

SolarWinds, Inc.
Form 8-K
July 21, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 8-K

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

July 21, 2010
Date of Report (Date of earliest event reported)

SOLARWINDS, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State or other
jurisdiction
of incorporation)

001-34358
(Commission File Number)

73-1559348
(IRS Employer
Identification No.)

3711 South MoPac Expressway
Building Two
Austin, Texas 78746
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (512) 682-9300

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (see General Instruction A.2. below):

- Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
- Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
- Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
- Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 2.02 Results of Operations and Financial Condition.

On July 21, 2010, SolarWinds, Inc. (“SolarWinds”) issued a press release regarding its financial results for the second fiscal quarter ended June 30, 2010. A copy of SolarWinds’ press release is attached hereto as Exhibit 99.1.

The information contained in this report shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), or otherwise subject to the liability of that section. The information in this report shall not be incorporated by reference in any filing under the Securities Act of 1933, as amended, or the Exchange Act, except as shall be expressly set forth by specific reference in such a filing.

Item 9.01 Financial Statements and Exhibits.

(d) Exhibits.

| Exhibit Number | Description |
|----------------|---|
| 99.1 | Press release issued by SolarWinds, Inc. dated July 21, 2010. |

SIGNATURE

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 hereunto duly authorized.

SOLARWINDS, INC.

Date: July 21, 2010

By: /s/ Michael J.
Berry
Michael J. Berry
Senior Vice President and Chief Financial Officer

EXHIBIT INDEX

| Exhibit Number | Description |
|-------------------|---|
| 99.1 | Press release issued by SolarWinds, Inc. dated July 21, 2010. |

Exhibit 99.1

SolarWinds Announces Second Quarter 2010 Results

- Record quarterly total revenue of \$35.5 million representing 31% year-over-year growth
- GAAP operating income of \$12.9 million, non-GAAP operating income of \$17.7 million, or 50% of revenue
- GAAP diluted earnings per share of \$0.12, non-GAAP diluted earnings per share of \$0.17

AUSTIN, Texas – July 21, 2010 – SolarWinds® (NYSE: SWI), a leading provider of powerful and affordable IT management software to more than 95,000 customers worldwide, today reported results for its second quarter ended June 30, 2010.

Financial Results

SolarWinds reported record total revenue for the second quarter of 2010 of \$35.5 million, a 31% increase over total revenue in the second quarter of 2009. License revenue was \$17.3 million in the second quarter of 2010, representing an 18% increase over license revenue in the second quarter of 2009. Maintenance revenue was \$18.2 million in the second quarter of 2010, representing a 47% increase over maintenance revenue in the second quarter of 2009, the 13th consecutive quarter of year-over-year growth greater than 40%.

On a GAAP basis, operating income was \$12.9 million, net income was \$8.8 million and diluted earnings per share was \$0.12 in the second quarter of 2010, compared to operating income of \$11.8 million, net income of \$6.8 million and diluted earnings per share of \$0.13 in the second quarter of 2009.

Non-GAAP operating income was \$17.7 million, or 50% of revenue, in the second quarter of 2010 compared to \$14.0 million in the second quarter of 2009. Non-GAAP net income in the second quarter of 2010 was \$12.5 million, a 40% increase over non-GAAP net income of \$8.9 million in the second quarter of 2009. Non-GAAP diluted earnings per share was \$0.17 in the second quarter of 2010 compared to \$0.14 in the second quarter of 2009.

Net cash provided by operating activities was \$16.9 million in the second quarter of 2010 and \$32.8 million for the first six months of 2010 compared to \$7.1 million for the second quarter of 2009 and \$22.0 million for the first six months of 2009, which is a year-to-date increase of 49%. Cash and cash equivalents at the end of the second quarter of 2010 were \$99.8 million, a decrease of only \$4.3 million from the end of the first quarter of 2010 despite the repayment of \$25.0 million of outstanding debt obligations.

Information about SolarWinds' use of non-GAAP financial information is provided under "Non-GAAP Financial Measures" below.

Recent Business Highlights

“This quarter, we continued to see strong demand for our products in the commercial markets,” said Kevin Thompson, SolarWinds’ President and Chief Executive Officer. “IT trends such as virtualization, data center consolidation and SaaS have increased the importance of monitoring and management technologies for companies of all sizes, including the Global 2000. We believe that SolarWinds is uniquely positioned with the right products and the right model to meet the significant market demand for better visibility into the entire IT infrastructure.”

Other business highlights:

- SolarWinds increased its total number of customers during the second quarter to over 95,000. Larger companies continued to come to SolarWinds for cost-effective, easier-to-use solutions, with five new customers during the quarter spending, on average, over \$60,000 in their first SolarWinds purchase.
- SolarWinds released new major versions of several important products, including Orion Network Performance Monitor (NPM) and Orion Network Configuration Manager (NCM), providing new features and functionality to both new and existing SolarWinds customers.
- SolarWinds released two new versions of its Storage Profiler product, acquired from Tek-Tools, Inc. in January 2010, designed to improve the download and evaluation experience and to simplify licensing for customers. SolarWinds also released the industry’s only free multi-vendor storage monitoring tool as part of its strategy to drive awareness and loyalty among potential customers.

“While we experienced lower close rates in sales to the U.S. federal government and a softening of the European market that we first began to see in June, our core business with customers in the global commercial market showed strong growth over the second quarter of 2009,” continued Thompson.

Financial Outlook

As of July 21, 2010, SolarWinds is providing its financial outlook for its third quarter of 2010 and updating its outlook for the full year ending December 31, 2010. The financial information below represents forward-looking non-GAAP financial information, including an estimate of non-GAAP operating income, non-GAAP net income and non-GAAP diluted earnings per share, for the third quarter of 2010 and for the full year 2010. These non-GAAP financial measures exclude, among other items mentioned below, stock-based compensation expense. SolarWinds cannot reasonably estimate the expected stock-based compensation expense for these future periods as the amounts depend upon such factors as the future price of SolarWinds’ stock for purposes of computation. In addition, costs related to non-recurring items and acquisitions are not something that SolarWinds can estimate because they are a function of what non-recurring items and acquisitions, if any, occur and the kind of costs incurred in connection with any such non-recurring items or acquisitions.

Financial Outlook for the Third Quarter of 2010

SolarWinds management currently expects to achieve the following results for the third quarter of 2010:

- Total revenue in the range of \$37.0–\$39.0 million
- Non-GAAP operating income representing 48%–50% of revenue
- Non- GAAP net income of \$12.5–\$13.5 million

- Non-GAAP diluted earnings per share of \$0.165–\$0.180
- Weighted average shares outstanding of approximately 74.5 million

Financial Outlook for Full Year 2010

SolarWinds is revising its outlook, previously announced on April 26, 2010, for the full year 2010 based on several factors, including:

- unfavorable trends in the exchange rate of Euros to US dollars;
- lengthening sales cycles to the U.S. federal government, resulting in decreased predictability of future results and an expected decline in sales to the U.S. federal government; and
- lower expectations for the growth in European sales due to economic issues impacting both the public sector and commercial business customers in the region.

SolarWinds management currently expects to achieve the following results for the full year 2010:

- Total revenue in the range of \$146.0–\$151.0 million, or year-over-year growth of 25%–30%
- Non-GAAP operating income representing 48%–50% of revenue
- Non-GAAP net income of \$49.3–\$52.2 million
- Non-GAAP diluted earnings per share of \$0.67–\$0.70
- Weighted average shares outstanding of approximately 74.0 million

Conference Call and Webcast

In conjunction with this announcement, SolarWinds will host a conference call today to discuss its financial results and other business at 4:00pm CDT (5:00pm EDT/2:00pm PDT). A live webcast of the event will be available on the SolarWinds Investor Relations website at <http://ir.solarwinds.com>. A live dial-in will be available domestically at 800-390-5311 and internationally at +1-719-325-2163. To access the live call, please dial in 5-10 minutes before the scheduled start time. A replay of the webcast will be available on a temporary basis shortly after the event on the SolarWinds Investor Relations website.

Forward-Looking Statements

This press release contains "forward-looking" statements relating to SolarWinds' possible or assumed future results of operations and potential growth and market opportunities. These forward-looking statements are based on management's beliefs and assumptions and on information currently available to management. Forward-looking statements include all statements that are not historical facts and may be identified by terms such as "expects," "believes" or similar expressions and the negatives of those terms. Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements to be

materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, the following: (a) the possibility that general economic conditions or uncertainty cause information technology spending to be reduced or purchasing decisions to be delayed; (b) the presence or absence of occasional large customer orders, including in particular those placed by the U.S. federal government; (c) the inability to increase sales to existing customers and to attract new customers; (d) SolarWinds' failure to integrate acquired businesses and any future acquisitions successfully; (e) the timing and success of new product introductions by SolarWinds or its competitors; (f) changes in SolarWinds' pricing policies or those of its competitors; (g) the loss of the relationship with a distributor that helps fulfill most of SolarWinds' sales orders from the U.S. federal government; (h) potential foreign exchange gains and losses related to expenses and sales denominated in currencies other than the functional currency of an associated entity; and (i) such other risks and uncertainties described more fully in documents filed with or furnished to the Securities and Exchange Commission, including the Form 10-K previously filed for the full year of 2009 and a Form 10-Q for the second quarter of 2010 that SolarWinds anticipates filing on or before August 15, 2010. All information provided in this release is as of the date hereof and SolarWinds undertakes no duty to update this information except as required by law.

Non-GAAP Financial Measures

In addition to disclosing financial measures prepared in accordance with GAAP, this press release and the accompanying tables contain the following non-GAAP financial measures: non-GAAP operating income, non-GAAP net income, non-GAAP diluted earnings per share, revenue on a constant currency basis and non-GAAP weighted average shares outstanding. Each of non-GAAP operating income, non-GAAP net income and non-GAAP diluted earnings per share exclude the impact of stock-based compensation expense, amortization of intangible assets, expenses related to potential and completed follow-on offering of common stock, lawsuit settlement and related legal fees and certain acquisition-related costs from the comparable GAAP measure. Non-GAAP net income and non-GAAP diluted earnings per share also exclude the write-off of debt issuance costs and the related tax benefits of the excluded items from the comparable GAAP measure. Non-GAAP diluted earnings per share is equal to non-GAAP net income divided by non-GAAP weighted average shares outstanding, which adjusts GAAP weighted average shares outstanding for the first and second quarters of 2009 to assume that the conversion of our preferred stock in May 2009 occurred at the beginning of the applicable period. This press release contains a reconciliation of each of these non-GAAP measures to its most comparable GAAP financial measure.

SolarWinds believes that each of these non-GAAP financial measures provides meaningful supplemental information regarding its performance by excluding certain expenses, expenditures that may not be indicative of its core business operations. SolarWinds' management and Board of Directors use these non-GAAP measures to assess operational performance as well as to determine employee incentive compensation. Accordingly, these measures may provide helpful insight to investors on the motivation and decision-making of management in operating the business.

SolarWinds also believes that these non-GAAP financial measures are used by investors and security analysts to (a) compare and evaluate its performance from period to period and (b) compare its performance to those of its competitors. These non-GAAP measures exclude certain items that can vary substantially from company to company depending upon their financing and accounting methods, the book value of their assets, their capital structures and the method by which their assets were acquired. These items are typically interest expense, income tax expense, depreciation and amortization and stock-based compensation expense.

SolarWinds understands that, although these non-GAAP financial measures are frequently used by investors and securities analysts in their evaluations of companies, there are limitations associated with the use of these non-GAAP financial measures. These non-GAAP financial measures are not prepared in accordance with GAAP, do not reflect a comprehensive system of accounting and may not be completely comparable to similarly titled measures of other companies due to potential differences in the exact method of calculation between companies. Items such as the amortization of intangible assets, stock-based compensation expense, interest expense and income tax expense that are

excluded from these non-GAAP financial measures can have a material impact on net earnings.

As a result, these non-GAAP financial measures have limitations and should not be considered in isolation from, or as a substitute for, operating income, net income, revenue or other measures of performance prepared in accordance with GAAP. SolarWinds' management and Board of Directors compensate for these limitations by using these non-GAAP financial measures as supplements to GAAP financial measures and by reviewing the reconciliations of the non-GAAP financial measures to their most comparable GAAP financial measure. Investors are encouraged to review the reconciliations of these non-GAAP financial measures to their most comparable GAAP financial measures that are included elsewhere in this press release.

About SolarWinds

SolarWinds (NYSE: SWI) provides powerful and affordable IT management software to more than 95,000 customers worldwide – from Fortune 500 enterprises to small businesses. We work to put our users first and remove the obstacles that have become “status quo” in traditional enterprise software. SolarWinds products are downloadable, easy to use and maintain, and provide the power, scale, and flexibility needed to address users’ management priorities. Our online user community, thwack, is a gathering-place where tens of thousands of IT pros solve problems, share technology, and participate in product development for all of SolarWinds’ products. Learn more today at <http://www.solarwinds.com>.

SolarWinds, SolarWinds.com and Orion are registered trademarks of SolarWinds. All other company and product names mentioned are used only for identification purposes and may be trademarks or registered trademarks of their respective companies.

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SolarWinds, Inc.
Condensed Consolidated Balance Sheets
(In thousands, except for share and per share information)
(unaudited)

| | June 30, 2010 | December 31, 2009 |
|--|------------------|-------------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$99,767 | \$129,788 |
| Accounts receivable, net of allowances of \$101 and \$149 as of June 30, 2010 and December 31, 2009, respectively | 17,013 | 15,786 |
| Income tax receivable | 572 | 109 |
| Deferred taxes | 289 | 252 |
| Prepaid income taxes | - | 4,675 |
| Other current assets | 2,877 | 2,116 |
| Total current assets | 120,518 | 152,726 |
| Property and equipment, net | 6,623 | 6,406 |
| Debt issuance costs, net | - | 399 |
| Deferred taxes | 2,960 | 2,078 |
| Goodwill | 40,372 | 15,444 |
| Intangible assets and other, net | 21,100 | 4,417 |
| Total assets | \$191,573 | \$181,470 |
| Liabilities and stockholders' equity | | |
| Current liabilities: | | |
| Accounts payable | \$2,131 | \$3,293 |
| Accrued liabilities | 4,449 | 4,937 |
| Accrued interest payable | - | 539 |
| Accrued earnout | 3,743 | - |
| Income taxes payable | 336 | 284 |
| Current portion of deferred revenue | 43,099 | 37,103 |
| Current portion of long-term debt | - | 16,871 |
| Total current liabilities | 53,758 | 63,027 |
| Long-term liabilities: | | |
| Deferred revenue, net of current portion | 3,144 | 1,544 |
| Deferred taxes | 778 | 153 |
| Other long-term liabilities | 621 | 454 |
| Long-term debt, net of current portion | - | 27,226 |
| Total long-term liabilities | 4,543 | 29,377 |
| Total liabilities | 58,301 | 92,404 |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Common stock, \$0.001 par value: 123,000,000 shares authorized and 68,504,017 and 66,502,098 shares issued as of June 30, 2010 and December 31, 2009, respectively | 69 | 67 |
| Additional paid-in capital | 151,215 | 123,083 |
| Accumulated other comprehensive loss | (1,851) | (159) |
| Accumulated deficit | (16,161) | (33,925) |
| Total stockholders' equity | 133,272 | 89,066 |

| | | |
|--|-----------|-----------|
| Total liabilities and stockholders' equity | \$191,573 | \$181,470 |
|--|-----------|-----------|

SolarWinds, Inc.
Condensed Consolidated Statements of Income
(In thousands, except per share information)
(unaudited)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|----------|------------------------------|----------|
| | 2010 | 2009 | 2010 | 2009 |
| Revenue: | | | | |
| License | \$17,264 | \$14,598 | \$34,885 | \$27,139 |
| Maintenance and other | 18,244 | 12,444 | 34,948 | 23,978 |
| Total revenue | 35,508 | 27,042 | 69,833 | 51,117 |
| Cost of license revenue | 462 | 154 | 817 | 305 |
| Cost of maintenance and other revenue | 1,458 | 1,039 | 2,802 | 2,017 |
| Gross profit | 33,588 | 25,849 | 66,214 | 48,795 |
| Operating expenses: | | | | |
| Sales and marketing | 10,688 | 7,225 | 20,937 | 13,925 |
| Research and development | 3,824 | 2,755 | 7,451 | 5,181 |
| General and administrative | 6,200 | 4,112 | 11,521 | 7,977 |
| Total operating expenses | 20,712 | 14,092 | 39,909 | 27,083 |
| Operating income | 12,876 | 11,757 | 26,305 | 21,712 |
| Other income (expense): | | | | |
| Interest income | 67 | 53 | 100 | 132 |
| Interest expense | (363) | (1,540) | (1,146) | (2,991) |
| Other income (expense) | 163 | (9) | 211 | (6) |
| Total other expense | (133) | (1,496) | (835) | (2,865) |
| Income before income taxes | 12,743 | 10,261 | 25,470 | 18,847 |
| Income tax expense | 3,916 | 3,443 | 7,706 | 6,041 |
| Net income | \$8,827 | \$6,818 | \$17,764 | \$12,806 |
| Net income per share: | | | | |
| Basic earnings per share | \$0.13 | \$0.15 | \$0.26 | \$0.35 |
| Diluted earnings per share | \$0.12 | \$0.13 | \$0.24 | \$0.30 |
| Weighted shares used to compute net income per share: | | | | |
| Shares used in computation of basic earnings per share | 68,202 | 44,907 | 67,738 | 36,544 |
| Shares used in computation of diluted earnings per share | 73,287 | 50,952 | 73,061 | 42,236 |

SolarWinds, Inc.
 Reconciliation of GAAP to Non-GAAP Financial Measures
 (In thousands)
 (unaudited)

| | Three Months Ended June 30, 2010 | | | Three Months Ended June 30, 2009 | | |
|----------------------------|-------------------------------------|-------------|----------|-------------------------------------|-------------|----------|
| | GAAP | Adjustments | Non-GAAP | GAAP | Adjustments | Non-GAAP |
| Total revenue | \$35,508 | \$ - | \$35,508 | \$27,042 | \$ - | \$27,042 |
| Gross profit | 33,588 | 502 | 34,090 | 25,849 | 171 | 26,020 |
| Operating expenses | 20,712 | (4,340) | 16,372 | 14,092 | (2,108) | 11,984 |
| Operating income | 12,876 | 4,842 (a) | 17,718 | 11,757 | 2,279 (a) | 14,036 |
| Total other expense | (133) | 131 (b) | (2) | (1,496) | 428 (b) | (1,068) |
| Income before income taxes | 12,743 | 4,973 | 17,716 | 10,261 | 2,707 | 12,968 |
| Income tax expense | 3,916 | 1,347 (c) | 5,263 | 3,443 | 609 (c) | 4,052 |
| Net income | \$8,827 | \$ 3,626 | \$12,453 | \$6,818 | \$ 2,098 | \$8,916 |

(a) Reflects the reversal of amortization of intangible assets, stock-based compensation expense and other excluded expenses as follows:

Amortization of intangible assets:

| | Three Months Ended June 30, | |
|----------------------------|--------------------------------|-------|
| | 2010 | 2009 |
| Cost of license revenue | \$458 | \$154 |
| Sales and marketing | - | - |
| Research and development | - | - |
| General and administrative | 387 | 39 |

Stock-based compensation expense:

| | Three Months Ended June 30, | |
|-----------------------------|--------------------------------|-------|
| | 2010 | 2009 |
| Cost of maintenance revenue | \$44 | \$17 |
| Sales and marketing | 817 | 467 |
| Research and development | 453 | 290 |
| General and administrative | 2,249 | 1,111 |

Other excluded expenses:

| | Three Months Ended June 30, | |
|---|--------------------------------|-------|
| | 2010 | 2009 |
| Lawsuit settlement and related legal fees | \$(69) | \$201 |
| Follow-on offering costs (d) | 151 | - |
| Acquisition related costs | 144 | - |
| Severance costs related to retirement of Executive Chairman | 208 | - |

(b) Represents a decrease in the amortization of debt issuance costs due to the repayment of all or a portion of the long-term debt.

(c) Reflects the removal of the tax benefits associated with amortization of intangible assets, stock-based compensation expense and other excluded expenses.

(d) Represents expenses of \$151 associated with preliminary work on a potential public offering that was cancelled during the second quarter of 2010.

SolarWinds, Inc.
Reconciliation of GAAP to Non-GAAP Financial Measures
(In thousands)
(unaudited)

| | Six Months Ended June 30, 2010 | | | Six Months Ended June 30, 2009 | | |
|----------------------------|-----------------------------------|-------------|----------|-----------------------------------|-------------|----------|
| | GAAP | Adjustments | Non-GAAP | GAAP | Adjustments | Non-GAAP |
| Total revenue | \$69,833 | \$ - | \$69,833 | \$51,117 | \$ - | \$51,117 |
| Gross profit | 66,214 | 888 | 67,102 | 48,795 | 339 | 49,134 |
| Operating expenses | 39,909 | (7,043) | 32,866 | 27,083 | (3,862) | 23,221 |
| Operating income | 26,305 | 7,931 (a) | 34,236 | 21,712 | 4,201 (a) | 25,913 |
| Total other expense | (835) | 334 (b) | (501) | (2,865) | 428 (b) | (2,437) |
| Income before income taxes | 25,470 | 8,265 | 33,735 | 18,847 | 4,629 | 23,476 |
| Income tax expense | 7,706 | 2,160 (c) | 9,866 | 6,041 | 968 (c) | 7,009 |
| Net income | \$17,764 | \$ 6,105 | \$23,869 | \$12,806 | \$ 3,661 | \$16,467 |

(a) Reflects the reversal of amortization of intangible assets, stock-based compensation expense and other excluded expenses as follows:

Amortization of intangible assets:

| | Six Months Ended June 30, | |
|----------------------------|------------------------------|-------|
| | 2010 | 2009 |
| Cost of license revenue | \$807 | \$305 |
| Sales and marketing | - | - |
| Research and development | - | - |
| General and administrative | 669 | 77 |

Stock-based compensation expense:

| | Six Months Ended June 30, | |
|-----------------------------|------------------------------|-------|
| | 2010 | 2009 |
| Cost of maintenance revenue | \$81 | \$34 |
| Sales and marketing | 1,395 | 894 |
| Research and development | 812 | 515 |
| General and administrative | 3,596 | 2,110 |

Other excluded expenses:

| | Six Months Ended June 30, | |
|---|------------------------------|-------|
| | 2010 | 2009 |
| Lawsuit settlement and related legal fees | \$(217) | \$266 |
| Follow-on offering costs (d) | 170 | - |
| Acquisition related costs | 410 | - |

Severance costs related to retirement of Executive Chairman 208 -

(b) Represents a decrease in the amortization of debt issuance costs due to the repayment of all or a portion of the long-term debt.

(c) Reflects the removal of the tax benefits associated with amortization of intangible assets, stock-based compensation expense and other excluded expenses.

(d) Represents expenses of \$151 associated with preliminary work on a potential public offering that was cancelled during the second quarter of 2010. The remaining expenses of \$19 related to a public offering completed in the fourth quarter of 2009.

SolarWinds, Inc.
 Reconciliation of Diluted Earnings Per Share to Non-GAAP Diluted Earnings Per Share
 (In thousands, except per share information)
 (unaudited)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|---------|------------------------------|----------|
| | 2010 | 2009 | 2010 | 2009 |
| Numerator: | | | | |
| Reconciliation between GAAP and non-GAAP net income: | | | | |
| Net income | \$8,827 | \$6,818 | \$17,764 | \$12,806 |
| Reversal of intangible assets amortization | 845 | 193 | 1,476 | 382 |
| Reversal of stock-based compensation expense | 3,563 | 1,885 | 5,884 | 3,553 |
| Reversal of debt issuance costs write-off | 131 | 428 | 334 | 428 |
| Reversal of follow-on offering costs | 151 | - | 170 | - |
| Reversal of lawsuit settlement costs and related legal fees | (69) | 201 | (217) | 266 |
| Reversal of acquisition related costs | 144 | - | 410 | - |
| Reversal of severance costs related to retirement of Executive Chairman | 208 | - | 208 | - |
| Reversal of tax benefits associated with above adjustments | (1,347) | (609) | (2,160) | (968) |
| Non-GAAP net income | \$12,453 | \$8,916 | \$23,869 | \$16,467 |
| Denominator: | | | | |
| Reconciliation between GAAP and non-GAAP weighted average shares used in computing diluted earnings per share: | | | | |
| Weighted average number of shares used in computing diluted earnings per share | 73,287 | 50,952 | 73,061 | 42,236 |
| Pro forma adjustments to reflect assumed weighted average effect of conversion of preferred stock (a) | - | 14,700 | - | 20,850 |
| Non-GAAP weighted average shares used in computing non-GAAP diluted earnings per share (b) | 73,287 | 65,652 | 73,061 | 63,086 |
| Diluted earnings per share | \$0.12 | \$0.13 | \$0.24 | \$0.30 |
| Non-GAAP diluted earnings per share | \$0.17 | \$0.14 | \$0.33 | \$0.26 |

(a) Represents common shares from the conversion of convertible preferred shares as if the shares were converted as of the beginning of the indicated period.

(b) If the company assumed the common shares issued in its initial public offering in May 2009 were issued as of the beginning of the comparable period, or January 1, 2009, then the weighted average shares used in computing non-GAAP diluted earnings per share and the non-GAAP diluted earnings per share would have been 71,004 shares and \$0.13 per share, respectively, for the

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three months ended June 30, 2009 and 70,624 shares and \$0.23 per share, respectively, for the six months ended June 30, 2009.

SolarWinds, Inc.

Reconciliation of Second Quarter of 2010 GAAP Revenue to Non-GAAP Revenue on a Constant Currency Basis
(In thousands)
(unaudited)

Revenue on a constant currency basis is calculated using the average foreign exchange rates in the monthly periods during a previous quarter and applying these rates to foreign-denominated revenue in the corresponding monthly periods in the second quarter of 2010. The difference between revenue calculated based on these foreign exchange rates and revenue calculated in accordance with GAAP is listed as foreign exchange impact in the table below.

| | Using Foreign Exchange Rates in First Quarter of 2010 | Using Foreign Exchange Rates in Second Quarter of 2009 |
|--|---|--|
| License revenue | \$17,264 | \$17,264 |
| Foreign exchange impact on license revenue | 392 | 373 |
| License revenue on a constant currency basis | \$17,656 | \$17,637 |
| Maintenance and other revenue | \$18,244 | \$18,244 |
| Foreign exchange impact on maintenance and other revenue | 288 | 234 |
| Maintenance and other revenue on a constant currency basis | \$18,532 | \$18,478 |
| Total revenue | \$35,508 | \$35,508 |
| Foreign exchange impact on total revenue | 680 | 607 |
| Total revenue on a constant currency basis | \$36,188 | \$36,115 |

SolarWinds, Inc.
Condensed Consolidated Statements of Cash Flows
(In thousands)
(unaudited)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|--------------------------------|-----------|------------------------------|-----------|
| | 2010 | 2009 | 2010 | 2009 |
| Cash flows from operating activities | | | | |
| Net income | \$8,827 | \$6,818 | \$17,764 | \$12,806 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | | |
| Depreciation and amortization | 1,388 | 538 | 2,492 | 1,031 |
| Provision for doubtful accounts | (9) | (8) | 15 | 115 |
| Stock-based compensation expense | 3,563 | 1,885 | 5,884 | 3,553 |
| Deferred taxes | 403 | 405 | (277) | (28) |
| Excess tax benefit from stock-based compensation | (3,310) | (1,721) | (7,193) | (1,721) |
| Other non-cash expenses | 197 | 491 | 501 | 864 |
| Changes in operating assets and liabilities, net of assets acquired and liabilities assumed in business combinations: | | | | |
| Accounts receivable | 1,469 | (1,481) | (1,991) | 875 |
| Income taxes receivable | (593) | 161 | (493) | 406 |
| Prepaid income taxes | 807 | (2,129) | 4,675 | (2,129) |
| Prepaid & other current assets | (99) | (180) | (622) | (499) |
| Accounts payable | (381) | 226 | (1,141) | 294 |
| Accrued liabilities | (699) | 691 | (308) | 767 |
| Accrued interest payable | (525) | (325) | (539) | (978) |
| Income taxes payable | 3,011 | (883) | 7,460 | 1,900 |
| Deferred revenue and other liabilities | 2,849 | 2,567 | 6,594 | 4,730 |
| Net cash provided by operating activities | 16,898 | 7,055 | 32,821 | 21,986 |
| Cash flows from investing activities | | | | |
| Purchases of property and equipment | (852) | (561) | (1,434) | (975) |
| Purchases of intangible assets | (108) | (50) | (209) | (200) |
| Acquisition of businesses | - | (26) | (28,039) | (46) |
| Net cash used in investing activities | (960) | (637) | (29,682) | (1,221) |
| Cash flows from financing activities | | | | |
| Repayment of long-term debt | (25,000) | (49,825) | (44,097) | (56,986) |
| Exercise of stock options | 2,567 | 2,311 | 5,836 | 2,391 |
| Net cash proceeds from initial public offering | - | 104,625 | - | 104,625 |
| Excess tax benefit from stock-based compensation | 3,310 | 1,721 | 7,193 | 1,721 |
| Repayments of capital lease obligations | (2) | (7) | (9) | (13) |
| Payments for initial public offering costs | - | (856) | - | (878) |
| Net cash (used in) provided by financing activities | (19,125) | 57,969 | (31,077) | 50,860 |
| Effect of exchange rate changes on cash and cash equivalents | (1,134) | 557 | (2,083) | (41) |
| Net (decrease) increase in cash and cash equivalents | (4,321) | 64,944 | (30,021) | 71,584 |

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| | | | | |
|---|----------|-----------|-----------|-----------|
| Cash and cash equivalents | | | | |
| Beginning of period | 104,088 | 47,206 | 129,788 | 40,566 |
| End of period | \$99,767 | \$112,150 | \$99,767 | \$112,150 |
| Supplemental disclosure of cash flow information | | | | |
| Cash paid for interest | \$742 | \$1,358 | \$1,280 | \$3,369 |
| Cash paid (received) for income taxes | \$289 | \$5,865 | \$(3,658) | \$5,865 |
| Noncash investing and financing transactions | | | | |
| Accrued earnout | \$- | \$- | \$3,743 | \$- |
| Stock issued for acquisition | \$- | \$- | \$9,221 | \$- |