MANAGEMENT DISCUSSION SECTION

Operator: Good day, and welcome everyone to the Guidance Software Third Quarter Earnings Results Conference Call. Today's call is being recorded. At this time for opening remarks and introduction I would like to turn the call over to the Director of Investor Relations, Mr. Bill Powell. Please go ahead, sir.

William Powell, Director of Investor Relations

Thanks. Hello, everyone, and thanks for joining us on Guidance Software's Third Quarter 2007 Earnings Conference Call. As your host for the call this afternoon I have the pleasure once again of introducing John Colbert, Chief Executive Officer of Guidance Software, and Frank Sansone, Chief Financial Officer of Guidance Software to present and discuss with you our financial performance and other operating metrics. Victor Limongelli, President of Guidance Software, is also present as he has been on our, excuse me, as he has been on all of our prior earnings calls and will be available during the Q&A session.

Before Frank and John begin I have a few administrative notes I'd like to go through for the benefit of our audience. First, we encourage everyone to review our financial results presented on a GAAP basis which are detailed in our press release issued today. And I understand that there were some difficulties with the provider in getting that release out, and it is now on the wires, so if you have not seen it, please go to your favorite news source, and pick that up.

These results may differ from results published by analysts or the media, featuring pro forma financial results, which may not be in conformity with regulatory standards. Second, I need to remind everyone that some of the information discussed on this call, including projections regarding revenue and operating results, may contain forward looking statements. These statements involve risks and uncertainties that may cause actual results to differ materially from those set forth in the statements. Additional information containing these risks and uncertainties, can be found in the company's most recent periodic reports filed with the U.S. Securities and Exchange Commission, including the company's most recent Annual Report on Form 10-K, and Guidance Software assumes no obligation to update any forward looking statements.

And finally, today's call will be divided into three parts. John will start the call with the review of our third quarter, what happened in the quarter, and what he sees on the horizon now that we're in the fourth quarter, and set to enter 2008. Frank will follow John with a detailed review and analysis of the numbers. And then, we'll open the call up to hear from you so that we can take your questions, and provide you with answers before ending our call today.

Now, my pleasure to turn the call over to John Colbert, CEO of Guidance Software. John?

John Colbert, Chief Executive Officer

Thanks, Bill. And thank you all for joining our Earnings Call, and for your continued interest in our company. I suspect that by now you've all had a chance to review our Press Release, and are aware that we have now reached pre-tax GAAP profitability. We beat our internal expectations and reached profitability, which came as a result of solid execution by both our sales functions, and our management focus on expense control.

These results denote our sixth consecutive quarter of record revenue, to which we owe a great deal of gratitude to our employees for coming together and working hard to support the sales of our product lines, increase the industry's acceptance of our Enterprise-based software product line, and achieve this significant milestone, pre-tax GAAP profitability.

We also owe appreciation to our customers. Many of our recent customers have permitted us to announce, via Press Release, the purchase of our Enterprise class products. This has truly helped with industry awareness and market acceptance of our products, which benefits the entire industry. Further, our law enforcement customer base continues to grow, which, as you know, greatly influences the legal acceptance of our solutions. Our Enterprise customer base is ever expanding, and now includes more than half of the Fortune 50, nearly half of the Fortune 100, and over 100 of the Fortune 500.

Those of you who listened to our previous calls may remember our continuing resolution disclosures regarding possible challenges to our third quarter civilian federal sales. We reported risks related to the lack of government appropriations bills for certain civilian federal agencies which we believe may have caused a bit of alarm. Certainly, that was not our intent. We were, actually somewhat adversely affected by the situation, but both the scalability of and the diversity provided by our multiple sources of revenue, led by higher commercial and international sales, offset the negative effects.

The continuing resolution issue has continued into the fourth quarter, which could challenge a small portion of our business. Frank will discuss that in more detail in his report. Despite the perceived risk to our third-quarter business, our employees pulled together and delivered growth and earnings. Another positive note in the federal space is the recent increased adoption of our Information Assurance Suite. We have high hopes for this technology and expect it to continue to gain traction and acceptance. Our third-quarter success resulted from government year-end business, increased EnCase forensics demand, execution from our sales and services team, development of new Enterprise customers, further Enterprise suite sales and infrastructure build-out from existing customers and, as expected, continued investigated infrastructure and eDiscovery product demand.

As you know, eDiscovery has been a key driver of our business this year. We continue to see growth in the eDiscovery markets and greater adoption of our eDiscovery solution and methodology, which focuses on obtaining just the relevant data and saving customers time and money. This approach to eDiscovery makes us more of a competitor to consulting firms rather than a competitor to other software providers or storage solution vendors. Though we have occasionally competed with certain archiving and document storage vendors. A recent article noting a litigation readiness survey by Contoural and Osterman Research revealed that more than 69% of companies surveyed are “largely unprepared” for responding to litigation and requests for electronically stored information. According to that survey, only 6% of the organizations surveyed stated that they could “immediately and confidently” handle eDiscovery requests and 51% do not yet have internal personnel that can competently handle an eDiscovery matter.

We, by the way, train a vast number of digital investigative experts, somewhere in the range of 4,500 a year, who naturally evolve to fill these competency deficiencies. You can easily see the value and strength this adds to our company’s mission and why our software is continuing to gain traction. This survey also specifically addressed the internal ability to provide court testimony regarding a collection of data, noting that most organizations do not have personnel who are still capable. That said, when somebody is going to testify in court they want to know that they are backed by solid practices and technology, which is why our history in the court systems has proven so valuable. These are our testament to the continued and expanded adoption of our eDiscovery technology by corporations.

With respect to other technologies designed to align – designed or aligned to solve eDiscovery matters we have found that certain opinion leaders in the industry are beginning to recognize and speak to the issue that archiving technologies are not practical solutions for eDiscovery which many archiving vendors currently promote. It’s been reported that these archiving solutions are unmanageable, constantly requiring maintenance. Most of these solutions deploy a massive index and we have heard that the index quickly becomes obsolete as it contains in depth data of deleted documents that causes significant problems in the eDiscovery collection process. A recent Forrester report mentioned that the "archive everything" approach such as archiving all email does not bring the relief and efficiencies that organizations expected. And the report suggests, in fact, that nothing could be further from the truth.

We believe that the proper approach to eDiscovery is, as we have designed it, a systematic ability to quickly locate and collect potentially relevant data without altering the data and without system down time that can then be processed by our software and ultimately hosted for review. The numbers of organizations that agree with this philosophy are expanding which is greatly beneficial to our business as our digital investigative platform coupled with our eDiscovery suite is, in our opinion, the best solution. We have also added the service to process and host data for those organizations who do not want to perform these functions internally. As an aside, Gartner has indicated that they intend to release their eDiscovery market scope later this month, which we are anxious to review as it will contain the latest information on the eDiscovery competitive landscape.

Closing out my commentary on eDiscovery. We believe that it is still our largest market opportunity and we'll continue to progress. The adoption of our eDiscovery software and methodology by influential organizations continues to rise and we believe the growing critical mass of customers using our solutions will lead others our direction. And just as our forensic product is the standard in law enforcement, our eDiscovery solution will emerge as the standard for eDiscovery.

Our services business, which incorporates training and professional services performed well in the third quarter. We continued to see a strong demand for training, which is another indicator of the progression of the digital investigative market. Our consulting business also continues to grow as we still maintained, to the best of our knowledge, the only consulting practice that specializes in Enterprise class digital investigative matters using our EnCase Enterprise software. Even though the option is open to other consulting firms, they avoid the use of our Enterprise software as it reduces the billable hours for a single consulting engagement. This leaves us in a very good position going forward.

Our 2007 mission was to increase the market's awareness and acceptance of our Enterprise solutions. The industry's general acceptance of our technology as a need-to-have would create a tipping point for our technology, propagating increased pipeline and decreased sales cycles and costs of sale. We made significant progress in this regard thus far, but there is still much room for improvement. For this reason, we intend to continue with the primary mission of increasing the market awareness and acceptance of our Enterprise solutions. There are still thousands of large organizations that do not own our Enterprise platform, and hundreds that do own it but have yet to purchase Suite. The two combined create a large immediate opportunity that we will continue to address to our established sales methods.

With eDiscovery as our largest market opportunity, we intend to further our development efforts and training and professional services efforts to better address this market's demands. We believe that we still have the best approach to eDiscovery, and plan to strengthen that position even more throughout 2008.

Our internal channel sales, I'm sorry international channel sales have increased over 2006, and signs indicate that the international market is primed for a strong Enterprise software growth. We plan to increase our international channel efforts to include training through authorized training partners in the EMEA, APAC and Latin America Regions.

Reseller training, localized customer education and localized services are significant challenges that we are addressing in 2008. Finally, I believe that we have the right combination of people, technology and infrastructure to lead us into and through 2008 and beyond. And now let me turn the call over to Frank for our financial discussion, Frank?

Frank Sansone, Chief Financial Officer

Thanks, John. The financial information presented on this call will be presented on a GAAP and non-GAAP basis. To reconcile between GAAP and non-GAAPs please see our third quarter press release.

I am proud to be able to report the results of the quarter, as this was our sixth consecutive quarter of record revenue, and the company achieved pre-tax GAAP and non-GAAP profitability for the first time as a public company. This was only accomplished through the hard work and dedication of the entire work force, and through our customers recognizing the value our products and services delivered to their organizations.

You've probably noticed that we have reported pre-tax non-GAAP and pre-tax GAAP numbers. We did this because this quarter's profitability coupled with our year end estimates, placed us in a distinctive tax position. On a tax basis, we are forecasting profitability as a result of certain timing differences between tax and financial reporting, including share based compensation and increases in deferred revenue. And as such, we are subject to a tax addition whereby we are incurring a $1 million tax revision in Q3, 2007, on approximately 600,000 of pre-tax income. This tax treatment on its face is not intuitive. However, GAAP requires such treatment, as we have been merged into tax profitability. Oddly enough, we expect to receive a tax benefit of approximately 500,000 in Q4, 2007 as a result of this tax position.

For the purposes of this call, and next call, we will be discussing the company net of this tax effect, unless otherwise noted. It bears mentioning that we do not expect this tax impact to continue into 2008. All in, this tax position is a good problem to have, as we have beat our internal expectation and have reached profitability.

For the third quarter of 2007, revenue was 20.3 million, up 5.5 million or 37% as compared to the third quarter of 2006. For the nine months ended, revenue was 56.4 million, which had exceeded the entirety of 2006 revenue. Non-GAAP pre-tax income increased to 1.6 million, or 7 cents per diluted share, where as last year in the same period, we reported a loss of 200,000 or 1 cent per share. Referencing our GAAP results, our pre-tax income was 621,000, or 3 cents per share as compared to pre-tax loss of 536,000 or 3 cents per share that we reported for the third quarter of 2006.

Share-based compensation for the third quarter of 2007 was 1 million, up approximately 600,000 year over year, and remaining flat sequentially. Product revenue increased from 9.2 million in Q3, 2006, to 11.6 million in Q3, 2007, a 26% increase. Enterprise license revenue grew from 5.7 million in Q3, 2006, to 8.3 million in Q3, 2007, a 46% increase.

As John mentioned, we did feel some effects of continuing resolution in our perpetual Enterprise license sales. Not only did we see delays in purchasing, we saw potential perpetual license transactions purchased on a term-based license structure. Historically the amount of term-based Enterprise license bookings have been immaterial. However, in Q3 2007 we booked approximately 1.4 million in term-based Enterprise licenses which will be primarily recognized over the next 12 months. These bookings are significantly higher than any previous quarter. As for Q4 2007, in our Federal business, certain civilian agencies remain under the continuing resolution. We do not expect this to have a significant affect on our results for the fourth quarter. As historically federal civilian Enterprise sales have been a small portion of our fourth quarter revenue. The growth at Enterprise license revenue was driven by sales of our Information Assurance Suite into our federal customers and Enterprise eDiscovery suite in our commercial customers. Specifically, in Q3 we sold 27 of our Enterprise product suites, nine of which were Information Assurance, and 10 of which were eDiscovery. For the same period last year we sold 17 suites of which eight were Information Assurance and seven were eDiscovery.

With the last earnings call we began to report Enterprise license transactions greater than 250,000 in recognized license value. In Q3 2007 we had eight sales that were greater than 250,000 in Enterprise license revenue as compared to five in Q3 2006, and nine in Q2 2007. These transactions have traditionally accounted for approximately half of our quarterly Enterprise license revenue. Services revenue increased from 5.6 million in Q3 2006 to 8.7 million in Q3 2007, a 55% increase. Third quarter is historically a seasonally slower period for our Services businesses, however, we saw growth of 37% in training, 32% in consulting and 93% in our maintenance revenues, as compared to Q3 2006. These areas are continuing to grow as the usage of our software expands into new and existing customers. On a non-GAAP basis we experienced a 2.2% increase in gross margin, and 7.9% increase in operating margin, as compared to Q3 2006, and a 3.1% increase in gross margin, an 8% increase in operating margin, as compared to Q2 2007. On a GAAP basis gross margin increased 1.6%, and operating margin increased 5.4%, as compared to Q3 2006, and a 3.1% increase in gross margin, an 8.9% increase in operating margin as compared to Q2 2007. As you can see, share-based compensation is having a significant impact on our GAAP margins.

On a non-GAAP basis, operating expenses remained flat at approximately 14 million, as compared to Q2 2007, although they were up 26% from 11 million in Q3 2006. On a GAAP basis, operating expenses increased approximately 200,000 as compared to Q2 2007, and 3.4 million as compared to Q3 2006. The most notable changes in operating expenses since Q2 2007 are as follows: Depreciation expense has increased 11% from Q2 2007 and 86% from Q3 2006 as a result of the investment we have made in our facilities over the past 12 months. We have one additional facility opening in Q4, at which point we believe we will have the infrastructure in place to cover our needs for the foreseeable future.

We have experienced increased costs in Q3 as a result of the implementation of Sarbanes-Oxley. In Q3 2007 we incurred approximately 500,000 in stocks implementation costs, as compared to approximately 200,000 in Q2 2007. Cash and investments increased from approximately 31.8 million at Q2 2007 to 35.1 million. This increase is the result of a seasonal increase in cash collection and exercises of employee stock options offset by purchases of property and equipment. For the quarter, we were cash flow from operations positive of 2.9 million and through the 9 months ended September 30, 2007, we are cash flows from operations positive of 5 million.

Deferred revenue increased 45% from 18.4 million at Q3 2006, to 26.6 million at Q3 2007, which is in line with our overall revenue growth. As compared to Q2 2007, deferred revenue increased 16% as a result of increased bookings of our forensic product, term-based Enterprise product and maintenance offerings. We saw our sales-weighted DSOs at 68 days in the third quarter, a six day increase from the 62 days we saw in the second quarter. Our DSOs typically fluctuate between 60 and 80 days.

Our international revenues remain consistent at approximately 25% of our total revenue. We have continued to see notable growth in our Europe and Asia revenue of approximately 78% for the 9 months of 2007 versus the first 9 months of 2006.

Now for an update on our fiscal 2007 expectations. As we have previously explained, our policy to provide annual guidance with quarterly updates if materially necessary. At this point with what we are seeing in the market in the demand for our products and services, we are tightening our annual revenue target to a range of approximately 74 to 76 million. Share-based compensation expectations are at an annual range of 4 million to 4.5 million. We have now adjusted our GAAP EPS estimate to include the net tax effects described earlier to a range of -$0.08 to -$0.16 per share. We adjusted the range of estimated by approximately two cents to account for these taxes. Our non-GAAP expectations including the net tax effects in a range of +$0.01 to +$0.09.

In our last call I mentioned we would provide preliminary 2008 guidance on this call. In this call I will be providing a fairly wide range of guidance for 2008 as we finish up our 2008 planning, and my expectation is that we will update our range on our Q4 earnings call in Q1 2008. Our expectations for 2008 are as follows. Our revenue range is expected to be between 94 to 99 million. Our EPS expectations on a GAAP basis are -$0.14 to -$0.01. On a non-GAAP basis our expectations are +$0.11 to +$0.24.

Our current diluted share count is approximately 22.7 million and our expectation is that this will increase approximately 300,000 shares per quarter throughout 2008. Additionally, I want to remind everyone of the seasonality in our revenue as has historically been reflected in our results. Our expectations are that there will be loss early in the year and revenue in Q1 will not exceed that of Q4 as a result of our historical seasonality. Please be mindful of this as you consider your analysis of our forecasted 2008 results.

Furthermore, with a growth in our business and infrastructure, we have begun to exceed the effectiveness of our current ERP System. As such we will be implementing a new Oracle ERP System in 2008. Guidance Software is focused on driving growth and driving the value from the leverage in our model. We believe we are taking reasonable approach in running the business and setting achievable financial expectations. We believe with our results thus far we are making headway toward achieving our objectives and look forward to continuing to provide positive shareholder value. Thank you. Bill?

William Powell, Director of Investor Relations

Thanks, Frank. Before we move into our question and answer period, first, we'd like to extend a warm welcome to Joshua Jabs of Roth Capital Partners, who initiated coverage on Guidance [inaudible] for us in the third quarter for the family of analysts who follow our company.

Next, I'd like to let our listeners know, we'll be presenting at three upcoming investor conferences over the next few weeks. As always, we're seeking the opportunities for you to get to know our company, and to meet with us on a more personal level.

On Thursday, November 15, at 1:15 Eastern Time, 10:15 Pacific, we'll be presenting at the UBS Global Technology and Services Conference at the Grand Hyatt, in New York, and we'll be meeting with investors outside of that event in New York City, Philadelphia and Delaware, between tomorrow and Friday, while we're on the East Coast.

After Thanksgiving, on Tuesday, November 27 at 1:30 Eastern Time, 10:30 a.m. Pacific, we'll be presenting at the Phoenician in Scottsdale, Arizona, at the Credit Suisse 2007 Annual Technology Conference, courtesy of Credit Suisse software analyst, Phil Winslow.

And, concluding our conference presentations for 2007, on Wednesday, December 5 at 1 p.m. Eastern Time, 10 a.m. Pacific, we'll be presenting at the Lehman Brothers Global Technology Conference at the Fairmont, in San Francisco, with a very special thanks to our covering analyst, Israel Hernandez.

Please be aware that the audio from each of these conference presentations will be broadcast live on the Internet, and will be accessible from the Investor portion of our website, which is investors.guidancesoftware.com.

With all that said, it's time to hear from you. We'd like to take your questions. Operator, would you please tell our listeners how to register their questions?

QUESTION AND ANSWER SECTION

Operator: Absolutely. [Operator Instructions] We'll pause for a moment to assemble the queue.

<A – William Powell>: All right, thanks, operator. Can you tell us who our first questioner is please and let's get them on the air?

Operator: First question will come from Philip Rueppel with Wachovia Securities.

<A – William Powell>: Great, thank you.

<Q – Philip Rueppel>: Great, thanks very much, and good afternoon, guys, a couple of things. One, could you talk about the pipeline? It looks like the number of big deals really increased, and I was wondering, and now that it sounds like you're becoming more reliant on that, could you talk about the pipeline, going forward, and especially, given the continuing resolution is still an issue, is there a log-jam there? And if that were ever to be resolved, would there be a potential increase in your pipeline? And then second of all, could just address financial services as an industry? Have you seen any push-outs or slowdowns there given the uncertainty in that industry? Thanks.

<A – John Colbert>: A lot of information in your question there. I may not cover it all in one answer here, so if I miss something by all means just let me know and we'll circle around and get the points that I miss. Starting with the pipeline, you know, as our business has been growing, obviously our pipelines has been growing along the way. We still feel good about the guidance that we provided for the year, and we don't have any real issues there, and I think you can see from the numbers that we're reporting that the larger deals are increasing. Somebody help me with another part of the question there.

<Q – Philip Rueppel>: Financial Services, is that any particular issues there?

<A – Frank Sansone>: Yes, Phil, it's Frank. We're not seeing any issues in financial services. Specifically, if you read a bunch of recent articles about our ability and our type of products being able to withstand economic downturns in certain areas and that as you know, usually bad news in a particular sector is good news for our company.

<A – John Colbert>: And at the end of the day we're definitely diversified across the industries. We're not dependent on any one group like financial our government, even though both of those are large market opportunities for us. Our software sells into just about any industry out there.

<Q – Philip Rueppel>: Okay, finally, and then I'll let others ask questions. Just on the competitive environment, you mentioned that there's a lot of archive-based solutions out there. Have you been able to replace any of those index-based solutions yet with your eDiscovery solution, or are you in any kind of bake-offs around that area? Thanks.

<A – John Colbert>: We've definitely been in those bake-offs in the past where we've won certain engagements. I think at the end of the day, we don't necessarily compete head-to-head with that technology, once we can get in and talk with the customer, because what they do and what we do are in fact distinctly different. The question is, if an organization only has X number of dollars to spend on an eDiscovery solution, where are they going to spend it? And we're finding more and more often that when we can get in front of the customers that those dollars are coming our way as opposed to going into e-mail archiving solutions, which six months ago or so, a couple of quarters ago, I may have had a different answer to that question. But I think over the past six months, the industry's acceptance of these e-mail archiving solutions has changed. And I think that as a result, a lot of business being won, where eDiscovery was purchased specifically to handle, I'm sorry, where these e-mail archiving solutions were purchased specifically to handle eDiscovery, and as I mentioned, they're beginning to fall down in a number of circumstances.

<Q – Philip Rueppel>: Great. That's helpful, thanks very much.

<A – William Powell>: Operator, who's next?

Operator: Joshua Jabs with Roth Capital

<Q – Joshua Jabs>: Hey, good afternoon.

<A – John Colbert>: How's it going?

<Q – Joshua Jabs>: There was a lot of talk recently down at the ICP Conference on Mobile Forensics. It looks like it's a pretty hot topic among local law enforcement agencies. Can you provide a little color on what you've seen in that market, and specifically with Neutrino?

<A – John Colbert>: Sure, absolutely. Mobile Forensics is something we jumped into in June when we released our Neutrino product. It certainly is a hot topic in the law enforcement community. As everybody here knows, we have a large and loyal forensic customer base that have been with us for many years, and we still provide the leading products for that community. We intend to continue that effort going forward, and Neutrino is a good example of that. Law enforcement officers are regularly challenged with the need to get information out of mobile devices, and the solutions in the industry were not really up to par, specifically on the ability to access the information in the phone without allowing it to reach out and connect to a cell tower, which is the technology that we developed. And as far as we know here, it's the first of its kind that actually works. So, with that said, it seems to be well received by the early adopters. It is a subscription product, so it will be a product with a revenue stream we'll have to build, but we are adding phones regularly, and have high hopes for the product.

<Q – Joshua Jabs>: Okay, great. And looking at gross margins that came in better than we had expected, not surprising given the strength and services. Do you see this level of gross margin as being sustainable?

<A – John Colbert>: You know, its part of where our targets are at, and where we would like to see them grow. The strength of our maintenance stream has been growing fairly rapidly. And the reason for that is, obviously the release of our suites in 2006, so it's increasing the overall maintenance renewal rates. So our expectation is that we have some potential growth areas in our margins still. However, as you know we have certain seasonality in our business. When you break down the overall margins we have a couple of areas that are very strong. Our Training business puts out very strong gross margins. And our, obviously, our maintenance and our software are great margins. And areas that we have some room for growth still is our professional services area. But overall I'd like to think that our margins can continue to expand and they're pretty good at where they are at right now as well.

<Q – Joshua Jabs>: Okay. And then in looking at guidance for next year. You mentioned the RTF upgrade. How, you know, is that expected to have a meaningful impact on expenses? And if so, can you quantify it?

<A – Frank Sansone>: My expectation right now is that it is in our current estimates that you see, that we just talked about. It will not start hitting the P&L obviously until it's up and operational and functioning which would not be until mid to late part of the year. And, you know, we hope that it does what we need it to do for us.

<Q – Joshua Jabs>: Okay. And then finally here. Guidance for Q4, you know, I'm looking at the numbers here. On and off basis it actually looks like at the high end of the guidance. The numbers are actually coming down from Q3 to Q4. Is there something unusual going into the guidance? Or something we should be looking for?

<A – Frank Sansone>: No. We feel good about our guidance and we are, you know, always going to be as conservative as we can about our forecasts and the way that we talk to the Street and our shareholders.

<Q – Joshua Jabs>: I guess maybe there are two approaches from a different direction. Q3, you know, is typically a good government spending quarter. But with, you know, a lot of the software vendors that's offset by Enterprise strength in Q4. And I'm just wondering if there was some one-time stuff going on in Q3 with – on the government side of that, that would kind of have that swapped for 2007.

<A – Frank Sansone>: No. I wouldn't see a swap in that. Q4 is typically our strongest commercial quarter. And our expectation is that, that will continue.

<Q – Joshua Jabs>: Okay. Great. Thanks, guys.

<A – Frank Sansone>: Thank you.

Operator: [Operator Instructions] We'll go next to Brian Essex with Morgan Stanley.

<Q – Brian Essex>: Hi. Good afternoon, guys.

<A – Frank Sansone>: How's it going, Brian?

<A – John Colbert>: Hey, Brian.

<Q – Brian Essex>: All right. Hey, I just wondered if we could dig in a little bit to the service and other line and was wondering if you could give any color behind maybe how much revenue there came off the balance sheet, how much is recurring, maybe related to maintenance and maybe how we can think about that going forward?

<A – Frank Sansone>: Brian, our Q will be filed today or tomorrow, which has all the details of those revenues and everything and what happened to them. I can give you a little feedback on that if I can pull up the page real quick, give me a second.

<Q – Brian Essex>: That or if you have even a sense of maintenance growth over last year just so we can get a handle on how to think about the recurring portion of that revenue.

<A – Frank Sansone>: Maintenance growth over last year was in the 93%, it's just continuing to grow our maintenance. Our renewals are strong and my expectation is that it will continue that growth going forward. As for the other areas of service in other, you've got the training business that is producing growth as well but obviously not as high as the maintenance goes, and our preferred professional services is fourth quarter is typically stronger than the third quarter, again because of seasonally slower services business time. Or if you look at our deferred revenue overall, we saw approximately 45% in our overall deferred revenue business and that is a good indicator for us going forward as to recognition of that.

<Q – Brian Essex>: Right and do you have a sense for in that deferred revenue base what the contract duration is in terms of what level of, what period of time that would amortize over?

<A – Frank Sansone>: Yes, so of the 26 plus million, 24 million of that is in short term so less than 12 months.

<Q – Brian Essex>: Okay and then maybe just one other question on guidance for next year. With the top end kind of at consensus, if you have a level of conservatism around 2008, I guess how much of your conservatism would be company specific versus general economics addition driven?

<A – Frank Sansone>: I think that it's a combination of both. As you know our Enterprise is becoming a bigger and bigger portion of our overall revenue and so we always want to be cautious when forecasting so that we are consistent and conservative with our expectations. Economically, we have been able to thrive in down economic times. As you know, our software is also used in internal investigations, etcetera, so when things are going bad, typically bad people do bad things. So our software is often used in, being able to search and collect information around that type of thing.

<A – John Colbert>: And just to add to that point, obviously we haven't finished this year, so it's a little early to have a laser focused on next year. So you know it's just a little early to have a good estimate as to what the economic conditions are going to look like next year, and you know direct on how the pipeline is going to shape up and those kind of things. But at this time, I think we're comfortable with the guidance that we've given and as Frank mentioned, we're going to be conservative and cautious in our approach.

<A – Victor Limongelli>: Brian, this is Victor Limongelli. One thing I want to add on that is that the litigation market which is a big driver of our, increasingly large driver of our business with the eDiscovery suite, is somewhat counter-cyclical so that when economic conditions are well, sure people are still suing each other, but when they are poor, they really sue each other.

<Q – Brian Essex>: All right, great. Thank you very much.

Operator: [Operator Instructions] We'll go next to Kevin Buttigieg with A. G. Edwards.

<A – John Colbert>: Hey, Kevin.

<Q – Kevin Buttigieg>: Hi, how are you?

<A – John Colbert>: Good.

<Q – Kevin Buttigieg>: I appreciated your discussion about competition against the archival products. I was wondering if you could talk a little bit about what you see in the competitive arena when it comes to the new range of data loss prevention products that are out there? Is that something where you are involved in any take-offs against those products or could you just generally discuss that environment?

<A – John Colbert>: Yes, I think I can definitely discuss that briefly. With respect to some of the data loss prevention companies out there, I think Vontu is probably is the most interest right now, especially being acquired by Symantec. We really haven't been going up against those companies lately. We seem to have a lot of activities there, the first part of this year, but that tapered off and any more we don't seem to be going head-to-head with those organizations for budget dollars or to solve specific business problems. I think the industry is now aware that there is a distinct difference between what they do and what we do.

<Q – Kevin Buttigieg>: Okay, great. And then for Frank, the – You know obviously you mentioned what the impact from the taxes is going to be on an EPS perspective. I was wondering if you would talk about, a little bit about that from a cash tax perspective?

<A – Frank Sansone>: Yes, so the unique portion of this is there will be zero cash taxes paid for this year. It's largely a financial reporting exercise. And as you know tax code is always fun.

<Q – Kevin Buttigieg>: Okay. Thanks very much.

Operator: And we'll go next with Vic Churamani with Lehman Brothers.

<Q – Vic Churamani>: Hi. Just a quick question on the guidance again. I don't mean to beat a dead horse, but you had a pretty solid third quarter and I guess the environment being in the current environment is supposed to be a catalyst for you guys, but at the same time Q4 guidance is a little shy of our estimates that we had here. Is there something that we're missing or is it just purely conservatism. And also when you look at '08 roughly at about 24% plus growth that's lower than what you guys exited in '07. Curious to get your thoughts on any product ramp or should we presume this also is just management conservatism at this point?

<A – Frank Sansone>: I think you can look at it as management conservatism. But if you take our top end of the range to the top end of the range of the guidance we provided, that's 30% growth which is something that we're comfortable with right now.

<Q – Vic Churamani>: And any thoughts on cash expectations for next year?

<A – Frank Sansone>: No. We haven't put any expectations out on next year yet.

<Q – Vic Churamani>: Thank you.

Operator: Okay. We'll go on to a follow-up for Brian Essex.

<Q – Brian Essex>: One more follow-up on I guess on the expense side. In looking how you had a little bit better performance than we expected [inaudible] some of that coming from sales and marketing. How are you doing head count wise based on your expansion efforts? And I guess if you could project a little bit into the forward quarters for employee head count, where do you kind of expect to be?

<A – Frank Sansone>: Yes. No problem. So at the end of September we had 348 full time employees. And that was an increase of seven from June 30. Our expectation is that we'll increase a little bit but nothing material over the next couple of quarters. As you know we made our major head count add at the beginning of this year and our expectations are that we'll add more needed, when needed in regards to growing our overall business.

<A – John Colbert>: And just to add to that, and to back that up a little bit. We do expect to continue hiring in the next year at about the same pace that we've been carrying through this year, with maybe a slight increase as we go into next year. But I think expenses have continued to moderate and we expect them to stay that way as we go forward here.

<Q – Brian Essex>: Okay but as we look back, recalling what happened in Q4, maybe some of the sales contracts kind of hit their accelerators, for lack of a better word, is the decline, even just in whole dollar amount sequentially, is that due to contracts or the sales mix or what caused that, I guess, sequential decline even though you had such robust growth?

<A – Frank Sansone>: The fourth quarter is largely variable as to which sales reps are selling which products and where it goes. As it stands right now there's always the risk that you could be paying someone at a higher commission rate because they're accelerators. However one of the things that we did going into this year is we kind of re-vamped our sales commission plan which is different from last year, and combined with that and obviously last year we had the significant sales force hiring.

<Q – Brian Essex>: Yes.

<A – Frank Sansone>: We don't have that same thing happening right now so our expectations are that Q4 should continue to moderate overall.

<Q – Brian Essex>: Okay, great. Thank you.

Operator: It appears that we have no further questions at this time. Mr. Powell, I would like to turn the conference back over to you for any additional or closing remarks.

William Powell, Director of Investor Relations

Great I think the best closing remark I can make is thank you very much for listening to us today and we look forward to speaking with you again next quarter. Have a good day and a great holiday. Good bye.

Operator: And that does conclude today's presentation. Thank you for you participation and have a great day.