SALESFORCE COM INC
Form 10-Q
November 25, 2009
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended October 31, 2009

OR

¨ **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
Commission File Number: 001-32224

salesforce.com, inc.

(Exact name of registrant as specified in its charter)

Delaware	**94-3320693**
(State or other jurisdiction of	**(IRS Employer**
incorporation or organization)	**Identification No.)**

The Landmark @ One Market, Suite 300

San Francisco, California 94105

(Address of principal executive offices)

Telephone Number (415) 901-7000

(Registrant s telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 (the Exchange Act) 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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

As of October 31, 2009, there were approximately 124.9 million shares of the Registrant s Common Stock outstanding.

Table of Contents

salesforce.com, inc.

INDEX

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

salesforce.com, inc.

Condensed Consolidated Balance Sheets

(in thousands)

	October 31, 2009 (unaudited)	January 31, 2009
Assets		
Current assets:		
Cash and cash equivalents	$ 242,888	$ 483,834
Short-term marketable securities	202,446	213,769
Accounts receivable, net	191,297	266,555
Deferred commissions	37,065	39,384
Deferred income taxes	26,992	31,900
Prepaid expenses and other current assets	62,227	33,115
Total current assets	762,915	1,068,557
Marketable securities, noncurrent	624,758	184,962
Fixed assets, net	95,598	77,027
Deferred commissions, noncurrent	17,077	17,699
Deferred income taxes, noncurrent	30,695	26,589
Capitalized software, net	32,780	29,989
Goodwill	45,402	44,872
Other assets, net	33,976	30,127
Total assets	$ 1,643,201	$ 1,479,822
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable	$ 15,617	$ 16,379
Accrued expenses and other current liabilities	174,309	163,205
Income taxes payable	3,050	3,619
Deferred revenue	533,502	583,763
Total current liabilities	726,478	766,966
Income taxes payable, noncurrent	19,298	12,490
Long-term lease liabilities and other	14,952	7,616
Deferred revenue, noncurrent	11,933	10,263
Total liabilities	772,661	797,335
salesforce.com stockholders equity:		
Common stock	125	123
Additional paid-in capital	775,838	648,724
Accumulated other comprehensive loss	(3,239)	(2,905)
Retained earnings	86,167	25,842

Total stockholders equity controlling interest	858,891	671,784
Total stockholders equity noncontrolling interest	11,649	10,703
Total stockholders equity	870,540	682,487
Total liabilities and stockholders equity	$ 1,643,201	$ 1,479,822

See accompanying Notes to Condensed Consolidated Financial Statements.

Table of Contents

salesforce.com, inc.

Condensed Consolidated Statements of Operations

(in thousands, except per share data)

(unaudited)

	Three months ended October 31, 2009	Three months ended October 31, 2008	Nine months ended October 31, 2009	Nine months ended October 31, 2008
Revenues:				
Subscription and support	$ 306,870	$ 253,403	$ 882,078	$ 718,464
Professional services and other	23,679	23,084	69,456	68,722
Total revenues	330,549	276,487	951,534	787,186
Cost of revenues (1):				
Subscription and support	40,745	32,424	116,744	91,802
Professional services and other	24,825	23,924	73,122	69,935
Total cost of revenues	65,570	56,348	189,866	161,737
Gross profit	264,979	220,139	761,668	625,449
Operating expenses (1):				
Research and development	32,763	26,270	95,450	70,070
Marketing and sales	152,166	136,452	436,647	389,930
General and administrative	49,909	41,284	139,818	117,797
Total operating expenses	234,838	204,006	671,915	577,797
Income from operations	30,141	16,133	89,753	47,652
Interest, net	7,211	3,840	18,987	17,270
Other income (expense)	(336)	534	(1,037)	(1,069)
Income before provision for income taxes and noncontrolling interest	37,016	20,507	107,703	63,853
Provision for income taxes	(15,573)	(8,824)	(45,426)	(29,693)
Consolidated net income	21,443	11,683	62,277	34,160
Less: Net income attributable to noncontrolling interest	(752)	(1,559)	(1,952)	(4,485)
Net income attributable to salesforce.com	$ 20,691	$ 10,124	$ 60,325	$ 29,675
Earnings per share - basic and diluted:				
Basic net income per share attributable to salesforce.com common shareholders	$ 0.17	$ 0.08	$ 0.49	$ 0.25
Diluted net income per share attributable to salesforce.com common shareholders	$ 0.16	$ 0.08	$ 0.48	$ 0.24
Shares used in computing basic net income per share	124,561	121,635	123,871	120,759
Shares used in computing diluted net income per share	128,596	125,133	126,993	125,173

(1) Amounts include stock-based expenses, as follows:

Cost of revenues	$ 2,995	$ 2,817	$ 9,322	$ 8,149
Research and development	2,707	2,494	8,741	6,852

Marketing and sales	9,055	9,235	28,314	26,105
General and administrative	5,650	4,730	16,570	15,119

See accompanying Notes to Condensed Consolidated Financial Statements

Table of Contents

salesforce.com, inc.

Condensed Consolidated Statements of Cash Flows

(in thousands)

(unaudited)

	Three months ended October 31, 2009	Three months ended October 31, 2008	Nine months ended October 31, 2009	Nine months ended October 31, 2008
Operating activities:				
Consolidated net income	$ 21,443	$ 11,683	$ 62,277	$ 34,160
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	13,601	7,910	37,890	24,938
Amortization of deferred commissions	15,698	14,784	45,959	43,414
Expenses related to stock-based awards	20,407	19,276	62,947	56,225
Excess tax benefits from employee stock plans	(7,401)	(17,706)	(32,536)	(42,247)
Loss on securities		2,052		2,052
Changes in assets and liabilities:				
Accounts receivable, net	(22,515)	(9,002)	75,355	64,077
Deferred commissions	(18,013)	(13,682)	(43,018)	(40,564)
Prepaid expenses and other current assets	(12,892)	(6,313)	(14,711)	(12,406)
Other assets	(506)	(2,943)	(624)	(429)
Accounts payable	2,228	6,621	(762)	12,951
Accrued expenses and other current liabilities	27,045	14,733	35,165	23,497
Deferred revenue	(3,575)	(10,292)	(48,591)	(11,640)
Net cash provided by operating activities	35,520	17,121	179,351	154,028
Investing activities:				
Purchase of subsidiary stock		(16,693)		(16,693)
Business combinations, net of cash acquired	(4,500)	(27,344)	(4,500)	(27,344)
Purchase of marketable securities	(218,056)	(123,476)	(980,519)	(323,415)
Sales of marketable securities	121,413	26,656	438,679	84,187
Maturities of marketable securities	55,400	66,557	119,566	200,387
Capital expenditures	(14,089)	(11,614)	(46,845)	(48,827)
Net cash used in investing activities	(59,832)	(85,914)	(473,619)	(131,705)
Financing activities:				
Proceeds from the exercise of stock options	18,559	6,595	32,866	40,605
Excess tax benefits from employee stock plans	7,401	17,706	32,536	42,247
Principal payments on capital lease obligations	(2,398)	(286)	(5,904)	(291)
Net cash provided by financing activities	23,562	24,015	59,498	82,561
Effect of exchange rate changes	(2,531)	49	(6,176)	(1,665)
Net (decrease) increase in cash and cash equivalents	(3,281)	(44,729)	(240,946)	103,219
Cash and cash equivalents, beginning of period	246,169	427,043	483,834	279,095

Cash and cash equivalents, end of period	$ 242,888	$ 382,314	$ 242,888	$ 382,314
Supplemental cash flow disclosure:				
Cash paid during the period for:				
Income taxes, net of tax refunds	$ 6,446	$ 1,894	$ 27,520	$ 7,309
Interest	$ 292	$ 47	$ 793	$ 47
Non-cash financing and investing activities				
Fixed assets acquired under capital leases	$ 3,105	$ 6,406	$ 17,897	$ 6,406

See accompanying Notes to Condensed Consolidated Financial Statements.

5

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements

1. Summary of Business and Significant Accounting Policies

Description of Business

Salesforce.com, inc. (the Company) provides a comprehensive customer relationship management (CRM) service to businesses of all sizes and industries worldwide and provides a technology platform for customers and developers to build and run applications. The Company offers its services on a subscription basis.

Fiscal Year

The Company s fiscal year ends on January 31. References to fiscal 2010, for example, refer to the fiscal year ending January 31, 2010.

Basis of Presentation

The accompanying condensed consolidated balance sheet as of October 31, 2009 and the condensed consolidated statements of operations and the condensed consolidated statements of cash flows for the three and nine months ended October 31, 2009 and 2008, respectively, are unaudited. The condensed consolidated balance sheet data as of January 31, 2009 was derived from the audited consolidated financial statements which are included in the Company s Form 10-K for the fiscal year ended January 31, 2009, which was filed with the Securities and Exchange Commission (the SEC) on March 9, 2009. The accompanying statements should be read in conjunction with the audited consolidated financial statements and related notes contained in the Company s fiscal 2009 Form 10-K.

The accompanying condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles, or U.S. GAAP, for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the financial information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of the Company s management, the unaudited condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements in the Form 10-K, except as described below, and include all adjustments necessary for the fair presentation of the Company s statement of financial position as of October 31, 2009, and its results of operations and its cash flows for the three and nine months ended October 31, 2009 and 2008. All adjustments are of a normal recurring nature. The results for the three and nine months ended October 31, 2009 are not necessarily indicative of the results to be expected for any subsequent quarter or for the fiscal year ending January 31, 2010.

Effective February 1, 2009, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 160, *Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51* (SFAS 160) now codified in Accounting Standards Codification (ASC) Topic 810, *Consolidation* (ASC 810). ASC 810 amends Accounting Research Bulletin No. 51, *Consolidated Financial Statements*, to establish accounting and reporting standards for any noncontrolling interest in a subsidiary (and for the deconsolidation of a subsidiary). ASC 810 clarifies that a noncontrolling interest in a subsidiary should be reported as a component of equity in the consolidated financial statements and requires disclosure, on the face of the consolidated statements of income, of the amounts of the consolidated net income attributable to the parent and to the noncontrolling interests.

Accordingly, noncontrolling interest of $11.6 million and $10.7 million as of October 31, 2009 and January 31, 2009, respectively, have been reflected in stockholders equity.

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions in the Company s consolidated financial statements and notes thereto.

Significant estimates and assumptions made by management include the determination of the provision for income taxes, whether an other-than-temporary decline has occurred in the fair value of certain investments in marketable securities, and the fair value of stock awards issued. Actual results could differ from those estimates.

Principles of Consolidation

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

The Company holds a controlling interest in Kabushiki Kaisha salesforce.com (Salesforce Japan), a Japanese joint venture. As of October 31, 2009, the Company owned a 72 percent interest in the joint venture.

Given the Company s controlling interest in the joint venture, the accounts of the joint venture have been consolidated with the accounts of the Company, and a noncontrolling interest has been recorded for the noncontrolling investors interests in the net assets and operations of the joint venture to the extent of noncontrolling investors individual investments.

Segments

The Company operates in one segment.

Foreign Currency Translation

The functional currency of the Company s major foreign subsidiaries is generally the local currency. Adjustments resulting from translating foreign functional currency financial statements into U.S. dollars are recorded as part of a separate component of stockholders equity. Foreign currency transaction gains and losses are included in net income for the period. All assets and liabilities denominated in a foreign currency are translated into U.S. dollars at the exchange rate on the balance sheet date. Revenues and expenses are translated at the average exchange rate during the period. Equity transactions are translated using historical exchange rates.

Concentrations of Credit Risk and Significant Customers

The Company s financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents, marketable securities and trade accounts receivable. Although the Company deposits its cash with multiple financial institutions, its deposits, at times, may exceed federally insured limits. Collateral is not required for accounts receivable. The Company maintains an allowance for doubtful accounts receivable balances. The allowance is based upon historical loss patterns, the number of days that billings are past due and an evaluation of the potential risk of loss associated with delinquent accounts.

One customer accounted for more than 5 percent of accounts receivable at October 31, 2009 and no customer accounted for more than 5 percent at January 31, 2009. No single customer accounted for 5 percent or more of total revenue in the three and nine months ended October 31, 2009 and 2008, respectively.

As of October 31, 2009 and January 31, 2009, assets located outside the Americas were 15 percent and 14 percent of total assets, respectively.

7

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

Revenues by geographical region are as follows (in thousands):

	Three months ended October 31,		Nine months ended October 31,	
	2009	2008	2009	2008
Americas	$ 232,802	$ 200,143	$ 679,460	$ 567,076
Europe	60,761	48,076	168,355	142,597
Asia Pacific	36,986	28,268	103,719	77,513
	$ 330,549	$ 276,487	$ 951,534	$ 787,186

Cash and Cash Equivalents

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. Cash and cash equivalents are at fair value.

Marketable Securities

Management determines the appropriate classification of investments in marketable securities at the time of purchase in accordance with SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, now codified into ASC Topic 320, *Investments* (ASC 320), and reevaluates such determination at each balance sheet date. Except for the money market mutual fund described below, securities are classified as available for sale and are carried at fair value, with the unrealized gains and losses, net of tax, reported as a separate component of stockholders equity. Fair value is determined based on quoted market rates when observable or utilizing data points that are observable such as quoted prices, interest rates and yield curves. Declines in fair value judged to be other-than temporary on securities available for sale are included as a component of interest, net. The cost of securities sold is based on the specific-identification method. Interest on securities classified as available for sale is also included as a component of interest, net. In order to determine whether a decline in value is other-than temporary, the Company evaluates, among other factors, the duration and extent to which the fair value has been less than the carrying value, the Company s financial condition and business outlook, including key operational and cash flow metrics, current market conditions and the Company s intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in fair market value.

Fair Value Measurement

In accordance with SFAS No. 157, *Fair Value Measurement* (SFAS 157), now codified into ASC Topic 820, *Fair Value Measurements and Disclosures* (ASC 820), the Company measures its cash equivalents, marketable securities and foreign currency derivative contracts at fair value. A majority of the Company s cash equivalents and its marketable securities are classified within Level 1 or Level 2, which are described below. This is because the Company s cash equivalents and marketable securities are valued using quoted market prices or alternative pricing sources and models utilizing market observable inputs.

A portion of the Company s money market mutual funds are classified within Level 3, described below, because they are invested in The Reserve Primary Fund (The Reserve Fund). At October 31, 2009 the Company s investment portfolio included $7.4 million invested in The Reserve Fund with an estimated fair value of $6.2 million. During the year ended January 31, 2009, the Company recorded a $1.2 million loss related to this decline in fair value that is considered other-than-temporary.

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

On February 26, 2009, The Reserve Fund announced its decision to initially set aside $3.5 billion in a special reserve under the plan of liquidation, to cover potential liabilities for damages and associated expenses related to lawsuits and regulatory actions against the fund. The special reserve may be increased or decreased as further information becomes available. As a result, pursuant to the liquidation plan, interim distributions will continue to be made up to 91.72 percent, unless The Reserve Fund determines a need to increase the special reserve. Amounts in the special reserve will be distributed to shareholders once claims, if any are successful, and the related expenses have been paid or set aside for payment. The determination of the total redemption to the Company is subject to the distribution available to all investors of the fund. While the Company believes it has the right to recover its entire remaining investment, the Company cannot predict the amount it will ultimately receive.

The Company s foreign currency derivative contracts are classified within Level 2 as the valuation inputs are based on quoted prices and market observable data of similar instruments in inactive markets.

ASC 820 establishes a three-tier value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:

Level 1. Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2. Include other inputs that are directly or indirectly observable in the marketplace.

Level 3. Unobservable inputs which are supported by little or no market activity.

The Company conducted its fair value assessment of The Reserve Fund using Level 3 inputs. Management has reviewed the Reserve s underlying securities portfolio which is substantially comprised of discount notes, certificates of deposit and commercial paper issued by highly-rated institutions. Management also evaluated the fair value of its ownership in The Reserve Fund, considering risk of extended timing and other factors. The assumption of timing for the actual repayment of the Company s ownership from The Reserve Fund is inherently subjective and involves significant management judgment. As a result, the Company classified its ownership in The Reserve Fund within Level 3 of the fair value hierarchy.

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

The following table presents information about the Company s assets that are measured at fair value on a recurring basis as of October 31, 2009 and indicates the fair value hierarchy of the valuation (in thousands):

Description	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of October 31, 2009
Cash equivalents (1):				
Government obligations	$ 3,494	$	$	$ 3,494
Time deposits	1,028			1,028
Money market mutual funds	135,201			135,201
Corporate notes and obligations		17,993		17,993
Marketable securities:				
Corporate notes and obligations		544,165		544,165
U.S. treasury securities	91,950			91,950
U.S. agency obligations		101,638		101,638
Mortgaged backed securities		56,582		56,582
Collateralized mortgage obligations		24,145		24,145
Municipal securities		2,526		2,526
Money market mutual fund			6,198	6,198
Foreign currency derivative contracts (2)		578		578
Total Assets	$ 231,673	$ 747,627	$ 6,198	$ 985,498
Liabilities				
Foreign currency derivative contracts (3)	$	$ 65	$	$ 65
Total Liabilities	$	$ 65	$	$ 65

(1) Included in cash and cash equivalents in the accompanying Condensed Consolidated Balance Sheet as of October 31, 2009, in addition to $85,172 of cash.
(2) Included in prepaid expenses and other current assets in the accompanying Condensed Consolidated Balance Sheet as of October 31, 2009.
(3) Included in accrued expenses and other current liabilities in the accompanying Condensed Consolidated Balance Sheet as of October 31, 2009.

The following table presents the Company s assets measured at fair value using significant unobservable inputs (Level 3) at October 31, 2009. This asset consists of the Company s investment in The Reserve Fund (in thousands):

Balance at February 1, 2009	$ 18,294
Redemptions	(12,096)
Balance at October 31, 2009	$ 6,198

10

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

The following table presents information about the Company s assets that are measured at fair value on a recurring basis as of January 31, 2009 and indicates the fair value hierarchy of the valuation (in thousands):

Description	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of January 31, 2009
Cash equivalents (1):				
Time deposits	$ 402	$	$	$ 402
Money market mutual funds	279,246			279,246
Corporate notes and obligations		7,990		7,990
U.S. agency obligations		87,852		87,852
Marketable securities:				
Corporate notes and obligations		215,140		215,140
U.S. agency obligations		165,297		165,297
Money market mutual funds			18,294	18,294
Foreign currency derivative contracts (2)		1,054		1,054
Total Assets	$ 279,648	$ 477,333	$ 18,294	$ 775,275
Liabilities				
Foreign currency derivative contracts (3)	$	$ 2,058	$	$ 2,058
Total liabilities	$	$ 2,058	$	$ 2,058

(1) Included in cash and cash equivalents in the accompanying Condensed Consolidated Balance Sheet as of January 31, 2009, in addition to $108,344 of cash.
(2) Included in prepaid expenses and other current assets in the accompanying Condensed Consolidated Balance Sheet as of January 31, 2009.
(3) Included in accrued expenses and other current liabilities in the accompanying Condensed Consolidated Balance Sheet as of January 31, 2009.

For the Company s investments in privately-held companies, management evaluated financial results, earnings trends, and subsequent financing of these companies, as well as general market conditions, to determine fair value. The following table presents information about the Company s assets that are measured at fair value on a non-recurring basis as of October 31, 2009 and the losses recorded during the three and nine months ended October 31, 2009 on these assets (in thousands):

Description	Net Carrying Value as of October 31, 2009	Significant Unobservable Inputs (Level 3)	Total Losses for Three Months Ended October 31, 2009	Total Losses for Nine Months Ended October 31, 2009
Investments in privately-held companies	$ 6,313	$ 6,313	$ (87)	$ (487)
Total Assets	$ 6,313	$ 6,313	$ (87)	$ (487)

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

The following table presents information about the Company s assets that are measured at fair value on a non-recurring basis as of January 31, 2009 and the losses recorded during the year ended January 31, 2009 on these assets (in thousands):

Description	Net Carrying Value as of January 31, 2009	Significant Unobservable Inputs (Level 3)	Total Losses for Year Ended January 31, 2009
Investments in privately-held companies	$ 2,400	$ 2,400	$ (100)
Total Assets	$ 2,400	$ 2,400	$ (100)

Derivative Financial Instruments

The Company enters into foreign currency derivative contracts with financial institutions to reduce the risk that its cash flows and earnings will be adversely affected by foreign currency exchange rate fluctuations. The Company uses foreign currency derivative contracts to minimize the Company s exposure of balances denominated in Australian dollars, British pounds, Euros, Japanese yen, Singapore dollars and Swiss francs. The Company s program is not designated for trading or speculative purposes. As of October 31, 2009 the foreign currency derivative contracts that were not settled are recorded at fair value on the condensed consolidated balance sheet.

The Company s foreign currency derivative contracts, which are not designated as hedging instruments under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133), now codified into ASC Topic 815, *Derivatives and Hedging* (ASC 815), are used to reduce the exchange rate risk associated primarily with intercompany receivables and payables. Foreign currency derivative contracts are marked-to-market at the end of each reporting period with gains and losses recognized as other income (expense) to offset the gains or losses resulting from the settlement or remeasurement of the underlying foreign currency denominated receivables and payables. While the contract or notional amount is often used to express the volume of foreign currency derivative contracts, the amounts potentially subject to credit risk are generally limited to the amounts, if any, by which the counterparties obligations under the agreements exceed the obligations of the Company to the counterparties.

Details on outstanding foreign currency derivative contracts related primarily to intercompany receivables and payables are presented below (in thousands):

	October 31, 2009	January 31, 2009
Notional amount of foreign currency derivative contracts	$ 69,104	$ 158,704
Fair value of foreign currency derivative contracts	513	(1,004)

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

Effective February 1, 2009, the Company adopted the disclosure requirements of SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities an Amendment of FASB Statement No. 133* (SFAS 161), now codified into ASC 815. At October 31, 2009 and January 31, 2009, the fair values of outstanding derivative instruments are summarized below (in thousands):

		Fair Value of Derivative Instruments	
	Balance Sheet Location	**As of October 31, 2009**	**As of January 31, 2009**
Derivative Assets			
Derivatives not designated as hedging instruments under ASC 815:			
Foreign currency derivative contracts	Prepaid expenses and other current assets	$ 578	$ 1,054
Derivative Liabilities			
Derivatives not designated as hedging instruments under ASC 815:			
Foreign currency derivative contracts	Accrued expenses and other current liabilities	$ 65	$ 2,058

The effect of the derivative instruments not designated as hedging instruments on the Condensed Statements of Operations for the three and nine months ended October 31, 2009 and October 31, 2008, respectively are summarized below (in thousands):

Derivatives Not Designated as Hedging Instruments under ASC 815	**Gains Recognized in Income on Derivative Instruments**		
		Three months ended October 31,	
	Location	**2009**	**2008**
Foreign currency derivative contracts	Other income (expense)	$ 513	$ 293

Derivatives Not Designated as Hedging Instruments under ASC 815	**Gains (Losses) Recognized in Income on Derivative Instruments**		
		Nine months ended October 31,	
	Location	**2009**	**2008**
Foreign currency derivative contracts	Other income (expense)	$ (151)	$ 293

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

Interest, net

The components of Interest, net are presented below (in thousands):

	Three months ended October 31, 2009	Three months ended October 31, 2008	Nine months ended October 31, 2009	Nine months ended October 31, 2008
Interest income, net	$ 5,529	$ 5,920	$ 15,380	$ 19,541
Realized gains	1,951	48	5,137	345
Realized losses	(269)	(2,128)	(1,530)	(2,616)
	$ 7,211	$ 3,840	$ 18,987	$ 17,270

Comprehensive Income

Comprehensive income consists of net income and accumulated other comprehensive income, which includes certain changes in equity that are excluded from net income. Specifically, cumulative foreign currency translation adjustments and unrealized gains and losses on marketable securities, net of tax, are included in accumulated other comprehensive income. Accumulated other comprehensive loss has been reflected in stockholders equity.

Comprehensive income consisted of the following (in thousands):

	Three months ended October 31, 2009	Three months ended October 31, 2008	Nine months ended October 31, 2009	Nine months ended October 31, 2008
Consolidated net income	$ 21,443	$ 11,683	$ 62,277	$ 34,160
Less: net income attributable to noncontrolling interest	(752)	(1,559)	(1,952)	(4,485)
Translation and other adjustments	(2,947)	1,947	(6,532)	1,766
Unrealized gain (loss) on marketable securities	1,724	(5,351)	6,198	(7,082)
Comprehensive income attributable to salesforce.com	$ 19,468	$ 6,720	$ 59,991	$ 24,359

The components of accumulated other comprehensive loss were as follows (in thousands):

	October 31, 2009	January 31, 2009
Foreign currency translation and other adjustments	$ (10,780)	$ (3,957)
Net unrealized gain on marketable securities	7,541	1,052
	$ (3,239)	$ (2,905)

Net Income Per Share

Basic net income per share attributable to salesforce.com is computed by dividing net income attributable to salesforce.com by the weighted-average number of common shares outstanding for the fiscal period. Diluted net income per share attributable to salesforce.com is computed giving effect to all potential dilutive common stock, including options and restricted stock units. The dilutive effect of outstanding awards is reflected in diluted earnings per share by application of the treasury stock method.

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

A reconciliation of the denominator used in the calculation of basic and diluted net income per share attributable to salesforce.com is as follows (in thousands):

	Three months ended October 31,		Nine months ended October 31,	
	2009	2008	2009	2008
Numerator:				
Net income attributable to salesforce.com	$ 20,691	$ 10,124	$ 60,325	$ 29,675
Denominator:				
Weighted-average shares outstanding for basic earnings per share	124,561	121,635	123,871	120,759
Effect of dilutive securities:				
Employee stock awards	4,035	3,498	3,122	4,414
Adjusted weighted-average shares outstanding and assumed conversions for diluted earnings per share	128,596	125,133	126,993	125,173

The following were excluded from the computation of diluted shares outstanding as they would have had an anti-dilutive impact. The dilutive securities are excluded when, for example, their exercise prices, unrecognized compensation and tax benefits are greater than the average fair values of the Company s common stock (in thousands).

	Three months ended October 31,		Nine months ended October 31,	
	2009	2008	2009	2008
Stock awards	3,751	4,440	4,611	3,328

Income Taxes

The Company uses the liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on temporary differences between the financial statement and tax basis of assets and liabilities and net operating loss and credit carry forwards using enacted tax rates in effect for the year in which the differences are expected to reverse. 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. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts more likely than not expected to be realized.

The total income tax benefit recognized in the accompanying condensed consolidated statements of operations related to SFAS No. 123R, *Share-Based Payment* (SFAS 123R), now codified into ASC Topic 718, *Compensation Stock Compensation* (ASC 718) was $22.8 million and $20.1 million for the nine months ended October 31, 2009 and 2008, respectively.

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

A reconciliation of income taxes at the statutory federal income tax rate to the provision for income taxes included in the accompanying condensed consolidated statements of operations is as follows (in thousands):

	Nine months ended October 31,	
	2009	2008
U.S. federal taxes at statutory rate	$ 37,696	$ 22,349
State, net of the federal benefit	6,220	3,564
Foreign taxes in excess of the U.S. statutory rate	4,121	3,156
Tax credits	(4,766)	(3,780)
Impact of tax law change	2,502	
Domestic manufacturing deduction	(1,443)	
Other, net	1,096	4,404
	$ 45,426	$ 29,693

The Company records liabilities related to uncertain tax positions in accordance with the provisions of Financial Accounting Standards Board Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, an interpretation of SFAS No. 109, *Accounting for Income Taxes* now codified into ASC Topic 740, *Income Taxes* (ASC 740). There were no material changes to the Company s unrecognized tax benefits for the nine months ended October 31, 2009.

Tax positions for the Company and its subsidiaries are subject to income tax audits by multiple tax jurisdictions throughout the world. Management does not believe that it is reasonably possible that the estimates of unrecognized tax benefits will change significantly in the next twelve months. However, an adverse resolution of one or more uncertain tax positions in any period could have a material impact on the results of operations for that period.

Revenue Recognition

The Company derives its revenues from two sources: (1) subscription revenues, which are comprised of subscription fees from customers accessing its enterprise cloud computing application service, and from customers purchasing additional support beyond the standard support that is included in the basic subscription fee; and (2) related professional services and other revenue. Other revenues consist primarily of training fees. Because the Company provides its application as a service, the Company follows the provisions of the Securities and Exchange Commission s, or SEC, Staff Accounting Bulletin No. 104 *Revenue Recognition* and Emerging Issues Task Force Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables* now codified into ASC Topic 605-25, *Revenue Recognition Multiple-Element Arrangements* (ASC 605-25). The Company recognizes revenue when all of the following conditions are met:

There is persuasive evidence of an arrangement;

The service has been provided to the customer;

The collection of the fees is reasonably assured; and

The amount of fees to be paid by the customer is fixed or determinable.

The Company s arrangements do not contain general rights of return.

Subscription and support revenues are recognized ratably over the contract terms beginning on the commencement date of each contract. Amounts that have been invoiced are recorded in accounts receivable and in deferred revenue or revenue, depending on whether the revenue recognition criteria have been met.

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

Professional services and other revenues, when sold with subscription and support offerings, are accounted for separately when these services have value to the customer on a standalone basis and there is objective and reliable evidence of fair value of each deliverable. When accounted for separately, revenues are recognized as the services are rendered for time and material contracts, and when the milestones are achieved and accepted by the customer for fixed price contracts. The majority of the Company s consulting contracts are on a time and materials basis. Training revenues are recognized after the services are performed. For revenue arrangements with multiple deliverables, such as an arrangement that includes subscription, premium support, consulting or training services, the Company allocates the total amount the customer will pay to the separate units of accounting based on their relative fair values, as determined by the price of the undelivered items when sold separately.

In determining whether the consulting services can be accounted for separately from subscription and support revenues, the Company considers the following factors for each consulting agreement: availability of the consulting services from other vendors, whether objective and reliable evidence for fair value exists for the undelivered elements, the nature of the consulting services, the timing of when the consulting contract was signed in comparison to the subscription service start date, and the contractual dependence of the subscription service on the customer s satisfaction with the consulting work. If a consulting arrangement does not qualify for separate accounting, the Company recognizes the consulting revenue ratably over the remaining term of the subscription contract. Additionally, in these situations, the Company defers only the direct costs of the consulting arrangement and amortizes those costs over the same time period as the consulting revenue is recognized. As of October 31, 2009 and January 31, 2009, the deferred cost on the accompanying condensed consolidated balance sheet totaled $17.9 million and $17.3 million, respectively. These deferred costs are included in prepaid expenses and other current assets and other assets.

Deferred Revenue

Deferred revenue primarily consists of billings or payments received in advance of revenue recognition from the Company s subscription service described above and is recognized as the revenue recognition criteria are met. The Company generally invoices its customers in annual or quarterly installments. Accordingly, the deferred revenue balance does not represent the total contract value of annual or multi-year, non-cancelable subscription agreements. Deferred revenue also includes certain deferred professional services fees which are recognized as revenue ratably over the subscription contract term. The Company defers the professional service fees in situations where the professional services and subscription contracts are accounted for as a single unit of accounting. Deferred revenue that will be recognized during the succeeding 12-month period is recorded as current deferred revenue and the remaining portion is recorded as noncurrent. Approximately 8 percent of total deferred revenue as of October 31, 2009 and 7 percent as of January 31, 2009 related to deferred professional services revenue.

Deferred Commissions

Deferred commissions are the incremental costs that are directly associated with non-cancelable subscription contracts with customers and consist of sales commissions paid to the Company s direct sales force. The commissions are deferred and amortized over the non-cancelable terms of the related customer contracts, which are typically 12 to 24 months. The commission payments are paid in full the month after the customer s service commences. The deferred commission amounts are recoverable through the future revenue streams under the non-cancelable customer contracts. The Company believes this is the preferable method of accounting as the commission charges are so closely related to the revenue from the non-cancelable customer contracts that they should be recorded as an asset and charged to expense over the same period that the subscription revenue is recognized. Amortization of deferred commissions is included in marketing and sales expense in the accompanying condensed consolidated statements of operations.

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

Accounting for Stock-Based Compensation

The Company accounts for its employee stock-based compensation pursuant to ASC 718. The Company recognizes share-based expenses on a straight-line over the requisite service period of the awards, which is the vesting term of four years. Stock-based expenses pursuant to ASC 718 are recognized net of estimated forfeiture activity.

The fair value of each option grant was estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions and fair value per share:

	Three months ended October 31,		Nine months ended October 31,	
	2009	2008	2009	2008
Volatility	52%	47%	52-60%	47%
Weighted-average estimated life	4 years	4 years	4 years	4 years
Weighted-average risk-free interest rate	2.16-2.26%	2.65-3.00%	1.78-2.39%	2.24-3.08%
Dividend yield				
Weighted-average fair value per share of grants	$ 23.03	$ 20.34	$ 20.24	$ 22.26

The weighted-average estimated life was based on the simplified calculation of expected life. Accordingly, the weighted-average estimated life assumption of 4 years was based on the average of the vesting term and the 5 year contractual lives of options awarded. The weighted average risk free interest rate is based on the rate for a 4 year U.S. government security at the time of the option grant.

The Company estimated its future stock price volatility considering both its observed option-implied volatilities and its historical volatility calculations. Management believes this is the best estimate of the expected volatility over the 4 year weighted-average expected life of its option grants.

During the three months ended October 31, 2009 and 2008, the Company capitalized $1.0 million and $0.4 million, respectively, of stock based expenses related to capitalized internal-use software development and deferred professional services costs and $2.1 million and $1.4 million for the nine months ended October 31, 2009 and 2008, respectively.

During the nine months ended October 31, 2009, the Company recognized stock-based expense of $62.9 million. As of October 31, 2009, the aggregate stock compensation remaining to be amortized to costs and expenses was $200.4 million. The Company expects this stock compensation balance to be amortized as follows: $25.9 million during the remaining three months of fiscal 2010; $87.3 million during fiscal 2011; $60.7 million during fiscal 2012; $23.9 million during fiscal 2013 and $2.6 million during fiscal 2014. The expected amortization reflects only outstanding stock awards as of October 31, 2009 and assumes no forfeiture activity. The Company expects to continue to issue share-based awards to its employees in future periods.

Warranties and Indemnification

The Company s enterprise cloud computing application service is typically warranted to perform in a manner consistent with general industry standards that are reasonably applicable and materially in accordance with the Company s online help documentation under normal use and circumstances.

The Company s arrangements generally include certain provisions for indemnifying customers against liabilities if its products or services infringe a third-party s intellectual property rights. To date, the Company has

18

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

not incurred any material costs as a result of such indemnifications and has not accrued any liabilities related to such obligations in the accompanying condensed consolidated financial statements.

The Company has also agreed to indemnify its directors and executive officers for costs associated with any fees, expenses, judgments, fines and settlement amounts incurred by any of these persons in any action or proceeding to which any of those persons is, or is threatened to be, made a party by reason of the person s service as a director or officer, including any action by the Company, arising out of that person s services as the Company s director or officer or that person s services provided to any other company or enterprise at the Company s request. The Company maintains director and officer insurance coverage that would generally enable the Company to recover a portion of any future amounts paid.

New Accounting Pronouncement

In September 2009, the FASB issued Accounting Standards Update No. 2009-13, *Revenue Recognition (Topic 605), Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force* (ASU 2009-13). It updates the existing multiple-element revenue arrangements guidance currently included under ASC 605-25. The revised guidance primarily provides two significant changes: 1) eliminates the need for objective and reliable evidence of the fair value for the undelivered element in order for a delivered item to be treated as a separate unit of accounting, and 2) requires the use of the relative selling price method to allocate the entire arrangement consideration. In addition, the guidance also expands the disclosure requirements for revenue recognition. ASU 2009-13 will be effective for the first annual reporting period beginning on or after fiscal 2011, with early adoption permitted provided that the revised guidance is retroactively applied to the beginning of the year of adoption. The Company is currently assessing the future impact of this new accounting pronouncement to its condensed consolidated financial statements.

Subsequent Events

The Company evaluated subsequent events through November 25, 2009, the date this Quarterly Report on Form 10-Q was filed with the SEC.

During fiscal 2010, the Company adopted SFAS No. 165, *Subsequent Events* (SFAS 165), now codified into ASC Topic 855, *Subsequent Events* (ASC 855), which established general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. ASC 855 also requires the disclosure of the date through which an entity has evaluated subsequent events and whether that evaluation date represents the date the financial statements were issued or were available to be issued. The adoption of ASC 855 did not have any impact on the Company s consolidated financial statements.

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

2. Balance Sheet Accounts

Marketable Securities

At October 31, 2009, marketable securities consisted of the following (in thousands):

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Corporate notes and obligations	$ 532,905	$ 11,423	$ (163)	$ 544,165
U.S. treasury securities	92,000	130	(180)	91,950
U.S. agency obligations	101,083	565	(10)	101,638
Mortgage backed securities	55,972	697	(87)	56,582
Collateralized mortgage obligations	23,819	369	(43)	24,145
Municipal securities	2,506	20		2,526
Money market mutual fund (see Note 1)	6,198			6,198
	$ 814,483	$ 13,204	$ (483)	$ 827,204

At January 31, 2009, marketable securities consisted of the following (in thousands):

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Corporate notes and obligations	$ 215,297	$ 1,173	$ (1,330)	$ 215,140
Money market mutual fund (see Note 1)	18,294			18,294
U.S. agency obligations	163,584	1,721	(8)	165,297
	$ 397,175	$ 2,894	$ (1,338)	$ 398,731

	October 31, 2009	January 31, 2009
Recorded as follows (in thousands):		
Short-term (due in one year or less)	$ 202,446	$ 213,769
Long-term (due in greater than one year)	624,758	184,962
	$ 827,204	$ 398,731

As of October 31, 2009, the following marketable securities were in an unrealized loss position (in thousands):

	Less than 12 Months	12 Months or Greater	Total

	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Corporate notes and obligations	$ 32,141	$ (160)	$ 6,498	$ (3)	$ 38,639	$ (163)
U.S. treasury securities	14,140	(180)			14,140	(180)
U.S. agency obligations	12,208	(10)			12,208	(10)
Mortgage backed securities	15,103	(87)			15,103	(87)
Collateralized mortgage obligations	2,928	(43)			2,928	(43)
	$ 76,520	$ (480)	$ 6,498	$ (3)	$ 83,018	$ (483)

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

The unrealized losses are substantially attributable to changes in interest rates. The unrealized loss for each of these fixed rate investments ranged from less than $1,000 to $180,000. The Company does not believe any of the unrealized losses represent an other-than temporary impairment based on its evaluation of available evidence as of October 31, 2009. The Company expects to receive the full principal and interest on all of these marketable securities.

Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consisted of the following (in thousands):

	October 31, 2009	January 31, 2009
Deferred professional services costs	$ 12,585	$ 13,069
Prepaid income taxes	14,401	12
Prepaid expenses and other current assets	35,241	20,034
	$ 62,227	$ 33,115

Fixed Assets

Fixed assets consisted of the following (in thousands):

	October 31, 2009	January 31, 2009
Computers, equipment and software	$ 85,241	$ 65,864
Furniture and fixtures	17,410	13,096
Leasehold improvements	70,994	54,032
	173,645	132,992
Less accumulated depreciation and amortization	(78,047)	(55,965)
	$ 95,598	$ 77,027

Depreciation and amortization expense totaled $8.4 million and $5.5 million for the three months ended October 31, 2009 and 2008, respectively, and $22.5 million and $15.0 million for the nine months ended October 31, 2009 and 2008, respectively.

Fixed assets at October 31, 2009 and January 31, 2009 included $25.6 million and $10.1 million, respectively, acquired under capital lease agreements. Accumulated amortization relating to equipment and software under capital leases totaled $8.7 million and $4.5 million at October 31, 2009 and January 31, 2009, respectively.

Amortization of assets under capital leases is included in depreciation and amortization expense.

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

Capitalized Software

Capitalized software consisted of the following (in thousands):

	October 31, 2009	January 31, 2009
Capitalized internal-use software development costs, net of accumulated amortization of $18,546 and $11,540, respectively	$ 21,953	$ 17,450
Acquired developed technology, net of accumulated amortization of $19,205 and $13,522, respectively	10,827	12,539
	$ 32,780	$ 29,989

Capitalized internal use software amortization expense totaled $2.5 million and $1.8 million for the three months ended October 31, 2009 and 2008, respectively. Acquired developed technology amortization expense for the three months ended October 31, 2009 and 2008 was $2.0 million and $2.1 million, respectively. Capitalized internal use software amortization expense totaled $7.0 million and $4.7 million for the nine months ended October 31, 2009 and 2008, respectively. Acquired developed technology amortization expense for the nine months ended October 31, 2009 and 2008 was $5.7 million and $4.8 million, respectively.

In the third quarter of fiscal 2010, the Company acquired a privately-held company for $4.5 million in cash. The Company accounted for this transaction as a business combination. Of the $4.5 million purchase price, the Company allocated $4.0 million to acquired developed technology with a useful life of 3 years and $0.5 million to goodwill. The Company does not believe this acquisition is material.

Other Assets

Other assets consisted of the following (in thousands):

	October 31, 2009	January 31, 2009
Deferred professional services costs, noncurrent portion	$ 5,274	$ 4,185
Long-term deposits	11,044	8,447
Purchased intangible assets, net of accumulated amortization of $5,019 and $2,573, respectively	7,232	9,679
Investments in privately-held companies	6,313	2,400
Other	4,113	5,416
	$ 33,976	$ 30,127

Purchased intangible assets amortization expense for the three months ended October 31, 2009 and 2008, was $0.8 million and $0.6 million, respectively and for the nine months ended October 31, 2009 and 2008 was $2.4 million and $0.9 million respectively.

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consisted of the following (in thousands):

	October 31, 2009	January 31, 2009
Accrued compensation	$ 64,598	$ 74,355
Accrued other liabilities	55,027	39,886
Accrued other taxes payable	23,617	27,596
Accrued professional costs	10,873	3,950
Accrued rent	20,194	17,418
	$ 174,309	$ 163,205

3. Stockholders Equity

Stock Options Issued to Employees

The 1999 Stock Option Plan (the 1999 Plan) provides for the issuance of incentive and non-statutory options to employees and nonemployees of the Company. On April 30, 2009, the 1999 Plan expired. Therefore, all remaining shares available expired. The expiration of the 1999 Plan did not affect awards outstanding under the 1999 Plan, which continue to be governed by the terms and conditions of the 1999 Plan. The Company also maintains the 2004 Equity Incentive Plan, 2004 Employee Stock Purchase Plan and the 2004 Outside Directors Stock Plan. These plans, other than the 1999 Plan and the 2004 Outside Directors Stock Plan, provide for annual automatic increases on February 1 to the shares reserved for issuance based on the lesser of (i) a specific percentage of the total number of shares outstanding at year end; (ii) a fixed number of shares; or (iii) a lesser number of shares set by the Company s Board of Directors, all as specified in the respective plans.

On February 1, 2009, 3.5 million additional shares were reserved under the 2004 Equity Incentive Plan pursuant to the automatic increase. The 2004 Employee Stock Purchase Plan will not be implemented unless and until the Company s Board of Directors authorizes the commencement of one or more offerings under the plan. No offering periods have been authorized to date.

In April 2006, the Company s Board of Directors approved the 2006 Inducement Equity Incentive Plan (the Inducement Plan) that allows for stock option and other equity incentive grants to employees in connection with merger or acquisition activity. In March 2009, the Board of Directors amended the Inducement Plan to increase the share reserve by 300,000 shares to 700,000 shares in total. As of October 31, 2009, there were 428,555 shares of common stock available for grant under the Inducement Plan.

Prior to February 1, 2006, options issued under the Company s stock option plans were generally for periods not to exceed 10 years and were issued at fair value of the shares of common stock on the date of grant as determined by the trading price of such stock on the New York Stock Exchange. After February 1, 2006, options issued to employees are for periods not to exceed 5 years. Grants made pursuant to the 2004 Equity Incentive Plan and the Inducement Plan do not provide for the immediate exercise of options.

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

Stock plan activity for the nine months ended October 31, 2009 is as follows:

	Shares Available for Grant	Outstanding Stock Options	Options Outstanding Weighted-Average Exercise Price	Aggregate Intrinsic Value (in thousands)
Balance as of January 31, 2009	4,191,642	14,917,520	$ 32.51	
Increase in options authorized:				
2004 Equity Incentive Plan	3,500,000			
Inducement Plan	300,000			
Options granted under all plans	(705,655)	705,655	47.11	
Restricted stock unit activity	(33,308)			
Stock grants to board members for board services and advisory board members	(37,650)			
Exercised		(1,504,904)	21.84	
1999 Plan shares expired	(141,499)			
Cancelled	848,823	(848,823)	41.76	
Balance as of October 31, 2009	7,922,353	13,269,448	$ 33.90	$ 307,391
Vested or expected to vest		12,837,872	$ 33.67	$ 300,213
Exercisable at October 31, 2009		6,455,330	$ 29.86	$ 175,072

The total intrinsic value of the options exercised during the nine months ended October 31, 2009 and 2008 were $36.1 million and $97.8 million, respectively. The intrinsic value is the difference between the current market value of the stock and the exercise price of the stock option.

The weighted-average remaining contractual life of vested and expected to vest options is approximately 4 years.

As of October 31, 2009, options to purchase 6,455,330 shares were vested at a weighted average exercise price of $29.86 per share and a remaining weighted-average remaining contractual life of approximately 4 years. The total intrinsic value of these vested options as of October 31, 2009 was $175.1 million.

The following table summarizes information about stock options outstanding as of October 31, 2009:

	Options Outstanding			Options Vested	
Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life (Years)	Weighted-Average Exercise Price	Number of Shares	Weighted-Average Exercise Price
$0.40 to $14.39	1,962,142	4.3	$ 8.25	1,961,620	$ 8.25
$15.00 to $25.19	729,332	5.3	20.89	718,484	20.84
$25.97	3,200,443	4.1	25.97		

$27.20 to $36.64	1,955,149	2.9	32.05	1,359,963	32.29
$36.90 to $52.28	2,370,182	3.1	44.26	1,279,569	43.41
$52.30 to $52.76	2,235,607	3.4	52.53	878,024	52.56
$54.22 to $70.86	816,593	3.7	61.57	257,670	62.11
	13,269,448	3.7	$ 33.90	6,455,330	$ 29.86

24

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

Restricted stock unit activity for the nine months ended October 31, 2009 is as follows:

	Restricted Stock Units Outstanding		
	Outstanding	**Weighted-Average Exercise Price**	**Aggregate Intrinsic Value (in thousands)**
Balance as of January 31, 2009	2,499,151	$ 0.001	
Granted	208,264	0.001	
Vested and converted to shares	(499,481)	0.001	
Cancelled	(177,872)	0.001	
Balance as of October 31, 2009	2,030,062	$ 0.001	$ 115,206
Expected to vest	1,875,870		$ 106,416

The restricted stock units, which upon vesting entitles the holder to one share of common stock for each restricted stock unit, have an exercise price of $0.001 per share, which is equal to the par value of the Company s common stock, and vest over 4 years.

Common Stock

The following shares of common stock are available for future issuance at October 31, 2009:

Options outstanding	13,269,448
Restricted stock units outstanding	2,030,062
Stock available for future grant:	
2004 Equity Incentive Plan	6,822,798
2006 Inducement Equity Incentive Plan	428,555
2004 Employee Stock Purchase Plan	1,000,000
2004 Outside Directors Stock Plan	671,000
	24,221,863

4. Commitments

Letters of Credit

As of October 31, 2009, the Company had a total of $10.5 million in letters of credit outstanding for office space in San Francisco, California, New York City, Singapore, Sweden, United Kingdom, Australia and Switzerland. These letters of credit renew annually and mature at various dates through October 2018.

Leases

The Company leases office space and equipment under noncancelable operating and capital leases with various expiration dates.

Table of Contents

salesforce.com, inc.

Notes to Condensed Consolidated Financial Statements (Continued)

As of October 31, 2009, the future minimum lease payments under noncancelable operating and capital leases are as follows (in thousands):

	Capital Leases	Operating Leases
Fiscal Period:		
Remaining three months in fiscal 2010	$ 1,909	$ 24,734
Fiscal 2011	8,436	75,210
Fiscal 2012	7,555	55,382
Fiscal 2013	1,074	42,126
Fiscal 2014		31,419
Thereafter		62,613
Total minimum lease payments	18,974	$ 291,484
Less: amount representing interest	(1,187)	
Present value of capital lease obligations	$ 17,787	

The Company s agreements for the facilities and certain services provide the Company with the option to renew. The Company s future contractual obligations would change if it were to exercise these options.

5. Legal Proceedings and Claims

The Company is involved in various legal proceedings and receives claims from time to time, arising from the normal course of business activities. In the Company s opinion, resolution of these matters is not expected to have a material adverse impact on its consolidated results of operations, cash flows or its financial position.

During fiscal 2009, the Company received a notice from a company alleging that the Company was infringing upon certain of that company s patents. No litigation has been filed to date. The Company continues to analyze the potential merits of the other company s claims, the potential defenses to such claims and potential counter claims. The Company intends to vigorously defend its interests in this matter and is uncertain as to when this matter will be resolved. In the Company s opinion, the resolution of this dispute is not expected to have a material adverse effect on its financial condition, but it could be material to the net income or cash flows of a particular quarter. This claim, or any claim of infringement or violation of intellectual property rights, with or without merit, could require the Company to change its technology, change its business practices, pay damages, enter into a licensing arrangement or take other actions that may result in additional costs or other actions that are detrimental to its business.

6. Related-Party Transactions

In January 1999, the salesforce.com/foundation, commonly referred to as the Foundation, a non-profit public charity, was chartered to build philanthropic programs that are focused on youth and technology. The Company s chairman is the chairman of the Foundation. He, one of the Company s officers and one of the Company s board members hold three of the Foundation s seven board seats. The Company is not the primary beneficiary of the Foundation s activities, and accordingly, the Company does not consolidate the Foundation s statement of activities with its financial results.

Since the Foundation s inception, the Company has provided at no charge certain resources to Foundation employees such as office space. The value of these items totals approximately $35,000 per quarter.

26

Table of Contents

In addition to the resource sharing with the Foundation, the Company issued the Foundation warrants in August 2002 to purchase 500,000 shares of common stock. The Foundation has exercised all of these warrants. As of October 31, 2009, the Foundation held 148,500 shares of salesforce.com common stock. Additionally, the Company has donated subscriptions to the Company s service to other qualified non-profit organizations. The Company plans to continue providing free subscriptions to qualified non-profit organizations through its relationship with the Foundation.

Table of Contents

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

The following discussion in Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements consist of, among other things, trend analyses, statements regarding future events, future financial performance, our business strategy and our plan to build our business, our service performance and security, the expenses associated with our data center capacity, our operating results, our anticipated growth, trends in our business, new application service features, our strategy of acquiring or making investments in complementary companies, services and technologies, the effect of general economic and market conditions including sudden declines in the fair value of our investments in cash equivalents and marketable securities, our ability to protect our intellectual property rights, our ability to develop our brands, the effect of evolving government regulations, the effect of foreign currency exchange rate and interest rate fluctuations on our financial results, the potential availability of additional tax assets in the future and related matters, the impact of expensing stock options, the sufficiency of our capital resources, and our strategy to be the leading provider of CRM application services and the leading platform on which customers and partners build enterprise cloud computing applications, of which are based on current expectations, estimates, and forecasts, and the beliefs and assumptions of our management. Words such as expects, anticipates, projects, intends, plans, believes, estimates, variations of such words, and similar expressions are also intended to identify such forward-looking statements. These forward-looking statements are subject to risks, uncertainties and assumptions that are difficult to predict. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. Readers are directed to risks and uncertainties identified below, under Risk Factors and elsewhere in this report, for factors that may cause actual results to be different than those expressed in these forward-looking statements. Except as required by law, we undertake no obligation to revise or update publicly any forward-looking statements for any reason.

Overview

We provide a comprehensive Customer Relationship Management, or CRM, service to businesses of all sizes and industries worldwide and we provide a technology platform for customers and developers to build and run business applications. Approximately 67,900 customers worldwide use salesforce.com to manage their customer, sales and operational data.

We were founded in February 1999 and began offering our enterprise CRM application service in February 2000.

Our objective is to be the leading provider of CRM application services and to be the leading platform on which our customers and partners build enterprise cloud computing applications. Key elements of our strategy include:

- Strengthening our existing CRM applications and extending into new functional areas within CRM;
- Pursuing new customers and new territories aggressively;
- Deepening relationships with our existing customer base;
- Continuing to lead the industry transformation to cloud computing; and
- Encouraging the development of third-party applications on our Force.com platform.

We believe the factors that will influence our ability to achieve our objectives include our prospective customers willingness to migrate to an enterprise cloud computing application service; the performance and security of our service; our ability to continue to release, and gain customer acceptance of new and improved features; successful customer adoption and utilization of our service; acceptance of our service in markets where

Table of Contents

we have few customers; increasing competition in our market and improved product offerings by existing and new competitors; the location of our data centers; third-party developers willingness to develop applications on our platform; and general economic conditions which could affect our customers ability and willingness to purchase additional or renew existing subscriptions to our application service, or delay the customers purchasing decisions and reduce the value and duration of new subscription contracts.

We anticipate revenue growth for our fiscal 2010 to be significantly lower than the 44 percent annual revenue growth in fiscal 2009. For the nine months ended October 31, 2009, our revenue increased by 21 percent compared to 48 percent during the same period a year ago.

During the three months ended October 31, 2009, market demand for our cloud computing services improved compared to the first half of fiscal 2010. Although the initial average customer order deployment size continued to be smaller than in the past, and we continued to experience longer sales cycles, new business increased slightly during the three months ended October 31, 2009 above the levels of new business during the same period a year ago and each of the three months ended April 30, 2009 and July 31, 2009. We define new business as orders for incremental or upgraded applications or subscriptions from new or existing customers.

Additionally, during the three months ended October 31, 2009, our subscription renewal rates improved slightly above the renewal rates we experienced during the first six months of fiscal 2010. However, our renewal rates for the nine months ended October 31, 2009 are below the renewal rates we experienced in previous years because some customers elected not to renew while other customers renewed for a reduced number of subscriptions. We believe this is caused by several factors, including spending constraints and reduced headcount levels at our customers.

In response to the economic environment and the slowdown in IT spending, we scaled back our hiring in the first six months of fiscal 2010. However, we decided to increase our hiring in the quarter ended October 31, 2009 as we experienced improved demand for our cloud computing services. During the nine months ended October 31, 2009, we added 567 employees compared to 930 employees during the same period a year ago. Our headcount as of October 31, 2009 was 3,814. We also reduced expenditures for customer events, internal meetings, travel and entertainment and outside contractors. However, as mentioned elsewhere in this report, we intend to continue to: invest in expanding our data center capacity; expand our domestic and international selling and marketing activities; add additional distribution channels, particularly in international regions; and add to our infrastructure in order to further scale our operations and increase productivity. Additionally, in our effort to further strengthen and extend our service offering, we may acquire or make investments in complementary companies, services and technologies.

Overall, we expect that increased revenue combined with headcount and cost management will increase our fiscal 2010 operating income as a percentage of revenues in comparison to fiscal 2009, as well as our earnings per share.

We expect marketing and sales costs, which were 46 percent of our total revenues for the nine months ended October 31, 2009 and 49 percent for the same period a year ago, to continue to represent a substantial portion of total revenues in the future as we seek to add more paying subscribers, and build brand awareness for salesforce.com and its services, and evangelize cloud computing.

Fiscal Year

Our fiscal year ends on January 31. References to fiscal 2010, for example, refer to the fiscal year ended January 31, 2010.

Table of Contents

Sources of Revenues

We derive our revenues from two sources: (1) subscription revenues, which are comprised of subscription fees from customers accessing our enterprise cloud computing application service, and from customers purchasing additional support beyond the standard support that is included in the basic subscription fee; and (2) related professional services and other revenues consisting primarily of training fees. Subscription and support revenues accounted for approximately 93 percent of our total revenues during the nine months ended October 31, 2009. Subscription revenues are driven primarily by the number of paying subscribers of our service and the subscription price of our service. None of our customers accounted for more than 5 percent of our revenues during the nine months ended October 31, 2009 and 2008.

Subscription and support revenues are recognized ratably over the contract terms beginning on the commencement dates of each contract. The typical subscription and support term is 12 to 24 months, although terms range from one to 60 months. Our subscription and support contracts are noncancelable, though customers typically have the right to terminate their contracts for cause if we materially fail to perform. We generally invoice our customers in advance, in annual or quarterly installments, and typical payment terms provide that our customers pay us within 30 days of invoice. Amounts that have been invoiced are recorded in accounts receivable and in deferred revenue, or in revenue depending on whether the revenue recognition criteria have been met. In general, we collect our billings in advance of the subscription service period.

Most of the subscription and support revenue we report each quarter is derived from the recognition of deferred revenue relating to subscription agreements entered into or renewed during previous quarters. Consequently, a decline in new or renewed subscriptions in any one quarter will be fully reflected in the deferred revenue balance on our consolidated balance sheet and the revenue in that quarter, and will negatively affect our revenue in future quarters.

Professional services and other revenues consist of fees associated with consulting and implementation services and training. Our consulting and implementation engagements are typically billed on a time and materials basis. We also offer a number of classes on implementing, using and administering our service that are billed on a per person, per class basis. Our typical payment terms provide that our customers pay us within 30 days of invoice.

We recognize revenue in accordance with the provisions of SEC Staff Accounting Bulletin No. 104, *Revenue Recognition*, and Emerging Issues Task Force Issue No. 00-21, *Revenue Arrangements with Multiple-Element Arrangements*, now codified into ASC Topic 605-25, *Revenue Recognition Multiple-Element Arrangements*. In determining whether professional services can be accounted for separately from subscription and support revenues, we consider a number of factors, which are described in Critical Accounting Policies and Estimates Revenue Recognition below. As we introduce new service offerings, we may not be able to establish objective and reliable evidence of fair value for these elements of our sales arrangements. As a result, when the professional services are sold together with subscription services that do not have objective and reliable evidence of fair value, the professional services fees cannot be accounted for separately, and the entire arrangement is accounted for as a single unit of accounting. In such situations, we recognize the entire arrangement fee ratably over the term of the subscription contract. Approximately 8 percent of our total deferred revenue as of October 31, 2009 and 7 percent as of January 31, 2009 related to deferred professional services revenue.

Seasonal Nature of Deferred Revenue and Accounts Receivable

Deferred revenue primarily consists of billings to customers for our subscription service. Over 90 percent of the value of our billings to customers is for our subscription and support service. We generally invoice our customers in either quarterly or annual cycles, with a disproportionate weighting towards annual billings in the fourth quarter, primarily as a result of large enterprise account buying patterns. Additionally, our fourth quarter has historically been our strongest quarter for new business. The year on year compounding effect of this seasonality in both billing patterns and overall new business is causing the value of invoices that we generate in the fourth quarter for both new and existing customers to increase as a proportion of our total annual billings.

Table of Contents

Accordingly, the sequential quarterly changes in accounts receivable and the related deferred revenue during the first three quarters of our fiscal year are not necessarily indicative of the billing activity that occurs in the fourth quarter.

The following table sets forth our accounts receivable and deferred revenue balances as of the end of each fiscal quarter:

(in thousands)	April 30, 2009	July 31, 2009	October 31, 2009	
Fiscal 2010				
Accounts receivable, net	$ 145,869	$ 168,842	$ 191,297	
Deferred revenue, current and noncurrent	549,373	549,010	545,435	
	April 30, 2008	**July 31, 2008**	**October 31, 2008**	**January 31, 2009**
Fiscal 2009				
Accounts receivable, net	$ 143,909	$ 146,982	$ 157,680	$ 266,555
Deferred revenue, current and noncurrent	470,297	479,546	469,534	594,026
	April 30, 2007	**July 31, 2007**	**October 31, 2007**	**January 31, 2008**
Fiscal 2008				
Accounts receivable, net	$ 105,013	$ 114,046	$ 121,961	$ 220,061
Deferred revenue, current and noncurrent	295,672	321,852	340,808	480,894

Cost of Revenues and Operating Expenses

Cost of Revenues. Cost of subscription and support revenues primarily consists of expenses related to hosting our service and providing support, the costs of data center capacity, depreciation or operating lease expense associated with computer equipment, costs associated with website development activities, allocated overhead and amortization expense associated with capitalized software related to our application service and acquired technology. We allocate overhead such as rent and occupancy charges based on headcount. Employee benefit costs and taxes are allocated based upon a percentage of total compensation expense. As such, general overhead expenses are reflected in each cost of revenue and operating expense category. Cost of professional services and other revenues consists primarily of employee-related costs associated with these services, including stock-based expenses, the cost of subcontractors and allocated overhead. The cost of providing professional services is significantly higher as a percentage of revenue than for our enterprise cloud computing subscription service due to the direct labor costs.

We intend to continue to invest additional resources in our enterprise cloud computing application service. The timing of these additional expenses will affect our cost of revenues, both in terms of absolute dollars and as a percentage of revenues, in a particular quarterly period. For example, we opened a data center in Singapore in fiscal 2010. We expect the annual cost to be significant.

Research and Development. Research and development expenses consist primarily of salaries and related expenses, including stock-based expenses, the costs of our development and test data center and allocated overhead. We continue to focus our research and development efforts on increasing the functionality and enhancing the ease of use of our enterprise cloud computing application service. Our proprietary, scalable and secure multi-tenant architecture enables us to provide all of our customers with a service based on a single version of our application. As a result, we do not have to maintain multiple versions, which enable us to have relatively lower research and development expenses as compared to traditional enterprise software companies. We expect that in the future, research and development expenses will increase in absolute dollars as we upgrade and extend our service offerings and develop new technologies.

Table of Contents

Marketing and Sales. Marketing and sales expenses are our largest cost and consist primarily of salaries and related expenses, including stock-based expenses, for our sales and marketing staff, including commissions, payments to partners, marketing programs and allocated overhead. Marketing programs consist of advertising, events, corporate communications and brand building and product marketing activities.

We plan to continue to invest in marketing and sales by expanding our domestic and international selling and marketing activities, building brand awareness and sponsoring additional marketing events. We expect that in the future, marketing and sales expenses will increase in absolute dollars and continue to be our largest cost.

General and Administrative. General and administrative expenses consist of salaries and related expenses, including stock-based expenses, for finance and accounting, human resources and management information systems personnel, legal costs, professional fees, other corporate expenses and allocated overhead. We expect that in the future, general and administrative expenses will increase in absolute dollars as we incur additional employee related costs, professional fees and insurance costs related to the growth of our business and international expansion. However, we expect general and administrative costs as a percentage of total revenues will decrease in future years.

Stock-Based Expenses. Our cost of revenues and operating expenses include stock-based expenses related to option and stock awards to employees and non-employee directors. We account for stock-based expenses pursuant to the provisions of ASC 718. ASC 718 requires that share-based payments, including grants of employee stock options be recognized as an expense in the statement of operations based on their fair values and vesting periods. These charges are significant and we expect them to increase in absolute dollars in the future.

Joint Venture

In December 2000, we established a Japanese joint venture, Kabushiki Kaisha salesforce.com, with SunBridge, Inc., a Japanese corporation, to assist us with our sales efforts in Japan. As of October 31, 2009, the Company owned 72 percent of the joint venture. Because of this majority interest, we consolidate the venture s financial results, which are reflected in each revenue, cost of revenues and expense category in our consolidated statement of operations. We then record a noncontrolling interest, which reflects the noncontrolling investors interest in the venture s results. Through October 31, 2009, the operating performance and liquidity requirements of the Japanese joint venture have not been significant. While we plan to expand our selling and marketing activities in Japan in order to add new customers, we believe the future operating performance and liquidity requirements of the Japanese joint venture will not be significant.

Critical Accounting Policies and Estimates

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and expenses, and related disclosures. On an ongoing basis, we evaluate our estimates and assumptions. Our actual results may differ from these estimates under different assumptions or conditions.

We believe that of our significant accounting policies, which are described in note 1 to our condensed consolidated financial statements, the following accounting policies involve a greater degree of judgment and complexity. Accordingly, these are the policies we believe are the most critical to aid in fully understanding and evaluating our condensed consolidated financial condition and results of operations.

Revenue Recognition. We recognize revenue in accordance with the provisions of SAB 104 and ASC 605.

Table of Contents

We recognize revenue when all of the following conditions are satisfied: (1) there is persuasive evidence of an arrangement; (2) the service has been provided to the customer; (3) the collection of our fees is reasonably assured; and (4) the amount of fees to be paid by the customer is fixed or determinable. Our arrangements do not contain general rights of return.

We recognize subscription revenues ratably over the contract terms beginning on the commencement dates of each contract. Support revenues from customers who purchase our premium support offerings are recognized similarly over the term of the support contract. As part of their subscription agreements, customers generally benefit from new features and functionality with each release at no additional cost. In situations where we have contractually committed to an individual customer specific technology, we defer all of the revenue for that customer until the technology is delivered and accepted. Once delivery occurs, we then recognize the revenue over the remaining contract term.

Consulting services and training revenues are accounted for separately from subscription and support revenues when these services have value to the customer on a standalone basis and there is objective and reliable evidence of fair value of each deliverable. When accounted for separately, revenues are recognized as the services are rendered for time and material contracts, and when the milestones are achieved and accepted by the customer for fixed price contracts. The majority of our consulting service contracts are on a time and material basis. Training revenues are recognized after the services are performed. For revenue arrangements with multiple deliverables, such as an arrangement that includes subscription, premium support, consulting or training services, we allocate the total amount the customer will pay to the separate units of accounting based on their relative fair values, as determined by the price of the undelivered items when sold separately.

In determining whether the consulting services can be accounted for separately from subscription and support revenues, we consider the following factors for each consulting agreement: availability of the consulting services from other vendors, whether objective and reliable evidence for fair value exists for the undelivered elements, the nature of the consulting services, the timing of when the consulting contract was signed in comparison to the subscription service start date, and the contractual dependence of the subscription service on the customer s satisfaction with the consulting work. If a consulting arrangement does not qualify for separate accounting, we recognize the consulting revenue ratably over the remaining term of the subscription contract. Additionally, in these situations we defer the direct costs of the consulting arrangement and amortize those costs over the same time period as the consulting revenue is recognized. The deferred cost on our condensed consolidated balance sheet totaled $17.9 million at October 31, 2009 and $17.3 million at January 31, 2009. Such amounts are included in prepaid expenses and other current assets and other assets, net.

Accounting for Deferred Commissions. We defer commission payments to our direct sales force. The commissions are deferred and amortized to sales expense over the non-cancelable terms of the related subscription contracts with our customers, which are typically 12 to 24 months. The commission payments, which are paid in full the month after the customer s service commences, are a direct and incremental cost of the revenue arrangements. The deferred commission amounts are recoverable through the future revenue streams under the non-cancelable customer contracts. We believe this is the preferable method of accounting as the commission charges are so closely related to the revenue from the non-cancelable customer contracts that they should be recorded as an asset and charged to expense over the same period that the subscription revenue is recognized.

During the nine months ended October 31, 2009, we deferred $43.0 million of commission expenditures and we amortized $46.0 million to sales expense. During the same period a year ago, we deferred $40.6 million of commission expenditures and we amortized $43.4 million to sales expense. Deferred commissions on our condensed consolidated balance sheet totaled $54.1 million at October 31, 2009 and $57.1 million at January 31, 2009.

Table of Contents

Accounting for Stock-Based Awards. We account for share-based compensation under ASC 718 . We recognize the fair value of our stock awards on a straight-line basis over the requisite service period of the award, which is the vesting term of four years.

We recognized stock-based expense of $62.9 million, or 7 percent of revenue, during the nine months ended October 31, 2009. The requirement to expense stock-based awards will continue to materially reduce our reported results of operations. As of October 31, 2009, we had an aggregate of $200.4 million of stock compensation remaining to be amortized to expense over the remaining requisite service period of the underlying awards. We currently expect this stock compensation balance to be amortized as follows: $25.9 million during the remaining three months of fiscal 2010; $87.3 million during fiscal 2011; $60.7 million during fiscal 2012; $23.9 million during fiscal 2013; and $2.6 million during fiscal 2014. These amounts reflect only outstanding stock awards as of October 31, 2009 and assume no forfeiture activity. We expect to continue to issue share-based awards to our employees in future periods.

We grant stock options and restricted stock units to employees throughout the world. In certain foreign jurisdictions, we are obligated for the payroll or social tax costs when employees exercise their vested awards. Pursuant to ASC 718, we recognize as an operating expense the payroll and social tax costs at the time of the stock option exercise. The impact of ASC 718 in the future is dependent upon, among other things, the timing of when we hire additional employees, the effect of long-term incentive strategies involving stock awards in order to continue to attract and retain employees, the total number of stock awards granted, the fair value of the stock awards at the time of grant, changes in estimated forfeiture assumption rates and the tax benefit that we may or may not receive from stock-based expenses. Additionally, the application of ASC 718 requires the use of an option-pricing model to determine the fair value of stock option awards. This determination of fair value is affected by our stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, our expected stock price volatility over the term of the awards.

As of October 31, 2009, there were 2.0 million restricted stock units outstanding. We plan to continue awarding restricted stock units to our employees in the future. The restricted stock units, which upon vesting entitles the holder to one share of common stock for each restricted stock unit, have an exercise price of $0.001 per share, which is equal to the par value of our common stock, and vest over 4 years. The fair value of the restricted stock units is based on our closing stock price on the date of grant, and compensation expense, net of estimated forfeitures, is recognized on a straight-line basis over the vesting period.

Accounting for Income Taxes. We account for income taxes using the liability method, which requires the recognition of deferred tax assets or liabilities for the tax-effected temporary differences between the financial reporting and tax bases of our assets and liabilities and for net operating loss and tax credit carryforwards. The tax expense or benefit for unusual items, prior year income tax uncertainties, or certain adjustments to the valuation allowance are treated as discrete items in the interim period in which the events occur.

Our effective tax rate could be adversely affected by changes in the mix of earnings and losses in countries with differing statutory tax rates, certain non-deductible expenses arising from stock option compensation and the valuation of deferred tax assets and liabilities and changes in tax laws and accounting principles.

Table of Contents

Results of Operations

The following tables set forth selected data for each of the periods indicated and are in thousands. All data is unaudited.

	Three months ended October 31,		Nine months ended October 31,	
	2009	**2008**	**2009**	**2008**
Revenues:				
Subscription and support	$ 306,870	$ 253,403	$ 882,078	$ 718,464
Professional services and other	23,679	23,084	69,456	68,722
Total revenues	330,549	276,487	951,534	787,186
Cost of revenues:				
Subscription and support	40,745	32,424	116,744	91,802
Professional services and other	24,825	23,924	73,122	69,935
Total cost of revenues	65,570	56,348	189,866	161,737
Gross profit	264,979	220,139	761,668	625,449
Operating expenses:				
Research and development	32,763	26,270	95,450	70,070
Marketing and sales	152,166	136,452	436,647	389,930
General and administrative	49,909	41,284	139,818	117,797
Total operating expenses	234,838	204,006	671,915	577,797
Income from operations	30,141	16,133	89,753	47,652
Interest, net	7,211	3,840	18,987	17,270
Other income (expense)	(336)	534	(1,037)	(1,069)
Income before provision for income taxes and noncontrolling interest	37,016	20,507	107,703	63,853
Provision for income taxes	(15,573)	(8,824)	(45,426)	(29,693)
Consolidated net income	21,443	11,683	62,277	34,160
Less: Net income attributable to noncontrolling interest	(752)	(1,559)	(1,952)	(4,485)
Net income attributable to salesforce.com	$ 20,691	$ 10,124	$ 60,325	$ 29,675

		As of	
	October 31, 2009	**January 31, 2009**	**October 31, 2008**
Balance sheet data:			
Cash, cash equivalents and marketable securities	$ 1,070,092	$ 882,565	$ 804,606
Deferred revenue, current and noncurrent	545,435	594,026	469,534

	Three months ended October 31,		Nine months ended October 31,	
	2009	**2008**	**2009**	**2008**
Revenues by geography:				
Americas	$ 232,802	$ 200,143	$ 679,460	$ 567,076

Europe	60,761	48,076	168,355	142,597
Asia Pacific	36,986	28,268	103,719	77,513
	$ 330,549	$ 276,487	$ 951,534	$ 787,186

Table of Contents

Cost of revenues and operating expenses include the following amounts related to stock-based awards.

	Three months ended October 31,		Nine months ended October 31,	
	2009	2008	2009	2008
Cost of revenues	$ 2,995	$ 2,817	$ 9,322	$ 8,149
Research and development	2,707	2,494	8,741	6,852
Marketing and sales	9,055	9,235	28,314	26,105
General and administrative	5,650	4,730	16,570	15,119

The following tables set forth selected consolidated statements of operations data for each of the periods indicated as a percentage of total revenues.

	Three months ended October 31,		Nine months ended October 31,	
	2009	2008	2009	2008
Revenues:				
Subscription and support	93%	92%	93%	91%
Professional services and other	7	8	7	9
Total revenues	100	100	100	100
Cost of revenues:				
Subscription and support	12	12	12	12
Professional services and other	8	8	8	9
Total cost of revenues	20	20	20	21
Gross profit	80	80	80	79
Operating expenses:				
Research and development	10	10	10	9
Marketing and sales	46	49	46	49
General and administrative	15	15	15	15
Total operating expenses	71	74	71	73
Income from operations	9	6	9	6
Interest, net	2	1	2	2
Other income (expense)				
Income before provision for income taxes and noncontrolling interest	11	7	11	8
Provision for income taxes	(5)	(3)	(5)	(4)
Consolidated net income	6	4	6	4
Less: Net income attributable to noncontrolling interest				
Net income attributable to salesforce.com	6%	4%	6%	4%

	Three months ended October 31,		Nine months ended October 31,	
	2009	2008	2009	2008
Revenues by geography:				

Americas	70%	72%	71%	72%
Europe	18	17	18	18
Asia Pacific	12	11	11	10
	100%	100%	100%	100%

Table of Contents

	Three months ended October 31, 2009	2008	Nine months ended October 31, 2009	2008
Stock-based expenses:				
Cost of revenues	1%	1%	1%	1%
Research and development	1	1	1	1
Marketing and sales	3	3	3	3
General and administrative	1	2	2	2

Three Months Ended October 31, 2009 and 2008

Revenues.

(In thousands)	Three Months Ended October 31, 2009	2008	Variance Dollars	Percent
Subscription and support	$ 306,870	$ 253,403	$ 53,467	21%
Professional services and other	23,679	23,084	595	3%
Total revenues	$ 330,549	$ 276,487	$ 54,062	20%

Total revenues were $330.5 million for the three months ended October 31, 2009, compared to $276.5 million during the same period a year ago, an increase of $ 54.1 million, or 20 percent. Subscription and support revenues were $306.9 million, or 93 percent of total revenues, for the three months ended October 31, 2009, compared to $253.4 million, or 92 percent of total revenues, during the same period a year ago. The increase in subscription and support revenues was due primarily to an increased number of new customers, additional paying subscriptions from existing customers, and customers who have upgraded. Professional services and other revenues were $23.7 million, or 7 percent of total revenues, for the three months ended October 31, 2009, compared to $23.1 million, or 8 percent of total revenues, for the same period a year ago. The increase in professional services and other revenues was due primarily to increased utilization of existing professional services staff.

Revenues in Europe and Asia Pacific accounted for $97.7 million, or 30 percent of total revenues, for the three months ended October 31, 2009, compared to $76.3 million, or 28 percent of total revenues, during the same period a year ago, an increase of $21.4 million, or 28 percent. The increase in revenues outside of the Americas was the result of our efforts to expand internationally. The foreign currency impact compared to the same period a year ago in total revenues was an increase of $4.3 million. As part of our overall growth, we expect the percentage of our revenue generated in Europe and Asia Pacific to continue to increase as a larger percentage of our total revenues world wide.

Cost of Revenues.

(In thousands)	Three Months Ended October 31, 2009	2008	Variance Dollars
Subscription and support	$ 40,745	$ 32,424	$ 8,321
Professional services and other	24,825	23,924	901
Total cost of revenues	$ 65,570	$ 56,348	$ 9,222
Percent of total revenues	20%	20%	

Table of Contents

Cost of revenues was $65.6 million, or 20 percent of total revenues, for three months ended October 31, 2009, compared to $56.3 million, or 20 percent of total revenues, for the same period a year ago, an increase of $9.2 million. The increase in absolute dollars was primarily due to an increase of $1.9 million in employee-related costs, an increase of $0.2 million in stock-based expenses, an increase of $2.4 million in service delivery costs, primarily due to our efforts in increasing data center capacity, an increase of $2.4 million in depreciation and amortization expenses, an increase of $1.9 million in outside subcontractor and other service costs and an increase in allocated overhead. The cost of the additional professional services headcount resulted in the cost of professional services and other revenues to be in excess of the related revenue for the three months ended October 31, 2009 by $1.1 million. We expect the cost of professional services and other revenue to continue to be in excess of the related revenue during the fourth quarter of fiscal 2010. We plan to continue to make this investment since our professional services are primarily designed to accelerate the adoption and expanded use by our customers of our enterprise cloud computing application service.

Research and Development.

(In thousands)	Three Months Ended October 31, 2009	2008	Variance Dollars
Research and development	$ 32,763	$ 26,270	$ 6,493
Percent of total revenues	10%	10%	

Research and development expenses were $32.8 million, or 10 percent of total revenues, during the three months ended October 31, 2009, compared to $26.3 million, or 10 percent of total revenues, during the same period a year ago, an increase of $6.5 million. The increase in absolute dollars was due to an increase of $5.5 million in employee-related costs, an increase of $0.2 million in stock-based expenses, and an increase in allocated overhead. We increased our research and development headcount by 31 percent since October 31, 2008 in order to upgrade and extend our service offerings and develop new technologies.

Marketing and Sales.

(In thousands)	Three Months Ended October 31, 2009	2008	Variance Dollars
Marketing and sales	$ 152,166	$ 136,452	$ 15,714
Percent of total revenues	46%	49%	

Marketing and sales expenses were $152.2 million, or 46 percent of total revenues, during the three months ended October 31, 2009, compared to $136.5 million, or 49 percent of total revenues, during the same period a year ago, an increase of $15.7 million. The increase in absolute dollars was primarily due to increases of $11.1 million in employee related costs, $0.2 million of amortized purchased intangibles, an increase of $1.8 million in professional and outside service costs, $1.2 million in allocated overhead and an increase of $1.4 million in advertising costs and marketing and event costs. Our marketing and sales headcount increased by 12 percent since October 31, 2008 as we hired additional sales personnel to focus on adding new customers and increasing penetration within our existing customer base which is less than the same period a year ago.

General and Administrative.

(In thousands)	Three Months Ended October 31, 2009	2008	Variance Dollars
General and administrative	$ 49,909	$ 41,284	$ 8,625
Percent of total revenues	15%	15%	

Table of Contents

General and administrative expenses were $49.9 million, or 15 percent of total revenues, during the three months ended October 31, 2009, compared to $41.3 million, or 15 percent of total revenues, during the same period a year ago, an increase of $8.6 million. The increase was primarily due to increases in employee-related costs, stock-based expenses, infrastructure related costs, and professional and outside service costs. Our general and administrative headcount increased by 18 percent since October 31, 2008 as we added personnel to support our growth.

Operating Income.

	Three Months Ended October 31,		Variance
(In thousands)	**2009**	**2008**	**Dollars**
Operating income	$ 30,141	$ 16,133	$ 14,008
Percent of total revenues	9%	6%	

Operating income during the three months ended October 31, 2009 was $30.1 million and included $20.4 million of stock-based expenses related to ASC 718. During the same period a year ago, operating income was $16.1 million and included $19.3 million of stock-based expenses.

Interest, Net.

	Three Months Ended October 31,		Variance
(In thousands)	**2009**	**2008**	**Dollars**
Interest, net	$ 7,211	$ 3,840	$ 3,371
Percent of total revenues	2%	1%	

Interest, net consists of investment income on cash and marketable securities balances and realized gains and losses. Interest, net was $7.2 million during the three months ended October 31, 2009 and was $3.8 million during the same period a year ago. The increase was due to the increased amount of cash and marketable securities balances for the three months ended October 31, 2009. Additionally, during the three months ended October 31, 2008, we recorded a $2.0 million loss related to marketable securities.

Other Income (expense).

	Three Months Ended October 31,		Variance
(In thousands)	**2009**	**2008**	**Dollars**
Other income (expense)	$ (336)	$ 534	$ (870)

Other expense primarily consists of foreign currency transaction gains and fees. Other expense increased due to realized and unrealized losses on foreign currency transactions for the three months ended October 31, 2009 when compared to the same period a year ago.

Provision for Income Taxes.

	Three Months Ended October 31,		Variance
(In thousands)	**2009**	**2008**	**Dollars**
Provision for income taxes	$ (15,573)	$ (8,824)	$ (6,749)
Effective tax rate	42%	43%	

Table of Contents

Our effective tax rate for the three months ended October 31, 2009 was 42 percent compared to 43 percent for the same period a year ago. The decrease in our third quarter effective tax rate was attributed to a higher proportion of income in countries with lower income tax rates than the U.S. statutory tax rate as well as tax benefits derived from domestic manufacturing deductions in this fiscal year.

Nine Months Ended October 31, 2009 and 2008

Revenues.

(In thousands)	Nine Months Ended October 31, 2009	2008	Variance Dollars	Percent
Subscription and support	$ 882,078	$ 718,464	$ 163,614	23%
Professional services and other	69,456	68,722	734	1%
Total revenues	$ 951,534	$ 787,186	$ 164,348	21%

Total revenues were $951.5 million for the nine months ended October 31, 2009, compared to $787.2 million during the same period a year ago, an increase of $164.3 million, or 21 percent. Subscription and support revenues were $882.1 million, or 93 percent of total revenues, for the nine months ended October 31, 2009, compared to $718.5 million, or 91 percent of total revenues, during the same period a year ago. The increase in subscription and support revenues was due primarily to an increased number of new customers, additional paying subscriptions from existing customers, and customers who have upgraded. Professional services and other revenues were $69.5 million, or 7 percent of total revenues, for the nine months ended October 31, 2009, compared to $68.7 million, or 9 percent of total revenues, for the same period a year ago.

Revenues in Europe and Asia Pacific accounted for $272.1 million, or 29 percent of total revenues, for the nine months ended October 31, 2009, compared to $220.1 million, or 28 percent of total revenues, during the same period a year ago, an increase of $52.0 million, or 24 percent. The increase in revenues outside of the Americas was the result of our efforts to expand internationally. The foreign currency impact compared to the same period a year ago in total revenue was a decrease of $8.3 million. As part of our overall growth, we expect the percentage of our revenue generated in Europe and Asia Pacific to continue to increase as a larger percentage of our total revenues world wide.

Cost of Revenues.

(In thousands)	Nine Months Ended October 31, 2009	2008	Variance Dollars
Subscription and support	$ 116,744	$ 91,802	$ 24,942
Professional services and other	73,122	69,935	3,187
Total cost of revenues	$ 189,866	$ 161,737	$ 28,129
Percent of total revenues	20%	21%	

Cost of revenues was $189.9 million, or 20 percent of total revenues, for nine months ended October 31, 2009, compared to $161.7 million, or 21 percent of total revenues, for the same period a year ago, an increase of $28.1 million. The increase in absolute dollars was primarily due to an increase of $5.7 million in employee-related costs, an increase of $1.2 million in stock-based expenses, an increase of $6.4 million in service delivery costs, primarily due to our efforts in increasing data center capacity, an increase of $3.6 million in depreciation and amortization expenses, an increase of $3.6 million of amortized purchased intangibles, an increase of $6.5 million in outside subcontractor and other service costs and an increase of $0.9 million in allocated overhead. The cost of the additional professional services headcount resulted in the cost of professional services

Table of Contents

and other revenues to be in excess of the related revenue for the nine months ended October 31, 2009 by $3.7 million.

Research and Development.

(In thousands)	Nine Months Ended October 31, 2009	2008	Variance Dollars
Research and development	$ 95,450	$ 70,070	$ 25,380
Percent of total revenues	10%	9%	

Research and development expenses were $95.5 million, or 10 percent of total revenues, during the nine months ended October 31, 2009, compared to $70.1 million, or 9 percent of total revenues, during the same period a year ago, an increase of $25.4 million. The increase in absolute dollars was due to an increase of $20.4 million in employee-related costs, an increase of $1.9 million in stock-based expenses, an increase of $1.5 million in infrastructure costs, an increase in professional and outside service costs of $1.3 million and an increase in allocated overhead. We increased our research and development headcount by 15 percent since January 31, 2009 in order to upgrade and extend our service offerings and develop new technologies.

Marketing and Sales.

(In thousands)	Nine Months Ended October 31, 2009	2008	Variance Dollars
Marketing and sales	$ 436,647	$ 389,930	$ 46,717
Percent of total revenues	46%	49%	

Marketing and sales expenses were $436.6 million, or 46 percent of total revenues, during the nine months ended October 31, 2009, compared to $389.9 million, or 49 percent of total revenues, during the same period a year ago, an increase of $46.7 million. The increase in absolute dollars was primarily due to increases of $29.7 million in employee related costs, $2.2 million in stock-based expenses, $1.6 million of amortized purchased intangibles, $4.4 million in allocated overhead, $4.7 million in professional and outside service costs and an increase of $4.1 million in advertising costs and marketing and event costs. Our marketing and sales headcount increased by 4 percent since January 31, 2009 as we hired additional sales personnel to focus on adding new customers and increasing penetration within our existing customer base which is less than the same period a year ago.

General and Administrative.

(In thousands)	Nine Months Ended October 31, 2009	2008	Variance Dollars
General and administrative	$ 139,818	$ 117,797	$ 22,021
Percent of total revenues	15%	15%	

General and administrative expenses were $139.8 million, or 15 percent of total revenues, during the nine months ended October 31, 2009, compared to $117.8 million, or 15 percent of total revenues, during the same period a year ago, an increase of $22.0 million. The increase was primarily due to increases in employee-related costs, stock-based expenses, infrastructure related costs, and professional and outside service costs. Our general and administrative headcount increased by 10 percent since January 31, 2009 as we added personnel to support our growth.

Table of Contents

Operating Income.

(In thousands)	Nine Months Ended October 31, 2009	2008	Variance Dollars
Operating income	$ 89,753	$ 47,652	$ 42,101
Percent of total revenues	9%	6%	

Operating income during the nine months ended October 31, 2009 was $89.8 million and included $62.9 million of stock-based expenses related to ASC 718. During the same period a year ago, operating income was $47.7 million and included $56.2 million of stock-based expenses.

Interest, Net.

(In thousands)	Nine Months Ended October 31, 2009	2008	Variance Dollars
Interest, net	$ 18,987	$ 17,270	$ 1,717
Percent of total revenues	2%	2%	

Interest, net consists of investment income on cash and marketable securities balances and realized gains and losses. Interest, net was $19.0 million during the nine months ended October 31, 2009 and was $17.3 million during the same period a year ago. The increase was primarily due to increased marketable securities balances resulting from the cash generated by operating activities and the proceeds from stock option exercises. Additionally, in fiscal 2009, we recorded a $2.0 million loss related to marketable securities.

Other Expense.

(In thousands)	Nine Months Ended October 31, 2009	2008	Variance Dollars
Other expense	$ (1,037)	$ (1,069)	$ 32

Other expense primarily consists of foreign currency transaction gains and losses.

Provision for Income Taxes.

(In thousands)	Nine Months Ended October 31, 2009	2008	Variance Dollars
Provision for income taxes	$ (45,426)	$ (29,693)	$ (15,733)
Effective tax rate	42%	47%	

Our effective tax rate for the nine months ended October 31, 2009 was 42 percent compared to 47 percent for the same period a year ago. The decrease in the effective tax rate for the nine months was attributable to a higher proportion of income in countries with lower income tax rates than the U.S. statutory tax rate as well as tax benefits derived from domestic manufacturing deductions in this fiscal year. See Note 1 Summary of Business and Significant Accounting Policies for our reconciliation of income taxes at the statutory federal rate to the provision for income taxes.

In addition, on February 20, 2009, the State of California enacted several income tax law changes which include an election to apply a single sales factor apportionment formula and adoption of a market sourcing approach for service income that will impact us beginning in fiscal 2012. As a result, we revalued the anticipated

42

future tax effects of our California temporary differences including stock based compensation and purchased intangibles. Accordingly, we recorded an income tax expense of $2.5 million during the nine months ended October 31, 2009.

New Accounting Pronouncement

In September 2009, the FASB issued Update No. 2009-13, *Revenue Recognition* (Topic 605)*, Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force* (ASU 2009-13). It updates the existing multiple-element revenue arrangements guidance currently included under ASC 605-25. The revised guidance primarily provides two significant changes: 1) eliminates the need for objective and reliable evidence of the fair value for the undelivered element in order for a delivered item to be treated as a separate unit of accounting, and 2) requires the use of the relative selling price method to allocate the entire arrangement consideration. In addition, the guidance also expands the disclosure requirements for revenue recognition. ASU 2009-13 will be effective for the first annual reporting period beginning on or after June 15, 2010, with early adoption permitted provided that the revised guidance is retroactively applied to the beginning of the year of adoption. We are currently assessing the future impact of this new accounting pronouncement to our condensed consolidated financial statements.

Liquidity and Capital Resources

At October 31, 2009, our principal sources of liquidity were cash, cash equivalents and marketable securities totaling $1.1 billion and accounts receivable of $191.3 million.

Net cash provided by operating activities was $179.4 million during the nine months ended October 31, 2009 and $154.0 million during the same period a year ago. The improvement in cash flow was due primarily to the growth in our customer base and the associated increase in billings and collections. Cash provided by operating activities has historically been affected by: the amount of net income; sales of subscriptions, support and professional services; changes in working capital accounts, particularly in accounts receivable and deferred revenue due to the seasonal nature of our customer invoicing, changes in the average invoice duration, rate of renewals and the rate of new business growth; the timing of commission and bonus payments; collections from large enterprise customers; add-backs of non-cash expense items such as depreciation and amortization; and the expense associated with stock-based awards.

Net cash used in investing activities was $473.6 million during the nine months ended October 31, 2009 and $131.7 million during the same period a year ago. The net cash used in investing activities during the nine months ended October 31, 2009 primarily related to the investment of operating cash balances and cash equivalents and capital expenditures in leasehold improvements, and the purchase of software licenses as we have expanded our infrastructure, number of offices around the world and work force, and the purchase of a privately-held company.

Net cash provided by financing activities was $59.5 million during the nine months ended October 31, 2009 and $82.6 million during the same period a year ago. Net cash provided by financing activities during the nine months ended October 31, 2009 consisted of $32.9 million of proceeds from the exercise of employee stock options, $32.5 million of excess tax benefits from employee stock plans and $5.9 million of principal payments on capital leases.

Our cash, cash equivalents and marketable securities are comprised of corporate notes and obligations, U.S. agency obligations, time deposits, money market mutual funds, asset-backed securities, government obligations, mortgage back securities, collateralized mortgage obligations and an investment in The Reserve Primary Fund (The Reserve Fund), a money market mutual fund that suspended redemptions and is in the process of being liquidated.

As of October 31, 2009 our investment portfolio included $7.4 million invested in The Reserve Fund with an estimated fair value of $6.2 million. During fiscal 2009 we recorded a $1.2 million loss related to this decline

Table of Contents

in fair value that is considered other-than-temporary. While we believe we have the rights to the recovery of the entire $7.4 million investment, we cannot predict the amount that we will ultimately receive. Therefore, we have recorded the aforementioned other-than-temporary loss.

As of October 31, 2009 we have a total of $10.5 million in letters of credit outstanding in favor of our landlords for office space in San Francisco, California, New York City, Singapore, Sweden, United Kingdom, Australia and Switzerland. To date, no amounts have been drawn against the letters of credit, which renew annually and mature at various dates through October 2018.

We do not have any special purpose entities, and other than operating leases for office space and computer equipment, we do not engage in off-balance sheet financing arrangements. Additionally, we currently do not have a bank line of credit.

Our principal commitments consist of obligations under leases for office space and co-location facilities for data center capacity and the development and test data center, and computer equipment and furniture and fixtures. At October 31, 2009, the future non-cancelable minimum payments under these commitments were as follows:

	Capital Leases	**Operating Leases**
Fiscal Period:		
Remaining three months in fiscal 2010	$ 1,909	$ 24,734
Fiscal 2011	8,436	75,210
Fiscal 2012	7,555	55,382
Fiscal 2013	1,074	42,126
Fiscal 2014		31,419
Thereafter		62,613
Total minimum lease payments	18,974	$ 291,484
Less: amount representing interest	(1,187)	
Present value of capital lease obligations	$ 17,787	

Our lease agreements provide us with the option to renew. Our future operating lease obligations would change if we exercised these options and if we entered into additional operating lease agreements as we expand our operations.

We believe our existing cash, cash equivalents and short-term marketable securities and cash provided by operating activities will be sufficient to meet our working capital and capital expenditure needs over the next 12 months.

In the future, we may enter into arrangements to acquire or invest in other businesses, services or technologies. While we believe we have sufficient financial resources, we may be required to seek additional equity or debt financing. Additional funds may not be available on terms favorable to us or at all.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign currency exchange risk

Our results of operations and cash flows are subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the Euro, British Pound Sterling, Canadian dollar, Japanese Yen and Australian dollar. We seek to minimize the impact of certain foreign currency fluctuations by entering into certain balance sheet exposures with foreign currency forward and option contracts. Any gain or loss from settling these contracts is offset by the loss or gain derived from the underlying balance sheet exposures. These foreign currency derivative contracts by policy have maturities of less than three months. Additionally, by policy, we do not enter into any of these foreign currency derivative contracts for trading or speculative purposes.

Interest rate sensitivity

We had cash, cash equivalents and marketable securities totaling $1.1 billion at October 31, 2009. These amounts were invested primarily in money market funds, government securities, corporate notes and obligations, agency securities and other debt securities with credit ratings of at least BBB or better by at least two credit agencies. The cash, cash equivalents and short-term marketable securities are held for working capital purposes. Our investments are made for capital preservation purposes. We do not enter into investments for trading or speculative purposes.

We account for our investment instruments in accordance with ASC 320. All of our cash and cash equivalents and marketable securities are treated as available for sale under ASC 320. Our marketable securities include corporate notes and obligations, U.S. treasuries, U.S. agency obligations, time deposits, asset-backed securities and money market mutual funds.

Our cash equivalents and our portfolio of marketable securities are subject to market risk due to changes in interest rates. Fixed rate interest securities may have their market value adversely impacted due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectation due to changes in interest rates or we may suffer losses in principal if we are forced to sell securities that decline in the market value due to changes in interest rates. However because we classify our debt securities as available for sale, no gains or losses are recognized due to changes in interest rates unless such securities are sold prior to maturity or declines in fair value are determined to be other-than-temporary. Our fixed-income portfolio is subject to interest rate risk. An immediate increase or decrease in interest rates of 100-basis points at October 31, 2009 could result in a $12.8 million market value reduction or increase of the same amount. This estimate is based on a sensitivity model that measures market value changes when changes in interest rates occur. Fluctuations in the value of our investment securities caused by a change in interest rates (gains or losses on the carrying value) are recorded in other comprehensive income, and are realized only if we sell the underlying securities.

As previously discussed in Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources, we have an investment in The Reserve Fund, a money market mutual fund. While we believe we have the rights to the recovery of our entire investment, we cannot predict the ultimate amount that we will receive.

At January 31, 2009, we had cash, cash equivalents and marketable securities totaling $882.6 million. The fixed-income portfolio was also subject to interest rate risk. Changes in interest rates of 100-basis points would have resulted in market value changes of $2.3 million.

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of disclosure controls and procedures

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act), as of the end of the period covered by this report (the Evaluation Date).

In designing and evaluating our disclosure controls and procedures, management recognizes that any disclosure controls and procedures, no matter how well designed and operated, can provide only reasonable

Table of Contents

assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply its judgment in evaluating the benefits of possible controls and procedures relative to their costs.

Based on management s evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures are designed to, and are effective to, provide assurance at a reasonable level that the information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission 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 disclosures.

(b) Changes in internal control over financial reporting

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during our most recently completed fiscal quarter. Based on that evaluation, our principal executive officer and principal financial officer concluded that there has not been any material change in our internal control over financial reporting during the quarter covered by this report that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS AND CLAIMS

We are involved in various legal proceedings and receive claims from time to time, arising from the normal course of business activities. In our opinion, resolution of these matters is not expected to have a material adverse impact on our consolidated results of operations, cash flows or our financial position.

During fiscal 2009, we received a notice from a company alleging that we were infringing upon certain of that company s patents. No litigation has been filed to date. We continue to analyze the potential merits of the other company s claims, the potential defenses to such claims and potential counter claims. We intend to vigorously defend our interests in this matter and we are uncertain as to when this matter will be resolved. In our opinion, the resolution of this dispute is not expected to have a material adverse effect on our financial condition, but it could be material to the net income or cash flows of a particular quarter. This claim, or any claim of infringement or violation of intellectual property rights, with or without merit, could require us to change our technology, change our business practices, pay damages, enter into a licensing arrangement or take other actions that may result in additional costs or other actions that are detrimental to our business.

ITEM 1A. RISK FACTORS

The risks and uncertainties described below are not the only ones facing us. Other events that we do not currently anticipate or that we currently deem immaterial also may affect our results of operations and financial condition.

Risks Related to Our Business and Industry

Defects or disruptions in our service could diminish demand for our service and subject us to substantial liability.

Because our service is complex and we have incorporated a variety of new computer hardware and software, both developed in-house and acquired from third party vendors, our service may have errors or defects that users identify after they begin using it that could result in unanticipated downtime for our subscribers and harm our reputation and our business. Internet-based services frequently contain undetected errors when first introduced or when new versions or enhancements are released. We have from time to time found defects in our service and new errors in our existing service may be detected in the future. In addition, our customers may use our service in unanticipated ways that may cause a disruption in service for other customers attempting to access their data. Since our customers use our service for important aspects of their business, any errors, defects, disruptions in service or other performance problems with our service could hurt our reputation and may damage our customers businesses. If that occurs, customers could elect not to renew, or delay or withhold payment to us, we could lose future sales or customers may make warranty claims against us, which could result in an increase in our provision for doubtful accounts, an increase in collection cycles for accounts receivable or the expense and risk of litigation.

Interruptions or delays in service from our third-party data center hosting facilities could impair the delivery of our service and harm our business.

We currently serve our customers from a third-party data center hosting facility located on the west coast of the United States and we plan to begin to serve some customers from a third-party data center hosting facility located on the east coast of the United States. Additionally, we recently started serving customers from a new data center hosting facility in Singapore. Any damage to, or failure of, our systems generally could result in interruptions in our service. As we continue to add capacity in our existing and future data centers, we may move or transfer data. Despite precautions taken during this process, any unsuccessful data transfers may impair the delivery of our service. Further, any damage to, or failure of, our systems generally could result in interruptions in our service. Interruptions in our service may reduce our revenue, cause us to issue credits or pay penalties, cause customers to terminate their subscriptions and adversely affect our renewal rates and our ability to attract new customers. Our business will also be harmed if our customers and potential customers believe our service is unreliable.

Table of Contents

As part of our current disaster recovery arrangements, our production environment and all of our customers data is currently replicated in near real-time in a separate standby facility located on the east coast. Features added through acquisition are temporarily served through alternate facilities. We do not control the operation of any of these facilities, and they are vulnerable to damage or interruption from earthquakes, floods, fires, power loss, telecommunications failures and similar events. They may also be subject to break-ins, sabotage, intentional acts of vandalism and similar misconduct. Despite precautions taken at these facilities, the occurrence of a natural disaster or an act of terrorism, a decision to close the facilities without adequate notice or other unanticipated problems at these facilities could result in lengthy interruptions in our service. Even with the disaster recovery arrangements, our service could be interrupted.

If our security measures are breached and unauthorized access is obtained to a customer s data or our data, our service may be perceived as not being secure, customers may curtail or stop using our service and we may incur significant legal and financial exposure and liabilities.

Our service involves the storage and transmission of customers proprietary information, and security breaches could expose us to a risk of loss of this information, litigation and possible liability. If our security measures are breached as a result of third-party action, employee error, malfeasance or otherwise, during transfer of data to additional data centers or at any time, and, as a result, someone obtains unauthorized access to our data or our customers data, our reputation could be damaged, our business may suffer and we could incur significant liability. Additionally, third parties may attempt to fraudulently induce employees or customers into disclosing sensitive information such as user names, passwords or other information in order to gain access to our data or our customers data, which could result in significant legal and financial exposure and a loss of confidence in the security of our service that would harm our future business prospects. Because the techniques used to obtain unauthorized access, or to sabotage systems, change frequently and generally are not recognized until launched against a target, we may be unable to anticipate these techniques or to implement adequate preventative measures. If an actual or perceived breach of our security occurs, the market perception of the effectiveness of our security measures could be harmed and we could lose sales and customers. In addition, our customers may authorize third party technology providers, whose applications are available through our AppExchange directory, to access their customer data. Because we do not control the transmissions between our customers and third-party AppExchange technology providers, or the processing of such data by third-party AppExchange technology providers, we cannot ensure the complete integrity or security of such transmissions or processing.

Weakened global economic conditions may adversely affect our industry, business and results of operations.

Our overall performance depends in part on worldwide economic conditions. The United States and other key international economies have been impacted by a severe recession, characterized by falling demand for a variety of goods and services, restricted credit, going concern threats to financial institutions, major multinational companies and medium and small businesses, poor liquidity, declining asset values, reduced corporate profitability, extreme volatility in credit, equity and foreign exchange markets and bankruptcies. These conditions affect the rate of information technology spending and could adversely affect our customers ability or willingness to purchase our enterprise cloud computing application service, delay prospective customers purchasing decisions, reduce the value or duration of their subscription contracts, or affect renewal rates, all of which could adversely affect our operating results. Companies that have competing products may reduce prices for competing products or services which could also reduce our average selling prices and harm our operating results.

Because we recognize revenue from subscriptions for our service over the term of the subscription, downturns or upturns in sales may not be immediately reflected in our operating results.

We generally recognize revenue from customers ratably over the terms of their subscription agreements, which are typically 12 to 24 months, although terms can range from one to 60 months. As a result, most of the revenue we report in each quarter is derived from the recognition of deferred revenue relating to subscription agreements entered into during previous quarters. Consequently, a decline in new or renewed subscriptions in any one quarter will be fully reflected in the deferred revenue balance on our consolidated balance sheet and the revenue in that quarter, and will negatively affect our revenue in future quarters. In addition, we may be unable to adjust our cost structure to reflect the changes in revenues. Accordingly, the effect of significant downturns in sales and market acceptance of our service, and potential changes in our rate of renewals may not be fully reflected in our results of operations until future periods. Our subscription model also makes it difficult for us to rapidly increase our revenue through additional sales in any period, as revenue from new customers must be recognized over the applicable subscription term.

If we experience significant fluctuations in our rate of anticipated growth and fail to balance our expenses with our revenue forecasts, our results could be harmed and our stock price may decline without advance notice.

Due to our evolving business model, the unpredictability of new markets that we enter and deteriorating general economic and financial market conditions, we may not be able to accurately forecast our rate of growth. We plan our expense levels and investment on estimates of future revenue and future anticipated rate of growth. We may not be able to adjust our spending quickly enough if the addition of new subscriptions or the renewal rate for existing subscriptions falls short of our expectations.

As a result, we expect that our revenues, operating results and cash flows may fluctuate significantly on a quarterly basis. Our recent revenue growth rates may not be sustainable and may decline in the future. We believe that period-to-period comparisons of our revenues, operating results and cash flows may not be meaningful and should not be relied upon as an indication of future performance.

We cannot accurately predict subscription renewal or upgrade rates and the impact these rates may have on our future revenue and operating results.

Our customers have no obligation to renew their subscriptions for our service after the expiration of their initial subscription period, which is typically 12 to 24 months, and in fact, some customers have elected not to renew. In addition, our customers may renew for fewer subscriptions or renew for shorter contract lengths. We cannot accurately predict renewal rates, particularly for our enterprise customers who purchase a large number of subscriptions under multi-year contracts and for our small and medium size business customers. Our renewal rates may decline or fluctuate as a result of a number of factors, including customer dissatisfaction with our service, customers   ability to continue their operations and spending levels, decreases in the number of users at our customers and deteriorating general economic conditions. If our customers do not renew their subscriptions for our service or reduce the number of paying subscriptions at the time of renewal, our revenue will decline and our business will suffer.

Our future success also depends in part on our ability to sell additional features and services, more subscriptions or enhanced editions of our service to our current customers. This may also require increasingly sophisticated and costly sales efforts that are targeted at senior management. Similarly to renewal rates, the rate at which our customers purchase new or enhanced services depends on a number of factors, including general economic conditions. If our efforts to upsell to our customers are not successful, our business may suffer.

Our quarterly results can fluctuate and if we fail to meet the expectations of analysts or investors, our stock price and the value of your investment could decline substantially.

Our quarterly operating results are likely to fluctuate, and if we fail to meet or exceed the expectations of securities analysts or investors, the trading price of our common stock could decline. Moreover, our stock price may be based on expectations of our future performance that may be unrealistic or that may not be met. Some of the important factors that could cause our revenues, operating results and cash flows to fluctuate from quarter to quarter include:

- our ability to retain and increase sales to existing customers, attract new customers and satisfy our customers requirements;
- the renewal rates for our service;
- the amount and timing of operating costs and capital expenditures related to the operations and expansion of our business;
- the number of new employees added;
- changes in our pricing policies whether initiated by us or as a result of intense competition;
- the cost, timing and management effort for the introduction of new features to our service;
- the rate of expansion and productivity of our sales force;
- the length of the sales cycle for our service;
- new product and service introductions by our competitors;
- our success in selling our service to large enterprises;
- variations in the revenue mix of editions of our service;
- technical difficulties or interruptions in our service;
- expenses related to increasing our data center capacity and expanding our data centers domestically and internationally;
- changes in foreign currency exchange rates;
- changes in interest rates, which would impact our return on our investments in cash and marketable securities;
- conditions, particularly sudden changes, in the financial markets have and may continue to impact the value of and access to our investment portfolio;

changes in the effective tax rates;

general economic conditions could adversely affect either our customers ability or willingness to purchase additional subscriptions or upgrade their service, or delay a prospective customers purchasing decision, or reduce the value of new subscription contracts, or affect renewal rates, all of which could adversely affect our operating results;

timing of additional investments in our enterprise cloud computing application service and in our consulting service;

changes in deferred revenue balances due to the seasonal nature of our customer invoicing, changes in the average duration of our invoices, rate of renewals and the rate of new business growth;

regulatory compliance costs;

the timing of customer payments and payment defaults by customers;

costs associated with acquisitions of companies and technologies;

extraordinary expenses such as litigation or other dispute-related settlement payments;

the impact of new accounting pronouncements; and

the timing of stock awards to employees and the related adverse financial statement impact of having to expense those stock awards ratably over their 4 year vesting schedules.

Many of these factors are not within our control, and the occurrence of one or more of them might cause our operating results to vary widely. As such, we believe that quarter-to-quarter comparisons of our revenues, operating results and cash flows may not be meaningful and should not be relied upon as an indication of future performance.

We rely on third-party computer hardware and software that may be difficult to replace or which could cause errors or failures of our service.

We rely on computer hardware purchased or leased and software licensed from third parties in order to offer our service, including database software from Oracle Corporation. This hardware and software may not continue to be available at reasonable prices or on commercially reasonable terms, or at all. Any loss of the right to use any of this hardware or software could significantly increase our expenses and otherwise result in delays in the provisioning of our service until equivalent technology is either developed by us, or, if available, is identified, obtained and integrated, which could harm our business. Any errors or defects in third-party hardware or software could result in errors or a failure of our service which could harm our business.

Efforts we are making to expand our service beyond the CRM market may not succeed and may reduce our revenue growth rate and cause us to incur additional liabilities.

In fiscal 2006 we introduced the AppExchange directory, an on-line marketplace for enterprise cloud computing applications that run on our Force.com cloud computing platform. The market for third-party on-demand applications and our platform is new and unproven, and it is uncertain whether the initiative will ever result in significant revenue for us. Among other things, the success of the AppExchange will depend to a substantial extent on the willingness of third-party technology providers to write enterprise cloud computing applications that run on our platform and the willingness of enterprises, large and small, to purchase and deploy these applications. If third-party technology providers or enterprises do not perceive the benefits of our on-line application marketplace, then the market for this initiative may not develop at all, or it may develop more slowly than we expect, either of which would affect our ability to grow our revenue. Given this new and unproven market, we have limited insight into trends that may develop and affect this initiative. In addition, our customers may not authorize such third-party technology providers to access their customer data. If our customers do authorize such access, we do not warrant the functionality, security and integrity of the data transmission or processing. Further, despite contract provisions designed to protect us, customers may look to us to support and warrant the third-party applications, which may expose us to potential claims, liabilities and obligations for applications we did not develop or sell. Moreover, the AppExchange directory, and other efforts to expand our service beyond the CRM market, may divert management resources from existing operations and require us to commit significant financial resources to an unproven business, which may harm our business.

The market for our technology delivery model and enterprise cloud computing application services is immature and volatile, and if it develops more slowly than we expect, our business could be harmed.

The market for enterprise cloud computing application services is not as mature as the market for packaged enterprise software, and it is uncertain whether these services will achieve and sustain high levels of demand and market acceptance. Our success will depend to a substantial extent on the willingness of enterprises, large and small, to increase their use of enterprise cloud computing application services in general, and for CRM in particular. Many enterprises have invested substantial personnel and financial resources to integrate traditional enterprise software into their businesses, and therefore may be reluctant or unwilling to migrate to an enterprise cloud computing application service. Furthermore, some enterprises may be reluctant or unwilling to use enterprise cloud computing application services because they have concerns regarding the risks associated with security capabilities, among other things, of the technology delivery model associated with these services. If enterprises do not perceive the benefits of enterprise cloud computing application services, then the market for these services may not develop at all, or it may develop more slowly than we expect, either of which would significantly adversely affect our operating results. In addition, we may make errors in predicting and reacting to

Table of Contents

relevant business trends, which could harm our business. Our success also depends on the willingness of third- party developers to build applications that are complementary to our service. Without the development of these applications, both current and potential customers may not find our service sufficiently attractive.

The market in which we participate is intensely competitive, and if we do not compete effectively, our operating results could be harmed.

The market for CRM, enterprise business applications, and development platforms is highly competitive, rapidly evolving and fragmented, and subject to changing technology, shifting customer needs and frequent introductions of new products and services. Many prospective customers have invested substantial personnel and financial resources to implement and integrate traditional enterprise software into their businesses, and therefore may be reluctant or unwilling to migrate to an enterprise cloud computing application service. Additionally, third party developers may be reluctant to build application services on our platform since they have invested significantly in other competing technology products.

We compete primarily with vendors of packaged CRM software, whose software is installed by the customer directly, and companies offering on-demand CRM applications. We also compete with internally developed applications and face, or expect to face, competition from enterprise software vendors and online service providers who may develop toolsets and products that allow customers to build new applications that run on the customers current infrastructure or as hosted services. Our current principal competitors include:

- enterprise software application vendors including Microsoft Corporation, Oracle Corporation, and SAP AG;
- packaged CRM software vendors, some of which offer hosted services, such as CDC Software Corporation, a subsidiary of chinadotcom corporation, Consona Corporation, Pivotal Corporation, which is owned by Sage Group plc, and SugarCRM;
- on-demand CRM application service providers such as Microsoft Corporation, NetSuite, Inc., Oracle Corporation, RightNow Technologies, Inc., and SAP AG;
- enterprise application service providers including IBM Corporation and Oracle Corporation;
- traditional platform and development environment companies, including established vendors, such as IBM Corporation, Microsoft Corporation, and Oracle Corporation; and an array of emerging vendors that have gained traction with the press and analyst communities; and
- cloud computing development platform companies, including some with whom we are partners, others such as Microsoft Corporation, which has initiated plans to enter this market, and a variety of smaller start up companies that have invested in cloud computing technology.

In addition, we face competition from businesses that develop their own CRM applications internally, as well as from enterprise software vendors and online service providers who may develop and/or bundle CRM products with their products in the future. For small business customers, we also face competition from companies whose offering is based on Microsoft Outlook and Excel for limited contact management functionality. We also face competition from some of our larger and more established competitors who historically have been packaged CRM software vendors, but who also have directly competitive on-demand CRM application services offerings.

Our professional services organization may compete with some systems integrators, including Accenture Ltd., Deloitte Consulting and IBM Corporation; it may also compete with some ISV service providers that have service practices. We have close relationships with many of these consulting companies and frequently work cooperatively on projects with them.

Many of our competitors and potential competitors enjoy substantial competitive advantages, such as greater name recognition, longer operating histories and larger marketing budgets, as well as substantially greater financial, technical and other resources. In addition, many of our competitors have established marketing relationships and access to larger customer bases, and have major distribution agreements with consultants, system integrators and resellers.

As a result, our competitors may be able to respond more quickly and effectively than we can to new or changing opportunities, technologies, standards or customer requirements. Furthermore, because of these advantages, even if our service is more effective than the products that our competitors offer, potential customers might accept competitive products and services in lieu of purchasing our service. For all of these reasons, we may not be able to compete successfully against our current and future competitors.

If our enterprise cloud computing application service is not widely accepted in markets where we have few customers, our future growth will be limited.

We derive substantially all of our revenue from subscriptions to our enterprise cloud computing application service, and we expect this will continue for the foreseeable future. As a result, widespread acceptance of our service by companies located outside the United States or in industries where we currently have few customers is critical to our future growth. Factors that may affect market acceptance of our service include:

- reluctance by enterprises to migrate to an enterprise cloud computing application service;
- a limited number of service offerings and risks associated with developing new service offerings;
- the price and performance of our service;
- the level of customization we can offer;
- the location of our data centers;
- the availability, performance and price of competing products and services;
- reluctance by enterprises to trust third parties to store and manage their internal data; and
- adverse publicity about us, our service or the viability, reliability or security of enterprise cloud computing application services generally from third party reviews, industry analyst reports and our competitors.

Many of these factors are beyond our control. The inability of our enterprise cloud computing application service to achieve widespread market acceptance as described above would harm our business.

Supporting our existing and growing customer base could strain our personnel resources and infrastructure, and if we are unable to scale our operations and increase productivity, we may not be able to successfully implement our business plan.

Since we were formed in 1999, we have experienced significant growth in our customer base, which has placed a strain on our management, administrative, operational and financial infrastructure. We anticipate that additional investments in our infrastructure and research and development spending will be required to scale our operations and increase productivity, to address the needs of our customers, to further develop and enhance our service, and to expand into new geographic areas.

Our success will depend in part upon the ability of our senior management to manage our projected growth effectively. To do so, we must continue to increase the productivity of our existing employees and to hire, train and manage new employees as needed. To manage the expected domestic and international growth of our operations and personnel, we will need to continue to improve our operational, financial and management controls and our reporting systems and procedures. The additional investments we are making will increase our cost base, which will make it more difficult for us to offset any future revenue shortfalls by reducing expenses in

Table of Contents

the short term. If we fail to successfully scale our operations and increase productivity, we will be unable to execute our business plan.

As more of our sales efforts are targeted at larger enterprise customers, our sales cycle may become more time-consuming and expensive, we may encounter pricing pressure and implementation challenges, and we may have to delay revenue recognition for some complex transactions, all of which could harm our business and operating results.

As we target more of our sales efforts at larger enterprise customers, we will face greater costs, longer sales cycles and less predictability in completing some of our sales. In this market segment, the customer s decision to use our service may be an enterprise-wide decision and, if so, these types of sales would require us to provide greater levels of education regarding the use and benefits of our service, as well as education regarding privacy and data protection laws and regulations to prospective customers with international operations. In addition, larger customers may demand more customization, integration services and features. As a result of these factors, these sales opportunities may require us to devote greater sales support and professional services resources to individual customers, driving up costs and time required to complete sales and diverting sales and professional services resources to a smaller number of larger transactions, while potentially requiring us to delay revenue recognition on some of these transactions until the technical or implementation requirements have been met.

Periodic restructurings of our sales organization can be disruptive and may negatively impact our revenues.

We periodically restructure or make other adjustments to our sales organization in response to market opportunities, competitive threats, management changes, product introductions or enhancements, sales performance, increases in sales headcount, cost levels, and other internal and external considerations. In the past, these restructurings sometimes resulted in a temporary lack of focus and reduced productivity; these effects could recur in connection with any future sales restructurings we might undertake and our rate of revenue growth could be negatively affected.

If we are not able to develop enhancements and new features to our existing service or acceptable new services that keep pace with technological developments, our business will be harmed.

If we are unable to develop enhancements to and new features for our existing service or acceptable new services that keep pace with rapid technological developments, our business will be harmed. The success of enhancements, new features and services depends on several factors, including the timely completion, introduction and market acceptance of the feature or edition. Failure in this regard may significantly impair our revenue growth. In addition, because our service is designed to operate on a variety of network hardware and software platforms using a standard browser, we will need to continuously modify and enhance our service to keep pace with changes in Internet-related hardware, software, communication, browser and database technologies. We may not be successful in either developing these modifications and enhancements or in timely bringing them to market. Furthermore, uncertainties about the timing and nature of new network platforms or technologies, or modifications to existing platforms or technologies, could increase our research and development expenses. Any failure of our service to operate effectively with future network platforms and technologies could reduce the demand for our service, result in customer dissatisfaction and harm our business.

Any failure to protect our intellectual property rights could impair our ability to protect our proprietary technology and our brand.

If we fail to protect our intellectual property rights adequately, our competitors might gain access to our technology, and our business might be harmed. In addition, defending our intellectual property rights might entail significant expense. Any of our trademarks or other intellectual property rights may be challenged by others or invalidated through administrative process or litigation. While we have a few U.S. patents and many other U.S.

Table of Contents

patent applications pending, we may be unable to obtain patent protection for the technology covered in our patent applications. In addition, our existing patents and any patents issued in the future may not provide us with competitive advantages, or may be successfully challenged by third parties. Furthermore, legal standards relating to the validity, enforceability and scope of protection of intellectual property rights are uncertain. Effective patent, trademark, copyright and trade secret protection may not be available to us in every country in which our service is available. The laws of some foreign countries may not be as protective of intellectual property rights as those in the U.S., and mechanisms for enforcement of intellectual property rights may be inadequate. Accordingly, despite our efforts, we may be unable to prevent third parties from infringing upon or misappropriating our intellectual property.

We might be required to spend significant resources to monitor and protect our intellectual property rights. We may initiate claims or litigation against third parties for infringement of our proprietary rights or to establish the validity of our proprietary rights. Any litigation, whether or not it is resolved in our favor, could result in significant expense to us and divert the efforts of our technical and management personnel.

We have been and may in the future be sued by third parties for alleged infringement of their proprietary rights.

The software and Internet industries are characterized by the existence of a large number of patents, trademarks and copyrights and by frequent litigation based on allegations of infringement or other violations of intellectual property rights. We have received in the past, have recently received and may receive in the future, communications from third parties claiming that we have infringed on the intellectual property rights of others. In addition, we have been, and may in the future be, sued by third parties for alleged infringement of their proprietary rights. Our technologies may not be able to withstand any third-party claims or rights against their use. Any intellectual property claims, with or without merit, could be time-consuming and expensive to resolve, could divert management attention from executing our business plan and could require us to pay monetary damages or enter into royalty or licensing agreements. In addition, many of our subscription agreements require us to indemnify our customers for third-party intellectual property infringement claims, which would increase the cost to us of an adverse ruling on such a claim. Any adverse determination related to intellectual property claims or litigation could prevent us from offering our service to others, could be material to our net income or cash flows of a particular quarter or could otherwise adversely affect our operating results.

If we fail to develop our brands cost-effectively, our business may suffer.

We believe that developing and maintaining awareness of the salesforce.com brand and our other brands in a cost-effective manner is critical to achieving widespread acceptance of our existing and future services and is an important element in attracting new customers. Furthermore, we believe that the importance of brand recognition will increase as competition in our market develops. Successful promotion of our brands will depend largely on the effectiveness of our marketing efforts and on our ability to provide reliable secure and useful services at competitive prices. In the past, our efforts to build our brands have involved significant expense. Brand promotion activities may not yield increased revenue, and even if they do, any increased revenue may not offset the expenses we incurred in building our brands. If we fail to successfully promote and maintain our brands, or incur substantial expenses in an unsuccessful attempt to promote and maintain our brands, we may fail to attract enough new customers or retain our existing customers to the extent necessary to realize a sufficient return on our brand-building efforts, and our business could suffer.

Our business could be adversely affected if our customers are not satisfied with implementation and customization services provided by us or our partners.

Our business depends on our ability to satisfy our customers, both with respect to our CRM service and platform and the professional services that customize our CRM service and platform to meet our customers business needs. Professional services may be performed by our own staff, or by a third party or a combination of

Table of Contents

the two. Our strategy is to work with third parties to increase the breadth of capability and depth of capacity for delivery of these services to our customers. If a customer is not satisfied with the quality of work performed by us or a third party or with the type of services or solutions delivered, then we could incur additional costs to address the situation, the profitability of that work might be impaired, and the customer s dissatisfaction with our services could damage our ability to obtain additional work from that customer. In addition, negative publicity related to our customer relationships, regardless of its accuracy, may further damage our business by affecting our ability to compete for new business with current and prospective customers.

Sales to customers outside the United States expose us to risks inherent in international sales.

Because we sell our service throughout the world, we are subject to risks and challenges that we would otherwise not face if we conducted our business only in the United States. For example, sales in Europe and Asia Pacific together represent over 25 percent of our total revenues, and we intend to continue to expand our international sales efforts. The risks and challenges associated with sales to customers outside the United States include:

- localization of our service, including translation into foreign languages and associated expenses;
- laws and business practices favoring local competitors;
- compliance with multiple, conflicting and changing governmental laws and regulations, including employment, tax, privacy and data protection laws and regulations;
- regional data privacy laws that apply to the transmission of our customers data across international borders;
- foreign currency fluctuations;
- different pricing environments;
- difficulties in staffing and managing foreign operations;
- different or lesser protection of our intellectual property;
- longer accounts receivable payment cycles and other collection difficulties;
- regional economic conditions, including the affect of general economic and financial market conditions in the markets in which we operate outside the United States; and
- regional political conditions.

Any of these factors could negatively impact our business and results of operations.

Additionally, some of our international subscription fees are currently paid in local currency. As a result, fluctuations in the value of the U.S. dollar and foreign currencies may make our service more expensive for international customers, which could harm our business.

Evolving regulation of the Internet may affect us adversely.

As Internet commerce continues to evolve, increasing regulation by federal, state or foreign agencies becomes more likely. For example, we believe increased regulation is likely in the area of data privacy, and laws and regulations applying to the solicitation, collection, processing or use of personal or consumer information could affect our customers ability to use and share data, potentially reducing demand for CRM solutions and restricting our ability to store, process and share data with our customers. In addition, taxation of services provided over the Internet or other charges imposed by government agencies or by private organizations for accessing the Internet may also be imposed. Any regulation imposing greater fees for Internet use or restricting information exchange over the Internet could result in a decline in the use of the Internet and the viability of Internet-based services, which could harm our business.

Table of Contents

Privacy concerns and laws or other domestic or foreign regulations may reduce the effectiveness of our solution and adversely affect our business.

Our customers can use our service to store contact and other personal or identifying information regarding their customers and contacts. Federal, state and foreign government bodies and agencies, however, have adopted or are considering adopting laws and regulations regarding the collection, use and disclosure of personal information obtained from consumers and individuals. The costs of compliance with, and other burdens imposed by, such laws and regulations that are applicable to the businesses of our customers may limit the use and adoption of our service and reduce overall demand for it. Furthermore, privacy concerns may cause our customers customers to resist providing the personal data necessary to allow our customers to use our service effectively. Even the perception of privacy concerns, whether or not valid, may inhibit market adoption of our service in certain industries.

For example, in the United States regulations such as the Gramm-Leach-Bliley Act, which protects and restricts the use of consumer credit and financial information, and the Health Insurance Portability and Accountability Act of 1996, which regulates the use and disclosure of personal health information, impose significant requirements and obligations on businesses that may affect the use and adoption of our service.

The European Union has also adopted a data privacy directive that requires member states to impose restrictions on the collection and use of personal data that, in some respects, are far more stringent, and impose more significant burdens on subject businesses, than current privacy standards in the United States. All of these domestic and international legislative and regulatory initiatives may adversely affect our customers ability to collect and/or use demographic and personal information from their customers, which could reduce demand for our service. Many if not most other jurisdictions, including Asia countries, have similar stringent privacy laws and regulations.

In addition to government activity, privacy advocacy groups and the technology and other industries are considering various new, additional or different self-regulatory standards that may place additional burdens on us. If the gathering of personal information were to be curtailed in this manner, CRM solutions would be less effective, which may reduce demand for our service and harm our business.

We are dependent on our management team and development and operations personnel, and the loss of one or more key employees or groups could harm our business and prevent us from implementing our business plan in a timely manner.

Our success depends substantially upon the continued services of our executive officers and other key members of management, particularly our Chief Executive Officer. From time to time, there may be changes in our executive management team resulting from the hiring or departure of executives. Such changes in our executive management team may be disruptive to our business.

We are also substantially dependent on the continued service of our existing development and operations personnel because of the complexity of our service and technologies.

We do not have employment agreements with any of our executive officers, key management, development or operations personnel and, therefore, they could terminate their employment with us at any time. We do not maintain key person life insurance policies on any of our employees. The loss of one or more of our key employees or groups could seriously harm our business.

Because competition for our target employees is intense, we may not be able to attract and retain the highly skilled employees we need to support our operations and increasing customer base.

In the technology industry, there is substantial and continuous competition for engineers with high levels of experience in designing, developing and managing software and Internet-related services, as well as competition

Table of Contents

for sales executives and operations personnel. We may not be successful in attracting and retaining qualified personnel. We have from time to time experienced, and we expect to continue to experience, difficulty in hiring and retaining highly skilled employees with appropriate qualifications. In addition, job candidates and existing employees often consider the value of the stock awards they receive in connection with their employment. If our stock price performs poorly, it may adversely affect our ability to retain highly skilled employees. In addition, since we expense all stock-based compensation, we may periodically change our stock compensation practices, which may include reducing the number of employees eligible for options or reducing the size of equity awards granted per employee. If we fail to attract new personnel or fail to retain and motivate our current personnel, our business and future growth prospects could be severely harmed.

As we acquire companies or technologies in the future, they could prove difficult to integrate, disrupt our business, dilute stockholder value and adversely affect our operating results and the value of our common stock.

As part of our business strategy, we may acquire, enter into joint ventures with or make investments in complementary companies, services and technologies in the future. Acquisitions and investments involve numerous risks, including:

- the potential failure to achieve the expected benefits of the combination or acquisition;
- difficulties in and the cost of integrating operations, technologies, services and personnel;
- diversion of financial and managerial resources from existing operations;
- risk of entering new markets in which we have little or no experience;
- potential write-offs of acquired assets or investments;
- potential loss of key employees;
- inability to generate sufficient revenue to offset acquisition or investment costs;
- the inability to maintain relationships with customers and partners of the acquired business;
- the difficulty of incorporating acquired technology and rights into our products and services and of maintaining quality standards consistent with our brand;
- potential unknown liabilities associated with the acquired businesses;
- unanticipated expenses related to acquired technology and its integration into existing technology;
- negative impact to our results of operations because of the depreciation and amortization of amounts related to acquired intangible assets, fixed assets and deferred compensation, and the loss of acquired deferred revenue;

- delays in customer purchases due to uncertainty;
- the need to implement controls, procedures and policies appropriate for a public company at companies that prior to the acquisition lacked such controls, procedures and policies; and
- challenges caused by distance, language and cultural differences.

In addition, if we finance acquisitions by issuing convertible debt or equity securities, our existing stockholders may be diluted which could affect the market price of our stock. Further, if we fail to properly evaluate and execute acquisitions or investments, our business and prospects may be seriously harmed and the value of our common stock may decline.

Our business is subject to changing regulations regarding corporate governance and public disclosure that have increased both our costs and the risk of non-compliance.

We are subject to rules and regulations by various governing bodies, including, for example, the Securities and Exchange Commission, which are charged with the protection of investors and the oversight of companies whose securities are publicly traded. Our efforts to comply with new and changing regulations have resulted in and are likely to continue to result in, increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities.

We are required to comply on an on-going basis with the Sarbanes-Oxley Act, or SOX, requirements involving the assessment of our internal controls over financial reporting. Our efforts to comply with the SOX requirements have required, and will continue to require the commitment of significant financial and personnel resources.

Moreover, because these laws, regulations and standards are subject to varying interpretations, their application in practice may evolve over time as new guidance becomes available. This evolution may result in continuing uncertainty regarding compliance matters and additional costs necessitated by ongoing revisions to our disclosure and governance practices. If we fail to address and comply with these regulations and any subsequent changes, our business may be harmed.

Unanticipated changes in our effective tax rate could adversely affect our future results.

We are subject to income taxes in the United States and various foreign jurisdictions, and our domestic and international tax liabilities are subject to the allocation of expenses in differing jurisdictions.

Our effective tax rate could be adversely affected by changes in the mix of earnings and losses in countries with differing statutory tax rates, certain non-deductible expenses arising from stock option compensation, the valuation of deferred tax assets and liabilities and changes in federal, state or international tax laws and accounting principles. Increases in our effective tax rate could materially affect our net results.

In addition, we are subject to income tax audits by many tax jurisdictions throughout the world. Although we believe our income tax liabilities are reasonably estimated and accounted for in accordance with applicable laws and principles, an adverse resolution of one or more uncertain tax positions in any period could have a material impact on the results of operations for that period.

Natural disasters and other events beyond our control could materially adversely affect us.

Natural disasters or other catastrophic events may cause damage or disruption to our operations, international commerce and the global economy, and thus could have a strong negative effect on us. Our business operations are subject to interruption by natural disasters, fire, power shortages, pandemics and other events beyond our control. Although we maintain crisis management and disaster response plans, such events could make it difficult or impossible for us to deliver our services to our customers, and could decrease demand for our services. The majority of our research and development activities, corporate headquarters, information technology systems, and other critical business operations, are located near major seismic faults in the San Francisco Bay Area. Because we do not carry earthquake insurance for direct quake-related losses, and significant recovery time could be required to resume operations, our financial condition and operating results could be materially adversely affected in the event of a major earthquake or catastrophic event.

Table of Contents

Risks Related to Ownership of Our Common Stock

The trading price of our common stock is likely to be volatile and could subject us to litigation.

The trading prices of the securities of technology companies have been highly volatile. Accordingly, the trading price of our common stock has been and is likely to continue to be subject to wide fluctuations. Factors affecting the trading price of our common stock include:

- variations in our operating results, earnings per share, cash flows from operating activities, deferred revenue, and other financial metrics and non-financial metrics, and how those results compare to analyst expectations;
- forward looking guidance to industry and financial analysts related to future revenue and earnings per share;
- the net increases in the number of customers and paying subscriptions, either independently or as compared with published expectations of industry, financial or other analysts that cover our company;
- changes in the estimates of our operating results or changes in recommendations by securities analysts that elect to follow our common stock;
- announcements of technological innovations, new services or service enhancements, strategic alliances or significant agreements by us or by our competitors;
- announcements by us or by our competitors of mergers or other strategic acquisitions, or rumors of such transactions involving us or our competitors;
- announcements of customer additions and customer cancellations or delays in customer purchases;
- recruitment or departure of key personnel;
- disruptions in our service due to computer hardware, software or network problems;
- the economy as a whole, market conditions in our industry, and the industries of our customers; and
- trading activity by a limited number of stockholders who together beneficially own a majority of our outstanding common stock.

In addition, if the market for technology stocks or the stock market in general experiences uneven investor confidence, the trading price of our common stock could decline for reasons unrelated to our business, operating results or financial condition. The trading price of our common stock might also decline in reaction to events that affect other companies within, or outside, our industry even if these events do not directly affect us.

If securities analysts stop publishing research or reports about us or our business or if they downgrade our stock, the price of our stock could decline.

The trading market for our common stock relies in part on the research and reports that industry or financial analysts publish about us or our business. We do not control these analysts. If one or more of the analysts who do cover us downgrade our stock or lower their future stock price targets or estimates of our operating results, our stock price could decline rapidly. Furthermore, if one or more of these analysts cease coverage of our company, we could lose visibility in the market, which in turn could cause our stock price to decline.

The concentration of our capital stock ownership with insiders will likely limit your ability to influence corporate matters.

Our executive officers, directors, and several stockholders and their affiliated entities together beneficially own a majority of our outstanding common stock.

As a result, these stockholders, if they act together or in a block, could have significant influence over most matters that require approval by our stockholders, including the election of directors and approval of significant corporate transactions, even if other stockholders oppose them. This concentration of ownership might also have the effect of delaying or preventing a change of control of our company that other stockholders may view as beneficial.

Provisions in our amended and restated certificate of incorporation and bylaws and Delaware law might discourage, delay or prevent a change of control of our company or changes in our management and, therefore, depress the trading price of our common stock.

Our amended and restated certificate of incorporation and bylaws contain provisions that could depress the trading price of our common stock by acting to discourage, delay or prevent a change in control of our company or changes in our management that the stockholders of our company may deem advantageous. These provisions among other things:

- establish a classified board of directors so that not all members of our board are elected at one time;
- permit the board of directors to establish the number of directors;
- provide that directors may only be removed for cause and only with the approval of 66 2 /3 percent of our stockholders;
- require super-majority voting to amend some provisions in our amended and restated certificate of incorporation and bylaws;
- authorize the issuance of blank check preferred stock that our board could use to implement stockholder rights (also known as a poison pill);
- eliminate the ability of our stockholders to call special meetings of stockholders;
- prohibit stockholder action by written consent, which requires all stockholder actions to be taken at a meeting of our stockholders;
- provide that the board of directors is expressly authorized to make, alter or repeal our bylaws; and
- establish advance notice requirements for nominations for election to our board or for proposing matters that can be acted upon by stockholders at annual stockholder meetings.

In addition, Section 203 of the Delaware General Corporation Law may discourage, delay or prevent a change in control of our company. Section 203 imposes certain restrictions on merger, business combinations and other transactions between us and holders of 15 percent or more of our common stock.

Table of Contents

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

Not applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

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

Not applicable.

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS

Exhibits

Exhibit 3.1(1)	Amended and Restated Certificate of Incorporation of salesforce.com, inc.
Exhibit 3.2(2)	Amended and Restated Bylaws of salesforce.com, inc.
Exhibit 31.1	Certification of Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a) and 15(d)-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
Exhibit 31.2	Certification of Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a) and 15(d)-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
Exhibit 32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
Exhibit 101.INS(3)	XBRL Instance Document
Exhibit 101.SCH(3)	XBRL Taxonomy Extension Schema Document
Exhibit 101.CAL(3)	XBRL Taxonomy Extension Calculation Linkbase Document
Exhibit 101.LAB(3)	XBRL Taxonomy Extension Label Linkbase Document
Exhibit 101.PRE(3)	XBRL Taxonomy Extension Presentation Linkbase Document

(1) Incorporated by reference from the Company s registration statement on Form S-1 (No. 333-111289) Amendment No. 3 as filed with the Securities and Exchange Commission on April 20, 2004.

(2) Incorporated by reference from the Company s Form 8-K as filed with the Securities and Exchange Commission on December 7, 2008.

(3) The financial information contained in these XBRL documents is unaudited and these are not the official publicly filed financial statements of salesforce.com, inc. The purpose of submitting these XBRL documents is to test the related format and technology, and, as a result, investors should continue to rely on the official filed version of the furnished documents and not rely on this information in making investment decisions. In accordance with Rule 402 of Regulation S-T, the information in these exhibits shall not be deemed to be filed for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and shall not be incorporated by reference into any registration statement or other document filed under the Securities Act, or the Exchange Act, except as shall be expressly set forth by specific reference in such filing.

Table of Contents

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.

Dated: November 25, 2009

salesforce.com, inc.

/s/ Graham Smith
Graham Smith
Chief Financial Officer

(Principal Financial Officer and Duly Authorized Officer)