neutral to positive.
Grade 3	Includes investments performing below expectations and indicates that the investment's risk has increased somewhat since origination. The issuer may be out of compliance with debt covenants; however, scheduled loan payments are generally not past due.
Grade 4	Includes an issuer performing materially below expectations and indicates that the issuer's risk has increased materially since origination. In addition to the issuer being generally out of compliance with debt covenants, scheduled loan payments may be past due (but generally not more than six months past due). For grade 4 investments, we intend to increase monitoring of the issuer.
Grade 5	Indicates that the issuer is performing substantially below expectations and the investment risk has substantially increased since origination. Most or all of the debt covenants are out of compliance or payments are substantially delinquent. Investments graded 5 are not anticipated to be repaid in full and we will reduce the fair market value of the loan to the amount we expect to recover.

Our investment performance risk ratings do not constitute any rating of investments by a nationally recognized statistical rating organization or reflect or represent any third-party assessment of any of our investments.

In the event of a delinquency or a decision to rate an investment grade 4 or grade 5, the applicable analyst, in consultation with a member of the investment committee, will develop an action plan. Such a plan may require a meeting with the borrower's management or the lender group to discuss reasons for the default and the steps management is undertaking to address the under-performance, as well as required amendments and waivers that may be required. In the event of a dramatic deterioration of a credit, MC Advisors intends to form a team or engage outside advisors to analyze, evaluate and take further steps to preserve its value in the credit. In this regard, we would expect to explore all options, including in a private equity sponsored investment, assuming certain responsibilities for the private equity sponsor or a formal sale of the business with oversight of the sale process by us. Several of Monroe Capital's professionals are experienced in running work-out transactions and bankruptcies.

The following table shows the distribution of our investments on the 1 to 5 investment performance rating scale as of June 30, 2017 (dollars in thousands):

Investment Performance Rating	Investments at Fair Value	Percentage of Total Investments	
1	\$ —	—	%
2	379,004	85.1	
3	48,208	10.8	
4	18,337	4.1	
5	—	—	
Total	\$ 445,549	100.0	%

The following table shows the distribution of our investments on the 1 to 5 investment performance rating scale as of December 31, 2016 (dollars in thousands):

Investment Performance Rating	Investments at Fair Value	Percentage of Total Investments	
1	\$ —	—	%
2	360,338	87.3	
3	40,192	9.7	
4	12,390	3.0	
5	—	—	
Total	\$ 412,920	100.0	%

Results of Operations

Operating results were as follows (dollars in thousands):

	Three months ended June 30,	
	2017	2016
Total investment income	\$ 12,268	\$ 11,118
Total expenses, net of incentive fee waiver	6,180	5,359
Net investment income	6,088	5,759
Net realized gain (loss) on investments	2,161	—
Net realized gain (loss) on secured borrowings	66	—
Net change in unrealized gain (loss) on investments	(7,270)	(541)
Net change in unrealized gain (loss) on secured borrowings	(5)	59
Net change in unrealized gain (loss) on foreign currency borrowings	(16)	—
Net increase (decrease) in net assets resulting from operations	\$ 1,024	\$ 5,277

	Six months ended June 30,	
	2017	2016
Total investment income	\$ 24,274	\$ 22,657
Total expenses, net of incentive fee waiver	12,152	11,111
Net investment income	12,122	11,546
Net realized gain (loss) on investments	2,328	587
Net realized gain (loss) on secured borrowings	66	—
Net change in unrealized gain (loss) on investments	(10,901)	1,001
Net change in unrealized gain (loss) on secured borrowings	(6)	87
Net change in unrealized gain (loss) on foreign currency borrowings	(16)	—
Net increase (decrease) in net assets resulting from operations	\$ 3,593	\$ 13,221

Investment Income

The composition of our investment income was as follows (dollars in thousands):

	Three months ended June 30,	
	2017	2016
Interest income	\$ 10,701	\$ 8,930
Dividend income	250	1,051
Fee income	637	516

Prepayment gain (loss)	322	232
Accretion of discounts and amortization of premium	358	389
Total investment income	\$ 12,268	\$ 11,118

	Six months ended June 30,	
	2017	2016
Interest income	\$ 21,089	\$ 17,534
Dividend income	500	2,913
Fee income	965	847
Prepayment gain (loss)	974	609
Accretion of discounts and amortization of premium	746	754
Total investment income	\$ 24,274	\$ 22,657

The increase in investment income of \$1.2 million and \$1.6 million during the three and six months ended June 30, 2017, as compared to the three and six months ended June 30, 2016, is primarily due to increases in average outstanding loan balances, partially offset by decreases in dividend income. The decrease in dividend income during the three and six months ended June 30, 2017, as compared to the prior year periods, is driven by decreases in dividend income from our investment in Rockdale Blackhawk, LLC (“Rockdale”) of \$0.8 million and \$2.4 million, respectively. While we have received significant equity distributions from our investment in Rockdale in the past, the timing and amount of these distributions are not within our control and are difficult to predict and may fluctuate significantly from period to period.

Operating Expenses

The composition of our operating expenses was as follows (dollars in thousands):

	Three months ended June 30,	
	2017	2016
Interest and other debt financing expenses	\$ 2,184	\$ 1,773
Base management fees	1,903	1,504
Incentive fees, net of incentive fee waiver	1,210	1,319
Professional fees	286	238
Administrative service fees	301	304
General and administrative expenses	259	182
Excise taxes	—	—
Directors' fees	37	39
Total expenses, net of incentive fee waiver	\$ 6,180	\$ 5,359

	Six months ended June 30,	
	2017	2016
Interest and other debt financing expenses	\$ 4,194	\$ 3,464
Base management fees	3,708	3,004
Incentive fees, net of incentive fee waiver	2,500	3,059
Professional fees	577	445
Administrative service fees	631	632
General and administrative expenses	468	346
Excise taxes	—	87
Directors' fees	74	74
Total expenses, net of incentive fee waiver	\$ 12,152	\$ 11,111

The composition of our interest and other debt financing expenses was as follows (dollars in thousands):

	Three months ended June 30,	
	2017	2016
Interest expense – revolving credit facility	\$ 1,385	\$ 1,188
Interest expense – SBA debentures	518	326
Amortization of deferred financing costs	255	199
Interest expense – secured borrowings	13	35
Other	13	25
Total interest and other debt financing expenses	\$ 2,184	\$ 1,773

	Six months ended June 30,	
	2017	2016
Interest expense – revolving credit facility	\$ 2,730	\$ 2,316
Interest expense – SBA debentures	924	652
Amortization of deferred financing costs	486	381
Interest expense – secured borrowings	34	72
Other	20	43
Total interest and other debt financing expenses	\$ 4,194	\$ 3,464

The increase in expenses of \$0.8 million and \$1.0 million during the three and six months ended June 30, 2017, as compared to the three and six months ended June 30, 2016, is primarily due to an increase in base management fees due to the growth in invested assets and an increase in interest expense as a result of additional borrowings (including SBA-guaranteed debentures) required to support the growth of the portfolio. During the three and six months ended June 30, 2017, these increases were partially offset by a decline in incentive fees. During the three and six months ended June 30, 2017, MC Advisors waived part one incentive fees (based on net investment income) of \$0.3 million and \$0.3 million, respectively. For the three and six months ended June 30, 2016, no incentive fees were waived.

Net Realized Gain (Loss) on Investments and Secured Borrowings

During the three months ended June 30, 2017 and 2016, we had sales of investments of \$2.1 million and zero resulting in \$2.1 million and zero of net realized gains, respectively. During the six months ended June 30, 2017 and 2016, we had sales of investments of \$4.2 million and \$0.6 million resulting in \$2.3 million and \$0.6 million of net realized gains, respectively.

During the three months ended June 30, 2017 and 2016, we had sales of secured borrowings of \$1.3 million and zero resulting in \$66 thousand and zero of net realized gains, respectively. During the six months ended June 30, 2017 and 2016, we had sales of secured borrowings of \$1.3 million and zero resulting in \$66 thousand and zero of net realized gains, respectively.

Net Change in Unrealized Gain (Loss) on Investments, Secured Borrowings and Foreign Currency Borrowings

For the three months ended June 30, 2017 and 2016, our investments had (\$7.3) million and (\$0.5) million of net change in unrealized gain (loss), respectively. During the three months ended June 30, 2017, the net change in unrealized losses on the portfolio was primarily attributable to a mark-to-market loss on the common equity investment in Rockdale. For the three months ended June 30, 2017 and 2016, our secured borrowings had (\$5) thousand and \$59 thousand of net change in unrealized gain (loss), respectively. For the three months ended June 30, 2017 and 2016, our foreign currency borrowings had (\$16) thousand and zero of net change in unrealized gain (loss), respectively.

For the six months ended June 30, 2017 and 2016, our investments had (\$10.9) million and \$1.0 million of net unrealized gain (loss), respectively. For the six months ended June 30, 2017 and 2016, our secured borrowings had (\$6) thousand and \$87 thousand of net unrealized gain (loss), respectively. For the six months ended June 30, 2017 and 2016, our foreign currency borrowings had (\$16) thousand and zero of net change in unrealized gain (loss), respectively.

Net Increase (Decrease) in Net Assets Resulting from Operations

For the three months ended June 30, 2017 and 2016, the net increase in net assets from operations was \$1.0 million and \$5.3 million, respectively. Based on the weighted average shares of common stock outstanding for the three months ended June 30, 2017 and 2016, our per share net increase in net assets resulting from operations was \$0.06 and \$0.41, respectively. The \$4.3 million decrease during the three months ended June 30, 2017, as compared to three months ended June 30, 2016, is primarily the result of an increase in net unrealized mark-to-market losses on investments in the portfolio during the three months ended June 30, 2017 as compared to the three months ended June 30, 2016. This decline was partially offset by an increase in realized gains on the portfolio.

For the six months ended June 30, 2017 and 2016, the net increase in net assets from operations was \$3.6 million and \$13.2 million, respectively. Based on the weighted average shares of common stock outstanding for the six months ended June 30, 2017 and 2016, our per share net increase in net assets resulting from operations was \$0.21 and \$1.02, respectively. The \$9.6 million decrease during the six months ended June 30, 2017, as compared to six months ended June 30, 2016, is primarily the result of net unrealized mark-to-market losses on investments in the portfolio during the six months ended June 30, 2017 as compared to net unrealized mark-to-market gains on investments in the portfolio during the six months ended June 30, 2016. This decline was partially offset by an increase in realized gains on the portfolio.

Liquidity and Capital Resources

As of June 30, 2017, we had \$9.9 million in cash, \$5.3 million in cash at MRCC SBIC, \$93.8 million of total debt outstanding on our revolving credit facility and \$85.6 million in outstanding SBA-guaranteed debentures. We had \$106.2 million available for additional borrowings on our revolving credit facility and \$29.4 million in available SBA-guaranteed debentures. See “*Borrowings*” below for additional information.

Cash Flows

For the six months ended June 30, 2017 and 2016, we experienced a net increase (decrease) in cash and restricted cash of \$6.9 million and (\$0.2) million, respectively. For the six months ended June 30, 2017, operating activities used \$29.4 million, primarily as a result of purchases of portfolio investments, partially offset by sales of and principal repayments on portfolio investments. For the six months ended June 30, 2016, operating activities provided \$6.5 million, primarily as a result of net income from operations, partially offset by net cash outflows for the settlement of open trades. During the six months ended June 30, 2017, we generated \$36.4 million from financing activities primarily as a result of net proceeds from capital raises and SBA debenture borrowings during the period, partially offset by net repayments on our revolving credit facility and distributions to stockholders. During the six months ended June 30, 2016, we used \$6.7 million for financing activities primarily as a result of distributions to stockholders, partially offset by net borrowings on our revolving credit facility.

Capital Resources

As a BDC, we distribute substantially all of our net income to our stockholders and have an ongoing need to raise additional capital for investment purposes. We intend to generate additional cash primarily from future offerings of securities, future borrowings and cash flows from operations, including income earned from investments in our portfolio companies. On both a short-term and long-term basis, our primary use of funds will be to invest in portfolio companies and make cash distributions to our stockholders.

As a BDC, we are generally not permitted to issue and sell our common stock at a price below net asset value per share. We may, however, sell our common stock, or warrants, options or rights to acquire our common stock, at a price below the then-current net asset value per share of our common stock if our Board, including independent directors, determines that such sale is in the best interests of us and our stockholders, and if our stockholders have approved such sales. On July 14, 2016, our stockholders voted to allow us to sell or otherwise issue common stock at a price below net asset value per share for a period of one year, subject to certain limitations. On July 21, 2017 our stockholders once again voted to allow us to sell or otherwise issue common stock at a price below net asset value per share for a period of one year, subject to certain limitations. As of June 30, 2017 and December 31, 2016, we had 20,239,957 and 16,581,869 shares outstanding, respectively.

On June 24, 2015, our stockholders approved a proposal to authorize us to issue warrants, options or rights to subscribe to, convert to, or purchase our common stock in one or more offerings. This is a standing authorization and does not require annual re-approval by our stockholders.

Stock Issuances: On July 1, 2016, we amended the ATM securities offering program with MLV & Co, LLC (“MLV”) and JMP Securities LLC to replace MLV with FBR Capital Markets & Co. (“FBR”), an affiliate of MLV (the “Prior ATM Program”). On May 12, 2017, we entered into new equity distribution agreements with each of FBR and JMP that reference our current registration statement (the “ATM Program”). All other material terms of the Prior ATM Program remain unchanged under the ATM Program. During the six months ended June 30, 2017, we sold 173,939 shares at an average price of \$15.71 per share for gross proceeds of \$2.7 million under the Prior ATM Program and no shares were sold under the ATM Program. Aggregate underwriters’ discounts and commissions were \$41 thousand and offering costs were \$23 thousand, resulting in net proceeds of approximately \$2.7 million. There were no stock

issuances during the six months ended June 30, 2016.

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On June 9, 2017, we closed a public offering of 3,000,000 shares of our common stock at a public offering price of \$15.00 per share, raising approximately \$45.0 million in gross proceeds. On June 14, 2017, pursuant to the underwriters' exercise of the over-allotment option, we sold an additional 450,000 shares of our common stock, at a public offering price of \$15.00 per share, and additional \$6.8 million in gross proceeds for a total of \$51.8 million. Aggregate underwriters' discounts and commissions were \$2.1 and offering costs were \$0.1 million, resulting in net proceeds of approximately \$49.6 million.

Borrowings

Revolving Credit Facility: As of June 30, 2017, we had U.S. dollar borrowings of \$91.5 million and non-U.S. dollar borrowings denominated in Great Britain pounds of £1.8 million (\$2.3 million in U.S. dollars) under our revolving credit facility with ING Capital LLC, as agent, to finance the purchase of our assets. The borrowings denominated in Great Britain pounds are translated into U.S. dollars based on the spot rate at each balance sheet date. The impact resulting from changes in foreign currency borrowings is included in change in unrealized gain (loss) on foreign currency borrowings in our consolidated statements of operations. The borrowings denominated in Great Britain pounds may be positively or negatively affected by movements in the rate of exchange between the U.S. dollar and the Great Britain pound. This movement is beyond our control and cannot be predicted. As of December 31, 2016, we had U.S. dollar borrowings of \$129.0 million outstanding under the revolving credit facility. As of June 30, 2017, the maximum amount we were able to borrow was \$200.0 million and this borrowing can be increased to \$300.0 million pursuant to an accordion feature (subject to maintaining 200% asset coverage, as defined by the 1940 Act). On February 22, 2017, we closed a \$40.0 million upsize to the revolving credit facility, bringing the maximum amount we are able to borrow from \$160.0 million to the now current maximum amount of \$200.0 million, in accordance with the facility's accordion feature. The maturity date on the facility is December 14, 2020.

The revolving credit facility is secured by a lien on all of our assets, including cash on hand, but excluding the assets of our wholly-owned subsidiary, MRCC SBIC. Our ability to borrow under the revolving credit facility is subject to availability under a defined borrowing base, which varies based on portfolio characteristics and certain eligibility criteria and concentration limits, as well as required valuation methodologies. We may make draws under the revolving credit facility to make or purchase additional investments through December 2019 and for general working capital purposes until the maturity date of the revolving credit facility. Borrowings under the revolving credit facility bear interest, at our election, at an annual rate of LIBOR (one-month, two-month, three-month or six-month at our discretion based on the term of the borrowing) plus 2.75% or at a daily rate equal to 2.00% per annum plus the greater of the prime interest rate, the federal funds rate plus 0.5% or LIBOR plus 1.0%. The LIBOR rate on the revolving credit facility was reduced to LIBOR plus 2.75% from LIBOR plus 3.00% in conjunction with our capital raise on June 9, 2017, as net worth (excluding investments in MRCC SBIC) exceeded \$225.0 million. In addition to the stated interest rate on borrowings under the revolving credit facility, we are required to pay a fee of 0.5% per annum on any unused portion of the revolving credit facility if the unused portion of the facility is less than 65% of the then available maximum borrowing or a fee of 1.0% per annum on any unused portion of the revolving credit facility if the unused portion of the facility is greater than or equal to 65% of the then available maximum borrowing. As of June 30, 2017 and December 31, 2016, the outstanding borrowings were accruing at a weighted average interest rate of 4.1% and 3.8%, respectively. The weighted average interest rate of the revolving credit facility borrowings (excluding debt

issuance costs) for the three and six months ended June 30, 2017 was 4.0% and 4.1%, respectively. The weighted average fee rate on the unused portion of the revolving credit facility for the three and six months ended June 30, 2017 was 0.5% and 0.5%, respectively. The weighted average interest rate of the revolving credit facility borrowings (excluding debt issuance costs) for the three and six months ended June 30, 2016 was 3.6% and 3.5%, respectively. The weighted average fee rate on the unused portion of the revolving credit facility for the three and six months ended June 30, 2016 was 0.5% and 0.5%, respectively.

Our ability to borrow under the revolving credit facility is subject to availability under the borrowing base, which permits us to borrow up to 70% of the fair market value of our portfolio company investments depending on the type of the investment we hold and whether the investment is quoted. Our ability to borrow is also subject to certain concentration limits, and our continued compliance with the representations, warranties and covenants given by us under the facility. The revolving credit facility contains certain financial and restrictive covenants, including, but not limited to, our maintenance of: (1) a minimum consolidated total net assets at least equal to the greater of (a) 40% of the consolidated total assets on the last day of each quarter or (b) \$120.0 million plus 65% of the net proceeds to us from sales of our securities after December 14, 2015; (2) a ratio of total assets (less total liabilities other than indebtedness) to total indebtedness of not less than 2.1 times; and (3) a ratio of earnings before interest and taxes to interest expense of at least 2.5 times. The credit facility also requires us to undertake customary indemnification obligations with respect to ING Capital LLC and other members of the lending group and to reimburse the lenders for expenses associated with entering into the credit facility. The revolving credit facility also has customary provisions regarding events of default, including events of default for nonpayment, change in control transactions at both Monroe Capital Corporation and MC Advisors, failure to comply with financial and negative covenants, and failure to maintain our relationship with MC Advisors. If we incur an event of default under the revolving credit facility and fail to remedy such default under any applicable grace period, if any, then the entire revolving credit facility could become immediately due and payable, which would materially and adversely affect our liquidity, financial condition, results of operations and cash flows.

Our revolving credit facility also imposes certain conditions that may limit the amount of our distributions to stockholders. Distributions payable in our common stock under the DRIP are not limited by the revolving credit facility. Distributions in cash or property other than common stock are generally limited to 115% of the amount of distributions required to maintain our status as a RIC.

SBA Debentures: On February 28, 2014, our wholly-owned subsidiary, MRCC SBIC, received a license from the SBA to operate as a SBIC under Section 301(c) of the Small Business Investment Act of 1958, as amended. MRCC SBIC commenced operations on September 16, 2013.

The SBIC license allows MRCC SBIC to obtain leverage by issuing SBA-guaranteed debentures, subject to the issuance of a leverage commitment by the SBA and other customary procedures. SBA-guaranteed debentures are non-recourse, interest only debentures with interest payable semi-annually and have a ten year maturity. The principal amount of SBA-guaranteed debentures is not required to be paid prior to maturity but may be prepaid at any time without penalty. The interest rate of SBA-guaranteed debentures is fixed on a semi-annual basis (pooling date) at a market-driven spread over U.S. Treasury Notes with 10-year maturities. The SBA, as a creditor, has a superior claim to MRCC SBIC's assets over our stockholders in the event we liquidate MRCC SBIC or the SBA exercises its remedies upon an event of default.

SBA regulations currently limit the amount that an individual SBIC may borrow to a maximum of \$150.0 million when it has at least \$75.0 million in regulatory capital, receives a leverage commitment from the SBA and has been through an audit examination by the SBA subsequent to licensing. The SBA also historically limited a related group of SBICs (commonly referred to as a "family of funds") to a maximum of \$225.0 million in total borrowings. On December 18, 2015, this family of funds limitation was raised to \$350.0 million in total borrowings. As we have other affiliated SBICs already in operation, MRCC SBIC was historically limited to a maximum of \$40.0 million in borrowings. Pursuant to the increase in the family of funds limitation, we submitted a commitment application to the SBA and on April 13, 2016 we were approved for \$75.0 million in additional SBA-guaranteed debentures for MRCC SBIC for a total of \$115.0 million in available debentures.

As of June 30, 2017, MRCC SBIC had \$57.6 million in leverageable capital and \$85.6 million in SBA-guaranteed debentures outstanding. As of December 31, 2016, MRCC SBIC had \$41.0 million in leverageable capital and \$51.5 million in SBA-guaranteed debentures outstanding. As of June 30, 2017, we have made all required leverageable capital contributions to MRCC SBIC in order to access the remaining \$29.4 million in available SBA-guaranteed debentures.

As of June 30, 2017, MRCC SBIC had the following SBA-guaranteed debentures outstanding (dollars in thousands):

Maturity Date	Interest Rate		Amount
September 2024	3.4	%	\$12,920
March 2025	3.3	%	14,800
March 2025	2.9	%	7,080
September 2025	3.6	%	5,200
March 2027	3.5	%	20,000

September 2027	2.2	% ⁽¹⁾	25,600
Total			\$85,600

(1) Represents an interim rate of interest as the SBA-guaranteed debentures had not yet pooled.

As of December 31, 2016, MRCC SBIC had the following SBA-guaranteed debentures outstanding (dollars in thousands):

Maturity Date	Interest Rate		Amount
September 2024	3.4	%	\$12,920
March 2025	3.3	%	14,800
March 2025	2.9	%	7,080
September 2025	3.6	%	5,200
March 2027	2.1	% ⁽¹⁾	9,200
March 2027	2.0	% ⁽¹⁾	2,300
Total			\$51,500

(1) Represents an interim rate of interest as the SBA-guaranteed debentures had not yet pooled.

On October 2, 2014, the Company was granted exemptive relief from the SEC for permission to exclude the debt of MRCC SBIC guaranteed by the SBA from the 200% asset coverage test under the 1940 Act. The receipt of this exemption for this SBA-guaranteed debt increases flexibility under the 200% asset coverage test.

Secured Borrowings: Certain partial loan sales do not qualify for sale accounting under Accounting Standards Codification (“ASC”) Topic 860 — *Transfers and Servicing* (“ASC Topic 860”) because these sales do not meet the definition of a “participating interest,” as defined in the guidance, in order for sale treatment to be allowed. Participations or other partial loan sales which do not meet the definition of a participating interest remain as an investment on the accompanying consolidated statements of assets and liabilities and the portion sold is recorded as a secured borrowing in the liabilities section of the consolidated statements of assets and liabilities. For these partial loan sales, the interest earned on the entire loan balance is recorded within “interest income” and the interest earned by the buyer in the partial loan sale is recorded within “interest and other debt financing expenses” in the accompanying consolidated statements of operations.

As of June 30, 2017, we did not have secured borrowings. As of December 31, 2016, secured borrowings at fair value totaled \$1.3 million and the fair value of the loans that are associated with these secured borrowings was \$5.8 million. These secured borrowings were created as a result of our completion of partial loan sales of certain unitranche loan assets during the year ended December 31, 2013, that did not meet the definition of a “participating interest.” As a result, sale treatment was not allowed and these partial loan sales were treated as secured borrowings. No such partial loan sales occurred during the year ended December 31, 2016 and the six months ended June 30, 2017. During the three and six months ended June 30, 2017, repayments on secured borrowings totaled \$1.3 million and \$1.3 million, respectively. During the three and six months ended June 30, 2016 repayments on secured borrowings totaled \$0.1 million and \$0.3 million, respectively. The weighted average interest rate on our secured borrowings was approximately zero and 6.3% as of June 30, 2017 and December 31, 2016, respectively.

Distribution Policy

Our Board will determine the timing and amount, if any, of our distributions. We intend to pay distributions on a quarterly basis. In order to avoid corporate-level tax on the income we distribute as a RIC, we must distribute to our stockholders at least 90% of our ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any, on an annual basis out of the assets legally available for such distributions. In addition, we also intend to distribute any realized net capital gains (i.e., realized net long-term capital gains in excess of realized net short-term capital losses) at least annually out of the assets legally available for such distributions. Distributions to stockholders for the three and six months ended June 30, 2017, totaled \$7.1 million (\$0.35 per share) and \$12.9 million (\$0.70 per share), respectively. Distributions to stockholders for the three and six months ended June 30, 2016 totaled \$4.5 million (\$0.35 per share) and \$9.1 million (\$0.70 per share), respectively. The tax character of such distributions is determined at the end of the fiscal year. However, if the character of such distributions were determined as of June 30, 2017 and 2016, no portion of these distributions would have been characterized as a tax return of capital to stockholders.

We have adopted an “opt out” dividend reinvestment plan (“DRIP”) for our common stockholders. As a result, if we declare a distribution, our stockholders’ cash distributions will be automatically reinvested in additional shares of our common stock unless a stockholder specifically “opts out” of our DRIP. If a stockholder opts out, that stockholder will receive cash distributions. Although distributions paid in the form of additional shares of our common stock will generally be subject to U.S. federal, state and local taxes in the same manner as cash distributions, stockholders participating in our DRIP will not receive any corresponding cash distributions with which to pay any such applicable taxes.

Related Party Transactions

We have a number of business relationships with affiliated or related parties, including the following:

We have an Investment Advisory and Management Agreement with MC Advisors, an investment advisor registered with the SEC, to manage our day-to-day operating and investing activities. We pay MC Advisors a fee for its services under the Investment Advisory and Management Agreement consisting of two components — a base management fee and an incentive fee. See Note 6 to our consolidated financial statements and “Significant Accounting Estimates and Critical Accounting Policies — *Capital Gains Incentive Fee*” for additional information.

We have an Administration Agreement with MC Management to provide us with the office facilities and administrative services necessary to conduct our day-to-day operations. See Note 6 to our consolidated financial statements for additional information.

Theodore L. Koenig, our Chief Executive Officer and Chairman of our Board is also a manager of MC Advisors and the President and Chief Executive Officer of MC Management. Aaron D. Peck, our Chief Financial Officer and Chief Investment Officer, serves as a director on our Board and is also a managing director of MC Management.

We have a license agreement with Monroe Capital LLC, under which Monroe Capital LLC has agreed to grant us a non-exclusive, royalty-free license to use the name “Monroe Capital” for specified purposes in our business.

In addition, we have adopted a formal code of ethics that governs the conduct of MC Advisors’ officers, directors and employees. Our officers and directors also remain subject to the duties imposed by both the 1940 Act and Maryland General Corporation Law.

Commitments and Contingencies and Off-Balance Sheet Arrangements

Commitments and Contingencies

As of June 30, 2017 and December 31, 2016, we had \$37.4 million and \$37.7 million, respectively, in outstanding commitments to fund investments under undrawn revolvers, capital expenditure loans and delayed draw commitments. Additionally, we have entered into certain contracts with other parties that contain a variety of indemnifications. Our maximum exposure under these arrangements is unknown. However, we have not experienced claims or losses pursuant to these contracts and believe the risk of loss related to such indemnifications to be remote.

Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Market Trends

We have identified the following trends that may affect our business:

Target Market: We believe that small and middle-market companies in the United States with annual revenues between \$10.0 million and \$2.5 billion represent a significant growth segment of the U.S. economy and often require substantial capital investments to grow. Middle-market companies have generated a significant number of investment opportunities for investment funds managed or advised by Monroe Capital, and we believe that this market segment will continue to produce significant investment opportunities for us.

Specialized Lending Requirements: We believe that several factors render many U.S. financial institutions ill-suited to lend to U.S. middle-market companies. For example, based on the experience of our management team, lending to U.S. middle-market companies (1) is generally more labor intensive than lending to larger companies due to the smaller size of each investment and the fragmented nature of information for such companies, (2) requires due diligence and underwriting practices consistent with the demands and economic limitations of the middle-market and (3) may also require more extensive ongoing monitoring by the lender.

Demand for Debt Capital: We believe there is a large pool of uninvested private equity capital for middle-market companies. We expect private equity firms will seek to leverage their investments by combining equity capital with senior secured loans and mezzanine debt from other sources, such as us.

Competition from Other Lenders: We believe that many traditional bank lenders, in recent years, de-emphasized their service and product offerings to middle-market businesses in favor of lending to large corporate clients and managing capital market transactions. In addition, many commercial banks face significant balance sheet constraints as they seek to build capital and meet future regulatory capital requirements. These factors may result in opportunities for alternative funding sources to middle-market companies and therefore drive increased new investment opportunities for us. Conversely, there is increased competitive pressure in the BDC and investment company marketplace for

senior and subordinated debt which could result in lower yields for increasingly riskier assets.

Pricing and Deal Structures: We believe that the volatility in global markets over the last several years and current macroeconomic issues such as a weakened U.S. economy has reduced access to, and availability of, debt capital to middle-market companies, causing a reduction in competition and generally more favorable capital structures and deal terms. Recent capital raises in the BDC and investment company marketplace have created increased competition; however, we believe that current market conditions may continue to create favorable opportunities to invest at attractive risk-adjusted returns.

Significant Accounting Estimates and Critical Accounting Policies

Revenue Recognition

We record interest and fee income on an accrual basis to the extent that we expect to collect such amounts. For loans and debt securities with contractual PIK interest, we do not accrue PIK interest if the portfolio company valuation indicates that such PIK interest is not collectible. We do not accrue as a receivable interest on loans and debt securities if we have reason to doubt our ability to collect such interest. Loan origination fees, original issue discount and market discount or premium is capitalized, and we then amortize such amounts using the effective interest method as interest income over the life of the investment. Upon the prepayment of a loan or debt security, any unamortized premium or discount or loan origination fees are recorded as interest income. We record prepayment premiums on loans and debt securities as interest income when we receive such amounts.

Dividend income on preferred equity securities is recorded as dividend income on an accrual basis to the extent that such amounts are payable by the portfolio company and are expected to be collected. Dividend income on common equity securities is recorded on the record date for private portfolio companies. Each distribution received from limited liability company (“LLC”) and limited partnership (“LP”) investments is evaluated to determine if the distribution should be recorded as dividend income or a return of capital. Generally, we will not record distributions from equity investments in LLCs and LPs as dividend income unless there are sufficient accumulated tax-basis earnings and profits in the LLC or LP prior to the distribution. Distributions that are classified as a return of capital are recorded as a reduction in the cost basis of the investment.

Valuation of Portfolio Investments

As a BDC, we generally invest in illiquid securities including debt and, to a lesser extent, equity securities of middle-market companies. Under procedures established by our Board, we value investments for which market quotations are readily available and within a recent date at such market quotations. We obtain these market values from an independent pricing service or at the mean between the bid and ask prices obtained from at least two brokers

or dealers (if available, otherwise by a principal market maker or a primary market dealer). When doing so, we determine whether the quote obtained is sufficient in accordance with generally accepted accounting principles in the United States (“GAAP”) to determine the fair value of the security. Debt and equity securities that are not publicly traded or whose market prices are not readily available or whose market prices are not regularly updated are valued at fair value as determined in good faith by our Board. Such determination of fair values may involve subjective judgments and estimates. Investments purchased within 60 days of maturity are valued at cost plus accreted discount, or minus amortized premium, which approximates fair value.

Our Board is ultimately and solely responsible for determining the fair value of the portfolio investments that are not publicly traded, whose market prices are not readily available on a quarterly basis in good faith or any other situation where portfolio investments require a fair value determination. Because we expect that there will not be a readily available market for many of the investments in our portfolio, we expect to value many of our portfolio investments at fair value as determined in good faith by our Board using a documented valuation policy and a consistently applied valuation process. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may differ significantly from the values that would have been used had a readily available market value existed for such investments, and the differences could be material.

With respect to investments for which market quotations are not readily available, our Board undertakes a multi-step valuation process each quarter, as described below:

the quarterly valuation process begins with each portfolio company or investment being initially evaluated and rated by the investment professionals responsible for the credit monitoring of the portfolio investment;

- preliminary valuation conclusions are then documented and discussed with the investment committee;

our Board engages one or more independent valuation firm(s) to conduct fair value appraisals of material investments for which market quotations are not readily available. These fair value appraisals for material investments are received at least once in every calendar year for each portfolio company investment, but are generally received quarterly;

our audit committee of the Board reviews the preliminary valuations of MC Advisors and of the independent valuation firm(s) and responds and supplements the valuation recommendations to reflect any comments; and

our Board discusses these valuations and determines the fair value of each investment in the portfolio in good faith, based on the input of MC Advisors, the independent valuation firm(s) and the audit committee.

The Board, together with our independent valuation firms, generally uses the yield approach to determine fair value for loans where market quotations are not readily available, as long as it is appropriate. If there is deterioration in credit quality or a debt investment is in workout status, we may consider other factors in determining the fair value, including the value attributable to the debt investment from the enterprise value of the portfolio company under the market approach or the proceeds that would be received in a liquidation analysis. We generally consider our debt to be performing if the borrower is not in default, the borrower is remitting payments in a timely manner; the loan is in covenant compliance or is otherwise not deemed to be impaired. In determining the fair value of the performing debt, the Company considers fluctuations in current interest rates, the trends in yields of debt instruments with similar credit ratings, financial condition of the borrower, economic conditions and other relevant factors, both qualitative and

quantitative. In the event that a debt instrument is not performing, as defined above, we will evaluate the value of the collateral utilizing the same framework described above for a performing loan to determine the value of the loan.

Under the yield approach, we utilize discounted cash flow models to determine the present value of the future cash flow streams of our debt investments, based on future interest and principal payments as set forth in the associated loan agreements. In determining fair value under the yield approach, we also consider the following factors: applicable market yields and leverage levels, credit quality, prepayment penalties, the nature and realizable value of any collateral, the portfolio company's ability to make payments, and changes in the interest rate environment and the credit markets that generally may affect the price at which similar investments may be made.

Under the market approach, we typically use the enterprise value methodology to determine the fair value of an investment. There is no one methodology to estimate enterprise value and, in fact, for any one portfolio company, enterprise value is generally best expressed as a range of values, from which we derive a single estimate of enterprise value. In estimating the enterprise value of a portfolio company, we analyze various factors consistent with industry practice, including but not limited to original transaction multiples, the portfolio company's historical and projected financial results, applicable market trading and transaction comparables, applicable market yields and leverage levels, the nature and realizable value of any collateral, the markets in which the portfolio company does business, and comparisons of financial ratios of peer companies that are public. Typically, the enterprise values of private companies are based on multiples of earnings before interest, income taxes, depreciation and amortization ("EBITDA"), cash flows, net income, revenues, or in limited cases, book value.

Net Realized Gains or Losses and Net Change in Unrealized Gain or Loss

We measure realized gains or losses by the difference between the net proceeds from the sale and the amortized cost basis of the investment, without regard to unrealized gain or loss previously recognized. Net change in unrealized gain or loss reflects the change in portfolio investment values during the reporting period, including any reversal of previously recorded unrealized gain or loss, when gains or losses are realized. We report changes in the fair value of secured borrowings that are measured at fair value as a component of the net change in unrealized gain (loss) on secured borrowings in the consolidated statements of operations. The impact resulting from changes in foreign exchange rates on the revolving credit facility borrowings is included in change in unrealized gain (loss) on foreign currency borrowings.

Capital Gains Incentive Fee

Pursuant to the terms of the Investment Advisory and Management Agreement with MC Advisors, the incentive fee on capital gains earned on liquidated investments of our portfolio is determined and payable in arrears as of the end of each calendar year (or upon termination of the investment advisory and administrative services agreement). This fee equals 20% of our incentive fee capital gains (i.e., our realized capital gains on a cumulative basis from inception, calculated as of the end of the applicable period, net of all realized capital losses and unrealized capital depreciation on a cumulative basis), less the aggregate amount of any previously paid capital gains incentive fees. On a quarterly basis, we accrue for the capital gains incentive fee by calculating such fee as if it were due and payable as of the end of such period.

While the Investment Advisory and Management Agreement with MC Advisors neither includes nor contemplates the inclusion of unrealized gains in the calculation of the capital gains incentive fee, pursuant to an interpretation of an American Institute for Certified Public Accountants Technical Practice Aid for investment companies, we include unrealized gains in the calculation of the capital gains incentive fee expense and related accrued capital gains incentive fee. This accrual reflects the incentive fees that would be payable to MC Advisors if our entire portfolio was liquidated at its fair value as of the balance sheet date even though MC Advisors is not entitled to an incentive fee with respect to unrealized gains unless and until such gains are actually realized.

During the three months ended June 30, 2017, we did not accrue capital gains incentive fees. During the six months ended June 30, 2017, we had a reduction in accrued capital gains incentive fees of \$0.2 million, primarily as a result of net declines in portfolio valuations during the period. During the three months ended June 30, 2016, we had a reduction in accrued capital gains incentive fees of \$97 thousand, all as a result of net declines in portfolio valuations during the period. During the six months ended June 30, 2016, we had a net increase in accrued capital gains incentive fees of \$138 thousand, of which \$117 thousand was related to realized capital gains and was therefore payable to MC advisors and \$21 thousand was a result of net increases in portfolio valuations during the period.

New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, *Revenue from Contracts with Customers* (ASC Topic 606) (“ASU 2014-09”). The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: Step 1: Identify the contract(s) with a customer. Step 2: Identify the performance obligations in the contract. Step 3: Determine the transaction price. Step 4: Allocate the transaction price to the performance obligations in the contract. Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

ASU 2014-09 also specified the accounting for some costs to obtain or fulfill a contract with a customer. In addition, ASU 2014-09 requires that an entity disclose sufficient information to enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The initial effective date of ASU 2014-09 was for fiscal periods beginning after December 15, 2016. However, in August 2015, the FASB issued ASU 2015-14, *Revenue from Contracts with Customers (ASC Topic 606): Deferral of the Effective Date*, which deferred the effective date to fiscal periods beginning after December 15, 2017. Management is currently evaluating the impact these changes will have on our consolidated financial statements and disclosures.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments — *Overall* (Subtopic 825-10): *Recognition and Measurement of Financial Assets and Financial Liabilities* (“ASU 2016-01”). ASU 2016-01 retains many current requirements for the classification and measurement of financial instruments; however, it significantly revises an entity’s accounting related to (1) the classification and measurement of investments in equity securities and (2) the presentation of certain fair value changes for financial liabilities measured at fair value. ASU 2016-01 also amends certain disclosure requirements associated with the fair value of financial instruments. This guidance is effective for annual and interim periods beginning after December 15, 2017, and early adoption is not permitted for public business entities. Management is currently evaluating the impact these changes will have on our consolidated financial statements and disclosures.

In October 2016, the U.S. Securities and Exchange Commission adopted new rules and amended rules (together “final rules”) intended to modernize the reporting and disclosures of information by registered investment companies. In part, the final rules amend Regulation S-X and require standardized, enhanced disclosure about derivatives in investment company financial statements, as well as other amendments. The compliance date for the amendments to Regulation S-X was August 1, 2017. Management is evaluating the impact that the adoption of the amendments to Regulation S-X will have on the Company’s consolidated financial statements and disclosures.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows* (Topic 230): *Restricted Cash* (“ASU 2016-18”). ASU 2016-18 requires that the statements of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statements of cash flows. The new guidance is effective for annual and interim periods, beginning after December 15, 2017, and early adoption is permitted and is to be applied on a retrospective basis. We have adopted ASU 2016-18 and the revised presentation is reflected in our consolidated financial statements for the periods presented.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are subject to financial market risks, including changes in interest rates. The majority of the loans in our portfolio have floating interest rates, and we expect that our loans in the future may also have floating interest rates. These loans are usually based on a floating LIBOR and typically have interest rate re-set provisions that adjust applicable interest rates under such loans to current market rates on a monthly or quarterly basis. The majority of the loans in our current portfolio have interest rate floors which have effectively converted the loans to fixed rate loans in the current interest rate environment. In addition, our credit facility has a floating interest rate provision and we expect that other credit facilities into which we enter in the future may have floating interest rate provisions.

Assuming that the consolidated statement of financial condition as of June 30, 2017 were to remain constant and that we took no actions to alter our existing interest rate sensitivity, the following table shows the annualized impact of hypothetical base rate changes in interest rates.

Change in Interest Rates	Increase (decrease) in interest income (in thousands)	Increase (decrease) in interest expense	Net increase (decrease) in net investment income
Down 25 basis points	\$ (867)	\$ (235)) \$ (632)
Up 100 basis points	4,163	938	3,225
Up 200 basis points	8,403	1,877	6,526
Up 300 basis points	12,642	2,815	9,827

Although we believe that this analysis is indicative of our existing sensitivity to interest rate changes, it does not adjust for changes in the credit market, credit quality, the size and composition of the assets in our portfolio and other business developments, including borrowing under the credit facility or other borrowings that could affect net increase in net assets resulting from operations, or net income. Accordingly, we can offer no assurances that actual results would not differ materially from the analysis above.

We may in the future hedge against interest rate fluctuations by using standard hedging instruments such as futures, options and forward contracts to the extent permitted under the 1940 Act and applicable commodities laws. While hedging activities may insulate us against adverse changes in interest rates, they may also limit our ability to participate in the benefits of lower interest rates with respect to the investments in our portfolio with fixed interest rates or interest rate floors.

We may also have exposure to foreign currencies (currently the Great Britain pound) related to certain investments. Such investments are translated into U.S. dollars based on the spot rate at each balance sheet date, exposing us to movements in the exchange rate. In order to reduce our exposure to fluctuations in exchange rates, we generally borrow in Great Britain pounds under our revolving credit facility to finance such investments. As of June 30, 2017, we have non-U.S. dollar borrowings denominated in Great Britain pounds of £1.8 million (\$2.3 million U.S. dollars) outstanding under the revolving credit facility.

ITEM 4. CONTROLS AND PROCEDURES

In accordance with Rules 13a-15(b) and 15d-15(b) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), we, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, carried out an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) of the Exchange Act). Based on that evaluation, our management, including the Chief Executive Officer and Chief Financial Officer, concluded that, at the end of the period covered by our Quarterly Report on Form 10-Q, our disclosure controls and procedures were effective and provided reasonable assurance that information required to be disclosed in our periodic SEC filings is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Notwithstanding the foregoing, a control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that it will detect or uncover failures within the Company to disclose material information otherwise required to be set forth in the Company’s periodic reports.

No change occurred in our internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) of the Exchange Act) during the six months ended June 30, 2017 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II

OTHER INFORMATION

Item 1. Legal Proceedings

Neither we nor our investment adviser are currently subject to any material legal proceedings.

Item 1A. Risk Factors

None.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

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Item 6. Exhibits

Exhibit

Number Description of Document

- | | |
|------|---|
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2 | Certification of Chief Financial Officer pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32.1 | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |

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SIGNATURES

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

Date: August 8, 2017 By /s/ Theodore L. Koenig
Theodore L. Koenig

Chairman, Chief Executive Officer and Director

(Principal Executive Officer)
Monroe Capital Corporation

Date: August 8, 2017 By /s/ Aaron D. Peck
Aaron D. Peck

Chief Financial Officer, Chief Investment Officer and Director

(Principal Financial and Accounting Officer)

Monroe Capital Corporation