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

FORM 10-K/A
(Amendment No. 1)

FOR ANNUAL AND TRANSITION REPORTS PURSUANT TO SECTIONS 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

(Mark one)

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2002

OR

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

COMMISSION FILE NUMBER 000-24733

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

MARYLAND	**62-1670648**
(State or other jurisdiction of incorporation or organization)	**(IRS employer identification no.)**

ONE HANOVER PARK, SUITE 800
16633 DALLAS PARKWAY
ADDISON, TX 75001
(Address of principal executive offices & zip code)

Registrant's telephone number, including area code: (972) 713-5800

Securities registered pursuant to Section 12(b) of the Act:	None
Securities registered pursuant to Section 12(g) of the Act:	Common Stock, $.01 par value

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

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes ☒ No ☐

The aggregate market value of the common equity held by non-affiliates of the registrant, computed using the closing sale price of common stock of $2.72 per share on June 28, 2002, as reported on the Nasdaq National Market, was approximately $125,343,000 (affiliates included for this computation only: directors, executive officers and holders of more than 5% of the registrant's common stock).

The number of shares outstanding of the registrant's common stock as of March 10, 2003 was 63,487,379.

INTRODUCTORY NOTE

This Amendment No. 1 to the Annual Report of Entrust, Inc. ("Entrust" or the "Company") on Form 10-K/A for the year ended December 31, 2002 is being filed to amend only the following items contained in our Annual Report on Form 10-K as originally filed with the Securities and Exchange Commission on March 14, 2003:

- Item 6 (Selected Financial Data);
- Item 7 (Management's Discussion and Analysis of Financial Condition and Results of Operations);
- Item 8 (Financial Statements and Supplementary Data); and
- Item 15 (Exhibits, Financial Statement Schedules, and Reports on Form 8-K).

All information contained in this Amendment No. 1 is subject to updating and supplementing as provided in Entrust's reports filed with the Securities and Exchange Commission, as amended, for periods subsequent to the date of the original filing of the Annual Report on Form 10-K.

FORWARD-LOOKING STATEMENTS

This Amendment No. 1 to the Annual Report on Form 10-K/A, contains forward-looking statements that involve risks and uncertainties, as well as assumptions that, if they do not materialize or prove incorrect, could cause the results of Entrust to differ materially from those expressed or implied by such forward-looking statements. All statements, other than statements of historical fact, are statements that could be deemed to be forward-looking statements, including any projections of results of operations, revenues, financial condition or other financial items; any statements of plans, strategies and objectives of management for future operations; any statements regarding proposed new products, services or developments; any statements regarding future economic conditions, prospects of performance; statements of belief and any statement of assumptions underlying any of the foregoing.

The forward-looking statements contained herein involve risks and uncertainties. To learn more about the risks and uncertainties that the Company faces, you should read the risk factors set forth in Entrust's Securities and Exchange Commission periodic reports and filings, including but not limited to the items discussed elsewhere in this report. The Company assumes no obligation to update these forward-looking statements to reflect events that occur or circumstances that exist after the date on which they were made.

ITEM 6. SELECTED FINANCIAL DATA

The data set forth below should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and notes thereto included elsewhere in this Annual Report. The 1998 and 1999 data has been amended to reflect the retroactive adjustment to our investment in Entrust Japan, as required by APB No. 18, "The Equity Method of Accounting for Investments in Common Stock" in applying the provisions regarding a step-by-step acquisition of an investment accounted for under the equity method.

	Year Ended December 31,				
	1998	1999	2000	2001	2002
	(in thousands, except per share data)				
Statement of Operations Data:					
Revenues:					
License	$ 36,773	$ 61,482	$ 93,112	$ 48,027	$ 42,252
Services and maintenance	12,215	23,732	55,265	69,938	60,495
Total revenues	48,988	85,214	148,377	117,965	102,747
Cost of revenues:					
License	1,985	2,286	4,418	4,515	3,674
Services and maintenance	7,546	13,016	32,418	43,640	33,680
Amortization of purchased product rights	—	—	2,751	3,322	1,136
Total cost of revenues	9,531	15,302	39,587	51,477	38,490
Gross profit	39,457	69,912	108,790	66,488	64,257
Operating expenses:					
Sales and marketing	26,802	40,900	73,248	87,439	44,128
Research and development	12,840	16,605	27,625	30,892	24,151
General and administrative	5,046	7,752	12,083	20,509	14,840
Acquired in-process research and development	20,208	—	29,614	—	—
Amortization of goodwill and other purchased intangibles	356	712	59,952	62,142	—
Impairment of goodwill, purchased product rights and other purchased intangibles	—	—	—	326,953	—
Restructuring charges and adjustments	—	—	—	65,511	(1,079)
Write-down of leaseholds and other long-lived assets	—	—	—	13,519	—
Total operating expenses	65,252	65,969	202,522	606,965	82,040
Income (loss) from operations	(25,795)	3,943	(93,732)	(540,477)	(17,783)
Other income (expense):					
Interest income	1,807	3,776	13,809	8,330	3,274
Loss from equity investment	(220)	(173)	—	—	(602)
Realized gain (loss) on investments	—	—	—	1,103	(220)
Write-down of long-term strategic investments	—	—	—	(10,800)	(1,238)
Total other income (expense)	1,587	3,603	13,809	(1,367)	1,214
Income (loss) before income taxes	(24,208)	7,546	(79,923)	(541,844)	(16,569)
(Provision) benefit for income taxes	160	(1,800)	(2,337)	(1,828)	(1,350)
Net income (loss)	$ (24,048)	$ 5,746	$ (82,260)	$(543,672)	$ (17,919)
Net income (loss) per basic share	$ (0.68)	$ 0.13	$ (1.44)	$ (8.57)	$ (0.28)
Net income (loss) per diluted share	$ (0.68)	$ 0.10	$ (1.44)	$ (8.57)	$ (0.28)
Shares used in basic per share computation	35,255	43,847	57,003	63,411	64,946
Shares used in diluted per share computation	35,255	54,803	57,003	63,411	64,946

	Year Ended December 31,				
	1998	1999	2000	2001	2002
	(in thousands)				
Balance Sheet Data:					
Cash, cash equivalents and short-term marketable investments	$ 81,067	$ 89,271	$227,687	$ 153,555	$118,023
Working capital	77,438	87,918	224,026	89,012	73,367
Long-term marketable investments	—	2,405	60	9,038	13,423
Total assets	107,609	130,127	733,713	229,045	189,571
Shareholders' equity	86,839	102,762	673,671	135,452	117,865

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with "Selected Financial Data" and our consolidated financial statements and notes thereto appearing elsewhere in this Annual Report. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Our actual results may differ *materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth under "Certain Factors That May Affect Our Business" and elsewhere in this Annual Report.*

OVERVIEW

Background

We are a leading global provider of software that secures digital identities and information. This software and the associated services enable businesses and governments around the world to securely execute transactions and communicate information over wired and wireless networks, including the Internet. We have a broad set of products that provides identification, entitlements, verification, privacy and security management capabilities. Major government agencies, financial institutions and Global 1500 enterprises in more than 40 countries have purchased our portfolio of award-winning security technologies.

We were incorporated in December 1996 with nominal share capital, all of which was contributed by Nortel Networks Corporation and its subsidiary Nortel Networks Inc. (collectively, "Nortel Networks"). At the close of business on December 31, 1996, Nortel Networks transferred to us certain of their assets and liabilities, intellectual property, rights, licenses and contracts. In exchange, Nortel Networks received Series A Common stock, Special Voting stock and cash consideration. At the close of business on December 31, 1996, we issued Series B Common stock in a private placement. After the completion of the private placement, Nortel Networks owned approximately 73% of the outstanding shares of our voting stock assuming conversion of the Series B Common stock and Series B Non-Voting Common stock.

On August 21, 1998, we closed our initial public offering, issuing 5,400,000 shares of our Common stock at an initial public offering price of $16 per share. The net proceeds from the offering, after deducting underwriting discounts and commissions and offering expenses incurred, were approximately $79.1 million.

On February 29, 2000 and March 2, 2000, we closed our follow-on offering, which included an over-allotment option closing, issuing an aggregate of 2,074,260 shares of our Common stock at an offering price $82 per share. The net proceeds from the offering, after deducting underwriting discounts and commissions and offering expenses incurred, were approximately $161.5 million.

On June 4, 2001, we changed our name to Entrust, Inc.

At December 31, 2002, Nortel Networks owned 9.6 million shares, or approximately 15%, of our Common stock. Nortel Networks owned 8.3 million shares of our Common stock, or 13%, as of March 10, 2003.

BUSINESS OVERVIEW

In 2002, Entrust continued its strategy of focusing on core vertical and geographic markets. We had success in the sales of our Secure Web Portal product solution and Secure VPN solution. Revenues from the Secure Web Portal solution, which is the combination of our TruePass and GetAccess products, increased 51% year-over-year and represented 38% of our software revenues for 2002. Revenues from our Secure VPN solution increased 241% year-over-year and represented more than 2% of our software revenues for 2002. The other major contributors to 2002 software revenue, representing 57% of software revenue, was our Secure Desktop Products and Security Infrastructure products.

Other highlights from 2002 included:

- We had success and key customer wins in our core vertical markets. Revenue from our extended government vertical accounted for 49% of total software revenue in 2002 and revenue from our financial vertical accounted for 10% of software revenue.
- We launched a new partner program which helped us to nearly double our revenue from partners.
- We had approximately 40 new companies join our EntrustReady program in 2002, which ensures that their solutions are interoperable with the Entrust portfolio.

- And we continually realigned the company's resources to better serve the current market opportunity and align ourselves for a return to profitability.

Our key technology-related accomplishments during 2002 included the following:

- We extended our leadership position in Internet security market with enhancements to our authentication and authorization product portfolios.
- We developed the Entrust Secure Transaction Platform, which enables organizations to securely integrate automated business processes while leveraging the return on investment and efficiencies inherent in using Web services to leverage their businesses and processes.
- We delivered the newest extension to our Secure Messaging Solution, which provides server-based, end-to-end secure messaging capabilities enabling users to securely communicate within the organization as well as to external businesses, government agencies and customers.
- In conjunction with the White House Strategy to Secure Cyberspace, the General Services Agreements (GSA) delivered a secure communications capability by cross-certifying a number of federal agencies in the Federal Bridge Certification Authority (FBCA). The FBCA, or Federal Bridge, is a multi-agency program powered by our expertise and public-key infrastructure (PKI) technology that was deployed by the end of the third quarter of 2002. This program allows employees of the Department of Treasury, NASA, NFC, Department of Defense and other U.S. government organizations to securely communicate with one another and share information.

CRITICAL ACCOUNTING POLICIES

We operate in one primary business. We develop, market and sell software that secures digital identities and information. We also perform professional services to install, support and integrate our software solutions with other applications. All of these activities may be fulfilled in conjunction with partners and managed through a global functional organization. We operate globally in a functional organization. We do not have any off-balance sheet financing, other than operating leases entered into in the normal course of business, and we do not actively engage in hedging transactions.

In 2002, our most complex accounting judgments were made in the areas of software revenue recognition, allowance for doubtful accounts, restructuring and other special non-recurring charges, impairment of long-term strategic investments, the provision of income taxes and stock-based compensation. The restructuring and other special non-recurring charges are not anticipated to be recurring in nature. However, the financial reporting of restructuring and other special non-recurring charges will continue to require judgments until such time as the corresponding accruals are fully paid out and/or no longer required. Software revenue recognition, allowance for doubtful accounts, impairment of long-term strategic investments, provision for income taxes and stock-based compensation are expected to continue to be ongoing elements of our accounting processes and judgments.

Software Revenue Recognition

With respect to software revenue recognition, we recognize revenues in accordance with the provisions of the American Institute of Certified Public Accountants' Statement of Position No. 97-2, "Software Revenue Recognition" and related accounting guidance and pronouncements.

Revenues from perpetual software license agreements are recognized upon receipt of an executed license agreement, or an unconditional order under an existing license agreement, and shipment of the software, if there are no significant remaining vendor obligations, collection of the receivable is probable and payment is due within twelve months. Revenues from license agreements requiring the delivery of significant unspecified software products in the future are accounted for as subscriptions and, accordingly, are recognized ratably over the term of the agreement from the first instance of product delivery. This policy is applicable to all sales transactions, including sales to resellers and end user customers. We do not offer a right of return on sales of our software products.

For arrangements involving multiple elements, we allocate revenue to each component of the arrangement using the residual value method, based on vendor-specific objective evidence of the fair value of the various elements. These elements may include one or more of the following: software licenses, maintenance and support, consulting services and training. We first allocate the arrangement fee, in a multiple-element transaction, to the undelivered elements based on the total fair value of those undelivered elements, as indicated by vendor-specific objective evidence. This portion of the arrangement fee is deferred. Then the difference between the total arrangement fee and the amount deferred for the undelivered elements is recognized as revenue related to the delivered elements. We attribute the discount offered in a multiple-element arrangement entirely to the delivered elements of the transaction, which are typically software licenses. Fair values for the future maintenance and support services are based upon separate sales of renewals of maintenance and support contracts. Fair value of future services training or consulting services is based upon separate sales of these services to other customers. In some instances, a group of contracts or agreements with the same customer may be so closely related that they are, in effect, part of a single multiple-element arrangement, and therefore, we would allocate the corresponding revenues among the various components, as described above.

Due to the complexity of some software license agreements, we routinely apply judgments to the application of software revenue recognition accounting principles to specific agreements and transactions. Different judgments and/or different contract structures could have led to different accounting conclusions, which could have had a material effect on our reported earnings.

Allowance for Doubtful Accounts

We maintain doubtful accounts allowances for estimated losses resulting from the inability of our customers to make required payments. At the time of a transaction, we assess whether the fee associated with the revenue transaction is fixed and determinable based on the payment terms associated with the transaction and the creditworthiness of the customer. We also assess whether collection is reasonably assured. If any portion of a fee is due after 365 days from the invoice date, we account for the fee as not being fixed and determinable. In these cases, we recognize revenue as the fees become due.

We assess collection based on a number of factors, including previous transactions with the customer and the creditworthiness of the customer. We do not request collateral from our customers. If we determine that collection of a fee is not reasonably assured, we defer the fee and recognize revenue at the time collection becomes reasonably assured, which is generally upon receipt of cash.

We base our ongoing estimate of allowance for doubtful accounts primarily on the aging of the balances in the accounts receivable, our historical collection patterns and changes in the creditworthiness of our customers. While credit losses have historically been within our expectations and the provisions established, we cannot guarantee that we will continue to experience the same credit loss rates that we have in the past. Our accounts receivable include material balances from a limited number of customers, with five customers accounting for 43% of accounts receivable at each of December 31, 2001 and 2002. For more information on our customer concentration, see our related discussion in “Certain Factors That May Affect Our Business”. Therefore, changes in the assumptions underlying this assessment or changes in the financial condition of our customers could result in a different required allowance, which could have a material impact on our reported earnings.

As of December 31, 2002, accounts receivable totaled $22.3 million, net of an allowance for doubtful accounts of $3.0 million.

Restructuring and Other Special Non-recurring Charges

On June 4, 2001, we announced that our board of directors had approved a restructuring program to refocus on the most significant market opportunities and to reduce operating costs due to the macroeconomic factors that were negatively affecting technology investment in the market. The restructuring program included a workforce reduction, consolidation of excess facilities, and discontinuance of non-core products and programs.

As a result of the restructuring program and the impact of the macroeconomic conditions on us and our global base of customers, we recorded restructuring and other special non-recurring charges, excluding goodwill impairment, of $106.6 million in the second quarter of 2001, with a subsequent increase of $1.4 million in the second half of 2001 and a reduction of $1.3 million in the first half of 2002.

We conducted our assessment of the accounting effects of the restructuring program in accordance with EITF No. 94-3, “Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity”, SFAS No. 121, “Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of”, APB Opinion No. 9, “Reporting the Results of Operations” and the relevant provisions of the SEC’s SAB No. 100, “Restructuring and Impairment Charges”.

Our assessment required assumptions in estimating the original accrued restructuring charges of $65.5 million on June 30, 2001, including estimating future recoveries of sublet income from excess facilities, liabilities from employee severances, and costs to exit business activities. Changes in these assessments with respect to the accrued restructuring charges of $33.2 million at December 31, 2002, could have a material effect on our reported results. During the second quarter of 2002, we recorded adjustments to reduce the accrued restructuring charges by $1.1 million, which were made to reflect savings realized as a result of the successful completion of certain contractual obligations in a cost-effective manner. As of June 2002, we had initiated all actions required by the restructuring plan. In addition, actual results could vary from these assumptions, in particular with regard to the sublet of excess facilities, resulting in an adjustment that could have a material effect on our future financial results.

Impairment of Long-term Strategic and Equity Investments

We assess the recoverability of the carrying value of strategic investments at least annually. Factors that we consider important in determining whether an assessment is warranted and could trigger impairment include, but are not limited to, the likelihood that the company in which we invested would have insufficient cash flows to operate for the next twelve months, significant changes in the company’s operating performance or business model and changes in overall market conditions. These investments are in private companies of which we typically own less than 10% of the outstanding stock. Because there is not a liquid market for these securities, we often must make estimates of the value of our investments. We recorded charges related to other than temporary declines in the value of certain strategic investments of $10.8 million in 2001. We also recorded a gain on the disposition of a long-term strategic investment of $1.6 million in 2001. It was also determined that a further adjustment to the carrying value of the investments was necessary during 2002 in the amount of $1.2 million, to reflect other than temporary declines in the value of certain strategic investments. Further write-downs may be required in future depending upon our assessment of the performance of the underlying investee companies at that time. As of December 31, 2002, long-term strategic investments, net of valuation allowances, amounted to $2.9 million.

In April 2002, we began accounting for our investment in Entrust Japan under the equity method in accordance with the provisions of APB No. 18, “The Equity Method of Accounting for Investments in Common Stock” and ARB No. 51, “Consolidated Financial Statements”. Accordingly, on the step-by-step acquisition method, we recorded a retroactive adjustment to consolidated accumulated deficit to record our share of the post-acquisition losses of Entrust Japan of prior years of $393,000, as required by this accounting guidance. This retroactive adjustment is attributable to our pro rata share of losses recorded by Entrust Japan during the period in which we owned less than 10% of their voting stock, to the extent of our previous investment. Our balance sheet at December 31, 2001, as reported in our consolidated financial statements included elsewhere in this Annual Report, has been restated to reflect this retroactive adjustment. Prior years’ comparative results have been restated in 1998 and 1999 to reflect this retroactive adjustment.

In addition, we recorded our share of post-acquisition losses of Entrust Japan, in the amount of $602,000 in our consolidated losses for 2002. These losses are attributable to our pro rata share of Entrust Japan’s losses in 2002, while we had an equity ownership of approximately 39% of their voting stock.

During 2002, Entrust Japan exceeded the performance targets established at the date of increased investment. However, due to Entrust Japan’s history of operating losses, it is possible that all or substantially all of the remaining $1.3 million equity investment in Entrust Japan at December 31, 2002 may be expensed through our operating earnings in future quarters as a result of our recognition of our equity share of losses in Entrust Japan. As of December 31, 2002, we believe that there has not been an impairment of our investment in Entrust Japan.

Provision for Income Taxes

The preparation of our consolidated financial statements require us to estimate our income taxes in each of the jurisdictions in which we operate, including those outside the United States. In addition, we have based the calculation of our income taxes in each jurisdiction based upon inter-company agreements. The income tax accounting process involves our estimating our actual current exposure in each jurisdiction together with assessing temporary differences resulting from differing treatment of items, such as deferred revenue, for tax and accounting purposes. These differences result in the recognition of deferred tax assets and liabilities. We then record a valuation allowance to reduce its deferred tax assets to the amount that is more likely than not to be realized.

Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against deferred tax assets. We recorded a valuation allowance of $114.2 million as of December 31, 2002, which represents the full value of our deferred tax assets, due to uncertainties related to our ability to utilize our deferred tax assets due to our recent history of financial losses. In the event that actual results differ from these estimates or we adjust these estimates in future periods we may need to adjust our valuation allowance, which could materially impact our financial position and results of operations.

Stock-Based Compensation

Our stock option program is a broad-based, long-term retention program that is intended to contribute to our success by attracting, retaining and motivating talented employees and to align employee interests with the interests of our existing stockholders. Stock options are typically granted to employees when they first join us but can also be granted when there is a significant change in an employee's responsibilities and, occasionally, to achieve equity within a peer group. The Compensation Committee of the Board of Directors may, however, grant additional options to executive officers and key employees for other reasons. Under the stock option plans, the participants may be granted options to purchase shares of Common stock and substantially all of our employees and directors participate in at least one of our plans. Options issued under these plans generally are granted at fair market value at the date of grant, become exercisable at varying rates, generally over three or four years and generally expire ten years from the date of grant.

We recognize that stock options dilute existing shareholders and have attempted to control the number of options granted while remaining competitive with our compensation packages. At December 31, 2002, a large percentage of our outstanding employee stock options carried exercise prices in excess of the closing market price on that day. All stock option grants are made with the approval of the Compensation Committee of the Board of Directors.

We account for our stock option plans under the recognition and intrinsic value measurement principles of APB Opinion No. 25, "Accounting for Stock Issued to Employees", and related accounting guidance. Accordingly, no stock-based compensation expense is reflected in net earnings for grants to employees under these plans, when the exercise price for options granted under these plans is equal to the market value of the underlying common stock on the date of grant. All of the options granted to employees in the periods after 1998 had exercise prices equal to the fair value of the underlying stock on the date of grant and therefore, no stock-based compensation costs are reflected in earnings for these options in these periods. Compensation expense was recognized for our stock-based compensation plans in 1998 because the exercise price of some options granted in that period were determined, for accounting purposes, to be below the fair value of the underlying stock as of the grant date for such stock options. In connection with the granting of these options, we recorded unearned compensation of $784 thousand for 1998. If we had applied the fair value recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation", to stock-based compensation, the effect would have been to increase our net loss in 2002, 2001 and 2000 to $42.4 million, $592.8 million and $177.5 million, respectively, and consequently, increase our net loss per share to $0.65, $9.35 and $3.11 for 2002, 2001 and 2000, respectively. However, Entrust believes that the expenses that would be recorded under SFAS No. 123 are not as meaningful as a careful consideration of the outstanding option data, which is disclosed in note 2(n) of our consolidated financial statements, included elsewhere in this Annual Report.

RESULTS OF OPERATIONS

The following table sets forth certain statement of operations data expressed as a percentage of total revenues for the periods indicated:

	Year Ended December 31,		
	2000	2001	2002
Revenues:			
License	62.8%	40.7%	41.1%
Services and maintenance	37.2	59.3	58.9
Total revenues	100.0	100.0	100.0
Cost of revenues:			
License	3.0	3.8	3.6
Services and maintenance	21.8	37.0	32.8
Amortization of purchased product rights	1.9	2.8	1.1
Total cost of revenues	26.7	43.6	37.5
Gross profit	73.3	56.4	62.5
Operating expenses:			
Sales and marketing	49.4	74.1	42.9
Research and development	18.6	26.2	23.5
General and administrative	8.1	17.4	14.4
Acquired in-process research and development	19.9	—	—
Amortization of goodwill and other purchased intangibles	40.4	52.7	—
Impairment of goodwill, purchased product rights and other purchased intangibles	—	277.2	—
Restructuring charges and adjustments	—	55.5	(1.0)
Write-down of leaseholds and other long-lived assets	—	11.5	—
Total operating expenses	136.4	514.6	79.8
Loss from operations	(63.1)	(458.2)	(17.3)
Other income (expense):			
Interest income	9.3	7.1	3.2
Loss from equity investment	—	—	(0.6)
Realized gain (loss) on investments	—	0.9	(0.2)
Write-down of long-term strategic investments	—	(9.1)	(1.2)
Total other income (expense)	9.3	(1.1)	1.2
Loss before income taxes	(53.8)	(459.3)	(16.1)
Provision for income taxes	(1.6)	(1.6)	(1.3)
Net loss	(55.4)%	(460.9)%	(17.4)%

YEARS ENDED DECEMBER 31, 2000, 2001 AND 2002

Revenues

We generate revenues from licensing the rights to our software products to end-users and, to a lesser extent, from sublicense fees from resellers. We also generate revenues from consulting, training and post-contract support, or maintenance, performed for customers who license our products. We recognize revenues in accordance with the provisions of the SOP No. 97-2, “Software Revenue Recognition,” SOP No. 98-9, “Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions” and related accounting guidance and pronouncements.

Revenues from perpetual software license agreements are recognized as revenue upon receipt of an executed license agreement, or an unconditional order under an existing license agreement, and shipment of the software, if there are no significant remaining vendor obligations, collection of the receivable is probable and payment is due within twelve months. Revenues from license agreements requiring the delivery of significant unspecified software products in the future are accounted for as subscriptions and, accordingly, are recognized ratably over the term of the agreement from the first instance of product delivery. This policy is applicable to all sales transactions, including sales to resellers and end user customers. We do not offer a right of return on sales of our software products.

For arrangements involving multiple elements, we allocate revenue to each component of the arrangement using the residual value method, based on vendor-specific objective evidence of the fair value of the various elements. These elements may include one or more of the following: software licenses, maintenance and support, consulting services and training. We first allocate the arrangement fee, in a multiple-element transaction, to the undelivered elements based on the total fair value of those undelivered elements, as indicated by vendor-specific objective evidence. This portion of the arrangement fee is deferred. Then the difference between the total arrangement fee and the amount deferred for the undelivered elements is recognized as revenue related to the delivered elements. We attribute the discount offered in a multiple-element arrangement entirely to the delivered elements of the transaction, which are typically software licenses. Fair values for the future maintenance and support services are based upon separate sales of renewals of maintenance and support contracts. Fair value of future services training or consulting services is based upon separate sales of these services to other customers. In some instances, a group of contracts or agreements with the same customer may be so closely related that they are, in effect, part of a single multiple-element arrangement, and therefore, we would allocate the corresponding revenues among the various components, as described above.

Revenues from maintenance services are recognized ratably over the term of the maintenance period, which is typically one year. If maintenance services are included free of charge or discounted in a license agreement, such amounts are unbundled from the license fee at their fair market value based upon the value established by independent sales of such maintenance services to other customers. Revenues from the sale of Web server certificates are also recognized ratably over the term of the certificate, which is typically one to two years.

Consulting and training revenues are generally recognized as the services are performed. Consulting services are typically performed under separate service agreements and are usually performed on a time and materials basis. Such services primarily consist of implementation services related to the installation and deployment of our products and do not include significant customization or development of the underlying software code.

We use the percentage-of-completion method to account for fixed price custom development contracts. Under this method, we recognize revenue and profit as the work on the contract progresses. Revenues are recognized by applying the percentage of the total cost incurred to date divided by the total estimated contract cost to the total contract value, and any projected loss is recognized immediately. The project cost estimates are reviewed on a regular basis.

Total Revenues. Total revenues in 2002 were $102.7 million, which represented a decrease of 13% from the $118.0 million of total revenues in 2001, which in turn, represented a 20% decrease from the $148.4 million of total revenues in 2000. Total revenues derived from North America of $71.3 million in 2002 represented a decrease of 10% from the $79.1 million in 2001, which in turn, represented a 24% decrease from the $103.5 million in 2000. Total revenues derived from outside of North America of $31.4 million in 2002 represented a decrease of 19% from the $38.9 million in 2001, which in turn, represented a 13% decrease from the $44.9 million in 2000. The majority of the overall decline in total revenues in 2002 and 2001 was experienced in Canada, Europe, Asia and other international locales, which was mainly due to the continued softening of the economic climate internationally and to our restructuring plan from the second quarter of 2001, which resulted in fewer sales resources being applied in all regions, particularly in Asia Pacific and Latin America. In addition, we generated $13.6 million of revenues from the Government of Canada Secure Channel project in 2001, from software deliveries, accounted for on a subscription basis, and the first phase of the professional services work related to this project. These revenues were difficult to replace in 2002. The level of non-North American revenues has fluctuated from period to period, and this trend is expected to continue for the foreseeable future. The decline in the level of North American revenues, in 2002 and 2001, reflected the prolonged economic downturn experienced in this region and throughout the industry, with customers buying to their immediate needs, as opposed to buying total project or enterprise wide, in the tough economic market. However, the lower percentage year-over-year decrease in revenues derived from North America, in 2002 compared to 2001, is due to increased activity in 2002 in the extended government vertical in the United States, resulting from a higher customer demand for our digital certificate solutions in that market sector. Extended government revenues, which include healthcare, generated in the United States increased from $18.0 million in 2001 to $23.3 million in 2002, or 29%. In 2002 and 2000, no individual customer accounted for 10% or more of revenues. In 2001, a single customer accounted for 11% of revenues, while no other customers accounted for 10% or more of revenues.

License Revenues. License revenues of $42.3 million in 2002 represented a decrease of 12% from the $48.0 million in 2001, which in turn, represented a decrease of 48% from the $93.1 million in 2000. These revenues represented 41%, 41% and 63% of total revenues in 2002, 2001 and 2000, respectively. The decrease in license revenues in absolute dollars in 2002 and 2001 was primarily driven by the softened economic climate internationally and the shift from new project software spending to service driven deployment in the extended government vertical. New project purchases remain subject to governmental budgetary constraints. In addition, the global downturn has had a significant impact on information technology projects and the commitments that customers have made to expenditures in this area. Highlighting this trend, we had 321 license revenue transactions (a transaction is defined as a license sale in excess of $10 thousand) in 2002, down from 443 in 2001, or a 28% decrease. The impact on revenue was partially offset by the fact that the average transaction size increased from $97 thousand in 2001 to $128 thousand in 2002, or an increase of 32%. License revenues as a percentage of total revenues remained flat from 2001 to 2002, due to decreased services and maintenance revenues in the first half of 2002, largely as a result of the timing delay in contracting additional services revenues from the Government of Canada Secure Channel project, coupled with continued demand for the Entrust Secure Web Portal Solutions and Enterprise Desktop suite, offset by decreased license revenues caused by the absence of Government of Canada Secure Channel software revenues in 2002, which were $4.4 million in 2002 versus $12.6 million in 2001. License revenues as a percentage of total revenues decreased from 2000 to 2001, primarily as a result of a continued strong demand for services and maintenance from our customers and increased professional services revenues of approximately $3.3 million from the addition of CygnaCom in March 2000, and enCommerce in June 2000, and partly due to decreased license revenues in 2001.

Services and Maintenance Revenues. Services and maintenance revenues of $60.5 million in 2002 represented a decrease of 13% from the $69.9 million in 2001, which in turn, represented an increase of 26% from the $55.3 million in 2000. These revenues represented 59%, 59% and 37% of total revenues in 2002, 2001 and 2000, respectively. The decrease in services and maintenance revenues in 2002 is due to slowed demand for consulting services, resulting from the diminished growth of the license revenue base of customers experienced during 2001 and 2002 and the timing of corresponding support contract renewals on this license revenue base. Consulting services revenues declined from $36.3 million in 2001 to $26.7 million in 2002. In addition, to a greater degree we have been fulfilling our customers' deployment needs in conjunction with partners, as our solutions are now easier to deploy and, as a result, the demand for our consulting services has declined for customer deployment and integration requirements. This is particularly true in Europe, where several large system integration contracts in Europe underpinned the 2001 services revenues in the first half of that year. The increase in services and maintenance revenues in absolute dollars from 2000 to 2001 was primarily the result of an increase in demand for consulting services and customer support, the acquisitions of CygnaCom and enCommerce, which added approximately $6.0 million, and an increase of $5.4 million in maintenance revenues from a larger installed product base and strong customer renewals of annual maintenance agreements. Services and maintenance revenues as a percentage of total revenues for 2002 compared to 2001 remained flat, mainly due to the continued improvements achieved in the utilization of our global professional services organization, offset with a shift in the mix of revenues from services and maintenance to license revenues during the first half of 2002. This shift was largely due to an increase in demand for our enhanced security solutions, particularly the Entrust Secure Web Portal Solutions, combined with the decrease in services and maintenance business in 2002 as a result of the timing of customer demand. The increase in services and maintenance revenues as a percentage of total revenues from 2000 to 2001 reflected a shift in the mix of revenues from license to services and maintenance revenues in 2001, compared to previous years. This shift was largely due to the continued growth of our services and maintenance business, which increased $8.6 million in response to customer demand, the impact of the professional services revenues of CygnaCom and enCommerce since their respective acquisitions, and the decrease in license revenues during 2001.

Cost of Revenues

Cost of License Revenues. Cost of license revenues consists primarily of costs associated with product media, documentation, packaging and royalties to third-party software vendors. Cost of license revenues was $3.7 million in 2002, $4.5 million in 2001 and $4.4 million in 2000, representing 4%, 4% and 3% of total revenues for the respective years. The decrease in cost of license revenues in absolute dollars was primarily a result of lower license revenues in 2002 with the corresponding expenses lower by $0.2 million compared to prior years and savings of $0.6 million realized as a result of renegotiated royalty agreements with some third-party software vendors. The cost of license revenues as a percentage of total revenues remained flat for 2002 compared to 2001 due to the overall lower total revenues in 2002. The mix of third-party products may vary from period to period and, consequently, our gross margins and results of operations could be adversely affected. The increase in the cost of license revenues as a percentage of total revenues from 2000 to 2001, despite the lower software license revenue levels, was primarily a result of higher royalty rates paid to third-party software vendors, which increased expenses by $0.5 million and an increase in the number of third-party technologies embedded in our products sold, which increased costs by an additional $0.5 million. The mix of third-party products may vary from period to period and, consequently, our gross margins and results of operations could be adversely affected.

Cost of Services and Maintenance Revenues. Cost of services and maintenance revenues consists primarily of personnel costs associated with customer support, training and consulting services, as well as amounts paid to third-party consulting firms for those services. Cost of services and maintenance revenues was $33.7 million in 2002, $43.6 million in 2001 and $32.4 million in 2000, representing 33%, 37% and 22% of total revenues for the respective years. The decrease in the cost of services and maintenance revenues in absolute dollars and as a percentage of total revenues in 2002 primarily reflected the decreased costs of $7.5 million associated with lower levels of services and maintenance revenues experienced during this year and the elimination of certain unprofitable services business lines as part of our restructuring in June 2001, which resulted in savings of $2.5 million in 2002. Further, the decrease of cost of services and maintenance revenues as a percentage of total revenues reflected a decline in services and maintenance revenues and an increase in license revenues in the first half of 2002, compared to the same period in 2001. The increase in absolute dollars in 2001 reflected the increased costs of $11.2 million associated with the increased levels of services and maintenance revenues experienced in those periods, of which $4.5 million related to increased costs associated with the CygnaCom and enCommerce resources. The increase in the cost of services and maintenance revenues as a percentage of total revenues in 2001 reflected the rapid growth of services and maintenance revenues in comparison to license revenues, and the significant shift in the mix of revenues from license to services and maintenance revenues during this period. As the services and maintenance revenues represented the larger proportion of total revenues and grew faster than total revenues, the cost of generating those services and maintenance revenues represented a much larger percentage when compared against total revenues, because significant investment was necessary in order to meet this demand. Also, we made significant investments of $2.4 million in additional customer support personnel in 2001.

Services and maintenance gross profit as a percentage of services and maintenance revenues was 44% in 2002, 38% in 2001 and 41% in 2000. The increase in the services and maintenance gross profit as a percentage of services and maintenance revenues from 2001 to 2002 reflected the lower costs associated with professional services and operating efficiencies achieved in the form of higher productivity and utilization of available services resources compared to the previous year, combined with a shift in the services revenues mix from lower margin professional services revenues to higher margin support and maintenance revenues. Each of these factors resulted in a one-percentage point improvement in our gross profit as a percentage of services and maintenance revenues. We also eliminated certain unprofitable services business lines as part of our restructuring plan in June 2001, which resulted in a four-percentage point improvement in our gross profit as a percentage of services and maintenance revenues. The decrease in the services and maintenance gross profit as a percentage of services and maintenance revenues from 2000 to 2001 reflected the investment we made in the professional services team primarily through the acquisition of CygnaCom late in the first quarter of 2000 and enCommerce at the end of the second quarter of 2000, which represented a shift in the mix of components within services revenues toward the lower-margin professional services revenues, resulting in a four-percentage point decrease in services and maintenance gross profit as a percentage of services and maintenance revenues. The impact of this decrease in the services and maintenance gross profit as a percentage of services and maintenance revenues was partly offset by the effect of improved customer support revenues in 2001.

Operating Expenses

Operating Expenses—Sales and Marketing

	Year Ended December 31,		
	2000	2001	2002
		(in thousands)	
Per statement of operations	$73,248	$87,439	$44,128
Less: Special non-recurring charges included	—	12,637	(371)
Pro forma	$73,248	$74,802	$44,499
Pro forma sales and marketing as a percentage of total revenues	49%	63%	43%

Sales and marketing expenses decreased to $44.5 million in 2002 from $74.8 million in 2001 and $73.2 million in 2000, on a pro forma basis, representing 43%, 63% and 49% of total revenues in the respective years. The decrease in absolute dollars in 2002 was due mainly to the cost reduction strategies implemented through our restructuring plan, which took effect in June 2001. Since the restructuring, our sales and marketing expenses have better matched our revenue generation. The increase in sales and marketing expenses in absolute dollars from 2000 to 2001 was primarily the result of costs associated with the expansion of our sales and marketing organization, both domestically and internationally, up until the end of the first half of 2001 and the implementation of our restructuring plan in June 2001. Until that time we had continued to make significant investments in sales and marketing to support the launch of new products, markets, services and marketing programs. The decrease in sales and marketing expenses as a percentage of total revenues in 2002, compared to 2001, reflected the cost savings from the restructuring plan, and the lower-than-expected revenue achievement in the first half of 2001 compared to 2002. In addition, we have implemented significant efficiencies into our sales processes and continued greater discipline in expense management. The cost savings from the restructuring accounted for approximately 21-percentage points of the decrease in sales and marketing expenses as a percentage of total revenues, while the lower revenue achievement in 2002 resulted in a five-percentage point increase. The efficiencies and discipline implemented in our sales processes accounted for a four-percentage point decrease in sales and marketing expenses as a percentage of total revenues. The increase in sales and marketing expenses as a percentage of total revenues in 2001, compared to 2000, was mainly due to the combination of lower-than-expected license revenues in the first half of 2001, and sales and marketing expenses that were largely fixed prior to the beginning of each of the first two quarters of 2001 based on the expectation of higher license revenues for that period that did not materialize. We intend to continue to focus on improving the productivity of our sales and marketing organizations and on gaining efficiencies in the related processes in light of current economic conditions. However, until the implementation of our restructuring plan, we continued to make significant investments in sales and marketing to support the launch of new products, services and marketing programs by maintaining our strategy of (a) investing in hiring and training our direct and partner sales organizations in anticipation of future market growth, and (b) investing in marketing efforts in support of new product launches. Failure of these investments in sales and marketing, as adjusted through our restructuring plan, to generate future revenues will have a significant adverse effect on our operations. While we are focused on marketing programs and revenue generating opportunities to increase software revenues, there can be no assurances that these initiatives will be successful.

During 2002, the allowance for doubtful accounts decreased by $0.9 million as a result of better cash collections during the period and, consequently, an additional bad debt expense was not required in 2002. We had recorded bad debt write-offs and additional provisions for doubtful accounts totaling $7.7 million in 2001, included in the above special non-recurring charges, which was recorded primarily in sales and marketing expenses. The credit to sales and marketing expenses for special non-recurring charges in 2002 reflected savings realized in the negotiation and completion of certain contractual obligations, identified under our restructuring program, in a cost-effective manner.

Operating Expenses—Research and Development

	Year Ended December 31,		
	2000	2001	2002
		(in thousands)	
Per statement of operations	$27,625	$30,892	$24,151
Less: Special non-recurring charges included	—	—	—
Pro forma	$27,625	$30,892	$24,151
Pro forma research and development as a percentage of total revenues	19%	26%	24%

Research and development expenses decreased to $24.2 million in 2002 from $30.9 million in 2001 and $27.6 million in 2000, representing 24%, 26% and 19% of total revenues in the respective years. The decrease in research and development expenses in absolute dollars in 2002 was due mainly to the cost reduction strategies implemented through our restructuring plan, which took effect in June 2001. In addition, employees were hired during the first half of 2001, primarily in connection with the continuing expansion and enhancement of our product offerings and our commitment to quality assurance and testing, and globalization of these product offerings. This also accounted for the increase in research and development expenses from 2000 to 2001. Research and development expenses as a percentage of total revenues for 2002 decreased compared to 2001 due mainly to the lower research and development spending resulting from a reprioritization of resources to strategic solutions, coupled with continued management discipline in operating expenses in 2002. The investment in research and development as a percentage of total revenues increased in 2001, compared to 2000, due primarily to the lower than expected license revenues in the first half of 2001, resulting in a five-percentage point increase in these costs as a percentage of total revenues, as these costs were largely fixed prior to the start of the first two quarters of 2001. In addition, the acquisition of enCommerce and the corresponding addition of the GetAccess ™ development team in June 2000 resulted in a four-percentage point increase in research and development expenses as a percentage of total revenues in 2001 compared to 2000. This was offset by a three-percentage point decrease primarily as a result of the cost reduction impact of our restructuring on research and development expenses that came into effect in June 2001. However, we believe that we must continue to maintain our investment in research and development in order to maintain our technological leadership position, software quality and security assurance leadership and thus, expect research and development expenses may have to increase in absolute dollars in the future if additional experienced security experts and software engineers are required.

Operating Expenses—General and Administrative

	Year Ended December 31,		
	2000	2001	2002
		(in thousands)	
Per statement of operations	$12,083	$20,509	$14,840
Less: Special non-recurring charges included	—	5,596	120
Pro forma	$12,083	$14,913	$14,720
Pro forma general and administrative as a percentage of total revenues	8%	13%	14%

General and administrative expenses decreased to $14.7 million in 2002 from $14.9 million in 2001 and $12.1 million in 2000, on a pro forma basis, representing 14%, 13% and 8% of total revenues in the respective years. General and administrative expenses in absolute dollars remained flat between 2001 and 2002, while the increase in these expenses from 2000 to 2001 reflected our continued investment in increased staffing and related expenses for the enhancement of the infrastructure necessary to support our changing business, including investor relations programs, improved management information systems and the increased utilization of outside professional services, prior to our restructuring in June 2001. General and administrative expenses as a percentage of total revenues increased in 2002 and 2001, compared to the prior years, due primarily to the lower than expected revenues in 2002 and 2001, as these expenses include a high degree of fixed costs. We continue to look for ways to gain additional efficiencies in our administrative processes and contain expenses.

Acquired In-process Research and Development and Amortization of Goodwill, Purchased Product Rights and Other Purchased Intangibles

In June 2001, the Financial Accounting Standards Board approved for issuance SFAS No. 142, "Goodwill and Intangible Assets", which revised the accounting for purchased goodwill and intangible assets. Under SFAS No. 142, goodwill and intangible assets with indefinite lives will no longer be amortized, but will be tested for impairment annually and also in the event of an impairment indicator. We adopted SFAS No. 142 as of January 1, 2002. This adoption has affected the amortization of intangibles, resulting from the following past acquisitions:

On March 14, 2000, we completed the acquisition of CygnaCom Solutions Inc., a company based in McLean, Virginia that delivers information technology products and services, with expertise in public key infrastructure, cryptographic technologies, security engineering and systems integration and development. Pursuant to the stock purchase agreement dated March 14, 2000, entered into between us, CygnaCom and the shareholders of CygnaCom, we agreed to acquire all of the outstanding shares of CygnaCom for an aggregate purchase price of $16.6 million, which included cash consideration of $16.0 million. The acquisition was recorded under the purchase method of accounting and, therefore, the results of operations of CygnaCom are included in our financial statements from the acquisition date. Upon consummation of the acquisition, CygnaCom became a wholly owned subsidiary. In connection with this acquisition, we recorded goodwill of $16.6 million and, accordingly, we expensed $5.5 million and $4.6 million of goodwill amortization in 2001 and 2000, respectively. No goodwill amortization was recorded in 2002, due to the adoption of SFAS No. 142.

On June 26, 2000, we completed the acquisition of enCommerce, Inc., a company based in Santa Clara, California that provides software and services for managing global e-business relationships. The acquisition of enCommerce's outstanding capital stock, options and warrants for a total consideration of $505.5 million was accounted for under the purchase method of accounting, which resulted in an allocation of $449.6 million to purchased product rights, goodwill and other purchased intangibles. Also, in connection with this acquisition, an appraisal was done of the intangible assets, resulting in $29.6 million of the purchase price being allocated to in-process research and development that had not yet reached technological feasibility and had no alternative future use. This in-process research and development was expensed in 2000. Amortization of goodwill and other purchased intangibles of $56.2 million and $54.4 million were expensed in 2001 and 2000, respectively. No amortization of these assets has been recorded in 2002, due to the adoption of SFAS No. 142. Amortization of purchased product rights of $1.1 million, $3.3 million and $2.8 million were expensed in 2002, 2001 and 2000, respectively.

In addition, we recorded goodwill amortization of $470,000 and $907,000 in 2001 and 2000, respectively, with respect to goodwill recorded as a result of the acquisition of r^3 in 1998. No amortization of this asset has been recorded since the goodwill was determined to be fully impaired when assessed in June 2001.

In general, total amortization expense related to goodwill, purchased product rights and other purchased intangibles that resulted from the above noted acquisitions decreased in 2002, compared to the prior years, due to the impairment of goodwill, purchased product rights and other purchased intangibles recorded in June 2001, as well as the adoption of SFAS No. 142 as of January 2002.

Restructuring and Other Special Non-recurring Charges

Entrust hired a new Chief Executive Officer, F. William Conner in April 2001. Immediately following his hiring, Management began a re-assessment of the Company to reduce the Company's cash flow outflow from operations. On June 4, 2001, we announced a Board-approved restructuring program to refocus on the most significant market opportunities and to reduce operating costs due to the macroeconomic factors that are negatively affecting technology investment in the market. The restructuring program included a workforce reduction, consolidation of excess facilities, and discontinuance of non-core products and programs. The restructuring resulted in the elimination of over 400 positions, or approximately 33% of the Company's total work force. Combined with the expense reduction associated with the consolidation of excess facilities it resulted in a reduction of the Company's cost of revenues from $15.6 million in the first quarter of 2001 to $11.2 million in the third quarter of 2001, or a reduction of approximately 28%. For the same comparable period, the first quarter 2001 to the third quarter of 2001, it resulted in the following reductions by expense line:

	Quarter Ended	
Expense line	**March 31, 2001**	**September 30, 2001**
Sales and marketing	26,580 to	13,971, a reduction of 47%
Research and development	9,487 to	6,527, a reduction of 31%
General and administrative	4,687 to	3,313, a reduction of 29%

As a result of the restructuring and other related special non-recurring charges and the impact of the macroeconomic conditions on us and our global base of customers, we recognized restructuring and special non- recurring charges of $433.6 million in the second fiscal quarter of 2001, with a subsequent increase of $1.4 million in the second half of 2001 and a reduction of $1.3 million in the first half of 2002, as outlined below (in millions):

	Accrued Restructuring Charges	Other Special Non-recurring Charges	Total Special Charges through June 30, 2001	Adjustments Recorded July 1, 2001 to Dec. 31, 2001	Adjustments Recorded July 1, 2001 to Dec. 31, 2001	Total Special Charges through Dec. 30, 2002
Workforce reduction and other personnel costs	$ 13.5	$ 4.1	$ 17.6	$ 0.3	$ 0.1	$ 18.0
Consolidation of excess facilities	38.2	13.5	51.7	0.5	(0.1)	52.1
Discontinuance of non-core products and programs	13.8	6.4	20.2	(0.8)	(1.3)	18.1
Impairment of goodwill, purchased product rights and other purchased assets	—	327.0	327.0	—	—	327.0
Write-down of long-term strategic investments	—	6.1	6.1	4.7	—	10.8
Bad debt write-offs and additional provisions to the allowance for doubtful accounts	—	11.0	11.0	(3.3)	—	7.7
Total	$ 65.5	$ 368.1	$ 433.6	$ 1.4	$ (1.3)	$433.7

An adjustment to reduce the accrued restructuring charges by $1.1 million was made during the second quarter of 2002 to reflect savings realized as a result of the successful completion of certain contractual obligations in a cost-effective manner. As of June 2002, we had initiated all actions required by the restructuring plan. In addition, we recorded a $0.2 million adjustment in the second quarter of 2002 to reflect a reduction in the accruals for special non-recurring charges, related to the discontinuance of non-core products and programs due to savings realized in completing contractual obligations offset by increased legal and other costs incurred to realize these savings. No further adjustments were required in 2002. The following paragraphs provide information relating to the restructuring programs that resulted in the total special charges listed above.

Workforce Reduction and Other Personnel Costs

The restructuring program resulted in the reduction of approximately 400 of our regular full-time employees, or 33% of the total workforce. The reduction was across all major geographic locations, all business programs and all functions within the organization. The reductions were more heavily weighted in sales and marketing, non-core business programs such as Entrust.Net ™ and Entrust@YourService ™ and secondary geographies such as Asia Pacific and Latin America. The majority of the affected employees were notified of their termination in the second quarter of 2001, and the workforce portion of the restructuring was largely completed by the end of the fourth quarter of 2001. We have recorded a cumulative workforce reduction charge of $13.5 million primarily related to severance costs, fringe benefits due to severed employees and outplacement services.

Other special non-recurring charges included employee relocation expenses, hiring fees and signing bonuses totaling $4.5 million on a cumulative basis, which were recorded primarily in general and administrative expenses.

Consolidation of Excess Facilities

We have recorded cumulative restructuring costs of $39.1 million relating to the consolidation of excess facilities. The consolidation of excess facilities included a total of eight offices in seven cities throughout the world. The costs for consolidation of excess facilities were related primarily to non-cancelable lease costs offset by estimated sublet recoveries. The majority (approximately 85%) of the costs were related to a 75,000 square foot facility in Santa Clara, California. The Santa Clara facility costs are payable contractually over the remaining term of the lease, which runs through to 2011. We will continue to evaluate ongoing possibilities to settle this obligation in the most economic manner.

As at December 31, 2002, we estimated a total of $33.2 million of estimated sublease recoveries in our restructuring accrual. Of this amount, $32.4 million is related to the Santa Clara facility. In addition, $12.1 million of the $33.2 million is recoverable under existing sublease agreements, the remaining $21.1 million of rent recoveries is based on estimates which may be subject to adjustment based upon changes in the real estate sublet markets.

In addition to the cumulative $39.1 million of restructuring costs related to excess facilities, an additional $13.0 million of facilities-related costs were recorded, on a cumulative basis, as a special non-recurring charge as a result of impairment of leasehold improvements and other property and equipment that was disposed of or removed from operations as a result of the consolidation of excess facilities, and were included in the write-down of leaseholds and other long-lived assets in accordance with the provisions of SFAS No. 121, “Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of”. These assets were identified as assets to be disposed of that would have no future benefit to us. Therefore, these assets were reported at the lower of carrying amount and fair value, less costs of disposition. The majority of these costs are non-cash charges.

Discontinuance of Non-Core Products and Programs

In support of the restructuring objective to reduce costs and focus on our core technologies, we discontinued several non-core products and programs. The discontinued products and programs, totaling $11.8 million on a cumulative basis, were primarily related to our services business initiatives and to certain desktop applications that did not achieve the growth and profitability targets in line with our core products and financial objectives. The restructuring charge also included costs related to the exit of certain marketing events and programs that had been committed to prior to the restructuring, but which were being cancelled due to the change in corporate focus. The cash outflow related to the majority of these items was substantially incurred by the end of the second quarter of fiscal 2002. Accrued estimated marketing and distribution agreement obligations related to certain discontinued products of $4.2 million are payable contractually through 2004.

The discontinuance of products and programs, and expenses related to rebranding of our identity and our products, resulted in $6.3 million of cumulative special non-recurring charges, which was primarily recorded in sales and marketing expenses.

Summary of Accrued Restructuring Charges

The following table is a summary of the accrued restructuring charges as at December 31, 2002 and 2001 (in millions):

	December 31, 2002			
	Total Charges Accrued at Beginning of Year	2002 Cash Payments	2002 Adjustments	Accrued Restructuring Charges at End of Year
Workforce reduction and other personnel costs	$ 2.3	$ 2.3	$ 0.1	$ 0.1
Consolidation of excess facilities	34.6	4.6	(0.1)	29.9
Discontinuance of non-core products and programs	10.1	5.8	(1.1)	3.2
Total	$ 47.0	$ 12.7	$ (1.1)	$ 33.2

	December 31, 2001			
	Total Charges Accrued at June 30, 2001	2001 Cash Payments	2001 Adjustments	Accrued Restructuring Charges at End of Year
Workforce reduction and other personnel costs	$ 13.5	$ 11.1	$ (0.1)	$ 2.3
Consolidation of excess facilities	38.2	4.6	1.0	34.6
Discontinuance of non-core products and programs	13.8	2.8	(0.9)	10.1
Total	$ 65.5	$ 18.5	$ —	$ 47.0

Impairment of Goodwill, Purchased Product Rights and Other Intangible Purchased Assets

Due to the decline in our market capitalization, the decline in current overall business conditions within our target market segments and the restructuring program, we completed an assessment of the recoverability of goodwill on our balance sheet as of June 2001, in accordance with APB Opinion No. 17 and the relevant guidance in SFAS No. 121. This impairment analysis indicated that the carrying amount of the goodwill, purchased product rights and other purchased intangible assets of the enCommerce and r^3 acquisitions would not be recovered through the estimated undiscounted future cash flows. We then completed an analysis of the discounted future cash flows from the enCommerce acquisition and the r^3 acquisition. The result of this analysis was a charge of $327.0 million related to the impairment of goodwill, purchased product rights and other purchased intangible assets. Goodwill, purchased product rights and other purchased intangibles from the enCommerce acquisition accounted for $325.4 million of the impairment. This acquisition failed to meet the financial planning forecasts made at the time of the acquisition due largely to the change in the economic conditions since the time of the acquisition and in part due to additional product development and maintenance costs related to the GetAccess ™ product that were estimated to be required in the future and were not known at the time of the acquisition. The remaining $1.6 million of goodwill impairment in 2001 was the result of the r^3 acquisition, which was impacted primarily by the workforce restructuring.

Revenues from the enCommerce products and services are estimated to have contributed approximately 20% to 25% of total revenues in 2002 and 2001, but are estimated to have generated operating losses since acquisition. The results of operations related to the r^3 acquisition were not significant.

Write-down of Long-term Strategic Investments

We assess the recoverability of the carrying value of our strategic investments on a regular basis. Factors that we consider important that could trigger impairment include, but are not limited to, the likelihood that the company in which we invested would have insufficient cash flows to operate for the next twelve months, significant changes in the company's operating performance or business model, and changes in overall market conditions. We recorded charges related to other than temporary declines in the value of certain strategic investments of $10.8 million in 2001 and $1.2 million in 2002. We also recorded a gain on the disposition of a long-term strategic investment of $1.6 million in 2001. These investments are reviewed each period for possible impairment, and therefore, further adjustments may be required in the future.

Bad Debt Write-offs and Additional Provisions to the Allowance for Doubtful Accounts

Due to the changes in the economic environment and the impact of the restructuring program, particularly the curtailment of certain products and presence in certain geographies, we recorded bad debt write-offs and additional provisions to the allowance for doubtful accounts totaling $7.7 million in 2001, which was recorded primarily in sales and marketing expenses. No additional provisions to the allowance for doubtful accounts were recorded in 2002.

Interest Income

Interest income decreased to $3.1 million in 2002 from $8.3 million in 2001 and $13.8 million in 2000, representing 3%, 7% and 9% of total revenues in the respective years. The decrease in investment income for 2002 and 2001, compared to the preceding year, reflected the reduced balance of funds invested, as these amounts have been drawn down to fund cash flow from operations and to acquire long-lived assets and long-term strategic investments. The funds invested decreased from $203.5 million at December 31, 2000 to $117.3 million and $99.4 million at December 31, 2001 and 2002, respectively. In addition, the decrease was due to the lower interest rates that have been available in 2002 and 2001, compared to the preceding years. In 2002, the rate of return on our marketable investments dropped to less than 1% compared to our historical rate of return of just under 5% on an annualized basis.

Loss from Equity Investment

We recorded $602,000 of losses related to our investment in Entrust Japan in 2002, which is accounted for under the equity method of accounting for investments in common stock, since we have the potential to significantly influence the operations and management of Entrust Japan. These losses represent our share of the operating losses of Entrust Japan for 2002, based on an approximate 7% and 39% ownership interest in the voting capital of Entrust Japan in the first and remaining quarters of 2002, respectively. We have included our share of post-acquisition losses of Entrust Japan on the step-by-step acquisition method in our consolidated losses for 2002, and accordingly, have included our share of Entrust Japan's first quarter operating losses, in addition to our share of their second, third and fourth quarter losses, in our 2002 operating results. In addition, we have made a retroactive adjustment to consolidated accumulated deficit to record our share of the post-acquisition losses of Entrust Japan of prior years, attributable to the less than 10% ownership prior to the increased investment, to the extent of our previous investment of $393,000.

Provision for Income Taxes

We recorded an income tax provision of $1.4 million in 2002, compared to $1.8 million in 2001 and $2.3 million in 2000. These provisions represent primarily the taxes payable in certain foreign jurisdictions. We account for income taxes in accordance with SFAS No. 109. The effective income tax rates differed from statutory rates primarily due to the non-deductibility of in-process research and development, amortization and impairment of goodwill, purchased product rights and other purchased intangible assets, as well as an adjustment of the valuation allowance that has offset substantially the tax benefits from the significant net operating loss and tax credit carry-forwards available.

QUARTERLY RESULTS OF OPERATIONS

Our quarterly operating results have varied substantially in the past and are likely to vary substantially from quarter to quarter in the future due to a variety of factors. In particular, our period-to-period operating results are significantly dependent upon the completion date of large license agreements. In this regard, the purchase of our products often requires a significant capital investment, which customers may view as a discretionary cost and, therefore, a purchase that can be deferred or canceled due to budgetary or other business reasons. Estimating future revenues is also difficult because we ship our products soon after an order is received and, therefore, we do not have a significant backlog. Thus, quarterly license revenues are heavily dependent upon orders received and shipped within the same quarter. Moreover, we have generally recorded a significant portion of our total quarterly revenues in the third month of a quarter, with a concentration of these revenues in the last half of that third month. This concentration of revenues is influenced by customer tendencies to make significant capital expenditures at the end of a fiscal quarter. We expect these revenue patterns to continue for the foreseeable future. In addition, quarterly license revenues are dependent on the timing of revenue recognition, which can be affected by many factors, including the timing of customer installations and acceptance. In these regards, we have from time to time experienced delays in recognizing revenues with respect to certain orders. In any period a significant portion of our revenue may be derived from large sales to a limited number of customers. Despite the uncertainties in our revenue patterns, our operating expenses are based upon anticipated revenue levels and such expenses are incurred on an approximately ratable basis throughout the quarter. As a result, if expected revenues are delayed or otherwise not realized in a quarter for any reason, our business, operating results and financial condition would be adversely affected in a significant way.

Under our restructuring program in 2001, as discussed earlier, the levels of operating expenses decreased and the net loss decreased in the third and fourth quarters of 2001 and throughout 2002.

The following tables set forth certain unaudited consolidated quarterly statement of operations data for the eight quarters in the two-year period ended December 31, 2002, as well as such data expressed as a percentage of our total revenues for the periods indicated. These data have been derived from unaudited consolidated financial statements that, in our opinion, include all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of such information when read in conjunction with our consolidated financial statements and related notes appearing elsewhere in this Annual Report.

The operating results for any quarter are not necessarily indicative of results for any future period.

	Quarter Ended							
	Mar. 31 2001	June 30 2001	Sept. 30 2001	Dec. 31 2001	Mar. 31 2002	June 30 2002	Sept. 30 2002	Dec. 31 2002
	(in thousands, except per share data)							
Statement of Operations Data:								
Revenues:								
License	$10,559	$12,554	$12,288	$12,626	$12,089	$11,905	$ 8,548	$ 9,710
Services and maintenance	20,946	17,462	15,732	15,798	15,434	14,601	15,460	15,000
Total revenues	31,505	30,016	28,020	28,424	27,523	26,506	24,008	24,710
Cost of revenues:								
License	901	1,207	1,247	1,160	942	1,023	803	906
Services and maintenance	13,346	11,312	9,710	9,272	8,494	8,551	8,177	8,458
Amortization of purchased product rights	1,377	1,377	284	284	284	284	284	284
Total cost of revenues	15,624	13,896	11,241	10,716	9,720	9,858	9,264	9,648
Gross profit	15,881	16,120	16,779	17,708	17,803	16,648	14,744	15,062
Operating expenses:								
Sales and marketing	26,580	38,219	13,971	8,669	12,145	10,732	11,043	10,208
Research and development	9,487	8,345	6,527	6,533	6,033	6,476	5,827	5,815
General and administrative	4,687	9,363	3,313	3,146	3,506	3,893	3,525	3,916

	Quarter Ended							
	Mar. 31 2001	June 30 2001	Sept. 30 2001	Dec. 31 2001	Mar. 31 2002	June 30 2002	Sept. 30 2002	Dec. 31 2002
	(in thousands, except per share data)							
Amortization of goodwill and other purchased intangibles	28,900	28,900	2,171	2,171	—	—	—	—
Impairment of goodwill, purchased product rights and other purchased intangibles	—	326,953	—	—	—	—	—	—
Restructuring charges and adjustments	—	65,511	—	—	—	(1,079)	—	—
Write-down of leaseholds and other long-lived assets	—	13,519	—	—	—	—	—	—
Total operating expenses	69,654	490,810	25,982	20,519	21,684	20,022	20,395	19,939
Loss from operations	(53,773)	(474,690)	(9,203)	(2,811)	(3,881)	(3,374)	(5,651)	(4,877)
Other income (expense):								
Interest income	3,244	2,399	1,511	1,176	1,152	608	850	664
Loss from equity investment	—	—	—	—	—	(370)	(135)	(97)
Realized gain (loss) on investments	—	—	1,103	—	(220)	—	—	—
Write-down of long-term strategic investments	—	(6,100)	(1,406)	(3,294)	—	(1,238)	—	—
Total other income (expense)	3,244	(3,701)	1,208	(2,118)	932	(1,000)	715	567
Loss before income taxes	(50,529)	(478,391)	(7,995)	(4,929)	(2,949)	(4,374)	(4,936)	(4,310)
Provision for income taxes	(350)	(396)	(303)	(779)	(395)	(400)	(276)	(279)
Net loss	$ (50,879)	$ (478,787)	$ (8,298)	$ (5,708)	$ (3,344)	$ (4,774)	$ (5,212)	$ (4,589)
Net loss per share:								
Basic	$ (0.81)	$ (7.58)	$ (0.13)	$ (0.09)	$ (0.05)	$ (0.07)	$ (0.08)	$ (0.07)
Diluted	$ (0.81)	$ (7.58)	$ (0.13)	$ (0.09)	$ (0.05)	$ (0.07)	$ (0.08)	$ (0.07)
Shares used in per share Computation:								
Basic	62,911	63,205	63,491	64,036	64,762	65,102	65,115	64,805
Diluted	62,911	63,205	63,491	64,036	64,762	65,102	65,115	64,805

	Quarter Ended							
	Mar. 31 2001	June 30 2001	Sept. 30 2001	Dec. 31 2001	Mar. 31 2002	June 30 2002	Sept. 30 2002	Dec. 31 2002
Statement of Operations Data:								
Revenues:								
License	33.5%	41.8%	43.9%	44.4%	43.9%	44.9%	35.6%	39.3%
Services and maintenance	66.5	58.2	56.1	55.6	56.1	55.1	64.4	60.7
Total revenues	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Cost of revenues:								
License	2.8	4.0	4.4	4.1	3.4	3.8	3.3	3.7
Services and maintenance	42.4	37.7	34.7	32.6	30.9	32.3	34.1	34.2
Amortization of purchased product rights	4.4	4.6	1.0	1.0	1.0	1.1	1.2	1.2
Total cost of revenues	49.6	46.3	40.1	37.7	35.3	37.2	38.6	39.1
Gross profit	50.4	53.7	59.9	62.3	64.7	62.8	61.4	60.9
Operating expenses:								
Sales and marketing	84.4	127.3	49.9	30.5	44.1	40.5	46.0	41.3
Research and development	30.1	27.8	23.3	23.0	21.9	24.4	24.2	23.5
General and administrative	14.9	31.2	11.8	11.1	12.8	14.7	14.7	15.8
Amortization of goodwill and other purchased intangibles	91.7	96.3	7.7	7.6	—	—	—	—
Impairment of goodwill, purchased product rights and other purchased intangibles	—	1,089.3	—	—	—	—	—	—
Restructuring charges and adjustments	—	218.3	—	—	—	(4.1)	—	—
Write-down of leaseholds and other long-lived assets	—	45.0	—	—	—	—	—	—
Total operating expenses	221.1	1,635.2	92.7	72.2	78.8	75.5	84.9	80.6
Loss from operations	(170.7)	(1,581.5)	(32.8)	(9.9)	(14.1)	(12.7)	(23.5)	(19.7)
Other income (expense):								
Interest income	10.3	8.0	5.4	4.1	4.2	2.3	3.5	2.7
Loss from equity investment	—	—	—	—	—	(1.4)	(0.6)	(0.4)
Realized gain (loss) on investments	—	—	3.9	—	(0.8)	—	—	—
Write-down of long-term strategic investments	—	(20.3)	(5.0)	(11.6)	—	(4.7)	—	—
Total other income (expense)	10.3	(12.3)	4.3	(7.5)	3.4	(3.8)	2.9	2.3
Loss before income taxes	(160.4)	(1,593.8)	(28.5)	(17.4)	(10.7)	(16.5)	(20.6)	(17.4)
Provision for income taxes	(1.1)	(1.3)	(1.1)	(2.7)	(1.4)	(1.5)	(1.1)	(1.2)
Net loss	(161.5)%	(1,595.1)%	(29.6)%	(20.1)%	(12.1)%	(18.0)%	(21.7)%	(18.6)%

LIQUIDITY AND CAPITAL RESOURCES

We used cash of $27.4 million from operating activities during 2002. This cash outflow was primarily a result of a net loss before non-cash charges of $7.5 million, a decrease in accounts payable and accrued liabilities of $6.8 million, a decrease in accrued restructuring charges of $13.8 million, and a decrease in deferred revenue of $1.4 million, partially offset by cash inflows resulting from a decrease in accounts receivable of $1.4 million. Our average days sales outstanding at December 31, 2002 was 81 days, which represents an increase from the 75 days that we reported at December 31, 2001. The overall increase in days sales outstanding from December 31, 2001 was mainly due to the decrease in allowance for doubtful accounts from the previous year and a slightly worse linearity of revenues during the last quarter of 2002. For purposes of calculating average days sales outstanding, we divide ending accounts receivable by the current quarter's revenues and multiply this amount by 90 days. The level of accounts receivable at each quarter end will be affected by the concentration of revenues in the final weeks of each quarter and may be negatively affected by expanded international revenues in relation to total revenues as licenses to international customers often have longer payment terms.

During 2002, we generated $14.4 million of cash in investing activities, primarily due to cash provided by reductions in our marketable investments in the amount of $17.9 million (net of $310.6 million of marketable investment purchases). This was partially offset by $2.0 million invested in property and equipment primarily for computer hardware, furniture and leasehold improvements required to complete the fit-up of our new Addison, Texas facility, $1.0 million invested in Entrust Japan and $0.6 million invested in other long-term assets.

We used cash of $0.3 million for financing activities in 2002 primarily for the repurchase of our Common stock, offset by cash provided by the exercise of employee stock options and the sale of shares under our employee stock purchase plan.

For disclosure regarding our contractual obligations and commercial commitments, please see notes 10 and 15 to our consolidated financial statements for the year ended December 31, 2002 contained elsewhere in this Annual Report on Form 10-K. There were no new significant contractual obligations or commitments incurred in 2002. For information on related-party transactions, please see note 14 to our consolidated financial statements.

As of December 31, 2002, our cash, cash equivalents and marketable investments in the amount of $131.4 million provided our principal sources of liquidity. Overall, we used $31.1 million from our cash, cash equivalents and marketable investments in 2002. Although we are targeting operating breakeven, based on top line revenue growth while maintaining the current operating expense structure, we estimate that we will continue to use cash throughout our fiscal 2003 to fund operating losses and to satisfy the obligations accrued for under our restructuring program. However, if revenue improvements do not materialize, then cash, cash equivalents and marketable investments will be negatively affected.

In addition, we announced in the third quarter of 2002 that we intend to repurchase up to an aggregate of 7,000,000 shares of our Common stock over the 12-month period ending July 28, 2003, or an earlier date determined by our board of directors, in open market, negotiated and block transactions. The timing and amount of shares repurchased under this program will be determined by our management based on its evaluation of market and business conditions, and will be funded using available working capital. During 2002, we repurchased 785,000 shares of

Common stock for an aggregate purchase price of $2.2 million. While there can be no assurance as to the extent of usage of liquid resources in future periods, we believe that our cash flows from operations and existing cash, cash equivalents and marketable investments will be sufficient to meet our needs for at least the next twelve months.

CERTAIN FACTORS THAT MAY AFFECT OUR BUSINESS

Our quarterly revenues and operating results are subject to significant fluctuations and such fluctuations may lead to a reduced market price for our stock.

Our quarterly revenues and operating results have varied in the past and may continue to fluctuate in the future. We believe that period-to-period comparisons of our operating results are not necessarily meaningful, but securities analysts and investors often rely upon these comparisons as indicators of future performance. If our operating results in any future period fall below the expectations of securities analysts and investors, or the guidance that we provide, the market price of our securities would likely decline. Factors that have caused our results to fluctuate in the past and which are likely to affect us in the future include the following:

- reduced capital expenditures for software;
- length of sales cycles associated with our product offerings;
- the timing, size and nature of our licensing transactions;
- the increased dependency on partners for end user fulfillment;
- market acceptance of new products or product enhancements by us;
- market acceptance of new products or product enhancements by our competitors;
- the relative proportions of revenues derived from licenses and services and maintenance;
- the timing of new personnel hires and the rate at which new personnel become productive;
- changes in pricing policies by our competitors;
- changes in our operating expenses; and
- fluctuations in foreign currency exchange rates.

Estimating future revenues is difficult, and our failure to do so accurately may lead to a reduced market price for our stock and reduced profitability.

Estimating future revenues is difficult because we ship our products soon after an order is received and, as such, we do not have a significant order backlog. Thus, quarterly license revenues depend heavily upon orders received and shipped within the same quarter. Moreover, we historically have recorded 50% to 80% of our total quarterly revenues in the third month of the quarter, with a concentration of revenues in the second half of that month. We expect that this concentration of revenues, which is attributable in part to the tendency of some customers to make significant capital expenditures at the end of a fiscal quarter and to sales patterns within the software industry, will continue for the foreseeable future.

Our expense levels are based, in significant part, upon our expectations as to future revenues and are largely fixed in the short term. We may be unable to adjust spending in a timely manner to compensate for any unexpected shortfall in revenues. Any significant shortfall in revenues in relation to our expectations could have an immediate and significant effect on our profitability for that quarter and may lead to a reduced market price for our stock.

Because of the lengthy and unpredictable sales cycle associated with our large software transactions, we may not succeed in closing transactions on a timely basis or at all, which would adversely affect our revenues and operating results.

Transactions for our solutions often involve large expenditures, and the sales cycles for these transactions are often lengthy and unpredictable. Factors affecting the sales cycle include:

- customers' budgetary constraints;
- the timing of customers' budget cycles; and
- customers' internal approval processes.

We may not succeed in closing such large transactions on a timely basis or at all, which could cause significant variability in our revenues and results of operations for any particular period. If our results of operations and cash flows fall below the expectations of securities analysts, or below the targeted guidance range that we have provided, our stock price may decline.

A limited number of customers has accounted for a significant percentage of our revenues, which may decline if we cannot maintain or replace these customer relationships.

Historically, a limited number of customers has accounted for a significant percentage of our revenues. In 2002, 2001 and 2000, our three largest customers accounted for 18%, 18% and 12% of revenues, respectively.

We anticipate that our results of operations in any given period will continue to depend to a significant extent upon revenues from a small number of large customers. In addition, we anticipate that such customers will continue to vary over time, so that the achievement of our long-term goals will require us to obtain additional significant customers on an ongoing basis. Our failure to enter into a sufficient number of large licensing agreements during a particular period could have a material adverse effect on our revenues.

The U.S. and Canadian Federal Governments account for a significant percentage of our revenues, which may decline or be subject to delays, which would adversely affect our operating results.

The extended government vertical (Governments, including Healthcare) accounted for 49% of our software revenue in 2002. Sustaining and growing revenues in the government market will depend, in large part, on the following:

- the adoption rate of our products within government departments and agencies;
- the timing and amount of budget appropriations for information technology and specifically information security;
- the timing of adoption of information security policies and regulations, including, but not limited to HIPPA and the Gramm-Leach-Bliley Act; and
- our ability to develop and maintain the appropriate business relationships with partners with whom the government contracts with for information security projects.

A decline, or delay in the growth of this market could reduce demand for our products, adversely affecting our revenues and results of operations.

The outbreak of war, significant threat of war, or a terrorist act could adversely affect our business.

Historically, the outbreak of war has had an adverse affect upon the economy. In the event of war or significant terrorist act, any of the following may occur:

- government spending could be reprioritized to wartime activities. The extended government vertical (Governments, including Healthcare) accounted for 49% of our software revenue in 2002;
- global enterprise spending budgets could be cut or delayed resulting in lower demand for our products; or
- widespread and unprecedented acts of cyber-terrorism could cause disruption of communications and technology infrastructures, which could impact our customers of products and could have unforeseen economic impacts.

A decline or delay in economic spending due to the outbreak of war, significant threat of war or a terrorist act could reduce demand for our products, materially adversely affecting our revenues and results of operations.

If the enterprise information technology budgets and the digital identity security market do not continue to grow, demand for our products and services will be adversely affected.

The market for digital identity security solutions is at an early stage of development. Continued growth of the digital identity security market will depend, in large part, on the following:

- the continued expansion of Internet usage and the number of organizations adopting or expanding intranets and extranets;
- the rate of adoption of Internet-based business applications such as Web Services;
- the ability of network infrastructures to support an increasing number of users and services;
- the public recognition of the potential threat posed by computer hackers and other unauthorized users; and
- the continued development of new and improved services for implementation across the Internet, intranets and extranets.

A decline in the growth of this market could reduce demand for our products, adversely affecting our revenues and results of operations.

A breach of security at one of our customers, whether or not due to our products, could harm our reputation and reduce the demand for our products.

The processes used by computer hackers to access or sabotage networks and intranets are rapidly evolving. A well-publicized actual or perceived breach of network or computer security at one of our customers, regardless of whether such breach is attributable to our products, third-party technology used within our products or any significant advance in techniques for decoding or “cracking” encrypted information, could adversely affect the market’s perception of us and our products, and could have an adverse effect on our reputation and the demand for our products.

In addition, the security level of our products is dependent upon the processes and procedures used to install and operate our products. Failure on the part of our customers to properly install and operate our products, could cause a security breach, which could adversely affect the market’s perception of us and our products, and could have an adverse effect on our reputation and the demand for our products.

As our products contain errors or bugs, sales of our products would likely decline if some of these bugs or the number of bugs were significant.

Like virtually all software systems, our products contain errors, failures or bugs that our existing testing procedures have not detected. The errors may become evident at any time during the life of our products. The discovery of any errors, failures or bugs in any products, including third-party technology incorporated into our products, may result in:

- adverse publicity;
- product returns;
- the loss or delay of market acceptance of our products; and
- third-party claims against us.

Accordingly, the discovery of any errors, failures or bugs would have a significant adverse effect on the sales of our products and our results of operations.

Our revenues may decline if we cannot compete successfully in an intensely competitive market.

We target our products at the rapidly evolving market for digital identity security solutions. Many of our current and potential competitors have longer operating histories, greater name recognition, larger installed bases and significantly greater financial, technical, marketing and sales resources than we do. As a result, they may be able to react more quickly to emerging technologies and changes in customer requirements, or to devote greater resources to the promotion and sale of their products. In addition, certain of our current competitors in particular segments of the security marketplace may in the future broaden or enhance their offerings to provide a more comprehensive solution competing more fully with our functionality.

Increased competition and increased market volatility in our industry could result in lower prices, reduced margins or the failure of our products and services to achieve or maintain market acceptance, any of which could have a serious adverse effect on our business, financial condition and results of operations.

Our business will not be successful if we do not keep up with the rapid changes in our industry.

The emerging market for digital identity security products and related services is characterized by rapid technological developments, frequent new product introductions and evolving industry standards. To be competitive, we have to continually improve the performance, features and reliability of our products and services, particularly in response to competitive offerings, and be first to market with new products and services or enhancements to existing products and services. Our failure to develop and introduce new products and services successfully on a timely basis and to achieve market acceptance for such products and services could have a significant adverse effect on our business, financial condition and results of operations.

We may have difficulty managing our operations, which could adversely affect our ability to successfully grow our business.

Our ability to manage future growth, if any, will depend upon our ability to:

- continue to implement and improve operational, financial and management information systems on a timely basis; and
- expand, train, motivate and manage our work force.

Our personnel, systems, procedures and controls may not be adequate to support our operations. The geographic dispersal of our operations, including the separation of our headquarters in Addison, Texas, from our research and development facilities in Ottawa, Canada, and Santa Clara, California and from our European headquarters in Reading, United Kingdom, may make it more difficult to manage our growth.

If we fail to continue to attract and retain qualified personnel, our business may be harmed.

Our future success depends upon our ability to continue to attract and retain highly qualified scientific, technical, sales and managerial personnel. Competition for such personnel is intense, particularly in the field of cryptography, and there can be no assurance that we can retain our key scientific, technical, sales and managerial employees or that we can attract, motivate or retain other highly qualified personnel in the future. If we cannot retain or are unable to hire such key personnel, our business, financial condition and results of operations could be significantly adversely affected.

We face risks associated with our international operations, which, if not managed properly, could have a significant adverse effect on our business, financial condition or results of operations.

In the future, we may establish additional foreign operations, hire additional personnel and establish relationships with additional partners internationally. This expansion would require significant management attention and financial resources and could have an adverse effect on our business, financial condition and results of operations. Although our international sales currently are primarily denominated in U.S. dollars, we may increasingly denominate sales in foreign currencies in the future. In addition, our international business may be subject to the following risks:

- difficulties in collecting international accounts receivable;
- difficulties in obtaining U.S. export licenses, especially for products containing encryption technology;
- potentially longer payment cycles for customer payments;
- increased costs associated with maintaining international marketing efforts;
- introduction of non-tariff barriers and higher duty rates;
- difficulties in enforcement of contractual obligations and intellectual property rights;
- difficulties managing personnel and operations in remote locations; and
- increased complexity in global corporate tax structure.

Any one of these could significantly and adversely affect our business, financial condition or results of operations.

If the laws regarding exports of our products further limit or otherwise restrict our business, we could be prohibited from shipping our products to restricted countries, which would result in a loss of revenues.

Some of our products are subject to export controls under laws of the U.S., Canada and other countries. The list of products and countries for which exports are restricted, and the relevant regulatory policies, are likely to be revised from time to time. If we cannot obtain required government approvals under these regulations, we may not be able to sell products abroad or make products available for sale internationally via computer networks such as the Internet. Furthermore, U.S. governmental controls on the exportation of encryption products and technology may in the future restrict our ability to freely export some of our products with the most powerful information security encryption technology.

We may not be able to protect our intellectual property rights, which could make us less competitive and cause us to lose market share.

Our future success will depend, in part, upon our intellectual property rights and our ability to protect these rights. We rely on a combination of patent, copyright, trademark and trade secret laws, nondisclosure agreements, shrink-wrap licenses and other contractual provisions to establish, maintain and protect our proprietary rights. Despite our efforts to protect our proprietary rights, unauthorized third parties may:

- copy aspects of our products;
- obtain and use information that we regard as proprietary; or

- infringe upon our patents.

Policing piracy and other unauthorized use of our products is difficult, particularly in international markets and as a result of the growing use of the Internet. In addition, third parties might successfully design around our patents or obtain patents that we would need to license or design around. Finally, the protections we have obtained may not be sufficient because:

- some courts have held that shrink-wrap licenses, because they are not signed by the licensee, are not enforceable;
- our trade secrets, confidentiality agreements and patents may not provide meaningful protection of our proprietary information; and
- we may not seek additional patents on our technology or products and such patents, even if obtained, may not be broad enough to protect our technology or products.

Our inability or failure to protect our proprietary rights could have a significant adverse effect on our business, financial condition or results of operations.

We have been subject to, and may in the future become subject to, intellectual property infringement claims that could be costly and could result in a diversion of management's attention.

As the number of security products in the industry and the functionality of these products further overlaps, software developers and publishers may increasingly become subject to claims of infringement or misappropriation of the intellectual property or proprietary rights of others. From time to time, we have received notices from third parties either soliciting our interest in obtaining a license under one or more patents owned or licensed by these third parties or suggesting that our products may be infringing one or more patents owned or licensed by these third parties. From time to time, we have received notices from various customers stating that we may be responsible for indemnifying such customers pursuant to indemnification obligations in product license agreements with such customers for alleged infringement of patents assigned to a third parties. To date, we are not aware that any customer has filed an action against us for indemnification. In addition, third parties may assert infringement or misappropriation claims against us in the future. Defending or enforcing our intellectual property could be costly and could result in a diversion of management's attention, which could have a significant adverse effect on our business, financial condition or results of operations. A successful claim against us could also have a significant adverse effect on our results of operations for the period in which damages are paid. Additionally, as a result of a successful claim, we could potentially be enjoined from using technology that is required for our products to remain competitive which could in turn have an adverse effect on our results of operations for subsequent periods.

We may lose access to technology that we license from outside vendors, which loss could adversely affect our ability to sell our products.

We rely on outside licensors for patent and/or software license rights in technology that is incorporated into and is necessary for the operation of our products. For example, our ability to provide Web server certificates in the future is dependent upon a licensing agreement we have with Baltimore Technologies, one of our primary competitors. Our success will depend in part on our continued ability to have access to such technologies that are or may become important to the functionality of our products. Any inability to continue to procure or use such technology could have a significant adverse effect on our ability to sell some of our products.

We sometimes enter into complex contracts which require ongoing monitoring and administration. Failure to monitor and administer these contracts properly could result in liability or damages.

We sometimes enter into complex contracts with our Government customers that contain clauses that provide that if a customer who falls within a specific category (known as a Relevant Customer) is offered better terms on the Company's software products and related services than had been offered to the Government customer, then the Government customer will be able to buy additional quantities of those software products and services for the same length of time, from the same effective date and on the better terms that were offered to the Relevant Customer. The Company monitors compliance with these contracts on a continuous basis. The Company also conducts periodic self-assessments to ensure that the contracts are being properly administered and that there are no accruing liabilities for non-compliance. If these contracts are not properly monitored and administered, they may be breached and could result in damages payable by us which, depending on their magnitude, could have a material adverse effect on our business, financial condition and results of operations.

Future acquisitions or investments could disrupt our ongoing business, distract our management and employees, increase our expenses and adversely affect our results of operations.

It is possible, as part of our future growth strategy, that we will from time-to-time acquire or make investments in companies, technologies, product solutions or professional services offerings. With respect to these acquisitions, we would face the difficulties of assimilating personnel and operations from the acquired businesses and the problems of retaining and motivating key personnel from such businesses. In addition, these acquisitions may disrupt our ongoing operations, divert management from day-to-day business, increase our expenses and adversely impact our results of operations. Any future acquisitions would involve certain other risks, including the assumption of additional liabilities, potentially dilutive issuances of equity securities and incurrence of debt. In addition, these types of transactions often result in charges to earnings for such items as amortization of goodwill or in-process research and development expenses.

Our stock price is volatile and may continue to be volatile in the future.

The trading price of our common stock has been, and is expected to continue to be, highly volatile and may be significantly and adversely affected by factors such as:

- actual or anticipated fluctuations in our operating results;
- announcements of technological innovations;
- new products or new contracts by us or our competitors;
- developments with respect to patents, copyrights or propriety rights;
- conditions and trends in the security industry;
- changes in financial estimates by securities analysts; and
- general market conditions and other factors.

Nortel Networks' ownership of approximately 15% of our voting stock could have the effect of impeding a change of control, and the sale of shares of Entrust Common stock held by Nortel Networks could negatively impact our share price.

As of December 31, 2002, Nortel Networks Limited, through its subsidiary, Nortel Networks Inc., beneficially owned approximately 15% of our outstanding voting stock. This concentration of ownership may have the effect of delaying or preventing a change in control that other stockholders may find favorable.

Nortel Networks also has the right to sell its shares under Rule 144 of the Securities Act of 1933 or through the exercise of demand registration rights. Nortel Networks' decisions to sell its shares could negatively affect our share price.

Provisions of our charter and bylaws may delay or prevent transactions that are in your best interests.

Our charter and bylaws contain provisions, including a staggered board of directors that may make it more difficult for a third party to acquire us, or may discourage bids to do so. These provisions could limit the price that investors might be willing to pay for shares of our common stock and could make it more difficult for a third party to acquire, or could discourage a third party from acquiring, a majority of our outstanding voting stock. Our board of directors also has the authority to issue up to 5,000,000 shares of preferred stock and to determine the price, rights, preferences, privileges and restrictions, including voting rights, of those shares without any further vote or action by the stockholders. The rights of the holders of common stock will be subject to, and may be adversely affected by, the rights of the holders of any preferred stock that may be issued in the future. The issuance of preferred stock could make it more difficult for a third party to acquire, or may discourage a third party from acquiring, a majority of our outstanding voting stock.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Our consolidated financial statements together with the related notes and the report of Deloitte & Touche, LLP, independent auditors, are set forth in the Index to Consolidated Financial Statements at Item 15 and incorporated herein by this reference.

Our "Quarterly Results of Operations" set forth in Item 7 is incorporated herein by reference.

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

(a) The following documents are filed as part of this Form 10-K:

1. *Consolidated Financial Statements.* The following consolidated financial statements of Entrust, Inc. are filed as part of this Form 10-K on the pages indicated:

2. Schedules other than the ones listed above are omitted as the required information is inapplicable or the information is presented in the consolidated financial statements or related notes.

3. *Exhibits*. The exhibits listed on the Exhibit Index immediately preceding such Exhibits are filed as part of this Annual Report on Form 10-K.

(b) Reports on Form 8-K

On October 2, 2002, we filed with the Securities and Exchange Commission a Current Report on Form 8-K dated September 30, 2002 to report under Item 5 (Other Events) that, on September 30, 2002, the U.S. District Court for the Eastern District of Texas issued an order dismissing a class action lawsuit pending against us.

SIGNATURES

Pursuant to the requirements of Section 13 of 15(d) 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, on the 23rd day of December, 2003.

ENTRUST, INC.
(Registrant)

By: /s/ F. William Conner

F. William Conner
President, Chief Executive Officer and Chairman of the Board

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on the 23rd day of December, 2003.

Signature	Title
/s/ F. William Conner **F. William Conner**	President, Chief Executive Officer and Chairman of the Board (Principal Executive Officer)
/s/ David J. Wagner **David J. Wagner**	Senior Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)
Butler C. Derrick, Jr.	Director
/s/ Anthony E. Hwang **Anthony E. Hwang**	Director
/s/ Jerry Jones **Jerry Jones**	Director
/s/ Terrell B. Jones **Terrell B. Jones**	Director
/s/ Michael P. Ressner **Michael P. Ressner**	Director
/s/ Douglas Schloss **Douglas Schloss**	Director
/s/ Liener Temerlin **Liener Temerlin**	Director
/s/ Edward O. Vetter **Edward O. Vetter**	Director

INDEPENDENT AUDITORS' REPORT

To the Directors and Shareholders of Entrust, Inc.:

We have audited the consolidated balance sheets of Entrust, Inc. as of December 31, 2001 and 2002, and the related consolidated statements of operations, shareholders' equity and comprehensive income, and cash flows for each of the three years in the period ended December 31, 2002. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Entrust, Inc. at December 31, 2001 and 2002, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2002, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Notes 2 and 5 to the consolidated financial statements, the Company changed its method of accounting for goodwill and other purchased intangibles, as of January 1, 2002, as required by Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets".

/s/ DELOITTE & TOUCHE LLP

Dallas, Texas

February 27, 2003

ENTRUST, INC.

CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

	December 31,	
	2001	**2002**
ASSETS		
Current assets:		
Cash and cash equivalents	$ 45,267	$ 32,043
Short-term marketable investments	108,288	85,980
Accounts receivable (net of allowance for doubtful accounts of $3,909 in 2001 and $2,976 in 2002)	23,732	22,323
Other receivables	1,720	1,050
Prepaid expenses	3,482	3,450
Total current assets	182,489	144,846
Long-term marketable investments	9,038	13,423
Property and equipment, net	17,390	12,795
Purchased product rights, net	2,838	1,702
Goodwill and other purchased intangibles, net	11,186	11,186
Long-term equity investment	—	1,264
Long-term strategic investments	4,683	2,858
Other long-term assets, net	1,421	1,497
Total assets	$ 229,045	$ 189,571
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 13,815	$ 11,226
Accrued liabilities	15,121	10,540
Accrued restructuring charges	46,988	33,166
Deferred revenue	17,553	16,547
Total current liabilities	93,477	71,479
Long-term liabilities	116	227
Total liabilities	93,593	71,706
Shareholders' equity:		
Common stock, par value $0.01 per share; 64,432,052 and 64,491,634 issued and outstanding shares at December 31, 2001 and 2002, respectively	645	645
Additional paid-in capital	781,879	781,842
Unearned compensation	(100)	(39)
Accumulated deficit	(645,583)	(663,502)
Accumulated other comprehensive loss	(1,389)	(1,081)
Total shareholders' equity	135,452	117,865
Total liabilities and shareholders' equity	$ 229,045	$ 189,571

See notes to consolidated financial statements

ENTRUST, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except share and per share data)

	Year Ended December 31,		
	2000	2001	2002
Revenues:			
License	$ 93,112	$ 48,027	$ 42,252
Services and maintenance	55,265	69,938	60,495
Total revenues	148,377	117,965	102,747
Cost of revenues:			
License	4,418	4,515	3,674
Services and maintenance	32,418	43,640	33,680
Amortization of purchased product rights	2,751	3,322	1,136
Total cost of revenues	39,587	51,477	38,490
Gross profit	108,790	66,488	64,257
Operating expenses:			
Sales and marketing	73,248	87,439	44,128
Research and development	27,625	30,892	24,151
General and administrative	12,083	20,509	14,840
Acquired in-process research and development	29,614	—	—
Amortization of goodwill and other purchased intangibles	59,952	62,142	—
Impairment of goodwill, purchased product rights and other purchased intangibles	—	326,953	—
Restructuring charges and adjustments	—	65,511	(1,079)
Write-down of leaseholds and other long-lived assets	—	13,519	—
Total operating expenses	202,522	606,965	82,040
Loss from operations	(93,732)	(540,477)	(17,783)
Other income (expense):			
Interest income	13,809	8,330	3,274
Loss from equity investment	—	—	(602)
Realized gain (loss) on investments	—	1,103	(220)
Write-down of long-term strategic investments	—	(10,800)	(1,238)
Total other income (expense)	13,809	(1,367)	1,214
Loss before income taxes	(79,923)	(541,844)	(16,569)
Provision for income taxes	(2,337)	(1,828)	(1,350)
Net loss	$ (82,260)	$ (543,672)	$ (17,919)
Net loss per share:			
Basic	$ (1.44)	$ (8.57)	$ (0.28)
Diluted	$ (1.44)	$ (8.57)	$ (0.28)
Weighted average common shares used in per share computations:			
Basic	57,003,479	63,410,786	64,946,246
Diluted	57,003,479	63,410,786	64,946,246

See notes to consolidated financial statements

ENTRUST, INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME

for the years ended December 31, 2000, 2001 and 2002

(in thousands, except share data)

	Common Stock		Special Voting Stock		Additional Paid-In Capital	Unearned Compen-sation	Accumulated Deficit	Accumulated Other Compre-hensive Income (Loss)	Compre-hensive Income (Loss)	Total Share-holders' Equity
	Shares	Amount	Shares	Amount						
Balances at December 31, 1999, as originally reported	45,203,448	$ 452	5,157,289	$ 52	$ 122,883	$ (439)	$ (19,258)	$ (535)	$ 103,155	
Retroactive recognition of Entrust Japan losses under the equity method	—	—	—	—	—	—	(393)	—	(393)	
Balances at December 31, 1999, as adjusted	45,203,448	452	5,157,289	52	122,883	(439)	(19,651)	(535)	102,762	
Unearned compensation related to non-employee stock options granted	—	—	—	—	101	(101)	—	—	—	
Unearned compensation amortized	—	—	—	—	—	224	—	—	224	
Special voting shares exchanged	5,157,289	52	(5,157,289)	(52)	—	—	—	—	—	
Common shares issued:										
Cash	2,074,260	21	—	—	162,622	—	—	—	162,643	
Acquisitions, including options and warrants	8,548,177	85	—	—	482,187	—	—	—	482,272	
Stock option exercises	1,701,659	17	—	—	6,320	—	—	—	6,337	
Employee Stock Purchase Plan	68,905	1	—	—	1,705	—	—	—	1,706	
Common shares issuance costs	—	—	—	—	(1,130)	—	—	—	(1,130)	
Tax equivalent related to non-qualified option exercises	—	—	—	—	916	—	—	—	916	
Comprehensive income (loss):										
Net loss	—	—	—	—	—	—	(82,260)	—	$ (82,260)	(82,260)
Unrealized loss on investments	—	—	—	—	—	—	—	(1,457)	(1,457)	(1,457)
Unrealized gain on gross-up receivable related to investments	—	—	—	—	—	—	—	1,457	1,457	1,457
Translation adjustment	—	—	—	—	—	—	—	201	201	201
Total comprehensive loss								$ (82,059)		
Balances at December 31, 2000	62,753,738	628	—	—	775,604	(316)	(101,911)	(334)	673,671	
Unearned compensation related to non-employee stock options granted	—	—	—	—	6	(6)	—	—	—	
Unearned compensation amortized	—	—	—	—	—	222	—	—	222	
Warrants and options issued to non-employees for services rendered	—	—	—	—	1,092	—	—	—	1,092	
Common shares issued:										
Stock option exercises	1,422,735	14	—	—	3,070	—	—	—	3,084	
Employee Stock Purchase Plan	255,579	3	—	—	2,107	—	—	—	2,110	
Comprehensive loss:										
Net loss	—	—	—	—	—	—	(543,672)	—	$ (543,672)	(543,672)
Unrealized loss on investments, net of reclassification adjustment	—	—	—	—	—	—	—	(220)	(220)	(220)
Translation adjustment	—	—	—	—	—	—	—	(835)	(835)	(835)
Total comprehensive loss							$ (544,727)			

	Common Stock		Special Voting Stock							
	Shares	Amount	Shares	Amount	Additional Paid-In Capital	Unearned Compen-sation	Accumulated Deficit	Accumulated Other Compre-hensive Income (Loss)	Compre-hensive Income (Loss)	Total Share-holders' Equity
Balances at December 31, 2001	64,432,052	645	—	—	781,879	(100)	(645,583)	(1,389)	135,452	
Unearned compensation related to non-employee stock options granted	—	—	—	—	18	(18)	—	—	—	
Unearned compensation amortized	—	—	—	—	—	79	—	—	79	
Common shares issued:										
Stock option exercises	541,320	5	—	—	1,145	—	—	—	1,150	
Employee Stock Purchase Plan	290,657	3	—	—	935	—	—	—	938	
Executive Stock Option Exchange and special recognition	18,470	—	—	—	103	—	—	—	103	
Common shares repurchased and retired	(790,865)	(8)	—	—	(2,238)	—	—	—	(2,246)	
Comprehensive income (loss):										
Net loss	—	—	—	—	—	—	(17,919)	—	$ (17,919)	(17,919)
Change in unrealized loss on investments, net of reclassification adjustment	—	—	—	—	—	—	—	220	220	220
Translation adjustment	—	—	—	—	—	—	—	88	88	88
Total comprehensive loss									$ (17,611)	
Balances at December 31, 2002	64,491,634	$ 645	—	$ —	$ 781,842	$ (39)	$ (663,502)	$ (1,081)	$ 117,865	

See notes to consolidated financial statements

ENTRUST, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Year Ended December 31,		
	2000	2001	2002
Operating activities:			
Net loss	$ (82,260)	$(543,672)	$ (17,919)
Non-cash items in loss:			
Depreciation and amortization	67,026	73,431	8,266
Tax equivalent related to non-qualified option exercises	916	—	—
Unearned compensation amortized	224	222	79
Acquired in-process research and development	29,614	—	—
Revenue from non-monetary transaction	(2,988)	(734)	—
Loss from equity investment	—	—	602
Loss on disposition of short-term marketable investments	—	261	220
Provision for doubtful accounts	1,688	8,508	—
Impairment of goodwill, purchase product rights and other purchased intangibles	—	326,953	—
Non-cash other special non-recurring charges	—	3,212	—
Gain on disposition of long-term strategic investments	—	(1,584)	—
Write-down of leaseholds and other long-lived assets	—	13,519	—
Write-down of long-term strategic investments	—	10,800	1,238
Changes in operating assets and liabilities, net of effects of acquisitions:			
Decrease (increase) in accounts receivable	(21,740)	13,642	1,408
Decrease (increase) in other receivables	(1,458)	1,736	670
Decrease (increase) in prepaid expenses	(3,788)	1,395	32
Increase (decrease) in accounts payable	5,879	(2,984)	(2,589)
Increase (decrease) in accrued liabilities	8,283	(7,601)	(4,205)
Increase (decrease) in accrued restructuring charges	—	46,988	(13,822)
Increase (decrease) in deferred revenue	5,777	(1,790)	(1,391)
Decrease due to related party	—	(799)	—
Net cash provided by (used in) operating activities	7,173	(58,497)	(27,411)
Investing activities:			
Purchases of marketable investments	(346,369)	(202,638)	(310,556)
Dispositions of marketable investments	216,062	288,737	328,479
Purchases of property and equipment	(19,717)	(13,629)	(2,050)
Proceeds on disposition of property and equipment	—	264	—
Increase in long-term equity investment	—	—	(957)
(Increase) decrease in long-term strategic investments	(14,922)	(2,308)	63
Proceeds on disposition of long-term strategic investments	—	4,632	—
Increase in other long-term assets	(1,218)	(1,692)	(562)
Net cash payments in purchase transactions	(7,739)	—	—
Net cash provided by (used in) investing activities	(173,903)	73,366	14,417
Repayment of long-term liabilities	(75)	(355)	(265)
Repurchase of common stock	—	—	(2,246)
Proceeds from exercise of stock options and employee stock purchase plan	8,043	6,287	2,191
Proceeds from issuance of common stock, net	161,513	—	—
Net cash provided by (used in) financing activities	169,481	5,932	(320)

	Year Ended December 31,		
	2000	2001	2002
Effect of exchange rate changes on cash	(387)	225	90
Net change in cash and cash equivalents	2,364	21,026	(13,224)
Cash and cash equivalents at beginning of year	21,877	24,241	45,267
Cash and cash equivalents at end of year	$24,241	$45,267	$ 32,043

See notes to consolidated financial statements

1. Company Background

Entrust, Inc. (the "Company") is a leading global provider of software that secures digital identities and information. This software and the associated services enable businesses and governments around the world to securely execute transactions and communicate information over wired and wireless networks, including the Internet. The Company has a broad set of products that provides identification, entitlements, verification, privacy and security management capabilities. Major government agencies, financial institutions and Global 1500 enterprises in more than 40 countries have purchased the Company's portfolio of award-winning security technologies.

The Company was incorporated in December 1996 with nominal share capital, all of which was contributed by Nortel Networks Corporation and its subsidiary Nortel Networks Inc (collectively, "Nortel Networks"). At the close of business on December 31, 1996, Nortel Networks transferred to the Company certain of its assets and liabilities, intellectual property, rights, licenses and contracts. In exchange, Nortel Networks received Series A Common stock, Special Voting stock and cash consideration. At the close of business on December 31, 1996, the Company issued Series B Common stock in a private placement. After the completion of the private placement, Nortel Networks owned approximately 73% of the outstanding shares of the Company's voting stock assuming conversion of the Series B Common stock and Series B Non-Voting Common stock.

On August 21, 1998, the Company closed its initial public offering, issuing 5,400,000 shares of its Common stock at an initial public offering price of $16 per share. The net proceeds to the Company from the offering, after deducting underwriting discounts and commissions and offering expenses incurred by the Company, were approximately $79,100.

On February 29, 2000 and March 2, 2000, the Company closed its follow-on offering, which included an over-allotment option closing, issuing an aggregate of 2,074,260 shares of its Common stock at an offering price of $82 per share. The net proceeds to the Company from the offering, after deducting underwriting discounts and commissions and offering expenses incurred by the Company, were approximately $161,500.

On June 4, 2001, the Company changed its name to Entrust, Inc.

At December 31, 2002, Nortel Networks owned 9,608,259 shares, or approximately 15%, of the Company's Common stock. Nortel Networks owned 8,330,359 shares of the Company's Common stock, or 13% as of March 10, 2003.

2. Significant Accounting Policies

(a) Consolidation

The consolidated financial statements of the Company include the accounts of its wholly-owned subsidiaries, Entrust Limited in Canada, Entrust (Europe) Limited and enCommerce Limited in the U.K., Entrust GmbH in Germany, r^3 Security Engineering AG ("r^3") and Entrust Technologies (Switzerland) GmbH in Switzerland, CygnaCom Solutions, Inc. ("CygnaCom") and enCommerce, Inc. ("enCommerce") in the U.S., Entrust s.a.r.l. in France, Entrust (China) Limited in Hong Kong, and enCommerce K.K. in Japan. During 2002, the Company acquired the outstanding minority interest in its Canadian subsidiary, which had been insignificant. All significant intercompany transactions and accounts are eliminated in consolidation.

(b) Translation of Foreign Currencies

The accounts of the Company's subsidiaries have been translated into U.S. dollars. Assets and liabilities have been translated at the exchange rates in effect at the balance sheet date. Revenues, expenses and cash flow amounts are translated at average rates for the period. The resulting translation adjustments are included in other comprehensive income as a separate component of shareholders' equity. Gains and losses from foreign currency transactions are included in the determination of net income and are not material.

The Company does not use derivative financial products for hedging or speculative purposes related to foreign currency. Therefore, the Company is subject to foreign currency exchange risk in the form of exposures to changes in currency exchange rates between the United States and Canada, the United Kingdom and the European Union. However, the Company transacts the majority of its international sales in U.S. dollars, except for Canada where the Company has both significant costs and revenues, which the Company believes mitigates the potential impact of currency fluctuations. Also, management periodically reviews the potential financial impact of this risk and currently believes that the Company is not subject to significant potential losses.

(c) Revenue Recognition

The Company generates revenues from licensing the rights to its software products to end-users and, to a lesser extent, from sublicense fees from resellers. The Company also generates revenues from consulting, training and post-contract support, or maintenance, performed for customers who license its products. The Company recognizes revenue in accordance with the provisions of the American Institute of Certified Public Accountants' Statement of Position ("SOP") No. 97-2, "Software Revenue Recognition," SOP No. 98-9, "Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions" and related accounting guidance and pronouncements.

Revenues from perpetual software license agreements are recognized as revenue upon receipt of an executed license agreement, or an unconditional order under an existing license agreement, and shipment of the software, if there are no significant remaining vendor obligations, collection of the receivable is probable and payment is due within twelve months. Revenues from license agreements requiring the delivery of significant unspecified software products in the future are accounted for as subscriptions and, accordingly, are recognized ratably over the term of the agreement from the first instance of product delivery. This policy is applicable to all sales transactions, including sales to resellers and end user customers. The Company does not offer a right of return on sales of its software products.

For arrangements involving multiple elements, the Company allocates revenue to each component of the arrangement using the residual value method, based on vendor-specific objective evidence of the fair value of the various elements. These elements may include one or more of the following: software licenses, maintenance and support, consulting services and training. The Company first allocates the arrangement fee, in a multiple-element transaction, to the undelivered elements based on the total fair value of those undelivered elements, as indicated by vendor-specific objective evidence. This portion of the arrangement fee is deferred. Then the difference between the total arrangement fee and the amount deferred for the undelivered elements is recognized as revenue related to the delivered elements. The Company attributes the discount offered in a multiple-element arrangement entirely to the delivered elements of the transaction, which are typically software licenses. Fair values for the future maintenance and support services are based upon separate sales of renewals of maintenance and support contracts. Fair value of future services training or consulting services is based upon separate sales of these services to other customers. In some instances, a group of contracts or agreements with the same customer may be so closely related that they are, in effect, part of a single multiple element arrangement, and therefore, the Company would allocate the corresponding revenues among the various components, as described above.

Revenues from maintenance services are recognized ratably over the term of the maintenance period, which is typically one year. If maintenance services are included free of charge or discounted in a license agreement, such amounts are unbundled from the license fee at their fair market value based upon the value established by independent sales of such maintenance to customers. Revenues from the sale of Web server certificates are also recognized ratably over the term of the certificate, which is typically one to two years.

Consulting and training revenues are generally recognized as the services are performed. Consulting services are typically performed under separate service agreements and are usually performed on a time and materials basis. Such services primarily consist of implementation services related to the installation and deployment of the Company's products and do not include significant customization or development of the underlying software code.

The Company uses the percentage-of-completion method to account for fixed price custom development contracts. Under this method, the Company recognizes revenue and profit as the work on the contract progresses. Revenues are recognized by applying the percentage of the total cost incurred to date divided by the total estimated contract cost to the total contract value, and any projected loss is recognized immediately. The total project cost estimates are reviewed on a regular basis.

(d) Cost of Revenues

Cost of licenses includes the cost of product media, product packaging, documentation, other production costs and third-party royalties.

Cost of services and maintenance consists primarily of salaries, benefits and allocated overhead costs related to consulting, training and customer support personnel, as well as amounts paid to third-party consulting firms for those services.

(e) Research and Development Costs

Research and development costs are expensed as incurred. The Company has defined attainment of technological feasibility as completion of a working model. The period of time beginning with the establishment of a working model and ending when a product is offered for sale is typically very short. Accordingly, costs eligible for capitalization have been insignificant. To date, the Company has not capitalized any internal software development costs and has capitalized, in limited circumstances, costs of software development by third-party contractors.

(f) Cash and Cash Equivalents

The Company considers all highly liquid investments with original maturities of three months or less to be cash equivalents. Cash and cash equivalents are maintained with financial and investment institutions.

(g) Marketable and Other Investments

The Company maintains marketable investments mainly in a strategic cash management account. This account is invested primarily in highly rated corporate securities, in securities guaranteed by the U.S. government or its agencies and highly rated municipal bonds, primarily with a remaining maturity of not more than 12 months. The Company has the intent and ability to hold all of these investments until maturity. Therefore, all such investments are classified as held to maturity investments, and are stated at amortized cost. At December 31, 2001 and 2002, the amortized cost of the Company's held to maturity investments approximated fair value. Based on contractual maturities, these marketable investments were classified in either current assets or long-term assets.

Realized gains and losses on disposition of available for sale marketable investments are included in other investment income in the results of operations. Unrealized gains and losses are included in other comprehensive income, except that the portion designated as being hedged in a fair value hedge is recognized in other investment income during the period of the hedge. As at March 31, 2003, the Company does not hold any available for sale investments.

The Company has a policy that allows for the use of hedges on equity investments in publicly traded companies. At December 31, 2002, the Company was not engaged in any such hedges. In 2000, the Company entered into and designated such a hedge on the investment classified as available for sale, in the form of a call option hedge that enabled the Company to receive, from the investee, a combination of cash and additional in-kind equity securities equal to any deficiency between the original cost basis of the equity securities of $3,400 and the aggregate of the market values on the dates that the securities were made available for sale on the applicable public equity market. This option was accounted for as a fair value hedge in accordance with SFAS No. 133. In 2001, the Company exercised the call option and, as a result, received additional common stock of the investee valued then at $1,700.

Effective January 1, 2001, the Company adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended by SFAS No. 137 and SFAS No. 138, which establishes accounting and reporting standards for derivative financial instruments and hedging activities and requires the recognition of all derivatives as either assets or liabilities on the balance sheet and measurement at fair value. The adoption of SFAS No. 133 did not have a significant impact on the Company's financial position or results of operations because the Company's use of derivatives is limited. In implementing SFAS No. 133, the Company reclassified both the unrealized loss on an investment and the offsetting unrealized gain on a related hedge of $1,457 at January 1, 2001, from accumulated other comprehensive income to results of operations with zero net effect on earnings.

The Company holds equity securities stated at cost, which represent long-term investments in private companies made for business and strategic alliance purposes. The Company's ownership share in these companies ranges from 1% to 10% of the outstanding voting share capital at December 31, 2002. Consistent with the Company's policies for other long-lived assets, the carrying value of these long-term strategic investments is periodically reviewed for impairment based upon such quantitative measures as expected undiscounted cash flows, as well as qualitative factors. In addition, the Audit Committee of the Board of Directors monitors and assesses the ongoing operating performance of the underlying companies for evidence of impairment. In 2001, the Company recorded impairments totaling $10,800 and a realized gain on disposition of $1,584 related to these investments. In 2002, the Company recorded additional impairments totaling $1,238. These strategic investments had a net remaining carrying value of $4,162 and $2,858 at December 31, 2001 and 2002, respectively.

In addition, the Company holds an equity interest in Entrust Japan, which represents approximately 39% of the voting share capital, and is accounted for by the Company using the equity method of accounting for investments in common stock (Note 3).

The Company recorded revenues representing 5%, 1% and 1% of total revenues in 2000, 2001 and 2002, respectively, with respect to arm's-length transactions with companies in which it has made strategic investments recorded at cost. Also, revenues recorded by the Company from Entrust Japan represented 1%, 3% and 3% of total revenues in 2000, 2001 and 2002, respectively. In 2002, the Company had recorded deferred revenue of $385 as a result of the increased investment in Entrust Japan (Note 3) and, to date, $141 of revenue has been recognized related to this balance.

(h) Accounts receivable and other current receivables

The Company's customer base consists primarily of large, well-established companies or government agencies. Five customers accounted for approximately 43% of accounts receivable at each of December 31, 2001 and 2002. One customer accounted for 16% of accounts receivable at December 31, 2001, and a single customer accounted for 10% of accounts receivable at December 31, 2002. Accounts receivable at December 31, 2001 also include an accrued unbilled receivable of $3,700 that was not billed until April 2002. There was no similar accrued unbilled receivable at December 31, 2002. The Company performs ongoing credit evaluations of its customers and, generally, does not require collateral from its customers to support accounts receivable. The Company maintains an allowance for potential losses due to credit risk, and believes that the allowance for losses is adequate. The following table summarizes the changes in the allowance for doubtful accounts:

	December 31		
	2000	2001	2002
Allowance for doubtful accounts, beginning of year	$ 703	$ 2,932	$ 3,909
Additional provision:			
Doubtful accounts	1,688	8,508	—
Arising from acquisitions	1,278	—	—
Amounts written-off, net of recoveries	(737)	(7,531)	(933)
Allowance for doubtful accounts, end of year	$ 2,932	$ 3,909	$ 2,976

Other current receivables include federal income tax and other tax refunds of $758 and $616 at December 31, 2001 and 2002, respectively, and work-in-process relating to time-and-materials services contracts of $490 at December 31, 2001. There was no balance of work-in-process at December 31, 2002. Other current receivables also include a sub-tenant lease receivable for recoverable operating costs of $301 at December 31, 2002.

(i) Property and equipment

Property and equipment is stated at cost. Depreciation is calculated generally using the straight-line method over the estimated useful lives of the assets. The expected useful lives of the furniture and fixtures, computer and telecom equipment and software is three to five years and the remaining term of the facility lease for leasehold improvements.

Recoverability of property, equipment and other long-lived assets is periodically reviewed for impairment on the basis of undiscounted cash flows. If the expected cash flows are less than the asset's carrying value, the asset is written down to its fair value.

(j) Goodwill, purchased product rights and other purchased intangibles

Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142"), which revises the accounting for purchased goodwill and intangible assets, became effective for the Company beginning January 1, 2002. Under SFAS No. 142, goodwill and other purchased intangible assets, with balances of $6,436 and $4,750, respectively, at December 31, 2002, with indefinite lives are no longer amortized, but are tested for impairment annually and also in the event of an impairment indicator.

The Company assessed the carrying value of its goodwill and other intangible assets in the first quarter of 2002 to complete its transitional impairment test and determine the effects, if any, of adopting SFAS No. 142. No further impairment (beyond the $326,953 recognized in 2001) was required as a result of that assessment. In addition, no further impairment was required as a result of the annual impairment test under SFAS No. 142 as of December 31, 2002.

The Company's net loss, on a pro forma basis, assuming that the cessation of amortization of goodwill and other purchased intangibles as required under SFAS No. 142 had been in effect from January 1, 2000, is as follows:

	Year Ended December 31,		
	2000	2001	2002
Reported net loss	$(82,260)	$(543,672)	$(17,919)
SFAS No. 142 adjustment	59,952	62,142	—
Pro forma net loss	$(22,308)	$(481,530)	$(17,919)
Pro forma net loss per share—basic and diluted	$ (0.39)	$ (7.59)	$ (0.28)

Purchased product rights are amortized using the straight-line method over their estimated useful lives of four years. These assets are reviewed for impairment whenever events indicate that their carrying amount may not be recoverable. In such reviews, the related undiscounted cash flows expected are compared with their carrying values to determine if a write-down to fair value is required.

(k) Other Long-Term Assets

Other long-term assets consist primarily of licenses of technology, used by the Company to provide services, and capitalized localization costs. These costs of $1,142 and $1,067 are amortized on a straight-line basis over three to four years and are stated net of accumulated amortization of $499 and $486 at December 31, 2001 and 2002, respectively. Other long-term assets also include long-term rent deposits of $279 and $430 at December 31, 2001 and 2002, respectively.

(l) Advertising Expense

Advertising costs are charged to expense as incurred and totaled $3,282, $7,101 and $3,129 in 2000, 2001 and 2002, respectively. These amounts include expenses of $1,311 in 2001 and recoveries of $351 in 2002, relating to special non-recurring charges and adjustments.

(m) Income Taxes

The Company uses the asset and liability method to account for income taxes. Deferred income tax assets and liabilities are recognized for the future tax consequences attributable to differences between the carrying amounts of existing assets and liabilities for accounting purposes, and their respective tax bases. Deferred income tax assets and liabilities are measured using statutory tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred income tax assets and liabilities of a change in statutory tax rates is recognized in net income in the year of change. A valuation allowance is recorded for those deferred income tax assets whose recoverability is not sufficiently likely.

(n) Stock-Based Compensation

Stock-based compensation arising from stock option grants is accounted for by the intrinsic value method under Accounting Principles Board (“APB”) Opinion No. 25, “Accounting for Stock Issued to Employees”. SFAS No. 123, “Accounting for Stock-Based Compensation” encourages, but does not require, the cost of stock-based compensation arrangements with employees to be measured based on the fair value of the equity instrument awarded. As permitted by SFAS No. 123, the Company applies APB Opinion No. 25 and related interpretations in accounting for stock-based compensation awards to employees under its stock option plans. Accordingly, compensation expense was recognized for its stock-based compensation plans in 1998 because the exercise price of some options granted in that period were determined, for accounting purposes, to be below the fair value of the underlying stock as of the grant date for such stock options. In connection with the granting of these options, the Company recorded unearned compensation of $784 for 1998. This amount is being amortized over the vesting period of four years from the date of grant, with $196, $196 and $49 amortized into compensation expense for 2000, 2001 and 2002. For all other options granted to employees in the periods disclosed, the exercise price of each option granted was equal to the fair value of the underlying stock at the date of grant and therefore, no stock-based compensation costs are reflected in earnings for these options. Had compensation costs for the Company’s 1996 Plan, 1999 Plan, Special Plan and enCommerce 1997 Plans been determined based on the fair value of the options at the grant date for awards to employees under these plans, consistent with the methodology prescribed under SFAS No. 123, the Company’s net loss and net loss per share would have been as follows, on a pro forma basis.

	Year Ended December 31,		
	2000	2001	2002
Net loss, as reported	$ (82,260)	$(543,672)	$(17,919)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related effects	(95,200)	(49,141)	(24,463)
Pro forma net loss	$(177,460)	$(592,813)	$(42,382)
Net loss per share:			
Basic—as reported	$ (1.44)	$ (8.57)	$ (0.28)
Basic—pro forma	$ (3.11)	$ (9.35)	$ (0.65)
Diluted—as reported	$ (1.44)	$ (8.57)	$ (0.28)
Diluted—pro forma	$ (3.11)	$ (9.35)	$ (0.65)

In the pro forma calculations above, the weighted average fair value for stock options granted during 2000, 2001 and 2002 was estimated at $34.43, $8.09 and $4.55 per option, respectively. The fair values of options were estimated as of the date of grant using the Black-Scholes option pricing model. The following weighted average assumptions were used in the calculations.

	Year Ended December 31,		
	2000	2001	2002
Expected option life, in years	5	5	5
Risk free interest rate	6.11%	4.79%	4.14%
Dividend yield	—	—	—
Volatility	127%	119%	116%

On April 22, 2001, the Company issued a warrant to purchase 258,333 shares of the Company's Common stock, with an exercise price of $6.87 per share and expiration date of April 22, 2004, to a consultant of the Company. In addition, the Company granted non-employee options to purchase 9,500 shares of Common stock to a consultant for services rendered in 2001, with an exercise price of $8.20 and term of ten years. The fair value of these options and warrants, granted to consultants of the Company, of $1,092 was recorded as an expense in 2001, when they vested. Also, in 2000, 2001 and 2002 the Company granted non-employee options to members of an advisory committee, to purchase 3,000, 1,500 and 5,000 shares of Common stock, respectively, at exercise prices of $44.00, $4.60 and $4.03 per share with a term of 10 years. The Company recorded unearned compensation of $102, $6, and $18 in 2000, 2001 and 2002, respectively, for these non-employees options, which is being amortized over the vesting period of four years from the date of grant. Accordingly, $28, $25 and $30 was amortized into compensation expense for 2000, 2001 and 2002, respectively.

(o) Net Income (Loss) Per Share

Basic net income (loss) per share is computed by dividing the net income (loss) by the weighted average number of shares of Common stock of all classes outstanding during the period. Diluted net income (loss) per share is computed by dividing the net income (loss) by the weighted average number of shares of Common stock and when dilutive, potential Common stock outstanding from exchangeable Special Voting stock on an as-if exchanged basis, and options to purchase Common stock using the treasury stock method. The exchangeable Special Voting stock and the options to purchase Common stock are excluded from the computation of diluted net income (loss) per share if their effect is antidilutive.

(p) Financial Instruments and Concentration of Credit Risk

The carrying amounts of cash and cash equivalents, accounts receivable and accounts payable approximate fair value due to the short-term nature of these instruments. Marketable investments consist of publicly traded debt and equity securities. The amortized cost basis of publicly traded debt securities classified as held to maturity approximates fair value due to the nature of these instruments, which generally have short-term maturities. Marketable investments classified as available for sale are recorded at market value based on specific identification.

Financial instruments that potentially subject the Company to interest rate and credit risk consist principally of cash equivalents, marketable investments and accounts receivable. The Company has investment policies that limit the amount of credit exposure to any one issuer and restrict placement of these investments to issuers evaluated as credit worthy. The Company maintains its cash equivalents and marketable investments with high quality financial institutions and investment managers. The Company performs periodic reviews of the credit standing of its investments and the financial institutions managing those investments.

(q) Recent Accounting Pronouncements

In June 2002, the Financial Accounting Standards Board ("FASB") approved for issuance SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities". SFAS No. 146 requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. This statement is effective for fiscal years beginning after December 31, 2002. The Company does not expect the adoption of SFAS No. 146 to have a material effect on the Company's financial position or results of operations.

In December 2002, the FASB issued SFAS No. 148, "Accounting for Stock-Based Compensation—Transition and Disclosure". SFAS No. 148 amends SFAS No. 123, to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No.

148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The transition guidance and annual disclosure provisions of SFAS No. 148 are effective for fiscal years ending after December 15, 2002. The interim disclosure provisions are effective for financial reports containing financial statements for interim periods beginning after December 15, 2002. As the Company did not make a voluntary change to the fair value based method of accounting for stock-based employee compensation in 2002, the adoption of SFAS No. 148 did not have a material impact on the Company's financial position and results of operations.

In July 2000, the Emerging Issues Task Force issued EITF No. 00-21, "Revenue Arrangements with Multiple Deliverables", with various subsequent discussions by the Task Force, most recently in March 2003. This Issue addresses certain aspects of the accounting by a vendor for arrangements under which it will perform multiple revenue-generating activities. Specifically, it addresses how to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting. In applying this Issue, separate contracts with the same entity or related parties that are entered into at or near the same time are presumed to have been negotiated as a package and should, therefore, be evaluated as a single arrangement in considering whether there are one or more units of accounting, unless there is sufficient evidence to the contrary to overcome this presumption. This Issue also addresses how arrangement consideration should be measured and allocated to the separate units of accounting in the arrangement. The guidance is effective for revenue arrangements entered into in fiscal periods beginning after June 15, 2003. Alternatively, entities may elect to report the change in accounting as a cumulative effect adjustment. If so elected, disclosure should be made in periods subsequent to the date of initial application of this consensus of the amount of recognized revenue that was previously included in the cumulative effect adjustment. The Company does not intend to report a cumulative effect adjustment and does not expect the adoption of this guidance to have a material impact on its consolidated financial position or results of operations.

(r) Use of Estimates

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

(s) Reclassifications

Certain reclassifications have been made to prior years' balances in order to conform to fiscal 2002 presentation.

3. Equity Investment in Entrust Japan Co., Ltd. ("Entrust Japan")

On April 12, 2002, the Company increased its investment in the voting capital of Entrust Japan from an ownership share of less than 10% to approximately 39% by converting a previous cash advance of $524, and by exchanging cash of approximately $957, Entrust software product valued at $385 and distribution rights for certain Entrust products for the Japanese market, for additional shares in Entrust Japan. The Company's increased investment follows additional investments made by Toyota and SECOM in the fourth quarter of 2001. The Company has concluded that because of the additional investment, as of the second quarter of 2002, it has the potential ability to exercise significant influence over the operations of Entrust Japan. Therefore, beginning in the same period of 2002, it has accounted for its investment in Entrust Japan under the equity method, in accordance with the provisions of APB No. 18, "The Equity Method of Accounting for Investments in Common Stock" and ARB No. 51, "Consolidated Financial Statements". Accordingly, as required by this accounting guidance, the Company has included its share of post-acquisition losses of Entrust Japan, in the amount of $602, on the step-by-step acquisition method in its consolidated losses for the year ended December 31, 2002. In addition, the Company has made a retroactive adjustment to consolidated accumulated deficit to record its share of the post-acquisition losses of Entrust Japan of prior years, attributable to the less than 10% ownership prior to the increased investment, to the extent of the Company's previous investment of $393. The balance sheet at December 31, 2001 has been restated to reflect this retroactive adjustment. Prior year's comparative results have not been impacted due to the fact that this retroactive adjustment would only affect the results of periods prior to those shown here.

4. Restructuring and Other Special Non-Recurring Charges

On June 4, 2001, the Company announced a Board-approved restructuring program to refocus on the Company’s most significant market opportunities and to reduce operating costs due to the macroeconomic factors that were negatively affecting technology investment in the market. The restructuring program included a workforce reduction, consolidation of excess facilities, and discontinuance of non-core products and programs.

The workforce portion of the restructuring was largely completed by the end of the fourth quarter of 2001 and primarily related to severance costs, fringe benefits due to severed employees and outplacement services.

The consolidation of excess facilities included the closure of eight offices throughout the world, but the majority of the costs related to the Company’s facility in Santa Clara, California. These costs are payable contractually over the remaining term of the Santa Clara facility lease, which runs through to 2011, reduced by estimated sublease recoveries. The Company continues to evaluate ongoing possibilities to settle this obligation in the most cost-effective manner and, therefore, it has been classified as current in nature. The discontinuance of non-core products and programs was primarily related to the discontinuance of certain of the Company’s business program initiatives and certain applications that had not achieved their growth and profitability objectives. In addition, the Company withdrew from certain committed marketing events and programs. The cash outflow related to the majority of these discontinued products and programs was substantially completed by the end of the second quarter of 2002, while estimated remaining marketing and distribution agreement obligations related to certain discontinued products of $2,750 are payable contractually through 2004. An adjustment to decrease the accrual for restructuring charges and to credit operations under “Restructuring charges and adjustments” of $1,079 was made during the second quarter of 2002 to reflect savings realized as a result of the successful completion of certain contractual obligations in a cost-effective manner. In addition, an adjustment of $251 was made in the same quarter to reduce other accruals for related special non-recurring charges and credit operating expenses to reflect savings realized. As of June 2002, the Company had initiated all actions required by the restructuring plan.

(a) Summary of Accrued Restructuring Charges

The following table is a summary of the accrued restructuring charges as at December 31, 2001 and 2002, including adjustments made during the second quarter of 2002 (table in millions):

	December 31, 2002			
	Accrued Restructuring Charges at Beginning of Year	Cash Payments	Adjustments	Accrued Restructuring Charges at End of Year
Workforce reduction and other personnel costs	$ 2.3	$ 2.3	$ 0.1	$ 0.1
Consolidation of excess facilities	34.6	4.6	(0.1)	29.9
Discontinuance of non-core products and programs	10.1	5.8	(1.1)	3.2
Total	$ 47.0	$ 12.7	$ (1.1)	$ 33.2

	December 31, 2001			
	Accrued Restructuring Charges at June 30, 2001	Cash Payments	Adjustments	Accrued Restructuring Charges at End of Year
Workforce reduction and other personnel costs	$ 13.5	$ 11.1	$ (0.1)	$ 2.3
Consolidation of excess facilities	38.2	4.6	1.0	34.6
Discontinuance of non-core products and programs	13.8	2.8	(0.9)	10.1
Total	$ 65.5	$ 18.5	$ —	$ 47.0

As at December 31, 2002, the Company estimated a total of $33.2 million of estimated sublease recoveries in our restructuring accrual. Of this amount, $32.4 million is related to the Santa Clara facility. In addition, $12.1 million of the $33.2 million is recoverable under existing sublease agreements and the remaining $21.1 million of rent recoveries is based on estimates that may be subject to adjustments based upon changes in the real estate sublet markets.

(b) Summary of Charges in 2001

As a result of the restructuring program in 2001 and the impact of the macroeconomic conditions on the Company and its global base of customers, the Company recognized restructuring and special non-recurring charges totaling of $433,600 in the second fiscal quarter of 2001, with subsequent adjustments in the third and fourth quarter of 2001 of $1,400, as outlined below (table in millions):

	Accrued Restructuring Charges	Other Special Non-recurring Charges	Total Special Charges through June 30, 2001	Adjustments Recorded July 1, 2001 to Dec. 31, 2001	Total Special Charges through Dec. 31, 2001
Workforce reduction and other personnel costs	$ 13.5	$ 4.1	$ 17.6	$ 0.3	$ 17.9
Consolidation of excess facilities	38.2	13.5	51.7	0.5	52.2
Discontinuance of non-core products and programs	13.8	6.4	20.2	(0.8)	19.4
Impairment of goodwill, purchased product rights and other purchased intangible assets	—	327.0	327.0	—	327.0
Write-down of long-term strategic investments	—	6.1	6.1	4.7	10.8
Bad debt write-offs and additional provisions to the allowance for doubtful accounts	—	11.0	11.0	(3.3)	7.7
Total	$ 65.5	$ 368.1	$433.6	$ 1.4	$435.0

The following paragraphs provide information relating to the restructuring programs that resulted in the total special charges listed above, which were recognized in 2001.

(c) Workforce Reduction and Other Personnel Costs

The restructuring program resulted in the reduction of approximately 400 regular full-time employees across the Company, or 33% of the total workforce. The reduction was across all major geographic locations, all business programs, and all functions within the organization. The reductions were more heavily weighted in sales and marketing, non-core business programs such as Entrust.Net ™ and Entrust@YourService ™ and secondary geographies such as Asia Pacific and Latin America. The majority of the affected employees were notified of their termination in the second quarter, and the workforce portion of the restructuring was largely completed by the end of the fourth quarter of 2001. The Company recorded a workforce reduction charge of $13,400 primarily related to severance costs, fringe benefits due to severed employees and outplacement services.

Other special non-recurring charges included employee relocation expenses, hiring fees and signing bonuses totaling $4,500, which were recorded primarily in general and administrative expenses.

(d) Consolidation of Excess Facilities

The Company recorded restructuring costs of $39,200 relating to the consolidation of excess facilities. The consolidation of excess facilities includes a total of eight offices in seven cities throughout the world. The majority (approximately 85%) of the costs are related to the 75,000 square foot facility in Santa Clara, CA. The costs for consolidation of excess facilities are related primarily to non-cancelable lease costs offset by estimated sublet recoveries. These costs are payable contractually over up to 10 years, which is the lease term of the Santa Clara facility. However, the Company will be evaluating ongoing possibilities to settle this obligation in the most economic manner. Therefore, it has been classified as current in nature.

In addition to the $39,200 of restructuring costs related to excess facilities, an additional $13,000 of facilities-related costs were recorded as a special non-recurring charge as a result of impairment of leasehold improvements and other property and equipment that was disposed of or removed from operations as a result of the consolidation of excess facilities, and were included in the write-down of leaseholds and other long-lived assets in accordance with the provisions of SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of". These assets were identified as assets to be disposed of that would have no future benefit to the Company. Therefore, these assets were reported at the lower of carrying amount and fair value, less costs of disposition. The majority of these costs are non-cash charges.

(e) Discontinuance of Non-Core Products and Programs

In support of the restructuring objective to reduce costs and focus the Company on core technologies, the Company discontinued several non-core products and programs. The discontinued products and programs, totaling $12,900, are primarily related to the Company's services business initiatives and to certain desktop applications for which the Company has not achieved the growth and profitability targets in line with its core products and financial objectives. The restructuring charge also includes costs related to the exit of certain marketing events and programs that had been committed to prior to the restructuring, but which are being cancelled due to the change in corporate focus. The cash outflow related to the majority of these items is expected to be substantially incurred by the end of the first quarter of fiscal 2002. Accrued estimated minimum royalty obligations related to certain discontinued products of $4,200 are payable contractually through 2004.

The discontinuance of products and programs, and expenses related to rebranding of the Company and its products, resulted in $6,500 of special non-recurring charges, which was primarily recorded in sales and marketing expenses.

(f) Impairment of Goodwill, Purchased Product Rights and Other Intangible Purchased Assets

Due to the decline in the Company's market capitalization, the decline in current overall business conditions within its target market segments and the restructuring program, the Company completed an assessment of the recoverability of goodwill on its balance sheet, in accordance with APB Opinion No. 17 and the relevant guidance in SFAS No. 121. This impairment analysis indicated that the carrying amount of the goodwill, purchased product rights and other purchased intangible assets of the enCommerce and r^3 acquisitions will not be recovered through the estimated undiscounted future cash flows. The Company then completed an analysis of the discounted future cash flows from the enCommerce acquisition and the r^3 acquisition. The result of this analysis is a charge of $327,000 related to the impairment of goodwill, purchased product rights and other purchased intangible assets. Goodwill, purchased product rights and other purchased intangibles from the enCommerce acquisition account for $325,400 of the impairment. This acquisition failed to meet the financial planning forecasts made at the time of the acquisition due largely to the change in the economic conditions since the time of the acquisition and in part due to additional product development and maintenance costs related to the GetAccess ™ product that are now estimated to be required in the future and were not known at the time of the acquisition. The remaining $1,600 of goodwill impairment is the result of the r^3 acquisition, which was impacted primarily by the workforce restructuring.

Revenues from the enCommerce products and services are estimated to have contributed approximately 20% to 25% of total revenues of the Company in 2001, but are estimated to have generated operating losses since acquisition. The results of operations related to the r^3 acquisition were not significant.

(g) Write-Down of Long-Term Strategic Investments

The Company assesses the recoverability of the carrying value of its strategic investments on a regular basis. Factors that the Company considers important that could trigger impairment include, but are not limited to, the likelihood that the company in which the Company invested would have insufficient cash flows to operate for the next twelve months, significant changes in such company's operating performance or business model, and changes in overall market conditions. The Company recorded charges related to other than temporary declines in the value of certain strategic investments of $10,800 in 2001. The Company also recorded a gain on the disposition of a long-term strategic investment of $1,584 in 2001.

(h) Bad Debt Write-Offs and Additional Provisions to the Allowance for Doubtful Accounts

Due to the changes in the economic environment and the impact of the restructuring program, particularly the curtailment of certain products and presence in certain geographies, the Company recorded bad debt write-offs and additional provisions to the allowance for doubtful accounts totaling $7,700 in the year ended December 31, 2001, which was recorded primarily in sales and marketing expenses.

5. Acquisitions and Related Intangible Assets

In June 2001, the Financial Accounting Standards Board ("FASB") approved for issuance Statement of Financial Accounting Standards No. 142 ("SFAS No. 142"), "Goodwill and Intangible Assets", which revised the accounting for purchased goodwill and intangible assets. Under SFAS No. 142, goodwill and intangible assets with indefinite lives will no longer be amortized, but will be tested for impairment annually and also in the event of an impairment indicator. We adopted SFAS No. 142 as of January 1, 2002. This adoption has affected the amortization of intangibles attributable to the past acquisitions discussed in the following paragraphs.

On June 26, 2000, the Company completed the acquisition of all of the outstanding capital stock, options and warrants of enCommerce, a global portal infrastructure company, based in Santa Clara, California, that provides software and services designed to manage electronic business relationships, in exchange for an aggregate of 8,548,177 shares of the Company's Common stock and options and warrants to purchase 1,701,823 shares of Common stock, with an aggregate fair value of $482,272. The Company also incurred approximately $23,246 in acquisition-related costs. The enCommerce acquisition was accounted for under the purchase method of accounting and, accordingly, the purchase price of approximately $505,518 was allocated to the fair value of the tangible and intangible assets and liabilities acquired, with the remaining $449,640 allocated to purchased product rights, goodwill and other purchased intangibles. Also, in connection with this acquisition, an appraisal was done of the intangible assets, resulting in $29,614 of the purchase price being allocated to in-process research and development that had not yet reached technological feasibility and had no alternative future use. This in-process research and development was expensed in June 2000. Amortization of $54,445 and $56,151 was recorded in 2000 and 2001, respectively, related to goodwill and other purchased intangible assets arising from this acquisition. No amortization of these assets has been recorded in 2002, due to the adoption of SFAS No. 142. The Company also recorded amortization expense of $2,751, $3,322 and $1,136 for purchased products rights in 2000, 2001 and 2002, respectively. In addition, the Company recorded an impairment of $325,379 related to the goodwill, purchased product rights and other purchased intangibles from this acquisition in 2001.

On March 14, 2000, the Company completed the acquisition of all of the outstanding stock of CygnaCom, a Virginia corporation, that delivers information technology products and services, with expertise in public key infrastructure, cryptographic technologies, security engineering and systems integration and development. All of the outstanding common shares of CygnaCom were exchanged, in the aggregate, for a purchase price of $16,000 in cash and $555 in assumed net liabilities and acquisition expenses. The acquisition was accounted for under the purchase method of accounting and, accordingly, the purchase price was allocated to the fair value of the assets and liabilities acquired, with the remainder allocated to goodwill. Goodwill of $16,555 was recorded as a result of this acquisition and, accordingly, $4,600 and $5,520 of goodwill amortization has been recorded in 2000 and 2001, respectively. No goodwill amortization was in 2002, due to the adoption of SFAS No. 142.

The results of operations of the businesses acquired in 2000 have been included in the Company's financial statements commencing from the respective effective acquisition dates for accounting purposes. The following unaudited pro forma data summarize the combined results of operations of Entrust, CygnaCom and enCommerce for the year ended December 31, 2000, as if the acquisitions had taken place as of the beginning of that period and, accordingly, excludes the $29,614 write-off of in-process research and development, a non-recurring charge directly attributable to the acquisition of enCommerce and includes a full period's amortization of goodwill and other purchased intangibles. Also, the per share data includes the Common shares of the Company issued in connection with the acquisition of enCommerce, but excludes options and warrants issued as their effect is antidilutive.

	Pro Forma Year Ended December 31, 2000
Revenues	$ 159,975
Net loss	$ (124,596)
Net loss per basic and diluted share	$ (2.03)

In addition, on June 8, 1998, the Company acquired r^3, a company based in Zurich, Switzerland, which was accounted for under the purchase method of accounting. The Company recorded goodwill of $4,016 as a result of this acquisition and, accordingly, has recorded $907 and $470 of amortization with respect to the goodwill in 2000 and 2001, respectively. In addition, the Company recorded an impairment of $1,574 to the goodwill related to this acquisition in 2001. No amortization of this asset has been recorded in 2002, as the goodwill was fully impaired in 2001.

The primary components of acquisition-related intangible assets, including goodwill and purchased product rights, are as follows:

	December 31, 2001	December 31, 2002
Goodwill	$ 365,127	$ 6,436
Less: accumulated amortization	(56,144)	—
Less: impairment of carrying value	(302,547)	—
Reclassification from other purchased intangibles	—	4,750
Goodwill, net	6,436	11,186
Other purchased intangibles	22,054	4,750
Less: accumulated amortization	(5,994)	—
Less: impairment of carrying value	(11,310)	—
Reclassification to goodwill	—	(4,750)
Other purchased intangibles, net	4,750	—
Total goodwill and other purchased intangibles, net	$ 11,186	$ 11,186
Purchased product rights	$ 19,259	$ 2,838
Less: accumulated amortization	(3,325)	(1,136)
Less: impairment of carrying value	(13,096)	—
Purchased product rights, net	$ 2,838	$ 1,702

In adopting SFAS No. 141 and 142, the Company evaluated the classification of the other purchased intangibles of $4,750, which related primarily to non-contractual customer relationships from the enCommerce acquisition. The Company concluded these intangibles do not meet the new criteria in SFAS No. 141 for separate recognition and, therefore, reclassified them as goodwill in 2002.

6. Investments

The Company's investments consist of the following:

	December 31,	
	2001	2002
Short-term marketable investments:		
Held to maturity, at amortized cost:		
U.S. government agency debt securities	$ 13,073	$ 7,889
Corporate debt securities	93,715	78,091
	106,788	85,980
Available for sale equity securities, at cost	1,720	—
Unrealized loss	(220)	—
At market	1,500	—
Total	$108,288	$85,980
Long-term investments:		
Marketable, held to maturity, at amortized cost:		
U.S. government agency debt securities	$ 2,776	$ —
Corporate debt securities	6,262	13,423
Total long-term marketable	$ 9,038	$13,423
Strategic:		
Other equity securities, at cost	$ 4,159	$ 2,858
Advances to strategic equity investee, at cost	524	—
Total long-term strategic	$ 4,683	$ 2,858
Equity:		
Entrust Japan Co., Ltd., equity basis	$ —	$ 1,264

As of December 31, 2001, the Company had recorded an aggregate unrealized loss, included in other comprehensive income, on the remaining balance of marketable equity securities, classified as available for sale, in the amount of $220, in order to adjust this investment to market value. This unrealized loss was reversed in other comprehensive income in 2002, upon the sale of the balance of the underlying securities at a realized loss of $220.

7. Property and Equipment

Property and equipment, at cost, consist of the following:

	December 31,	
	2001	2002
Computer and telecom equipment	$ 9,535	$ 10,708
Furniture and fixtures	3,898	4,308
Leasehold improvements	8,760	9,431
Internal-use software	4,394	4,811
Equipment under capital lease	92	—
	26,679	29,258
Less: accumulated depreciation and amortization	(9,819)	(16,463)
Subtotal	16,860	12,795
Assts to be placed in service	530	—
Total property and equipment, net	$17,390	$ 12,795

8. Accrued Liabilities

Accrued liabilities consist of the following:

	December 31,	
	2001	2002
Payroll and related benefits	$ 9,383	$ 8,037
Other	5,738	2,503
	$15,121	$10,540

9. Income Taxes

The following table presents the U.S. and foreign components of income (loss) before income taxes and the provision for income taxes.

	December 31,		
	2000	2001	2002
Income (loss) before income taxes:			
United States	$(85,876)	$(519,062)	$ (9,665)
Foreign	5,953	(22,782)	(6,904)
	$(79,923)	$(541,844)	$(16,569)
Provision for income taxes			
Current:	$ —	$ —	$ —
Federal	—	(147)	(129)
State and local	(1,421)	(1,681)	(1,221)
Foreign			
	(1,421)	(1,828)	(1,350)
Deferred	—	—	—
Federal and State tax equivalent related to non-qualified option exercises (credited to additional paid-in capital)	(916)	—	—
Total provision for income taxes	$ (2,337)	$ (1,828)	$ (1,350)

A reconciliation between income taxes computed at the federal statutory rate and income tax provision is shown below:

	December 31,		
	2000	2001	2002
Income tax provision at federal statutory rate	$ 27,174	$ 184,227	$ 5,633
State and local taxes, net of federal benefits	(65)	5,599	(200)
Foreign earnings benefit (tax) at different rate	(38)	1,975	161
Acquired in-process research and development	(10,069)	—	—
Amortization and impairment of goodwill, purchased product rights and other purchased intangibles	(19,755)	(131,546)	(386)
Foreign research and development tax credits	2,065	1,719	1,390
Tax write-offs of intercompany investment in, advances to and operations of foreign subsidiary	2,602	—	—
Other	(2,222)	1,246	(4,540)
Valuation allowances on future benefits of tax losses and credits available	(2,029)	(65,048)	(3,408)
Total provision for income taxes	$ (2,337)	$ (1,828)	$(1,350)

Deferred income taxes represent the net tax effects of (a) temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes, and (b) net operating loss (NOL) and tax credit carry-forwards. The tax effects of significant items comprising the Company's net deferred tax benefits (liabilities) are as follows:

	December 31,	
	2001	2002
Current asset (liability)		
Accrued restructuring charges not currently deductible	$ 17,855	$ 19,344
Other allowances and accruals not currently deductible	1,300	1,478
Deferred income currently taxable	183	(415)
Total	19,338	20,407
Non-current asset:		
Deferred depreciation and amortization for tax purposes	4,864	5,014
Write-downs of long-lived assets and strategic investments not currently deductible	9,242	4,823
United States and Foreign NOL and tax credit carry-forwards	76,182	83,967
Total	90,288	93,804
Total deferred tax asset	109,626	114,211
Valuation allowance	(109,626)	(114,211)
Net deferred tax asset	$ —	$ —

United States and foreign NOL and tax credit carry-forwards include $13,808 and $14,984 at December 31, 2001 and December 31, 2002, respectively, related to NOL carry-forwards resulting from the exercise in 2001 and 2002 of non-qualified stock options with a corresponding amount included in the valuation allowance, the tax benefit of which, when recognized, will be credited to additional paid-in capital. In addition, United States and foreign NOL and tax credit carry-forwards include NOL carry-forwards of approximately $12,937 from enCommerce at the date of acquisition, with a corresponding amount included in the valuation allowance, the tax benefit of which, when recognized, will be first credited to the applicable goodwill and other intangibles arising from the acquisition and then to income tax expense. The annual utilization of acquired NOL and tax credit carry-forwards may be limited by certain historical ownership changes at enCommerce.

As at December 31, 2002, the Company has available the following income tax carry-forwards to reduce future income tax liabilities:

	Amount	Period Expiring
Net operating losses (tax benefits)		
United States	$58,435	2012-2022
Foreign	16,839	2005-2009
	75,274	
United States research and development tax credits	903	2016-2019
Foreign research and development tax credits	7,790	2007-2012
	$83,967	

10. Long-Term Liabilities

Long-term liabilities includes notes payable of $266 and $44 at December 31, 2001 and 2002, respectively, and capital lease obligations of $65 at December 31, 2001, assumed as a result of the acquisition of enCommerce in 2000. These notes were entered into by enCommerce to finance the purchase of fixed assets, and will be retired by January 2003. The current portions of the notes and lease obligations, of $256 and $44 at December 31, 2001 and 2002, respectively, have been included in accrued liabilities. These long-term liabilities bear interest at rates ranging from 8% to 14% and are collateralized by the financed assets.

The remaining balance of long-term liabilities consists primary of long-term deposits received through the sub-leasing of various U.S. facility locations.

11. Capital Stock

Concurrent with the closing of the follow-on offering on February 29, 2000 and March 2, 2000, the remaining 5,157,289 shares of Special Voting stock and Exchangeable shares were exchanged into an equivalent number of shares of Common stock.

On January 26, 2001, the Company's Board of Directors adopted, and recommended to the stockholders to approve, articles of amendment to the Company's charter to (i) increase the total number of authorized shares of Common stock, $0.01 par value per share, from 100,000,000 shares to 250,000,000 shares and (ii) eliminate the Special Voting stock from the Company's authorized capital and delete all references to Special Voting stock contained in the Company's charter. The stockholders adopted this proposal at their annual meeting on April 27, 2001.

(a) Common Stock

The holders of Common stock are entitled to one vote per share and are entitled to dividends when and if declared by the Board of Directors of the Company. The Company is authorized to issue up to 250,000,000 shares of Common stock.

(b) Preferred Stock

The Company is authorized to issue up to 5,000,000 shares of Preferred stock in one or more series. Each such series of Preferred stock would have such rights, preferences, privileges and restrictions, including voting rights, dividend rights, conversion rights and liquidation preferences, as determined by the Board of Directors. As of December 31, 2002, the Company had not issued any shares of Preferred stock.

(c) Stock Repurchase Program

On July 29, 2002, the Company announced that its board of directors had authorized the Company to repurchase up to an aggregate of 7,000,000 shares of its Common stock. As of December 31, 2002, the Company has repurchased 785,000 shares of its Common stock under this program, for a total cash outlay of $2,246, at an average price of $2.83 per share. This price does not include the commission paid to brokers by the Company, which averaged $0.03 per share for a gross purchase price of $2.86 per share.

Repurchases under the stock repurchase program may take place from time to time until July 28, 2003, or an earlier date determined by the Company's board of directors, in open market, negotiated and block transactions, and may be suspended or discontinued at any time. The timing and amount of shares repurchased will be determined by the Company's management based on its evaluation of market and business conditions. The repurchases of stock will be transacted during the insider trading window, which runs from the third day following the public release of the Company's quarterly results to the last day of the second month of each fiscal quarter. The repurchased shares will be considered authorized but unissued shares of the Company and will be available for issuance under the Company's stock incentive, employee stock purchase and other stock benefit plans, and for general corporate purposes, including possible acquisitions. The stock repurchase program will be funded using the Company's working capital.

12. Stock Options and Warrants

(a) Stock Option Plans

In 2000, the Company's Board of Directors increased the number of authorized shares under the 1999 Non-Officer Employee Stock Incentive Plan (the "1999 Plan") to 7,600,000 shares. Also in 2000, the Company's Board of Directors approved an increase to 14,600,000 as the total number of authorized shares available for issuance under the 1996 Stock Incentive Plan (the "1996 Plan") applicable to the Company's full-time employees, officers, directors and consultants, plus an annual increase to be added on each of January 1, 2001 and January 1, 2002, equal to the lower of (i) 5% of the total number of outstanding shares of Common stock on such date or (ii) a lesser amount determined by the Board; provided, however, that the maximum number of shares of Common stock available for issuance under the 1996 Plan is 26,000,000 shares. In addition, concurrent with the acquisition of enCommerce, the Company's Board of Directors approved the assumption of all outstanding options under the enCommerce 1997 Stock Option Plan and the enCommerce 1997B Stock Option Plan (collectively, the "enCommerce 1997 Plans"), and all outstanding warrants of enCommerce, and authorized an aggregate of 1,701,823 shares for issuance upon the exercise of such options and warrants. As of January 1, 2001, the Company reserved an additional 3,137,101 shares of Common stock for issuance under the 1996 Plan, as a result of the annual increase provision described above. In April 2001, the Board of Directors increased the Common stock reserved for issuance under the 1999 Plan by an additional 2,000,000 shares. On April 22, 2001, the Company entered into a Special Nonstatutory Stock Option Agreement (the "Special Plan") whereby an option was granted to acquire 2,000,000 shares of Common stock. Accordingly, the Company has reserved 2,000,000 shares of Common stock for issuance under the Special Plan. As of January 1, 2002, the Company reserved an additional 3,221,603 shares of Common stock for issuance under the 1996 Plan, as a result of the annual increase provision described above. On October 25, 2002, the Board of Directors increased the Common stock reserved for issuance under the 1999 Plan by an additional 2,000,000 shares. The options under the 1996 Plan, 1999 Plan and Special Plan are granted at the then-current fair market value of the Common stock of the Company and generally may be exercised in equal proportions over the defined vesting period for each grant, generally two to four years, and generally expire on the tenth anniversary of the grant date or upon termination of employment. The options granted under enCommerce 1997 Plans generally may be exercised in equal proportions over the defined vesting period of four years for each grant and expire on the tenth anniversary of the grant date or upon termination of employment of the option holder. The Board of Directors does not intend to grant any additional options under the enCommerce 1997 Plans.

In June 2001, the Company announced a voluntary stock option exchange program for its eligible employees (the "Offer to Exchange"). Under the program, Company employees were offered the opportunity to cancel certain outstanding stock options to purchase shares of Common stock previously granted to them. In exchange, these employees received new options granted under the 1999 Plan. The number of shares subject to the new options granted to each eligible employee was dependant upon the exercise price of the options tendered by the eligible employee and accepted for exchange. If the tendered options carried an exercise price of less than $50 per share, then the number of shares subject to new options was equal to the number of shares subject to the options cancelled. If the tendered options carried an exercise price of $50 per share or more, then the number of shares subject to new options was equal to one-half (1/2) the number of shares subject to the options cancelled. The new options were granted on January 31, 2002, which was six months and one day from the cancellation date of July 30, 2001. The exercise price of these new options was $6.75 and was equal to the fair market value of the Company's Common stock on the date of grant. The Company provided no promise to compensate the employees for any increases in the market price of the stock after the cancellation date. In addition, based on the July 30, 2001 cancellation date, those employees that chose to participate in the offer were also required to tender all options granted to them since January 30, 2001. New options issued had terms and conditions that are substantially the same as those of the cancelled options. This voluntary exchange program complies with FASB Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation" and related FASB Emerging Issues Task Force ("EITF") guidance and, accordingly, did not result in any variable accounting compensation charges. Members of the Company's Board of Directors and executive officers were not eligible to participate in this program.

Pursuant to the terms and conditions of the Offer to Exchange, a total of 592 eligible optionees participated in the option exchange program. The Company accepted for cancellation options to purchase 5,480,261 shares of its Common stock. Subject to the terms and conditions of the Offer to Exchange, the Company subsequently granted new options to purchase 5,033,822 shares of its Common stock on January 31, 2002, at an exercise price of $6.75 per share, in exchange for the options surrendered and accepted under the program.

Additionally, three executive officers that were not eligible to participate in the option exchange program received a nominal cash or stock award in exchange for the cancellation of a portion of their out-of-the-money stock options. Options to purchase an aggregate of 334,000 shares of Common stock with exercise prices ranging from $19.25 per share to $50.00 per share were cancelled in exchange for an aggregate of 15,220 shares of Common stock and $4 in cash. The expense related to the fair value of these shares and the cash was recorded in operating expense in 2002. The Company has provided no promise to compensate these executive officers for any increases in the price of the Common stock after the cancellation date. Further, the Company did not issue additional options to these executive officers within six months and one day of the date of cancellation.

During 2002, the Company issued a total of 3,250 shares of Common stock to two former members of the Board of Directors in recognition of past contributions. The expense related to the fair value of these shares was recorded in operating expenses in 2002.

In connection with acquisitions in 2000, the Company assumed options to purchase 1,542,131 shares of Common stock held by employees of the acquired company and a warrant to purchase 159,692 shares of Common stock held by a non-employee third party. The fair values of these options and warrants were included in the total purchase price of the acquired businesses.

A summary of the activity under the 1996 Plan, 1999 Plan, Special Plan and enCommerce 1997 Plans is set forth below:

		Options and Warrants Outstanding	
	Shares Available	Number of Shares	Weighted Average Exercise Price
Balance at December 31, 1999	2,025,849	7,418,823	13.76
Authorized	11,801,823	—	
Granted	(6,158,836)	6,158,836	39.76
Assumed in acquisition	(1,701,823)	1,701,823	7.13
Forfeited	357,661	(357,661)	35.70
Exercised	—	(1,701,659)	3.77
Balance at December 31, 2000	6,324,674	13,220,162	25.68
Authorized	7,137,101	—	
Granted	(9,470,721)	9,470,721	9.55
Cancelled under voluntary stock option exchange program	5,480,261	(5,480,261)	33.82
Forfeited	3,327,658	(3,327,658)	27.28
Exercised	—	(1,422,735)	2.20
Balance at December 31, 2001	12,798,973	12,460,229	11.98
Authorized	5,479,936	—	
Restricted stock issued to executive officers and former members of Board of Directors	(18,470)	—	
Granted under voluntary stock option exchange program	(5,033,822)	5,033,822	6.75
Granted	(3,399,708)	3,399,708	3.90
Forfeited	3,076,663	(3,076,663)	19.17
Exercised	—	(541,320)	2.15
Balance at December 31, 2002	12,903,572	17,275,776	7.90

The number of outstanding options and warrants exercisable into Common stock was 4,142,586, 5,414,036 and 8,610,674 at December 31, 2000, 2001 and 2002, respectively. The weighted average exercise price of these exercisable outstanding options and warrants was $8.73, $11.57 and $9.09, respectively.

The following tables summarize information concerning currently outstanding options and warrants as at December 31, 2002:

	Options and Warrants Outstanding			Options and Warrants Exercisable	
Range of Exercise Prices	Number of Options and Warrants Outstanding	Weighted Average Remaining Contractual Live	Weighted Average Exercise Price	Number of Options and Warrants Exercisable	Weighted Average Exercise Price
$0.12 to $2.44	1,174,201	4.7 years	1.92	1,118,014	1.91
$2.46 to $5.00	2,943,313	9.1 years	3.02	305,990	2.94
$5.01 to $6.72	1,867,322	6.1 years	5.85	859,256	5.96
$6.75 to $6.86	4,644,493	7.2 years	6.75	2,833,710	6.75
$6.87 to $10.00	4,379,041	7.9 years	6.90	1,952,808	6.90
$10.01 to $25.00	1,710,882	6.2 years	16.93	1,165,916	17.91
$25.01 to $50.00	477,479	7.1 years	36.65	317,211	37.43
$50.01 to $112.50	79,045	7.2 years	80.95	57,769	82.57
	17,275,776		7.90	8,610,674	9.09

(b) Employee Stock Purchase Plan

The Company's 1998 Employee Stock Purchase Plan (the "Purchase Plan") initially authorized the issuance of up to a total of 400,000 shares of Common stock to participating employees. All employees of the Company, including directors of the Company who are employees, and all employees of any participating subsidiaries whose customary employment is more than 20 hours per week and more than five months in any calendar year are eligible to participate in the Purchase Plan.

Under the terms of the Purchase Plan, as amended, the price per share paid by each participant on the last day of an offering period is an amount equal to 85% of the lesser of the fair market value per share of the Common stock on the first business day of an offering period or the last business day of such period.

At the Annual Meeting of Stockholders held April 27, 2001, the stockholders of the Company approved an amendment to the Purchase Plan whereby the Common stock reserved for issuance under the 1998 Plan was increased to 1,000,000 shares.

Termination of the Purchase Plan is at the discretion of the Board of Directors. Upon termination of the Purchase Plan, all amounts in the accounts of participating employees will be promptly refunded.

13. Net Income (Loss) Per Share

For the years ended December 31, 2000, 2001 and 2002, the antidilutive effect excluded from the diluted net loss per share computation due to options to purchase Common stock was 4,783,877, 1,984,917 and 1,036,944 shares, respectively. The antidilutive effect excluded from the diluted net loss per share computation due to the exchangeable Special Voting stock outstanding was 644,661 for the year ended December 31, 2000.

14. Related Party Transactions

Significant related party transactions with the Company's largest shareholder, Nortel Networks, and affiliated companies, not otherwise disclosed in the financial statements, include the following:

Revenues include sales to Nortel Networks for 2000, 2001 and 2002 of $751, $119 and $132, respectively.

The Company reimburses Nortel Networks for expenses paid by Nortel Networks on behalf of the Company, net of revenues collected by Nortel Networks on behalf of the Company. The net expenses reimbursed amounted to $295 and $210 for 2000 and 2001, respectively. The net expenses reimbursed for 2002 were insignificant. These amounts have been recorded in these financial statements at the carrying amount of the transactions involved.

Significant related party transactions with Entrust Japan, an investee accounting for on the equity basis, not otherwise disclosed in the financial statements, include the following:

Revenues include sales to Entrust Japan for 2000, 2001 and 2002 of $1,014, $3,296 and $2,598, respectively.

Entrust Japan reimburses the Company for expenses paid related to employees on secondment to Entrust Japan. The expenses reimbursed in 2002 amounted to $852. These amounts have been recorded in these financial statements at the carrying amount of the transactions involved. In addition, the Company paid sales commissions and market development fees to Entrust Japan totaling $367 and $507 in 2001 and 2002, respectively.

Balances due to/from the related party, arising from the sales of product and receipt of services referred to above, are typically payable net 30 days from the date of the related intercompany invoice. The accounts receivable at December 31, 2001, related to Nortel Networks and its affiliates, was insignificant. The accounts receivable at December 31, 2002 related to Nortel Networks was $172. The accounts receivable at December 31, 2001 and 2002, from Entrust Japan was $448 and $424, respectively.

15. Commitments and Contingencies

(a) Lease Commitments

The Company leases administrative and sales offices and certain property and equipment under noncancelable operating leases that will expire in 2011 with certain renewal options. Total rent expenses under such leases for 2000, 2001 and 2002 were $7,288, $10,106 and $7,869, respectively. At December 31, 2002, the future minimum lease payments under operating leases were as follows:

2003	$ 5,553
2004	4,201
2005	3,764
2006	3,897
2007	3,940
Thereafter	10,179
Total future minimum lease payments	$31,534

In addition to the lease commitments included above, the Company has provided letters of credit totaling $10,700 as security deposits in connection with certain office leases. The Company has noncancelable subleases of certain facilities included above. Payments to be received under these subleases will total $66 in 2003.

(b) Legal Proceedings

On September 30, 2002, Judge T. John Ward of the U.S. District Court for the Eastern District of Texas (the “Court”) issued an order dismissing a class action lawsuit pending against the Company.

As previously disclosed, on July 7, 2000, an action entitled Frankel v. Entrust Technologies Inc., et al., No. 2-00-CV-119, was filed in the Court. Subsequently, several similar actions were also filed. All of these actions were consolidated and on January 22, 2001, a consolidated complaint was filed. The consolidated complaint purported to be a class action lawsuit brought on behalf of persons who purchased or otherwise acquired Common stock of the Company during the period from October 19, 1999 through July 3, 2000. The consolidated complaint alleged that the defendants misrepresented and failed to disclose certain information about the Company’s business and prospects, as required by the Securities Exchange Act of 1934. It did not specify the amount of damages sought.

On September 21, 2001, the Company moved to dismiss an amended complaint filed on August 30, 2001. On September 30, 2002, the Court found that the Private Securities Litigation Reform Act required dismissal of the case because of the lack of specificity with which the amended complaint was pleaded. The case was dismissed with prejudice; however, the order is subject to the possibility of an appeal. As of the date of this filing, the Company had not learned of any appeal being filed. If an appeal is granted, an adverse judgment or settlement in this lawsuit could have a significant adverse impact on the Company's future financial condition or results of operations.

The Company is subject, from time to time, to various other legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. While the outcome of these claims cannot be predicted with certainty, management does not believe that the outcome of any of these other legal matters will have a material adverse effect on the Company's consolidated results of operations or consolidated financial position.

(c) Contingencies

Entrust entered into a contract with the General Services Administration ("GSA") on March 31, 2000. The Company is conducting a self-assessment of its compliance and internal processes with respect to the agreement, as well as the pricing requirements of the agreement. As a result, the Company may have a potential liability to the GSA under this contract, and the Company has advised the GSA of this matter. However, at this time, the Company's self-assessment of its compliance is incomplete and, as a result, the Company is unable to ascertain the extent of its potential liability, if any, including the amount or type of any damages. Management believes, based on the current information available, that the outcome will not have a material adverse effect on the Company's consolidated results of operations or consolidated financial position.

16. Employee Savings Plan

The Company has a defined contribution retirement savings plan covering substantially all of its full-time employees. This plan qualifies under Section 401(k) of the Internal Revenue Code for participating U.S. based employees. The Company matches 50% of employee contributions up to 3% of their individual compensation. Matching contributions made by the Company totaled $1,732, $2,627 and $1,094 for 2000, 2001 and 2002, respectively.

17. Supplemental Cash Flows Information

The following is provided as supplemental information to the consolidated statements of cash flows:

	Year Ended December 31,		
	2000	2001	2002
Non-cash investing and financing activities:			
Increases in long-term equity investment in Entrust Japan:			
Conversion of advances	$ —	$ —	$ 524
Value of Entrust software product inventory exchanged	—	—	385
Issuance of Common stock, stock options and warrants related to the acquisition of enCommerce, Inc	482,272	—	—
Income taxes paid, net	$ 243	$ 1,594	$ 1,829

18. Segment, Geographic and Major Customer Information

(a) Segment Information

The Company conducts business in one operating segment: namely, the design, production and sale of software products and related services for securing digital identities and information. The nature of the Company's different products and services is similar and, in general, the type of customers for those products and services is not distinguishable.

The Company does, however, prepare information for internal use by the President and Chief Executive Officer, who, from an accounting perspective, is the Chief Operating Decision Maker ("CODM"), on a geographic basis. Accordingly, the Company has included a summary of the segment financial information reported to the CODM as follows in the next section regarding geographic information. The Company's CODM does not view geographic segment results below net income (loss) before income taxes and, therefore, the provision for income taxes is not broken out by geographic segment below. The accounting policies of the reportable geographic segments are the same as those described in the summary of significant accounting policies.

(b) Geographic information

Revenues are attributed to specific geographical areas based on where the sales order originated. Long-lived assets and total assets of the Company are those that are identified with operations in the respective geographic areas.

The Company operates in three main geographic areas as follows:

	Year Ended December 31,		
	2000	2001	2002
Revenues			
United States	$ 81,245	$ 48,634	$ 50,587
Canada	22,282	30,450	20,764
Europe, Asia and Other	44,850	38,881	31,396
Total revenues	148,377	117,965	102,747
Segment operating income (loss):			
United States	(6,171)	(57,898)	(9,561)
Canada	3,749	(10,140)	(3,417)
Europe, Asia and Other	5,330	6,975	2,382
Total segment operating income (loss)	2,908	(61,063)	(10,596)
Depreciation and amortization expense:			
United States	63,900	66,739	2,397
Canada	2,687	5,954	5,478
Europe, Asia and Other	439	738	391
Total depreciation and amortization	67,026	73,431	8,266
Other income (expense):			
United States	13,809	(1,367)	1,214
Acquired in-process research and development:			
United States	29,614	—	—
Impairment of intangibles, write-downs of other long-lived assets, and restructuring charges:			
United States	—	393,058	(1,079)
Canada	—	9,739	—
Europe, Asia and Other	—	3,186	—
Total	—	405,983	(1,079)
Income (loss) before income taxes:			
United States	(85,876)	(519,062)	(9,665)
Canada	1,062	(25,833)	(8,895)
Europe, Asia and Other	4,891	3,051	1,991
Total income (loss) before income taxes	$ (79,923)	$(541,844)	$ (16,569)

	Year Ended December 31,		
	2000	2001	2002
Long-lived assets (generally depreciated over three to five years):			
United States	$429,003	$ 31,949	$ 34,188
Canada	19,690	13,753	9,816
Europe, Asia and Other	1,429	854	721
Total long-lived assets	$450,122	$ 46,556	$ 44,725
Total assets:			
United States	$670,710	$191,493	$159,143
Canada	45,628	32,916	26,824
Europe, Asia and Other	17,375	4,636	3,604
Total	$733,713	$229,045	$189,571

(c) Major Customer Information

In 2000 and 2002, no individual customer accounted for 10% or more of revenues. In 2001, a single customer accounted for 11% of revenues, and no other customers accounted for 10% or more of revenues.

EXHIBIT INDEX

Exhibit Number	Description	Form	Number
2.1(1)†	Stock Purchase Agreement dated March 14, 2000 by and among the Registrant, Cygnacom Solutions Inc. and the Stockholders of Cygnacom Solutions Inc.	8-K	2
2.2(2)†	Agreement and Plan of Merger dated April 18, 2000 by and among the Registrant, Enable Acquisition Corp. and enCommerce, Inc.	8-K	2
3.1(9)	Articles of Amendment and Restatement of Charter, as amended, of the Registrant	10-K	3.1
3.2(3)	Amended and Restated Bylaws of the Registrant	S-1	3.4
4.1(4)	Specimen certificate for shares of Common Stock, $.01 par value, of the Registrant	10-Q	4.1
4.2(11)	Common Stock Purchase Warrant issued to Lehman Brothers Inc. for shares of Common Stock of the Registrant, dated April 22, 2001	10-Q	4
4.3(6)	Common Stock Warrant No. 1 of the Registrant dated June 26, 2000 issued to Andersen Consulting LLP	10-K	10.17
10.1(3)	Amended and Restated Registration Rights Agreement dated as of July 30 1998, by and among the Registrant and certain stockholders	S-1	10.3
10.2(3)	Strategic Alliance Agreement dated as of December 31, 1996 between the Registrant and Northern Telecom Limited	S-1	10.5
10.3*	Letter Agreement dated May 21, 2001 between the Registrant and Milan Bekich	#	
10.4*	Officer Retention Program and Agreement dated March 27, 2001 between Colin Wyatt and the Registrant	#	
10.5*	Non-Competition and Non-Solicitation Agreement dated March 27, 2001 between Colin Wyatt and the Registrant	#	
10.6*	Letter Agreement dated September 6, 2002 between Entrust (Europe) Limited and Colin Wyatt	#	
10.7*	Compromise Agreement dated February 10, 2003 between Entrust (Europe) Limited and Colin Wyatt	#	
10.6(5)*	Amended and Restated 1996 Stock Incentive Plan, as amended	10-Q	10.10
10.7(3)	Lease Agreement dated as of January 28, 1998, between Colonnade Development Incorporated and Entrust Technologies Limited	S-1	10.16
10.8(9)	Lease Agreement dated November 16, 2001 between Intervest-Parkway, Ltd. and the Registrant	10-K	10.9
10.9(8)*	Letter Agreement dated October 11, 1999 between the Registrant and David L. Thompson	S-3	10.3
10.10(8)	Development Agreement dated December 29, 1999 between Canderel Management Inc. and Entrust Technologies Limited	S-3	10.4
10.11(8)	Lease dated December 29, 1999 in Pursuance of the Short Forms of Lease Act between 786473 Ontario Limited, Entrust Technologies Limited and Registrant	S-3	10.5
10.12(8)	Lease dated December 29, 1999 by and between 3559807 Canada Inc., Entrust Technologies Limited and the Registrant	S-3	10.6
10.13(5)*	enCommerce, Inc. 1997 Stock Option Plan	10-Q	10.1
10.14(5)	enCommerce, Inc. 1997B Stock Option Plan	10-Q	10.2
10.15*	1999 Non-Officer Employee Stock Incentive Plan, as amended	#	
10.16(9)	Lease Agreement dated November 14, 2000 between Sobrato Interest II and the Registrant	10-K	10.20
10.17(9)	First Amendment to Lease dated July 26, 2001 by and between Sobrato Interests II and the Registrant	10-K	10.21
10.18(4)*	Employment Agreement dated as of April 22, 2001 by and between F. William Conner and the Registrant	10-Q	10.1
10.19(4)*	Special Nonstatutory Stock Option Agreement dated April 22, 2001 between the Registrant and F. William Conner	10-Q	10.2

10.20(4)*	Nonstatutory Stock Option Agreement Granted Under the Amended and Restated 1996 Stock Incentive Plan dated April 22, 2001 between the Registrant and F. William Conner	10-Q	10.3

Exhibit Number	Description	Form	Number
10.21(4)*	Form of Nonstatutory Stock Option Agreement Granted Under the Amended And Restated 1996 Stock Incentive Plan to Non-Employee Directors of the Registrant	10-Q	10.7
10.22(9)*	Officer Retention Program and Agreement effective as of March 6, 2001 between David L. Thompson and the Registrant, as amended	10-K	10.31
10.23(9)*	Non-Competition and Non-Solicitation Agreement effective as of March 6, 2001 between the Registrant and David L. Thompson	10-K	10.32
10.24(9)*	Letter Agreement dated May 17, 2001 between the Registrant and Edward J. Pillman	10-K	10.33
10.25(10)*	Option Exchange Agreement dated February 21, 2002 between the Registrant and F. William Conner	10-Q	10.1
10.26(10)*	Restricted Stock Agreement Granted under the Amended and Restated 1996 Stock Incentive Plan, as amended, dated February 21, 2002 between the Registrant and David L. Thompson	10-Q	10.2
10.27(9)	Lease Agreement dated November 1, 2001 by and between the Registrant and Intervest-Parkway, Ltd.	10-K	10.9
21	Subsidiaries of the Registrant	#	
23.1	Consent of Deloitte & Touche LLP	Enclosed herewith	
31.1	Rule 13a-14(a) Certification of Chief Executive Officer	Enclosed herewith	
31.2	Rule 13a-14(a) Certification of Chief Financial Officer	Enclosed herewith	
32.1	Section 1350 Certification of Chief Executive Officer	Enclosed herewith	
32.2	Section 1350 Certification of Chief Financial Officer	Enclosed herewith	

* Management contract or compensatory plan or arrangement filed in response to Item 15(a)(3) of the instructions to Form 10-K.

(1) Incorporated herein by reference to the Registrant's Current Report on Form 8-K dated March 14, 2000 filed with the Securities and Exchange Commission on March 24, 2000 (File No. 000-24733).

(2) Incorporated herein by reference to the Registrant's Current Report on Form 8-K dated April 18, 2000 filed with the Securities and Exchange Commission on May 1, 2000 (File No. 000-24733).

(3) Incorporated herein by reference to the Registrant's Registration Statement on Form S-1 (File No. 333-57275).

(4) Incorporated herein by reference to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2001 (File No. 000-24733).

(5) Incorporated herein by reference to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2000 (File No. 000-24733).

(6) Incorporated herein by reference to the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2000 (File No. 000-24733).

(7) Incorporated herein by reference to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2001 (File No. 000-24733).

(8) Incorporated herein by reference to the Registrant's Registration Statement on Form S-3 (File No. 333-95375).

(9) Incorporated herein by reference to the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2001 (File No. 000-24733).

(10) Incorporated herein by referenced to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2002 (File No. 000- 24733).

(11) Incorporated herein by reference to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2002. (File No. 000-24733).

\+ The Registrant agrees to furnish supplementary a copy of any omitted schedules to this agreement to the Securities and Exchange Commission upon its request.

\# Incorporated herein by reference to the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 2002 (File No. 000-24733).