

NETWORKS ASSOCIATES INC/

Form 10-K/A

June 28, 2002

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K/ A

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

For the fiscal year ended December 31, 2001

or

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

For the transition period from to

Commission file number: 0-20558

Networks Associates, Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

77-0316593

(I.R.S. Employer
Identification Number)

3965 Freedom Circle
Santa Clara, California

(Address of principal executive offices)

95054

(Zip Code)

Registrant's telephone number, including area code: (408) 988-3832

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: Common Stock, \$0.01 Par Value

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

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

The aggregate market value of the voting stock held by non-affiliates of the issuer as of December 31, 2001 was approximately \$3,582,411,290. The number of shares outstanding of the issuer's common stock as of December 31, 2001 was 140,699,222.

EXPLANATORY NOTE

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THIS 10-K/ A IS BEING FILED FOR THE PURPOSE OF AMENDING AND RESTATING ITEMS 1, 6, 7, 8 AND 14 TO REFLECT THE RESTATEMENT OF OUR CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2000, 1999 AND 1998 AND THE EFFECT OF THE RESTATEMENT OF OUR CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2000, 1999 AND 1998 AND THE EFFECT OF THE RESTATEMENT OF OUR CONSOLIDATED BALANCE SHEET FOR DECEMBER 31, 2001. WE HAVE MADE NO FURTHER CHANGES TO THE PREVIOUSLY FILED FORM 10-K. ALL INFORMATION IN THIS FORM 10-K/ A IS AS OF DECEMBER 31, 2001 AND DOES NOT REFLECT ANY SUBSEQUENT INFORMATION OR EVENTS OTHER THAN THE RESTATEMENT.

DOCUMENTS INCORPORATED BY REFERENCE

Items 10, 11, 12, and 13 of Part III are incorporated by reference from the Registrant's Proxy Statement for the Annual Meeting of Stockholders to be held May 15, 2002.

PART I

Item 1. *Business*

General

This 10-K/ A is being filed for the purpose of amending and restating Items 1, 6, 7, 8 and 14 to reflect the restatement of our Consolidated Financial Statements for the years ended December 31, 2001, 2000, 1999 and 1998 and a reclassification in our statements of operations for these years to reflect the retroactive adoption of a new accounting principle. We have made no further changes to the previously filed Form 10-K. All information in this Form 10-K/ A is as of December 31, 2001 and does not reflect any subsequent information or events other than the restatement.

Some of the statements contained in this Annual Report on Form 10-K/ A are forward-looking statements, including but not limited to those specifically identified as such, that involve risks and uncertainties. The statements contained in the Report on Form 10-K/ A that are not purely historical are forward looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act, including, without limitation, statements regarding our expectations, beliefs, intentions or strategies regarding the future. All forward looking statements included in this Report on Form 10-K/ A are based on information available to us on the date hereof, and we assume no obligation to update any such forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors, which may cause our actual results to differ materially from those implied by the forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as *may*, *will*, *should*, *expects*, *plans*, *anticipates*, *believes*, *estimates*, *predicts*, *continue* or the negative of these terms or other comparable terminology. In some instances, we have also indicated forward looking statements with an asterisk (*). Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. Moreover, neither any other person nor we assume responsibility for the accuracy and completeness of such statements. Important factors that may cause actual results to differ from expectations include those discussed in *Risk Factors* beginning on page 11 in this document.

Networks Associates, Inc. was formed in December 1997, by the combination of McAfee Associates, Inc. and Network General Corporation. Following the combination, McAfee changed its legal name to Networks Associates, Inc. and we do business under the name Network Associates. In 1999, our subsidiary McAfee.com sold to the public its Class A common stock as a part of its initial public offering.

OVERVIEW

We are a leading supplier of network security and network management solutions. We operate through two businesses consisting of our infrastructure business and McAfee.com, our publicly traded subsidiary. Our infrastructure business is operated in six geographic regions: the United States, Europe, Japan, Canada, Asia-Pacific and Latin America. McAfee.com is an application service provider, or ASP, targeted at consumers and small to medium-sized businesses.

The majority of our net revenue has historically been derived from our McAfee anti-virus products and our Sniffer Technologies network fault and performance products. In addition to these two flagship products, we have focused our efforts on building a full line of complementary network security and network management solutions. On the network security side, we strengthened our anti-virus lineup by adding complementary products in the firewall, intrusion detection, encryption, and virtual private networking categories. On the network management side, we built upon our Sniffer Technologies line by adding products in the help desk, asset management, network monitoring, and network reporting categories. We continuously seek to expand our product lines.

To more effectively market our infrastructure products in our various geographic regions, we have combined complementary products into separate product groups, as follows:

McAfee, which delivers world-class anti-virus and security products and services;

Sniffer Technologies, which is a leader in network availability and system security products; and

Magic Solutions, which is a leading provider of web-based service desk solutions.

In the fourth quarter of 2001, we substantially completed integrating the activities of our PGP product group into our McAfee and Sniffer product groups. The PGP product group accounted for approximately 6% of our net revenue in 2001. Former PGP products now marketed and sold as McAfee products include the McAfee VPN, McAfee Desktop Firewall (our distributed firewall) for corporate users and the McAfee E-Business Server. The CyberCop vulnerability assessment technology was integrated into the Sniffer product line. We are seeking buyers for the PGP desktop encryption and Gauntlet firewall products.

In 2001, our infrastructure business, including the recently integrated PGP product group, accounted for approximately \$749.0 million in net revenue and a net operating loss of \$81.8 million. In 2001, McAfee.com accounted for approximately \$62.0 million in net revenue and a net operating loss of approximately \$192,000.

McAfee Product Group

McAfee's products and services provide solutions designed to enforce anti-virus policies and measure the performance of anti-virus activities and deliver network security. The McAfee product group includes products and services that provide multi-layer anti-virus protection, management and reporting for desktops, servers, GroupWare, Internet technologies, and wireless technologies. The McAfee product group also includes distributed firewalls and virtual private network products for corporate users. McAfee's services are provided by McAfee's Anti-Virus Emergency Response Team (AVERT). AVERT augments McAfee's product offerings by identifying new viruses and deploying anti-virus solutions to our customers. McAfee customers are primarily corporate customers, including customers in the managed service market (such as, ASPs, and managed service providers, or MSPs).

Sniffer Technologies Product Group

Sniffer Technologies' products and services provide customers with network and application management solutions designed to maximize network availability and performance and system security. Sniffer Technologies' products capture data, monitor network traffic and collect key network statistics. Sniffer Technologies' products are also designed to optimize network and application performance and increase network reliability by uncovering and analyzing network problems and system vulnerabilities and recommending solutions to such problems, automatically and in real-time for mid-level and high-speed networks. Sniffer Technologies' products also proactively monitor and diagnose network and application-level problems on complex, multi-segment networks from centralized locations as well as troubleshooting high-speed telecommunications and Internet service provider networks. Sniffer Technologies' customers are primarily corporate customers, including customers in the managed service market.

Magic Solutions Product Group

Magic Solutions' products provide customers with a web-based set of tools to manage their customer support and problem management needs. Magic Solutions' product group consists of products that promote information sharing, facilitate workflow, and improve service delivery. Magic Solutions' products include the Magic Total Service Desk Suite, a 100% browser-based service desk and problem management solution. In addition, Magic Solutions' stand-alone products include Magic HelpDesk, Self Service Desk, Remote Desktop and Event Management. Magic Solutions' customers are primarily corporations.

McAfee.com Our Publicly Traded Subsidiary

McAfee.com is a security ASP delivering security applications software and related services through an Internet browser. The McAfee.com applications allow users to detect and eliminate viruses on their PCs, repair their PCs from damage caused by viruses, optimize their hard drives and update their PCs virus protection system with current software patches and upgrades. McAfee.com also offers customers access to McAfee.com Personal Firewall, McAfee.com Wireless Security Center and McAfee.com Internet Privacy Service.

Under the terms of our licensing agreement with McAfee.com, McAfee.com's business has historically been targeted exclusively at consumers. In March 2001, we entered into a reseller agreement with McAfee.com allowing it to expand its product offerings with McAfee.com for Business. McAfee.com for Business is a website serving the security needs for small and medium-sized businesses delivering managed applications services that allow businesses to provide anti-virus and firewall security for their desktop PCs.

As of December 31, 2001, we owned 36.0 million shares of McAfee.com Class B common stock, entitled to three votes per share and representing approximately 76% of McAfee.com's outstanding common stock and 90% of its total voting power.

Professional Services & Technical Support

As our products and computer networks become more complex, customers increasingly require greater professional assistance in the design, installation, configuration and implementation of their networks and acquired products. To meet these evolving customer needs, we have established Professional Services and Technical Support. Professional Services is focused on two service segments: Consulting Services and Education Services. Technical Support consists primarily of one program called PrimeSupport.

Consulting Services supports product integrations and deployment with an array of standardized and custom offerings. Consulting Services also offers other services ranging from proactive and emergency troubleshooting to network design, planning and simulation. We supplement our consulting service capabilities through the use of outside professional service providers, including system integrators. Our consulting services organization is organized around our three product groups.

Education Services represents the combined training organizations of Sniffer University, McAfee University and Magic University. Together, these training organizations offer customers an extensive curriculum of computer network technology courses, including protocol analysis and troubleshooting, security, help-desk and network management tools. Education Services provides public classes and customized on-site training at customer locations.

The PrimeSupport program provides our customers online and telephone-based technical support in an effort to ensure that our products are installed and working properly. To meet customers' varying needs, PrimeSupport offers a choice of the online KnowledgeCenter or the telephone-based Connect, Priority and Enterprise. All PrimeSupport programs include software updates and upgrades. PrimeSupport is available to all customers on a worldwide basis from various regional support centers.

PrimeSupport KnowledgeCenter Consists of a searchable, knowledge base of technical solutions and links to a variety of technical documents such as product FAQs and technical notes.

PrimeSupport Connect Provides toll-free telephone access to technical support during regular business hours and access to the online KnowledgeCenter.

PrimeSupport Priority Provides support for critical operations with priority, unlimited, toll-free telephone access to technical support 24 hours a day, 7 days a week and access to the online KnowledgeCenter.

PrimeSupport Enterprise Offers proactive, personalized service for the most business critical operations and includes an assigned technical support engineer from our elite Enterprise support team,

proactive support contact (telephone or email) with customer-defined frequency, election of five designated customer contacts and access to the online KnowledgeCenter.

NAI Labs

NAI Labs is our research and development organization dedicated to advanced network and information systems security technology. NAI Labs is actively conducting research in the areas of network security, cryptography, security infrastructure and other network security and network defense projects. NAI Labs has ongoing projects funded through DARPA (the U.S. Defense Advanced Research Projects Agency), Air Force, Navy, Army, NSA and other Department of Defense and U.S. government agencies. NAI Labs makes a number of its research prototypes available as open source software and support several open source community initiatives.

Product Licensing Model

We typically license our products to corporate and government customers on a subscription basis, for a period of two years or on a perpetual basis. Beginning in October 2000, we began selling our two-year subscription licenses with one-year (first year) of maintenance. Previously, our two-year subscription licenses included two years of maintenance. During the first year of the two-year subscription license, the customer has the option to purchase the second year of maintenance. The purchase price for the second year of maintenance is set at the time of purchase of the two-year subscription license. As the software licenses or maintenance contracts near expiration, we contact customers to renew their licenses or maintenance contracts, as applicable. We believe that providing the customer the option to purchase the second year of maintenance provides the customer greater flexibility in selecting the appropriate level of maintenance support. Electronic distribution of our products and upgrades allows us to offer upgrades and updates on a more regular basis than companies using traditional distribution methods.

Our licensing model also creates the opportunity for recurring revenue for us through the renewal of existing licenses. By offering two-year licenses as opposed to traditional perpetual licenses, we are also able to meet a lower initial cost threshold for customers with annual budgetary constraints. The renewal process also provides an opportunity to cross-sell new products and product lines to existing customers.

We also provide single user and corporate user licenses for our products under traditional perpetual licenses with product updates, upgrades and support available to customers under separate maintenance contracts. As compared to subscription licenses, sales of perpetual licenses typically result in significantly higher up-front revenue and lower recurring and future revenues as the sales price for upgrades and updates tends to be significantly lower than that of a perpetual license. We typically sell perpetual licenses in connection with sales of our hardware-based Sniffer and E-ppliance products where software is bundled with the hardware platform.

Hosted Applications Subscription Model

For our ASP or hosted products and services, customers essentially rent the use of our software. Because our ASP services are version-less, or self updating, customers using these services are assured of using the most recent version of the software application, eliminating the need to purchase product updates or upgrades. McAfee.com provides software using a related subscription model. Paid McAfee Clinic subscribers receive a time-based subscription to the service.

In 2001, the McAfee Product Group introduced its ASaP offerings. These are hosted products and services which provide the most up-to-date anti-virus software to corporate customers. These offerings include VirusScan ASaP, which provides anti-virus protection to desktops and file servers, VirusScreen ASaP, which screens e-mails to detect and quarantine viruses and infected attachments, and WebShield e500 ASaP, which combines a McAfee WebShield e-ppliance with hosted monitoring services that keep the e-ppliance continuously up to date to stop viruses at the Internet gateway before they enter an organization.

Sales and Marketing

To augment and capitalize upon our marketing efforts, our sales and marketing activities are directed primarily at large corporate and government customers, as well as to resellers, distributors and system integrators worldwide through the channels listed below.

United States Direct Sales

Our United States direct sales force, constituting the majority of our sales force, is organized by product group, with three separately focused sales organizations selling by product group. Each of these sales organizations consists of field sales representatives who are located regionally and outbound telesales representatives who actively market our individual product groups, focusing on small customers and transactions. Our corporate telesales representatives also respond to prospective customers who contact us as a result of a particular marketing program or after electronically evaluating one of our products. To augment our sales organization, our executives are involved with sales to many major accounts.

All of our United States sales representatives are responsible for developing new business as well as the renewal of our existing licenses. Prior to expiration of a license, a sales representative contacts the customer and encourages the customer to renew the expiring license and determines if the number of computers licensed needs adjustment and, additionally, markets new products and product groups to this existing customer.

International Sales

We have sales and support operations in Europe, Japan, Canada, Asia-Pacific and Latin America. In 2001, international revenues accounted for approximately 35% of our net revenues. In 2001, we announced our intention to significantly expand our international sales activities, and we hired new heads of our Asia-Pacific, European and Latin American operations.

We recently organized our international sales forces by region. In addition to the United States, the principal geographic regions are Europe, Japan, Canada, Asia-Pacific, and Latin America. Within these regions, sales forces are organized by country where appropriate. Our international direct sales force is organized by our three product groups when and where local demand and sales force considerations make this action advisable. Outside of the United States, each product group's sales force reports to the regional sales head.

Resellers and Distributors

To complement our direct sales efforts, we market many of our products through corporate resellers and distributors, and indirectly through retailers. We currently utilize corporate resellers, including ASAP Software, Corporate Software & Technology, Softmart, Software House International and Software Spectrum, which focus primarily on selling site licenses of our software to corporate customers.

Independent software distributors who currently market our products include Ingram Micro, Merisel America, MOCA and Tech Data. These distributors market our products primarily to large retailers, value added resellers, or VARs, and mail order companies. Through our authorized distributors, we sell our retail packaged products to several of the larger computer and software retailers in the United States, including Best Buy, Comp USA, Fry's, Office Depot, Office Max and Staples. Several members of our channel sales force work closely with our major reseller and distributor accounts to manage orders, promotions and selling activities.

Our top ten distributors in the United States typically account for between 38% and 43% of our net revenue each quarter. Our agreements with our distributors are not exclusive and may be terminated by either party without cause. Terminated distributors may not continue to represent our products. If one of our significant distributors terminated its relationship with us, we could experience a significant interruption in the distribution of our products.

Commencing January 1, 2001, we implemented a sell-through business model for distributors under which we recognize revenue on products sold through distributors at the time our distributors resell the products to their customers. Under this business model, our distributors are permitted to purchase software licenses at the same time they fill customer orders and to pay for hardware and retail products only when these products are resold to the distributors' customers. In addition, prior to the resale of our products, our distributors are permitted unlimited unconditional rights of return. After sale by the distributor to its customer, there is no right of return from the distributor to us with respect to such product, unless we approve the return from the final customer to the distributor.

Original Equipment Manufacturers

Original Equipment Manufacturers, or OEMs, license our products and bundle them with PC hardware or software. OEMs typically sublicense a single version of our products to end users who must contact us in order to receive their updates. We typically receive a per-copy royalty from our OEMs. Subject to limited exceptions, our OEM activities are conducted through McAfee.com.

Other Marketing Activities

Our principal means of marketing our products and services is through the Internet. In addition to the NAI.com website, each of our product groups and McAfee.com have their own individual websites. A number of these websites are localized to serve the various geographic regions in which we operate. Not only do each of these websites contain various marketing materials and information about our products, but website visitors may download and purchase products or obtain free trials of our products or trial subscriptions for hosted products and services. We also promote our products and services through advertising activities in trade publications and direct mail campaigns and strategic arrangements. In addition, we attend trade shows, sponsor conferences and publish a quarterly newsletter, which is mailed to existing and prospective customers.

Customers

We primarily market our products to large corporate and government customers directly through our direct sales organization and indirectly through resellers and distributors. A majority of our products are distributed indirectly through resellers and distributors. In the U.S., substantially all our indirect sales are through four major distributors. In Europe, substantially all indirect sales are made through five major distributors. During 2001, one customer, Ingram Micro, accounted for approximately 28% of our net revenue.

We primarily market our products directly to individual consumers through online distribution channels and indirectly through traditional distribution channels, such as retail stores. McAfee.com is responsible for online distribution of our products sold to individual consumers over the Internet or for Internet-based products and for the licensing of technology to OEMs for sale to individual consumers, subject to certain exceptions.

Product Development and Acquisition

We believe that our ability to maintain our competitiveness will depend in large part upon our ability to successfully enhance existing products, develop and acquire new products and develop and integrate acquired products. The market for computer software includes low barriers to entry, rapid technological change, and is highly competitive with respect to timely product introductions. As part of our growth strategy, we have made and expect to continue to make investments in complementary businesses, products and technologies.

In addition to developing new products, our internal development staff is also focused on developing upgrades and updates to existing products and modifying and enhancing any acquired products. Future upgrades and updates may include additional functionality, respond to user problems or address compatibility problems with new or changing operating systems and environments.

Excluding stock-based compensation charges, we expended \$142.1 million, \$171.1 million and \$148.2 million in 2001, 2000 and 1999, respectively, on research and development.

Manufacturing and Suppliers

Our manufacturing operations consist primarily of assembly, testing and quality control of materials, components, subassemblies and systems for our Sniffer hardware-based and E-ppliance products. We use a limited number of third-party manufacturers for these manufacturing operations. Reliance on third-party manufacturers involves a number of risks, including the lack of control over the manufacturing process and the potential absence or unavailability of adequate capacity. The loss of one of our third-party manufacturers could disrupt our business. Hardware-based products entail other risks, such as the unavailability of critical components which are supplied by a limited number of parties and greater obsolescence risks.

We have developed software-only versions of some of our Sniffer products. Purchasers of these Sniffer software products are required to already own, or purchase directly from the manufacturer or other vendors, the necessary hardware products, such as computer platforms and components. Customers may require that we continue to provide the necessary hardware products.

Competition

The markets for our products are intensely competitive and we expect competition to increase in the near-term. We believe that the principal competitive factors affecting the markets for our products include:

performance;

functionality;

quality;

customer support;

breadth of product group;

frequency of upgrades and updates;

integration of products;

manageability of products;

brand name recognition;

reputation; and

price.

We believe that we compete favorably against our competitors in each of these areas. However, some of our competitors have longer operating histories, greater name recognition, larger technical staffs, established relationships with hardware vendors and/or greater financial, technical and marketing resources. These factors may provide our competitors with an advantage in penetrating the market with their network security and management products.

Anti-Virus. Our principal competitor in the anti-virus market is the Norton Product Group of Symantec. Trend Micro remains the strongest competitor in the Asian anti-virus market, with Dr. Ahn's making recent inroads, particularly in Japan and Korea.

Network Security. Our principal competitors in the security market vary by product type. For firewalls, our principal competitors include CheckPoint, Symantec, and larger companies such as Cisco Systems and Microsoft. For intrusion detection products, we compete with Cisco Systems, Internet Security Systems and Symantec. The markets for encryption and virtual private network, or VPN, products are highly fragmented with numerous small and large vendors. VPN competitors include hardware and software vendors, including telecommunications companies and traditional networking suppliers.

Network Management. Our principal competitor in the network management market is Agilent. Other competitors include Acterna Corporation, Cisco Systems, Computer Associates, Compuware, Concord

Communications, DeskTalk Systems, GN Nettest, Network Instruments, Radcom Technologies, Shomiti Systems and WildPackets.

Help Desk. Our principal competitors in the help desk market are Computer Associates, FrontRange Solutions and Peregrine Systems.

Other Competitors. We also face competition from large software companies such as HP, Intel, Microsoft and Novell, which may offer network security and management products as enhancements to their operating systems.

Proprietary Technology

Our success depends significantly upon proprietary software technology. We rely on a combination of contractual rights, trademarks, trade secrets and copyrights to establish and protect proprietary rights to our software. However, these protections may be inadequate or competitors may independently develop technologies or products that are substantially equivalent or superior to our products. We do not typically obtain signed license agreements from customers who license products directly from us. Rather we include an electronic version of a shrink-wrap license in all of our electronically distributed software and a printed license in the box for our products. Since none of these licenses are signed by the licensee, many legal authorities believe that such licenses may not be enforceable under the laws of many states and foreign jurisdictions. In addition, the laws of some foreign countries either do not protect these rights at all or offer only limited protection for these rights. The steps taken by us to protect our proprietary software technology may be inadequate to deter misuse or theft of this technology. For example, we are aware that a substantial number of users of our anti-virus products have not paid any registration or license fees to us.

Network Associates/ McAfee.com Intercompany Agreements

For the purposes of defining our ongoing relationship with McAfee.com, our publicly traded subsidiary, we have entered into a number of ongoing agreements. These agreements are filed as exhibits to the public disclosure documents that we file with the Securities and Exchange Commission and are described briefly below. The description is subject in all respects to the terms of the actual agreements.

License Agreement. Under the terms of our license agreement:

Licensed Technology. Network Associates and McAfee.com granted to each other limited rights to each others' patents, copyrights, trademarks and trade secrets for use in defined markets. McAfee.com granted us worldwide, non-exclusive rights to McAfee.com's patents and exclusive rights to use McAfee.com's copyrights, trademarks and trade secrets to deliver products and services to enterprise customers and individual consumers by any means other than the Internet. Under the agreement, McAfee.com was granted worldwide, non-exclusive rights to our patents and exclusive rights to use our copyright, trademark and trade secret rights to create and deliver products and services directly or indirectly to individual consumers over the Internet or for Internet-based products. Each party is also permitted to create products derived from the technology licensed to it by the other. The creating party retains ownership of their newly derived products but these derived products are licensed to the other party subject to the terms of the license agreement.

Royalty Payments. In consideration for the rights granted under the license agreement, we are required to pay McAfee.com a flat quarterly royalty of \$250,000. In consideration for the rights granted by us to McAfee.com under the license agreement, McAfee.com is required to pay us a 7% royalty on revenues recognized from product and subscription sales that include our technology.

Limitations on Offered Products. During the term of the agreement, each party has agreed that it will not offer products incorporating third-party technology if those products are competitive with the products offered by the other party.

Indemnification. Under the agreement, each party has agreed to indemnify, defend and hold harmless the other for any losses incurred in connection with claims arising in the covered countries if the

technology licensed under the agreement violates the patent, copyright, trademark or trade secrets or other proprietary rights of a third party. Covered countries are those countries that are party to the Berne Convention for the Protection of Literary and Artistic Works, which include the U.S. and substantially all U.N. member nations.

Term and Termination. The license agreement will remain in effect perpetually, but may be terminated, among other circumstances, by the non-defaulting party, in the event of a material breach by the other party that remains uncured for 30 days following notice of the breach, subject to mandatory dispute resolution prior to the effectiveness of any proposed termination.

Reseller Agreements. In March 2001, we entered into reseller agreements with McAfee.com. Under these agreements, McAfee.com may resell our products to business customers, except in Japan, and in certain countries, we may resell McAfee.com products to OEMs and end-users directly or through ASPs.

Services Agreement. Under this agreement, we provide services relating to tax, insurance, employee benefits and administration, corporate record keeping and information technology. For these services, we charge a portion of the cost of our provision of the services to McAfee.com, including all related expenses, which is allocated based on headcount, plus a ten percent mark-up. In addition, from time to time, we may provide additional services, including legal and accounting services. The services agreement may be terminated either by McAfee.com on 30 days notice or by us when we cease to own a majority of the outstanding voting stock of McAfee.com.

Registration Rights Agreement. Under this agreement, we, or any transferee of at least 10% of our McAfee.com shares, can include such shares of McAfee.com common stock in any future registration of common stock made by McAfee.com, other than any registration statement relating to an acquisition or stock option plan. In addition, we or any transferee of at least 10% of our McAfee.com shares can request that McAfee.com file a registration statement for the public sale of such shares of McAfee.com stock.

Joint Cooperation Agreement. The joint cooperation and master services agreement with McAfee.com governs the provision of technology services among the parties. Under this agreement, our anti-virus emergency response team, or AVERT, will provide McAfee.com with research and solutions for virus events. The agreement also contains standard terms and conditions governing the provision of technology services from one party to the other under statements of work that may be negotiated from time to time. We pay McAfee.com a fee for these services in an amount equal to 10% of McAfee.com's total quarterly technology costs plus a 10% service charge.

Tax Sharing Agreement. Under this agreement, McAfee.com pays federal, state and local income tax liability amounts to us, determined on a pro forma basis as if McAfee.com filed its own separate income tax returns for each year. We will not reimburse McAfee.com for McAfee.com's or any other group member's use of their net operating loss or other tax benefits in any consolidated or combined return. However, McAfee.com will be able, during the term of the agreement, to take into account its past and future net operating loss and other tax attributes for purposes of computing its hypothetical separate income tax return liability payment to, or refund from, us.

The tax sharing agreement will terminate if McAfee.com is no longer eligible to join us in the filing of a consolidated federal income tax return. In the event of such termination, any net operating losses or other carryforward amounts would not be available to McAfee.com upon departure from the group. Under the agreement, McAfee.com will not be reimbursed for any such loss of tax benefits.

Indemnification and Voting Agreement. Under this agreement, except as contemplated below, we will indemnify and defend McAfee.com harmless for all losses related to any third party claims relating to events or circumstances arising out of any action or inaction of us, including our subsidiaries and officers and directors, on or prior to December 2, 1999, the date on which McAfee.com completed its initial public offering. Matters for which we are not obligated to indemnify McAfee.com include:

any obligations assumed by McAfee.com, or payments required to be made by McAfee.com, under its agreements with us;

any losses resulting from third party claims that are related to intellectual property developed by McAfee.com between August 20, 1999 and December 2, 2000;

any obligations incurred by McAfee.com in the ordinary course of business;

any losses resulting from third parties claims made against McAfee.com alleging infringement of intellectual property rights unknown as of the closing of McAfee.com's initial public offering; and

any losses resulting from third parties claims related to or arising from a material misstatement contained in or material omission from the prospectus or the registration statement for McAfee.com's initial public offering.

In the event of a claim relating to a product that includes components supplied by McAfee.com and components supplied by us, we have the right to determine whether and to what extent McAfee.com is entitled to indemnification, after reasonable consultation with McAfee.com.

For so long as we own at least 20% of McAfee.com's outstanding voting power, we must vote our shares of McAfee.com's capital stock in favor of the election of two independent directors. Additionally, if, as describ