

PERFICIENT INC
Form 10KSB
March 30, 2004

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-KSB

Annual Report Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934
For the Fiscal Year Ended December 31, 2003
Commission File Number: 1-15169

PERFICIENT, INC.

(Name of Small Business Issuer in its Charter)

DELAWARE
(State or Other Jurisdiction of
Incorporation or Organization)

74-2853258
(IRS Employer
Identification No.)

**1120 South Capital of Texas Highway, Bldg. 3, Suite 220
Austin, Texas 78746**

(Address of principal executive offices)

(512) 531-6000

(Issuer's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Exchange Act:

Title of Class
Common Stock, \$.001 par value

Name of each exchange on which registered:
Boston Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

NONE
(Title of Class)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act during the past 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

Check if disclosure of delinquent filers in response to Item 405 of Regulations S-B is not contained in this filing, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB.

State issuer's revenues for its most recent fiscal year: \$30,191,922

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State the aggregate market value of the voting and nonvoting common equity held by non-affiliates computed by reference to the price at which the common equity was sold, or the average bid and asked prices of such common equity as of a specified date within the past 60 days.

\$49,101,598 AS OF MARCH 29, 2004

State the number of shares of common stock outstanding as of March 29, 2004: 15,087,566

Portions of the definitive proxy statement relating to the 2004 Annual Meeting of Stockholders, which will be filed with the commission not later than April 29, 2004 are incorporated by reference in Part III of this Form 10-KSB.

Transitional Small Business Disclosure Format: Yes No

PERFICIENT, INC.

FORM 10-KSB ANNUAL REPORT

FOR THE YEAR ENDED DECEMBER 31, 2003

TABLE OF CONTENTS

| | | |
|-------------------|---|----|
| Part I | | |
| Item 1. | Description of Business | 2 |
| Item 2. | Description of Property | 13 |
| Item 3. | Legal Proceedings | 13 |
| Item 4. | Submission of Matters to a Vote of Security Holders | 13 |
| Part II | | |
| Item 5. | Market for Common Equity and Related Stockholder Matters | 14 |
| Item 6. | Management's Discussion and Analysis of Financial Condition and Results of Operations | 15 |
| Item 7. | Consolidated Financial Statements | 20 |
| Item 8. | Changes in and Disagreements with Accountants on Accounting and Financial Disclosures | 21 |
| Item 8A. | Controls and Procedures | 21 |
| Part III | | |
| Item 9. | Directors, Executive Officers, Promoters and Control Persons of the Registrant | 21 |
| Item 10. | Executive Compensation | 21 |
| Item 11. | Security Ownership of Certain Beneficial Owners and Management | 21 |
| Item 12. | Certain Relationships and Related Transactions | 21 |
| Item 13. | Exhibits, Financial Statements and Reports on Form 8-K | 21 |
| Item 14. | Principal Accountant Fees and Services | 24 |
| SIGNATURES | | 25 |

The statements contained in this annual report on Form 10-KSB that are not purely historical statements are forward looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, including statements regarding our expectations, beliefs, hopes, intentions or strategies regarding the future. These forward-looking statements include, among other things, references to the market potential for Internet implementation, our competitive advantage over systems integrators and technology professionals, potential demand for our services, and the benefits and advantages of our business model and involve substantial risks and uncertainties. Actual results may differ materially from those indicated in such forward-looking statements. Please see "Risk Factors," "Special Cautionary Note Regarding Forward-Looking Statements" and the factors and risks discussed in the reports we file from time to time with the Securities and Exchange Commission.

PART I

ITEM 1 DESCRIPTION OF BUSINESS

Overview

We are an eBusiness solutions services provider to large and major midsize companies. We use a solutions delivery approach we call the Enabled Enterprise, that helps clients reach new markets and increase revenues, acquire and strengthen customer relationships, reduce costs and increase productivity and empower employees. Our Enabled Enterprise is an Internet-based infrastructure with integrated business applications that extend enterprise technology assets to customers, suppliers, partners and employees. We market our eBusiness solutions services directly to large and major midsize companies, principally in the Midwestern United States through a seven person direct sales force.

In addition to our direct-to-end customer solutions business, our Advanced Technology Services (ATS) group exclusively serves IBM Corporation and its customers throughout the United States. Our ATS group employs more than 55 employees with experience in a variety of IBM software products, including WebSphere middleware and application servers and WebSphere portal server. We have a services agreement with IBM under which our ATS group provides deployment, integration and training services to IBM's WebSphere customers. Under the agreement with IBM, we are paid for services rendered. Our current agreement with IBM expires in September 2004 and may be cancelled prior to that date upon five days written notice. In 2003, revenue from IBM accounted for approximately 35% of total revenues. Any termination of our relationship with, or significant reduction or modification of the services we perform for, IBM would materially reduce our revenue and net income.

We were incorporated in Texas in September 1997. In May 1999 we reincorporated in Delaware. We employed 147 full-time professionals in 5 offices in the United States and Canada as of March 29, 2004.

Our eBusiness Solutions Services

We help our clients use Internet-based technologies to reach new markets and increase revenues, strengthen customer relationships, reduce operating costs and increase productivity, and empower their workers. We employ a broad-based approach, grounded in a thorough understanding of our clients' overall business strategy and competitive environment. Our services strive to help clients develop new business opportunities by taking advantage of existing distribution channels, customer service networks, and information systems.

For our project engagements, we perform any or all of the following services:

analyze end-user customer business goals and requirements;

define the scope of the implementation project;

2

design a project plan; and

custom develop solutions as well as install, configure, and integrate our partners' Internet software products.

Our goal is to reduce significantly the time required for our clients to implement an effective eBusiness solution. This enables our customers to quickly realize the benefits associated with our strategic partners' software products and allows our strategic partners to more rapidly expand their market share.

Our approach includes an integrated set of real-world solutions that leverage Internet technologies to extend our clients' legacy systems to customers, employees, suppliers, and partners through:

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eBusiness infrastructure;

eCommerce platforms;

Online customer management (eCRM);

Supply chain Web-enablement (SCWE); and

Enterprise portals.

Our target market for eBusiness solutions services is large and major midsize corporations, principally located in the Midwestern United States. We believe that these businesses invest in technology products and related services for four principal reasons:

to reach new markets and increase revenues;

to strengthen customer relationships;

to reduce operating costs and increase productivity; and

to empower their workers.

In addition, we believe that these companies require, as a predicate to making such investment, a demonstrable positive return-on-investment potential and an eBusiness solutions partner with both proven experience in delivering similar projects and familiarity with the issues and concerns specific to the industry in which they operate.

Accordingly, we focus on a targeted number of industries for which we have developed domain expertise and offer eBusiness solutions services that we believe can generate a meaningful positive return-on-investment for our customers. Our primary eBusiness solutions services offerings are described below:

eBusiness Infrastructure. Middleware and Enterprise Application Integration (EAI) software are two key components to developing enterprise-class, eCommerce platforms for large and mid-size companies. Perficient designs and implements complex website-to-legacy system integrations that significantly reduce round-trip transaction times for enterprise-class websites. This umbrella of technologies is commonly called Web Services. To maximize our value to customers, we have strategic relationships with Web Services firms such as IBM and Microsoft.

eCommerce Platforms. We develop eCommerce applications and further enhance existing sites to introduce new technology. We design systems that manage the "back-end" order fulfillment process to leading ERP systems such as SAP and JD Edwards for business-to-consumer and business-to-business Web sites. We provide commerce site enhancements, including advanced catalog management and search and cross-sell and up-sell capabilities. We offer clients packaged or custom electronic bill presentation and implementation solutions based on an individual company's needs.

eCRM. Customer Relationship Management provides businesses with information on the wants and needs of its customers. We integrate data from disparate information sources to provide continuous, interactive and multi-platform customer interaction and value exchange. We deliver CRM components including: personalization, point of sale, telesales, Web-based selling, data mining, online advertising, call/contact center information and systems integration, field service dispatch, lead tracking, geocoding, and multiple front and back-office applications.

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Supply Chain Web Enablement. In the manufacturing and service industries, the implementation of a portal, business hub, Net exchange or extranet system enables established companies to build new business models, alliances, partnerships and other business relationships. Each company and industry has unique design and build requirements to support purchasing, distribution and sales. We help companies develop strategies and build the solutions they need to facilitate the exchange of information and transactions at critical points along the supply-chain.

Enterprise Portals. Communication is the basis of success for any organization. We design, build and deploy "self-service" and collaborative solutions for business-to-employee, business-to-consumer and business-to-business implementations and enable workflow efficiencies by exchanging data and information in a cost-efficient, effective manner. Many organizations implement business-to-employee portals to improve employee communication. We help clients to extend these benefits externally in business-to-consumer and business-to-business portals that provide a secure line of business application integration and personalized buying communities.

Our Strategy

Our objective is to be a leading eBusiness solutions services provider to large and major midsize companies and Internet software vendors. To achieve our goal, our strategy is to:

target for expansion vital but underserved markets in the Midwestern and Southwestern United States;

use selective acquisitions to supplement organic growth and achieve critical mass;

continue to grow our IBM relationship and expand it to include more solutions-oriented services and software sales;

provide our customers end-to-end solutions that generate a demonstrable positive return on investment;

continue to invest in the professional development of our consulting staff and provide them with entrepreneurial opportunities within Perficient; and

retain and strengthen a culture built on teamwork, a passion for technology and client service, and a focus on cost control and the bottom line.

Sales and Marketing

eBusiness Solutions Services. Our business development approach is market-focused with specific and tailored strategies for the industry market segments we serve. We target companies with annual revenues between \$250 million and \$5 billion, specifically focused in financial services (insurance, banking and brokerage), healthcare (pharmacy benefit managers and pharmaceutical manufacturers) and commodity (agribusiness and energy) markets. We also pursue opportunities in other industries where we can leverage our expertise. We utilize a direct sales force that consists of seven consultative sales professionals.

IBM Partnership. Our ATS service engagements are generated through or with IBM. As a result, our principal sales and marketing activity consists of marketing our services in concert with IBM's sales and services organizations. We have a general manager dedicated to coordinating projects and stimulating additional demand from IBM. Early in 2004 we realigned our sales force and sales processes in support of IBM's new organization and solutions-oriented sales process.

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We have strategic relationships with eBusiness technology and services providers including IBM, Digex, Tibco, Wily Technology, Bowstreet, Stellent, and Microsoft. These companies are key vendors in middleware and application servers, enterprise application integration, content management, and Web services. We believe these relationships enable us to leverage our core competencies, extend our service offerings, reach new clients and decrease costs/time-to-market for us and our customers.

Technology Professionals

Recruiting. Our most valuable assets are our technology professionals. We are dedicated to hiring, developing and retaining technology professionals who combine a depth of understanding of current Internet and legacy technologies with the ability to implement complex and cutting-edge solutions.

Our recruiting efforts are an important element of our continuing operations and future growth. We generally target technology professionals with extensive experience and demonstrated expertise. To attract technology professionals, we use a broad range of sources including outside recruiters, internal referrals, other technology companies and technical associations, the Internet and advertising in technical periodicals. After initially identifying qualified candidates, we conduct an extensive screening and interview process.

We believe that our focus on a target set of core Internet technologies and our commitment to continuing training and advancement opportunities makes us an attractive career choice for experienced professionals. Because our strategic partners are established and emerging market leaders, our technology professionals have an opportunity to work with cutting-edge information technology. We foster professional development by training our technology professionals in the skills critical to successful consulting engagements such as implementation methodology and project management.

Training. To ensure continued development of our technical staff, we place a high priority on training. We offer extensive training for our professionals around industry-leading technologies, including an on-line, Internet-based education and training program that offers more than 200 topics, including CORBA, EJB architecture, HTML, J2EE, Linux, Network Security and XML fundamentals. This web-based education system is offered to all of our technology professionals to facilitate their ongoing professional development and increase their technical expertise.

Technology Leadership Council. Our technology leadership council performs a critical role in maintaining our technology leadership. Consisting of key employees from each of our practice areas, the council frames our new strategic partner strategies, conducts regular conferences on the Internet with our technology professionals on specific partner and general technology issues and trends, conducts promotional activities, such as white paper publication and speaking engagements by our professionals, identifies services opportunities between and among our strategic partners' products, oversees our quality assurance programs and assists in acquisition-related technology due diligence.

The Perficient Promise. We continue to build our corporate culture around a common set of values based on expertise, honesty and teamwork.

We have codified our commitments to each other in The Perficient Promise, which consist of the following seven simple commitments our management and technology professionals make to each other:

we work with cutting-edge technologies and leading-edge clients;

5

we maintain an informal team culture;

we provide our technology professionals with high-quality infrastructure support services;

we provide competitive incentives including equity ownership;

we reinvest in continuing training and education; and

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we treat each other with respect.

We take these commitments extremely seriously, because we believe that we can succeed only if The Perficient Promise is kept.

MyPerficient.com The Corporate Portal. To ensure ubiquitous access to a wide range of information and tools, we have created a corporate portal, MyPerficient.com. It is a secure, centralized communications tool implemented using IBM's Websphere Portal Server product. It allows each of our technology professionals unlimited access to information, productivity tools, time and expense entry, benefits administration and quality management information directories and documentation.

Employees

As of March 29, 2004, we employed 147 full-time employees. Of our total employees, 126 were technology professionals and 21 were involved in sales, general administration and marketing. Our employees are not represented by any collective bargaining unit, and we have never experienced a work stoppage.

Competition

The markets for the services that we provide are highly competitive. We believe that our competitors fall into several categories, including:

in-house information technology and professional services and support departments of software companies;

systems integrators, such as Sapien Corporation, SBI and Company, and Braun Consulting;

large consulting firms, such as Accenture, Bearing Point, Braxton (formerly Deloitte Consulting) and Cap Gemini Ernst & Young;

information technology staffing firms, such as Keane, Inc. and Aquent (formerly Renaissance Worldwide); and

other eBusiness solutions service providers engaged by IBM as subcontractors.

We believe that the principal competitive factors affecting our market, and on which we focus our efforts, include experience of personnel, number of customers, the breadth and depth of a given solution, service quality and performance, core technologies, product scalability, reliability and product features and the ability to implement solutions quickly and respond timely to customer needs. In addition, there are relatively low barriers to entry into this market, and we expect to face additional competition from new entrants. We expect competition from offshore outsourcing and development companies to increase in the future.

Most of our competitors have longer operating histories, larger client bases, and greater name recognition and possess significantly greater financial, technical and marketing resources than we do. As a result, our competitors may be better able to attract customers to which we market our services and adapt more quickly to new technologies or evolving customer or industry requirements. Many competitive factors are outside of our control, such as the ability of our competitors to hire, retain and motivate qualified technology professionals.

RISK FACTORS

Risks Specific to Our Business

We have incurred losses during most of the quarters during which we have been in business and we may incur losses in the future.

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We have incurred operating losses in most of the quarters during which we have been in business. Although we have recently achieved profitability, we may not be able to sustain or increase profitability on a quarterly or annual basis in the future. We cannot assure you of any operating results. In future quarters, our operating results may not meet public market analysts' and investors' expectations. If that happens, the price of our common stock will likely fall.

We have a limited number of customers and the loss of sales to IBM would materially reduce our revenue and net income.

We have arrangements with a limited number of customers. Revenue from IBM accounted for approximately 35% of total revenues for both the years ended December 31, 2002 and December 31, 2003. Any termination of our relationship with, or significant reduction or modification of the services we perform for, IBM would materially reduce our revenue and net income.

The failure of IBM to pay our accounts receivable would materially impact our cash and working capital balances.

Amounts owed to us by IBM represented 37% of our accounts receivable, or \$2,276,000, as of December 31, 2003. Failure of IBM to pay that amount would have a material adverse effect on our working capital, cash position, business, operating results and financial condition. Failure of IBM to pay us timely could also have a material impact our cash and working capital balances.

IBM may reduce substantially its use of our services, which would materially reduce our revenue and net income.

Our current agreement with IBM will expire on September 1, 2004, and may be terminated by IBM prior to that date upon five (5) days written notice. A decision by IBM to reduce the amount of services performed by us or to terminate the agreement would have an adverse effect on our business, operating results and financial condition. In the event IBM decides not to use our services, our revenue and net income could be materially reduced.

Our customers may not be obligated to use our services.

Our contracts with some of our customers do not obligate them to use our services. A customer may choose at any time to use another consulting firm or to perform the services we provide through internal resources. Termination of a relationship with certain customers, or the decision of such customers to employ other consulting firms or perform services in-house, could materially harm our business.

Our quarterly operating results may be volatile and may cause our stock price to fluctuate.

A high percentage of our operating expenses, particularly personnel and rent, are fixed in advance of any particular quarter. As a result, if we experience unanticipated changes in the number or nature of our projects or in our employee utilization rates, we could experience large variations in quarterly operating results and losses in any particular quarter. Due to these factors, we believe that our historical quarter-to-quarter operating results should not be used to predict our future performance.

7

Our quarterly revenue, expenses and operating results have varied significantly in the past and are likely to vary significantly in the future. These quarterly fluctuations have been and may continue to be affected by a number of factors, including:

the loss of a significant customer or project;

the number and types of projects that we undertake;

our ability to attract, train and retain skilled management and technology professionals;

seasonal variations in spending patterns;

our employee utilization rates, including our ability to transition our technology professionals from one project to another;

changes in our pricing policies;

our ability to manage costs; and

costs related to acquisitions of other businesses.

In addition, many factors affecting our operating results are outside of our control, such as:

demand for Internet software;

end-user customer budget cycles;

changes in end-user customers' desire for our partners' products and our services;

pricing changes in our industry;

government regulation and legal developments regarding the use of the Internet; and

general economic conditions.

We expect that we may experience seasonal fluctuations in revenues. We expect that revenues in the quarter ending December 31 of a given year may typically be lower than in other quarters in that year as there are fewer billable days in this quarter as a result of vacations and holidays. This seasonal trend may materially affect our quarter-to-quarter operating results.

Our revenues are difficult to predict because they are derived from project-based engagements.

Almost all of our revenues are from project-based client engagements, which vary in size and scope. Our revenue is difficult to predict since a client that accounts for a significant portion of revenues in one period may not generate a similar amount of revenue, if any, in subsequent periods. In addition, because many of our project-based client engagements involve sequential stages, each of which may represent a different contractual commitment, a client may choose not to retain us for subsequent stages of an engagement or for new service projects.

Our gross margins are subject to fluctuations as a result of variances in utilization rates.

Our services gross margins are affected by trends in the utilization rate of our professionals, defined as the percentage of our professionals' time billed to customers divided by the total available hours in a period. Our operating expenses, including employee salaries, rent and administrative expenses are relatively fixed and cannot be reduced on short notice to compensate for unanticipated variations in the number or size of projects in process. If a project ends earlier than scheduled, we may need to redeploy our project personnel. Any resulting non-billable time may adversely affect our gross margins. The absence of long-term contracts and the need for new partners and business create an uncertain revenue stream, which could negatively affect our financial condition.

We may not grow, or we may be unable to manage our growth.

Our success will depend on our ability to increase the number of our partners, end-user customers and our teams of technology professionals. However, we may not grow as planned or at all. Many of our competitors have longer operating histories, more established reputations, more potential partner and end-user customer relationships and greater financial, technical and marketing resources than we do. If we experience growth, our growth will place significant strains on our management, personnel and other resources. If we are unable to grow or

manage our growth effectively, this inability will adversely affect the quality of our services and our ability to retain key personnel, and could materially harm our business.

We may not be able to attract and retain technology professionals, which could affect our ability to compete effectively.

Our business is labor intensive. Accordingly, our success depends in large part upon our ability to attract, train, retain, motivate, manage and utilize highly skilled technology professionals. Additionally, our technology professionals are at-will employees. Any inability to attract, train and retain highly skilled technology professionals would impair our ability to adequately manage, staff and utilize our existing projects and to bid for or obtain new projects, which in turn would adversely affect our operating results.

Our success will depend on retaining our senior management team and key technical personnel.

We believe that our success will depend on retaining our senior management team and key technical personnel. Retention is particularly important in our business as personal relationships are a critical element of obtaining and maintaining our partners. If any of these individuals stops working for us, our level of management, technical, marketing and sales expertise could significantly diminish. These individuals would be difficult to replace, and losing them could seriously harm our business. We may not be able to prevent key personnel, who may leave our employ in the future, from disclosing or using our technical knowledge, practices or procedures. One or more of our key personnel may resign and join a competitor or form a competing company. As a result, we might lose existing or potential clients.

We face risks associated with finding and integrating acquisitions.

We made three acquisitions during 2000 and we completed the acquisitions of Vertecon and Javelin in April 2002. We may continue to expand our technological expertise and geographical presence through selective acquisitions. Any acquisitions or investments we make in the future will involve risks. We may not be able to make acquisitions or investments on commercially acceptable terms. If we do buy a company, we could have difficulty retaining and assimilating that company's personnel. In addition, we could have difficulty assimilating acquired products, services or technologies into our operations and retaining the customers of that company. Our operating results may be adversely affected by increased intangibles amortization, stock compensation expense and increased compensation expense attributable to newly hired employees. Furthermore, our management's attention may be diverted from other aspects of our business and our reputation may be harmed if an acquired company performs poorly. These difficulties could disrupt our ongoing business, distract our management and employees, increase our expenses and materially and adversely affect our results of operations. Furthermore, we may incur debt or issue equity securities to pay for any future acquisitions. If we issue equity securities, your ownership share of our common stock will be diluted.

We may face potential liability to customers if our customers' systems fail.

Our professional services and software are often critical to the operation of our customers' businesses and provide benefits that may be difficult to quantify. If one of our customers' systems fails, the customer could make a claim for substantial damages against us, regardless of our responsibility for that failure. The limitations of liability set forth in our contracts may not be enforceable in all instances and may not otherwise protect us from liability for damages. Our insurance coverage may not continue

to be available on reasonable terms or in sufficient amounts to cover one or more large claims. In addition, a given insurer might disclaim coverage as to any future claims. If we experience one or more large claims against us that exceed available insurance coverage or result in changes in our insurance policies, including premium increases or the imposition of large deductible or co-insurance requirements, our business and financial results could suffer.

Risks Relating to Our Industry

The Internet services market demand is subject to uncertainty.

The market for Internet services is relatively new and is evolving rapidly. Our future growth is dependent upon our ability to provide strategic Internet services that are accepted by our end-user customers. Demand and market acceptance for recently introduced services are subject to a high level of uncertainty. The level of demand and acceptance of strategic Internet services is dependent upon a number of factors, including:

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the growth in consumer access to and acceptance of new interactive technologies such as the Internet;

companies adopting Internet-based business models; and

the development of technologies that facilitate two-way communication between companies and targeted audiences.

Significant issues concerning the commercial use of these technologies include security, reliability, cost, ease of use and quality of service. These issues remain unresolved and may inhibit the growth of Internet business solutions providers that use these technologies.

We are dependent on the demand for Internet software and services, which may fluctuate.

The market for Internet software and services has changed rapidly over the last four years. The market for Internet software and services expanded dramatically during 1999 and most of 2000, but declined significantly in 2001 and 2002. Market demand for internet software and service began to stabilize and improve throughout 2003, but there can be no assurances that this trend will continue. Our future growth is dependent upon the demand for Internet software and services and our ability to provide strategic Internet services that are accepted by our end-user customers. Demand and market acceptance for Internet services are subject to a high level of uncertainty. If companies continue to cancel or delay their business and technology initiatives or choose to move these initiatives in-house because of the current economic climate, or for other reasons, our business, financial condition and results of operations could be materially and adversely affected.

Businesses may decrease or delay their use of advanced technologies as a means for conducting commerce.

Our future success depends heavily on the acceptance and use of advanced technologies as a means for conducting commerce and streamlining operations. We focus our services on the development and implementation of advanced technology strategies and solutions. If the use of these technologies does not grow, or such growth is delayed due to economic uncertainty or other conditions, our revenue could be less than we anticipate and our business, financial condition and results of operations could be materially adversely affected.

Our business will suffer if we do not keep up with rapid technological change, evolving industry standards or changing partner requirements.

10

Rapidly changing technology, evolving industry standards and changing partner needs are common in the Internet professional services market. Accordingly, our success will depend, in part, on our ability to:

continue to develop our technology expertise;

enhance our current services;

develop new services that meet changing partner and end-user customer needs;

advertise and market our services; and

influence and respond to emerging industry standards and other technological changes.

We must accomplish all of these tasks in a timely and cost-effective manner. We might not succeed in effectively doing any of these tasks, and our failure to succeed could have a material and adverse effect on our business, financial condition or results of operations, including materially reducing our revenue and operating results.

We may also incur substantial costs to keep up with changes surrounding the Internet. Unresolved critical issues concerning the commercial use and government regulation of the Internet include the following:

security;

cost and ease of Internet access;

intellectual property ownership;

privacy;

taxation; and

liability issues.

Any costs we incur because of these factors could materially and adversely affect our business, financial condition and results of operations, including reduced net income.

Our market is highly competitive and has low barriers to entry.

The market for Internet professional services is relatively new, intensely competitive, rapidly evolving and subject to rapid technological change. In addition, there are relatively low barriers to entry into this market. Because of the rapid changes to, and volatility in, the Internet software and service industry, many well-capitalized companies that may have chosen sectors of the industry that are not competitive with our business, including some of our partners, may refocus their activities and resources. As a result, they could deploy their resources and enter into a business that is competitive with ours.

Many of our current and potential competitors have longer operating histories, more established reputations and potential partner relationships and greater financial, technical, industry and marketing resources than we do. This may place us at a disadvantage to our competitors, which may harm our ability to grow or maintain revenue or generate net income.

Risks Relating to Ownership of Our Stock

The trading volume of our common stock has been limited and, as a result, our stock price has been, and will likely continue to be, volatile.

Our common stock is traded on the NASDAQ SmallCap Market under the symbol "PRFT." The trading volume of our common stock has been limited, and the stock prices have been volatile. Our

common stock price may continue to be highly volatile and may fluctuate as a result of the limited trading volume.

Our officers, directors, and 5% and greater stockholders own a large percentage of our voting securities.

Our executive officers, directors and existing 5% and greater stockholders beneficially own or control greater than 38% of the voting power of our common stock. This concentration of ownership of our common stock may make it difficult for other Perficient stockholders to successfully approve or defeat matters that may be submitted for action by our stockholders. It may also have the effect of delaying, deterring or preventing a change in control of our company.

It may be difficult for another company to acquire us, and this could depress our stock price.

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Provisions of our certificate of incorporation, by-laws and Delaware law could make it difficult for a third party to acquire us, even if doing so would be beneficial to our stockholders. In addition, under our agreement with IBM, we have granted IBM a right of first offer and a right to terminate its agreement with us with respect to any change of control transaction with a company that has a substantial portion of its business in the web application server product and services market, other than a systems integrator or professional services firm. As a result, a potential acquirer may be discouraged from making an offer to buy us.

We may need additional capital in the future, which may not be available to us. The raising of any additional capital may reduce the ownership percentages of our existing shareholders.

We believe our existing line of credit and working capital should provide sufficient resources to satisfy our near term capital requirements. Our existing line of credit facility expires in December 2004. If we are unable to renew our line of credit, we may need to obtain an alternate debt financing facility. In the future we may decide to raise additional funds through public or private debt or equity financing in order to:

take advantage of opportunities, including more rapid expansion or acquisitions of, or investments in, businesses or technologies;

develop new services; or

respond to competitive pressures.

Any additional capital raised through the sale of equity will reduce the ownership percentages of existing shareholders. Furthermore, we cannot be certain that any additional financing we may need will be available on terms favorable to us, or at all. In such case, our business results would suffer.

SPECIAL NOTE REGARDING FORWARD LOOKING STATEMENTS

Some of the statements contained in or considered a part of this annual report on Form 10-KSB that are not purely historical statements discuss future expectations, contain projections of results of operations or financial condition or state other forward-looking information. Those statements are subject to known and unknown risks, uncertainties and other factors that could cause the actual results to differ materially from those contemplated by the statements. The "forward-looking" information is based on various factors and was derived using numerous assumptions. In some cases, you can identify these so-called forward-looking statements by words like "may," "will," "should," "expects," "plans," "anticipates," "believes," "estimates," "predicts," "potential," or "continue" or the negative of those words and other comparable words. You should be aware that those statements only reflect our predictions. Actual events or results may differ substantially. Important factors that could cause our actual results to be materially different from the forward-looking statements are disclosed under the heading "Risks Factors" in this Report on Form 10-KSB. Moreover, neither we nor any other person

12

assumes responsibility for the accuracy and completeness of such statements. We are under no duty to update any of the forward-looking statements after the date of this Report to conform such statements to actual results.

ITEM 2 DESCRIPTION OF PROPERTY

We lease approximately 2,700 square feet of office space in Austin, Texas from CarrAmerica Realty, L.P.. The initial term of the lease is two years from April 2003 with the right to extend the lease for one additional period of two years. We lease approximately 25,952 square feet of office space in the St. Louis, Missouri area from Creve Coeur Development LLC that extends through October 2005. We lease approximately 18,889 square feet of office space in Minneapolis, Minnesota under an agreement with Butler Properties, LLC that extends through May 2007. We also sublease approximately 4,200 square feet of office space in Downers Grove, Illinois from ICS Deloitte Management LLC. The term of the sublease is from September 2003 through May 2009. We also lease office space in London, Ontario under an agreement that expires in 2004.

ITEM 3 LEGAL PROCEEDINGS

We are not currently a party to any material legal proceedings.

ITEM 4 SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The following matters were voted upon at the Annual Meeting of Stockholders held on December 30, 2003, and received the votes set forth below:

- Each of our directors were nominated for reelection and were elected to serve as directors as indicated below. There were no abstentions.

| | For | Withheld |
|-----------------------|------------|-----------------|
| John T. McDonald | 8,775,118 | 490,279 |
| David S. Lundeen | 8,695,506 | 569,891 |
| Dr. W. Frank King | 9,134,112 | 131,285 |
| Philip J. Rosenbaum | 9,133,862 | 131,535 |
| Max D. Hopper | 9,037,766 | 227,631 |
| Robert Pickering, Jr. | 9,254,512 | 10,885 |

- A proposal to ratify the appointment of Ernst & Young, LLP as Perficient's independent auditors for the fiscal year ended December 31, 2003 was approved, receiving 9,130,185 votes FOR and 126,800 votes AGAINST, with 8,412 abstentions.

13

PART II**ITEM 5 MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS**

Our common stock is traded on the Nasdaq SmallCap Market under the symbol "PRFT." Public trading of our common stock commenced on July 29, 1999. Prior to that, there was no public market for our common stock. The following table sets forth, for the periods indicated, the high and low closing price per share of our common stock on the Nasdaq SmallCap Market.

| | High | Low |
|--------------------------------------|-------------|------------|
| Year Ended December 31, 2002: | | |
| First Quarter | \$ 2.25 | \$ 0.95 |
| Second Quarter | 1.65 | 0.90 |
| Third Quarter | 1.61 | 0.43 |
| Fourth Quarter | 2.48 | 0.33 |
| Year Ended December 31, 2003: | | |
| First Quarter | \$ 1.07 | \$ 0.50 |
| Second Quarter | 1.29 | 0.55 |
| Third Quarter | 3.03 | 0.94 |
| Fourth Quarter | 3.82 | 2.15 |

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As of December 31, 2003, there were in excess of 2,400 holders of our common stock. On March 29, 2004, the last sale price reported on the Nasdaq SmallCap Market for our common stock was \$3.73 per share.

We have never declared or paid any cash dividends on our common stock and do not anticipate paying cash dividends in the foreseeable future. Our line of credit currently prohibits the payment of cash dividends without the prior written consent of Silicon Valley Bank. Our Series A Preferred Stock accrued dividends at an annual rate of the prime rate plus 1.5% and our Series B Preferred stock accrued dividends at an annual rate of 8%. On November 10, 2003 all outstanding shares of Series A Preferred Stock and Series B Preferred Stock were automatically converted into common stock, and as a result all accrued dividends were forfeited. During 2003, the Company paid \$45,457 in dividends to certain holders of Series A Preferred Stock that had voluntarily converted their holdings into common stock prior to the date of automatic conversion.

14

Equity Compensation Plan Information

The following table provides information with respect to the equity securities that are authorized for issuance under our compensation plans as of December 31, 2003:

| | (a) | (b) | (c) |
|---|---|---|---|
| | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) |
| Equity compensation plans approved by security holders(1) | 5,234,896 | \$ 2.49 | 677,192 |
| Equity compensation plans not approved by security holders(2)(3)(4) | 106,383 | \$ 0.31 | |
| Total | 5,341,279 | \$ 2.45 | 677,192 |

- (1) Represents 6,189,063 shares authorized for issuance under the Perficient, Inc. 1999 Stock Option/Stock Issuance Plan. The automatic share increase program provides for an increase each year equal to 8% of the outstanding Common Stock on the last trading day in December of the previous year. Pursuant to our automatic share increase program, 1,122,660 additional shares were authorized for issuance under the plan as of January 1, 2004.
- (2) Represents options to purchase 106,383 shares of our Common Stock with an exercise price of \$0.31 per share that were granted in September 2001 to John T. McDonald, our Chief Executive Officer and Chairman of the Board, in lieu of a \$50,000 cash bonus.
- (3) In connection with the merger of Javelin Solutions, Inc. into our wholly-owned subsidiary and the merger of Primary Webworks, Inc. d/b/a Vertecon, Inc. into our wholly-owned subsidiary, we assumed Javelin's stock option plan and Vertecon's stock option plan and all the outstanding options thereunder. Each outstanding option under the Javelin plan and the Vertecon plan was converted into an option to purchase our Common Stock. No future awards may be made under the respective plans. These amounts exclude (i) options to purchase approximately 182,106 shares of our Common Stock exercisable for a weighted-average exercise price of \$1.08 per share

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issued in connection with our assumption of the Javelin plan and (ii) options to purchase approximately 64,291 shares of our Common Stock exercisable for a weighted average exercise price of \$4.40 per share issued in connection with our assumption of the Vertecon plan.

(4)

These amounts exclude options to purchase 91,817 shares of our Common Stock with an exercise price of \$3.36 per share and options to purchase 46,699 shares of our Common Stock with an exercise price of \$0.02 per share that were issued to certain employees of Compete, Inc. and assumed in connection with our May 2000 acquisition of Compete, Inc.

ITEM 6 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 our financial statements and notes thereto and the other financial information included elsewhere in this annual report on Form 10-KSB. In addition to historical information, this management's discussion and analysis of financial condition and results of operations and other parts of

15

this annual report contain forward-looking information that involves risks and uncertainties. Our actual results could differ materially from those indicated in such forward-looking information as a result of certain factors, including but not limited to, those set forth under Risk Factors and elsewhere in this annual report.

We were incorporated in September 1997 and began generating revenue in February 1998. We generate revenue from professional services performed for our end-user customers, and the end-user customers of our software partners. Additionally, we generate revenue from reselling software.

In August 2003, we entered into a one-year extension of our existing services agreement with IBM under which we provide deployment, integration and training services to IBM's WebSphere customers. The current agreement will terminate on September 1, 2004. Prior to that date, IBM has the right to terminate the agreement upon five (5) days prior written notice. Revenue from IBM accounted for approximately 35% of total revenue for both 2002 and 2003, and accounts receivable from IBM comprise approximately 35% and 37% of gross accounts receivable as of December 31, 2002 and December 31, 2003, respectively. Accordingly, any deterioration in our relationship with IBM could have a material adverse effect on our consulting revenue and net income. Our agreements generally do not obligate our customers to use our services for any minimum amount, or at all, and our customers may use the services of our competitors.

Revenue is derived primarily from professional services provided on a time and materials basis, with the remaining revenue provided from fixed fee engagements and software sales. For time and material contracts, revenue is recognized and billed by multiplying the number of hours expended by our professionals in the performance of the contract by the established billing rates. For fixed fee projects, revenue is generally recognized using the proportionate performance method. Provisions for estimated losses on uncompleted contracts are made on a contract-by-contract basis and are recognized in the period in which such losses are determined. Billings in excess of costs plus earnings are classified as deferred revenues. On many projects we are also reimbursed for out-of-pocket expenses such as airfare, lodging and meals. These reimbursements are included as a component of revenue. Revenue from resold software is recorded on a gross basis provided we act as a principal in the transaction. In the event we do not meet the requirements to be considered a principal in the software resale transaction and act as an agent, the revenue is recorded on a net basis.

Our revenue and operating results are subject to substantial variations based on our customers' expenditures and the frequency with which we are chosen to perform services for our customers. Revenue from any given customer will vary from period to period. We expect, however, that IBM will remain a significant customer for the foreseeable future. To the extent that IBM, or any other significant customer, uses less of our services or terminates its relationship with us, our revenue could decline substantially.

Our gross margins are affected by trends in the utilization rate of our professionals (defined as the percentage of our professionals' time billed to customers, divided by the total available hours in the respective period), the salaries we pay our consulting professionals, and the average rate we receive from our customers. If a project ends earlier than scheduled or we retain professionals in advance of receiving project assignments, our utilization rate will decline and adversely affect our gross margins.

During 2002, we implemented certain workforce reductions and office closures resulting in charges of \$579,427, consisting of severance pay and related benefits for former employees in addition to the costs associated with the closure of our London office. As part of these restructurings, we reduced our workforce by a total of 30 employees, of which 17 were technology professionals and 13 were involved in

selling, general administration and marketing. As of December 31, 2002, approximately \$228,000 of restructuring costs is included in other current liabilities, all of which was paid during 2003. There was no restructuring expense during 2003.

Results of Operations

Year Ended December 31, 2002 Compared to Year Ended December 31, 2003

Revenue. Total gross revenue increased from \$22,450,284 for the year ended December 31, 2002 to \$30,191,922 for the year ended December 31, 2003. Services revenue increased from \$20,391,587 in 2002 to \$24,534,617 in 2003. The increase in services revenue resulted in part from the additional headcount related to the April 2002 acquisitions of Vertecon and Javelin, which impacted revenue for the full period in 2003, as well as the use of additional subcontractors during 2003. The increase in services revenue is also the result of an improvement in employee utilization rates. For the years ended December 31, 2002 and 2003, 35% of our revenue was derived from IBM. Revenue from resold software increased from \$402,889 in 2002 to \$3,786,864 in 2003. Revenue from reselling software is expected to fluctuate between periods depending on our customers' demand for such software. Generally we are reimbursed for our out-of-pocket expenses incurred in connection with our customers' consulting projects. Reimbursable expenses increased from \$1,655,808 in 2002 to \$1,870,441 in 2003. The aggregate amount of reimbursed expenses will fluctuate depending on the location of our customers, the general fluctuation of travel costs such as airfare, and the total number of our projects that require travel.

Cost of Revenue. Cost of revenue, consisting of salaries and benefits associated with our technology professionals, subcontractor costs, cost of resold software, and reimbursed and project related expenses, increased from \$13,539,219 for the year ended December 31, 2002 to \$18,816,509 for the year ended December 31, 2003. The increase in cost of revenue is due to the increase in average salaries as compared to the same period in 2002 as well as an increase in the number of billable employees, and the increase in headcount as a result of the acquisitions of Vertecon and Javelin in April 2002 being included in the full year for 2003. Subcontractor costs increased from \$449,000 in 2002 to \$977,000 in 2003. In addition, costs associated with resold software increased by \$2,737,855 in connection with the increased software revenue in 2003 compared to 2002. Reimbursable expenses will fluctuate with the associated revenue because our customers reimburse us for these costs. Other project related expenses consist of travel and other out-of-pocket costs that are not reimbursed by our customers. These expenses will fluctuate depending generally on outside factors including the costs of travel and the location of our customers.

Gross Margin. Gross margin increased from \$8,911,065 for the year ended December 31, 2002 to \$11,375,413 for the year ended December 31, 2003. Gross margin as a percentage of revenue decreased slightly from 40% in 2002 to 38% in 2003. The decrease in gross margin as a percentage of revenue is primarily due to the increase in average salaries as well as the increase in software resales, which typically yield a lower margin than our services revenue. Services gross margin was 43% in 2002 and 2003. Software gross margin was 15% in 2002 and 19% in 2003. Gross margins can fluctuate depending upon a number of factors including our ability to successfully manage the utilization rates and salaries of our consultants, and the rates we can charge for our services.

Selling, General and Administrative. Selling, general and administrative expenses consist of salaries and benefits for sales, executive and administrative employees, training, marketing activities, investor relations, recruiting, non-reimbursable travel costs and expenses and miscellaneous expenses. Selling, general and administrative expenses decreased from \$8,327,010 for the year ended December 31, 2002 to \$7,857,081 for the year ended December 31, 2003. The decrease is the result of deliberate cost reductions including: a \$292,000 reduction in administrative salaries and benefits, a \$189,000 reduction in computer equipment leasing costs and other information technology related expenses, which were partially offset by a \$151,000 increase in office costs resulting from the inclusion of Javelin and Vertecon expenses for the full period in 2003, and a \$150,000 increase in costs related to the 2003 company meeting. Selling, general and administrative expenses as a percentage of revenue decreased from 37% for the year ended December 31, 2002 to 26% for the year ended December 31, 2003. The

decrease in selling, general and administrative expenses as a percent of revenue is the result of an increase in software resales, for which there are generally less incremental costs, as well as a general reduction of costs in proportion to total revenue during the applicable periods.

Stock Compensation. Stock compensation expense consists of non-cash compensation arising from certain option grants to employees with exercise prices below fair market value at the date of grant, option grants made to outside consultants, and compensation expense associated with unvested stock options assumed in business combinations. Stock compensation expense decreased from \$240,688 during the year ended December 31, 2002 to \$135,927 for the year ended December 31, 2003 due to the fact that most unearned stock compensation

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became fully amortized to expense during 2003. Deferred stock compensation remaining at December 31, 2003 totaled \$26,623 and is expected to be amortized to expense in its entirety during 2004.

Depreciation. Depreciation expense decreased slightly from \$687,570 during 2002 to \$670,436 during 2003. The decrease is due to a general decrease in purchases along with an increasing number of fully depreciated assets.

Restructuring. During 2002, we implemented certain workforce reductions and office closures resulting in charges of \$579,427, consisting of severance pay and related benefits for former employees as well as costs associated with the closure of the London office. We recognized \$118,000 of restructuring expense during 2002 related to the closure of the London office, which consisted of severance and benefits, lease commitments, as well as expected losses on the disposal of fixed assets, attorney and accounting fees, and other costs. As part of these restructurings, we reduced our workforce by a total of 30 employees, of which 17 were technology professionals and 13 were involved in selling, general administration and marketing. As of December 31, 2002, approximately \$228,000 of restructuring costs are included in other current liabilities, all of which were paid during 2003. There was no workforce restructuring during 2003.

Intangibles Amortization. Intangibles amortization expense consists of amortization of intangibles arising from our acquisitions of Compete, Inc. in May 2000, Core Objective, Inc. in November 2000, and Vertecon and Javelin in April 2002. Amortization decreased from \$1,285,524 during the year ended December 31, 2002 to \$610,421 during the year ended December 31, 2003. The decrease in amortization expense reflects the end of the assigned three-year useful life for the Compete and Core Objective intangible assets.

Interest Expense Interest expense was \$203,569 during the year ended December 31, 2002 compared to \$285,938 for the year ended December 31, 2003. The increase in interest expense is due to increases of approximately \$31,000 related to capital leases, approximately \$9,000 related to imputed interest expense on the notes issued to the Javelin shareholders, and approximately \$43,000 in bank audit fees, letter of credit renewal fees, and other costs associated with our line of credit facility.

Provision for Income Taxes. Our 2003 income tax provision was accrued for federal, state and foreign income tax at the applicable statutory rates. Although we have certain net operating loss carryforwards, substantially all of these losses relate to acquired entities and are subject to limitations due to "Change in control" provisions in the Internal Revenue Code. As such, the deferred tax asset resulting from these net operating loss carryforwards have a valuation allowance against them, and our tax provision does not materially benefit from these net operating loss carryforwards. There was no tax provision for 2002 as a result of the net loss for that period.

Liquidity And Capital Resources

We have a line of credit arrangement with Silicon Valley Bank that will expire in December 2004. The agreement allows us to borrow up to 80% of eligible accounts receivable as defined in the

18

agreement up to a maximum of \$6,000,000. We are also required to comply with certain financial covenants under this agreement which require us to maintain a minimum tangible net worth of at least \$3,000,000 and to maintain a ratio of cash plus accounts receivable to current liabilities of at least 1.25 to 1.00 through March 31, 2004, at which time the ratio will increase to at least 1.50 to 1.00. Borrowings under the agreement bear interest at the bank's prime rate plus 1.00% (5.0% as of December 31, 2003). As of December 31, 2003, there were no amounts outstanding under this line of credit and available borrowings totaled \$3,072,591.

In connection with the acquisitions of Javelin and Vertecon in April 2002, we were required to establish various letters of credit totaling \$550,000 to serve as collateral for certain office space and equipment leases. These letters of credit reduce the borrowings available under our line of credit facility with Silicon Valley Bank. The letters of credit totaling \$300,000 will remain in effect through 2005, and the remaining letter of credit of \$250,000 will remain in effect through 2007.

Cash provided by operations for the year ended December 31, 2003 was \$1,885,477. As of December 31, 2003, we had \$1,989,395 in cash and working capital of \$4,013,373.

On December 21, 2001, we entered into a Convertible Preferred Stock Purchase agreement under which we sold 1,984,000 shares of Series A Convertible Preferred Stock for a purchase price of \$1.00 per share. In November 2003, all shares of then outstanding Series A Preferred Stock were automatically converted into 2,003,840 shares of common stock. We also issued Warrants to purchase up to 992,000 shares of our common stock in connection with this issuance. As a result of the Series B Preferred Stock issuance (described below), the number of warrants issued to the Series A investors increased to 1,001,604 and the exercise price was adjusted to \$1.98 per share.

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We entered into a Convertible Preferred Stock Purchase Agreement, dated as of June 26, 2002, with 2M Technology Ventures, L.P. under which we sold 1,111,000 shares of our Series B Convertible Preferred Stock to 2M for a purchase price of approximately \$0.90 per share. In November 2003, the Series B Preferred stock was automatically converted into 1,111,000 shares of common stock. We have also issued to 2M, a Warrant to purchase up to 555,500 shares of our Common Stock in connection with this sale of Series B Preferred Stock. In February 2004, 2M exercised 277,750 warrants.

2M had the option to purchase up to an additional 1,666,500 shares of our Series B Convertible Preferred Stock at a price of approximately \$0.90 per share exercisable on or before June 26, 2003. 2M would have received a Warrant to purchase one share of our common stock for every two shares of Series B Preferred Stock it purchases pursuant to the option. The option to 2M expired unexercised in June 2003.

In connection with the acquisition of Javelin, we issued \$1.5 million in notes, of which \$1 million of the notes are payable in four equal annual installments on the anniversary of the closing date of the acquisition. The other \$500,000 is payable in eight equal quarterly installments that commenced in July 2002. Accordingly, we paid \$125,000 in 2002 and \$500,000 in 2003. We expect to make payments on these notes totaling \$375,000 in 2004, \$250,000 in 2005, and \$250,000 in 2006.

We have incurred commitments to make future payments under contracts such as leases and certain long-term liabilities. Maturities under these contracts are set forth in the following table of December 31, 2003, in thousands:

| | Payments due by Period | | | | | |
|-------------------------------|------------------------|----------|--------|--------|-------|------------|
| | 2004 | 2005 | 2006 | 2007 | 2008 | Thereafter |
| Operating lease obligations | \$ 1,183 | \$ 1,237 | \$ 574 | \$ 243 | \$ 87 | \$ 35 |
| Note payable to Related Party | \$ 333 | \$ 226 | \$ 244 | \$ | \$ | \$ |

We expect to fund our operations during 2004 from cash generated from operations and short-term borrowings as necessary from our line of credit facility. We believe our existing working

19

capital and line of credit should provide sufficient resources to satisfy our capital requirements through at least 2004. The amount of borrowings available to us is based on a percentage of our receivables. If our capital is insufficient to fund our activities in either the short or long term, we may need to raise additional funds. In the ordinary course of business, we may engage in discussions with various persons in connection with additional financing. If we raise additional funds through the issuance of equity securities, our existing stockholders' percentage ownership will be diluted. These equity securities may also have rights superior to our common stock. Additional debt or equity financing may not be available when needed or on satisfactory terms. If adequate funds are not available on acceptable terms, we may be unable to expand our services, respond to competition, pursue acquisition opportunities or continue our operations.

Critical Accounting Policies

Consulting revenues are comprised of revenue from professional services fees recognized primarily on a time and materials basis as performed. For fixed fee engagements, revenue is recognized using the proportionate performance method (based on the ratio of hours expended to total estimated hours). Provisions for estimated losses on uncompleted contracts are made on a contract-by-contract basis and are recognized in the period in which such losses are determined. Billings in excess of costs plus earnings are classified as deferred revenues. Our normal payment terms are net 30 days. Our agreement with IBM provides for net 60 days payment terms. Reimbursements for out-of-pocket expenses are included in gross revenue. Revenue from resold software is recorded on a gross basis provided that we act as the principal in the transaction. In the event we do not meet the requirements to be considered the principal in the software resale transaction, we record the revenue on a net basis. There is no effect on net income between recording the software sales on a gross basis versus a net basis. We record an expense for the expected losses on uncollectible accounts receivable each period based on known facts and circumstances for the respective period.

We adopted Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* ("Statement 142") on January 1, 2002. In accordance with Statement 142, we replaced the ratable amortization of goodwill and other indefinite-lived intangible assets with a periodic review and analysis of such intangibles for possible impairment. In accordance with Statement 142, we assess our goodwill on October 1 of each year or more frequently if events or changes in circumstances indicate that goodwill might be impaired.

Business acquisitions typically result in goodwill and other intangible assets, and the recorded values of those assets may become impaired in the future. The determination of the value of such intangible assets requires us to make estimates and assumptions that affect our consolidated financial statements. We assess potential impairments to intangible assets on an annual basis or when there is evidence that events or changes in

circumstances indicate that the carrying amount of an asset may not be recovered. Our judgments regarding the existence of impairment indicators and future cash flows related to intangible assets are based on operational performance of the acquired businesses, market conditions and other factors. Future events could cause us to conclude that impairment indicators exist and that goodwill associated with the acquired businesses is impaired. Any resulting impairment loss could have an adverse impact on our results of operations by decreasing net income.

ITEM 7 CONSOLIDATED FINANCIAL STATEMENTS

The financial statements required by this Item 7 are listed in Item 13(a)(1) and begin at page F-1 of this Report.

20

ITEM 8 CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURES

Not applicable.

ITEM 8A CONTROLS AND PROCEDURES

We performed an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, our management, including our Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective as of December 31, 2003.

There have been no changes in internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect our internal control over financial reporting.

PART III

Certain information required by Part III is omitted from this report because we intend to file a definitive Proxy Statement pursuant to Regulation 14A no later than April 29, 2004, and certain information to be included therein is incorporated herein by reference.

ITEM 9 DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS OF REGISTRANT

The information required by this Item is incorporated by reference to the Proxy Statement under the sections captioned "Proposal 1 Election of Directors," "Executive Compensation" and "Compliance with Section 16(a) of the Securities Exchange Act of 1934."

ITEM 10 EXECUTIVE COMPENSATION

The information required by this Item is incorporated by reference to the Proxy Statement under the sections captioned "Proposal 1 Election of Directors," "Executive Compensation" and "Compliance with Section 16(a) of the Securities Exchange Act of 1934."

ITEM 11 SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information under the caption "Ownership of Securities," appearing in the Proxy Statement, is incorporated herein by reference.

ITEM 12 CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

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The information under the heading "Certain Transactions," appearing in the Proxy Statement, is incorporated herein by reference.

ITEM 13 EXHIBITS, FINANCIAL STATEMENTS AND REPORTS ON FORM 8-K

(a)

(1) Financial Statements

21

The following consolidated financial statements of the Company are filed as part of this Annual Report on Form 10-KSB as follows:

| | |
|---|-----|
| Report of Independent Auditors | F-2 |
| Consolidated Balance Sheets at December 31, 2002 and 2003 | F-3 |
| Consolidated Statements of Operations for the years ended December 31, 2002 and 2003 | F-4 |
| Consolidated Statements of Changes in Stockholders' Equity for the years ended December 31, 2002 and 2003 | F-5 |
| Consolidated Statements of Cash Flows for the years ended December 31, 2002 and 2003 | F-6 |
| Notes to Consolidated Financial Statements | F-7 |

(a)

(2) Financial Statement Schedules

Not applicable.

(a)

(3) Exhibits

| Exhibit Number | Description |
|----------------|---|
| 2.1## | Agreement and Plan of Merger, dated as of September 30, 2001, by and among Perficient, Inc., Perficient Vertecon, Inc., Primary Webworks, Inc. d/b/a Vertecon, Inc., and certain shareholders of Vertecon, Inc. |
| 2.2## | Agreement and Plan of Merger, dated as of October 26, 2001, by and among Perficient, Inc., Perficient Javelin, Inc., Javelin Solutions, Inc. and the shareholders of Javelin Solutions, Inc. |
| 3.1+ | Certificate of Incorporation of Perficient, Inc. |
| 3.2+ | Bylaws of Perficient Inc. |
| 4.1+ | Specimen Certificate for shares of common stock. |
| 4.2+ | Warrant granted to Gilford Securities Incorporated. |
| 4.3+++ | Certificate of Designation, Rights and Preferences of Series A Preferred Stock. |
| 4.4+++ | Form of Common Stock Purchase Warrant. |
| 4.5### | Certificate of Designation, Rights and Preferences of Series B Preferred Stock. |
| 4.6### | Form of Common Stock Purchase Warrant. |
| 10.1** | 1999 Stock Option/Stock Issuance Plan, including all amendments thereto. |

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| Exhibit Number | Description |
|-------------------|---|
| 10.2## | Employment Agreement between the Company and John T. McDonald. |
| 10.3+ | Form of Indemnity Agreement between Perficient and its directors and officers. |
| 10.4* | Agreement and Plan of Merger, dated as of December 10, 1999, by and among the Registrant, Perficient Acquisition Corp., LoreData, Inc. and John Gillespie (including amendments thereto). |
| 10.5** | Agreement and Plan of Merger, dated as of February 16, 2000 by and among the Registrant, Perficient Compete, Inc., Compete Inc., and the Shareholders of Compete, Inc. |
| 10.6*** | Registration Rights Agreement, dated as of January 3, 2000 between Perficient and John Gillespie. |

22

| | |
|----------|---|
| 10.7*** | Subcontract Agreement, dated as of November 4, 1999 between Perficient and Plumtree, Inc. |
| 10.8++ | Lease by and between HUB Properties Trust and Perficient. |
| 10.9# | Agreement dated October 10, 2000 between Perficient and International Business Machines, Inc. |
| 10.10## | Employment Agreement with Jeffrey Davis |
| 10.11## | Employment Agreement with Dale Klein |
| 10.12## | Form of Voting Agreement regarding Vertecon Stock Issuance |
| 10.13## | Form of Voting Agreement regarding Javelin Stock Issuance |
| 10.14## | Form of Voting Agreement regarding Series A Preferred Stock and Warrants |
| 10.15+++ | Convertible Stock Purchase Agreement, dated as of December 21, 2001 by and among Perficient and the Investors listed on Schedule 1 thereto |
| 10.16### | Convertible Stock Purchase Agreement, dated as of June 26, 2002 by and between Perficient and the Investor listed on Schedule 1 thereto. |
| 10.17### | First Amended and Restated Investor Rights Agreement dated as of June 26, 2002 by and between Perficient, Inc. and the Investors listed on Exhibits A and B thereto. |
| 10.18 | Amendment dated August 28, 2003 to existing agreement dated August 17, 2000 between International Business Machines Corporation and Perficient, Inc. |
| 10.19 | Employment agreement with John T. McDonald and Perficient, Inc. dated January 1, 2004. |
| 21.1## | Subsidiaries. |
| 23.1 | Consent of Ernst & Young LLP. |
| 31.1 | Certification to the Securities and Exchange Commission by Small Business Issuer's Chief Executive Officer and Chief Financial Officer, as required by Section 302 of the Sarbanes-Oxley Act of 2002. |

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32.1 Certification of Chief Executive Officer and Chief Financial Officer of Perficient, Inc. pursuant to 18 U.S.C. Section 1350.

99.1 Loan and security agreement dated December 5, 2003 between Silicon Valley Bank and Perficient, Inc.

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Previously filed with the Securities and Exchange Commission as an Exhibit to the Company's Registration Statement on Form SB-2 (File No. 333-78337) declared effective on July 28, 1999 by the Securities and Exchange Commission and incorporated herein by reference.

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Previously filed with the Securities and Exchange Commission as an Exhibit to the Company's Registration Statement on Form SB-2 (File No. 333-35948) declared effective on July 6, 2000 by the Securities and Exchange Commission and incorporated herein by reference.

+++

Previously filed with the Securities and Exchange Commission as an Exhibit to the Company's Current Report on Form 8-K filed on January 17, 2002 and incorporated herein by reference.

*

Previously filed with the Securities and Exchange Commission as an Exhibit to the Company's Current Report on Form 8-K filed on January 14, 2000 and incorporated herein by reference.

23

**

Previously filed with the Securities and Exchange Commission as an Appendix to the Company's Proxy Statement filed on April 7, 2000 and incorporated herein by reference.

Previously filed with the Securities and Exchange Commission as an Exhibit to the Company's Annual Report on Form 10-KSB filed on March 30, 2000 and incorporated herein by reference.

#

Previously filed with the Securities and Exchange Commission as an Exhibit to the Company's Annual Report on Form 10-KSB filed on April 2, 2001 and incorporated herein by reference.

##

Previously filed with the Securities and Exchange Commission as an Exhibit to the Company's Registration Statement on Form S-4 (File No. 333-73466) incorporated herein by reference.

###

Previously filed with the Securities and Exchange Commission as an Exhibit to the Company's Current Report on Form 8-K filed on July 18, 2002 and incorporated by reference herein.

(b)

Reports on Form 8-K

On October 20, 2003, we filed a Current Report on Form 8-K pursuant to Item 5 (Other Events) to report the voluntary resignation of Michael J. Cromwell, III as a member of the Board of Directors of Perficient, Inc.

On October 28, 2003, we filed a Current Report on Form 8-K pursuant to Item 12 (Results of Operations and Financial Condition) to report our financial results for the quarter ended September 30, 2003.

On November 3, 2003, we filed a Current Report on Form 8-K pursuant to Item 9 (Regulation FD Disclosure) to announce updated guidance on revenue for the year ended December 31, 2003, and announced revenue guidance for the quarter ended December 31, 2003.

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We filed a Form 8-K with the Securities and Exchange Commission on November 17, 2003 to report the automatic conversion of outstanding Series A Preferred Stock and Series B Preferred Stock into approximately 2.9 million shares of Perficient common stock.

ITEM 14 PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information under the caption "Principal Accountant Fees and Services," appearing in the Proxy Statement, is incorporated herein by reference.

24

SIGNATURES

In accordance with Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

PERFICIENT, INC.
(Registrant)

/s/ JOHN T. MCDONALD

John T. McDonald
Chief Executive Officer

March 30, 2004

Date

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

| <u>Name</u> | <u>Title</u> | <u>Date</u> |
|---|--|----------------|
| <u>/s/ JOHN T. MCDONALD</u> John T. McDonald | Chief Executive Officer and Chairman of the Board (Principal Executive Officer) | March 30, 2004 |
| <u>/s/ MICHAEL D. HILL</u> Michael D. Hill | Chief Financial Officer | March 30, 2004 |
| <u>/s/ DAVID S. LUNDEEN</u> David S. Lundeen | Director | March 30, 2004 |
| <u>/s/ DR. W. FRANK KING</u> Dr. W. Frank King | Director | March 30, 2004 |
| <u>/s/ PHILIP J. ROSENBAUM</u> | Director | March 30, 2004 |

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| Name | Title | Date |
|------------------------------|----------|----------------|
| Philip J. Rosenbaum | | |
| /s/ ROBERT E. PICKERING, JR. | Director | March 30, 2004 |
| Robert E. Pickering, Jr. | | |
| /s/ MAX HOPPER | Director | March 30, 2004 |
| Max Hopper | | |

25

PERFICIENT, INC.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

| | |
|---|-----|
| Report of Independent Auditors | F-2 |
| Consolidated Balance Sheets at December 31, 2002 and 2003 | F-3 |
| Consolidated Statements of Operations for the years ended December 31, 2002 and 2003 | F-4 |
| Consolidated Statements of Changes in Stockholders' Equity for the years ended December 31, 2002 and 2003 | F-5 |
| Consolidated Statements of Cash Flows for the years ended December 31, 2002 and 2003 | F-6 |
| Notes to Consolidated Financial Statements | F-7 |

F-1

REPORT OF INDEPENDENT AUDITORS

The Board of Directors and Stockholders
Perficient, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of Perficient, Inc. and Subsidiaries as of December 31, 2002 and 2003, and the related consolidated statements of operations, changes in stockholders' equity and cash flows for the years then ended. 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. 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, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Perficient, Inc. and Subsidiaries at December 31, 2002 and 2003, and the consolidated results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States.

/s/ Ernst & Young LLP

Austin, Texas
January 9, 2004

F-2

PERFICIENT, INC.

CONSOLIDATED BALANCE SHEETS

| | December 31, | |
|---|---------------|---------------|
| | 2002 | 2003 |
| ASSETS | | |
| Current assets: | | |
| Cash | \$ 1,525,002 | \$ 1,989,395 |
| Accounts receivable, net of allowance for doubtful accounts of \$661,248 in 2002 and \$622,995 in 2003 | 3,938,373 | 5,534,607 |
| Other current assets | 382,542 | 297,058 |
| Total current assets | 5,845,917 | 7,821,060 |
| Property and equipment: | | |
| Hardware | 1,496,429 | 1,685,577 |
| Furniture and fixtures | 726,861 | 655,662 |
| Leasehold improvements | 234,285 | 234,671 |
| Software | 248,697 | 263,059 |
| Accumulated depreciation | (1,495,254) | (2,139,824) |
| Net property and equipment | 1,211,018 | 699,145 |
| Net intangible assets | 12,380,039 | 11,693,834 |
| Other noncurrent assets | 156,129 | 45,944 |
| Total assets | \$ 19,593,103 | \$ 20,259,983 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 426,686 | \$ 129,895 |
| Line of credit | 540,011 | |
| Current portion of capital lease obligation | 235,034 | |
| Other current liabilities | 2,304,433 | 3,310,872 |
| Current portion of note payable to related party | 485,477 | 366,920 |
| Total current liabilities | 3,991,641 | 3,807,687 |
| Note payable to related party, less current portion | 745,318 | 436,258 |
| Capital lease obligation, less current portion | 334,661 | |
| Total liabilities | 5,071,620 | 4,243,945 |
| Stockholders' equity: | | |
| Preferred stock, \$0.001 par value; 8,000,000 shares authorized; 3,095,000 shares in 2002 and 0 shares in 2003 issued and outstanding | 3,095 | |
| Common stock, \$0.001 par value; 40,000,000 shares authorized; 10,537,226 shares in 2002 and 14,033,246 shares in 2003 issued and outstanding | 10,537 | 14,033 |
| Additional paid-in capital | 75,993,344 | 76,315,780 |
| Unearned stock compensation | (164,773) | (26,623) |
| Accumulated other comprehensive loss | (35,366) | (51,830) |
| Retained deficit | (61,285,354) | (60,235,322) |

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| | December 31, | |
|--|---------------|---------------|
| | 2002 | 2003 |
| Total stockholders' equity | 14,521,483 | 16,016,038 |
| Total liabilities and stockholders' equity | \$ 19,593,103 | \$ 20,259,983 |

See accompanying notes.

F-3

PERFICIENT, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

| | Year Ended December 31, | |
|--|-------------------------|---------------------|
| | 2002 | 2003 |
| Revenue | | |
| Services | \$ 20,391,587 | \$ 24,534,617 |
| Software | 402,889 | 3,786,864 |
| Reimbursable expenses | 1,655,808 | 1,870,441 |
| Total revenue | 22,450,284 | 30,191,922 |
| Cost of revenue | | |
| Project personnel costs | 11,210,272 | 13,411,762 |
| Software costs | 343,039 | 3,080,894 |
| Reimbursable expenses | 1,655,808 | 1,870,441 |
| Other project related expenses | 330,100 | 453,412 |
| Total cost of revenue | 13,539,219 | 18,816,509 |
| Gross margin | 8,911,065 | 11,375,413 |
| Selling, general and administrative | 8,327,010 | 7,857,081 |
| Stock compensation | 240,688 | 135,927 |
| Depreciation | 687,570 | 670,436 |
| Intangibles amortization | 1,285,524 | 610,421 |
| Restructuring, severance and other | 579,427 | |
| Income (loss) from operations | (2,209,154) | 2,101,548 |
| Interest income | 17,732 | 3,286 |
| Interest expense | (203,569) | (285,938) |
| Other | (53) | (13,459) |
| Income (loss) before income taxes | (2,395,044) | 1,805,437 |
| Provision for income taxes | | 755,405 |
| Net income (loss) | \$ (2,395,044) | \$ 1,050,032 |

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| | Year Ended December 31, | |
|--|-------------------------|------------|
| | 2002 | 2001 |
| Beneficial conversion charge on preferred stock | (1,672,746) | |
| Accretion of dividends on preferred stock | (163,013) | (157,632) |
| Net income (loss) available to common stockholders | \$ (4,230,803) | \$ 892,400 |
| Basic net income (loss) per share | \$ (0.53) | \$ 0.08 |
| Diluted net income (loss) per share | \$ (0.53) | \$ 0.07 |

See accompanying notes.

F-4

PERFICIENT, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

| | Preferred Stock | | Common Stock | | Subscription Receivable | Warrants | Additional Paid-in Capital | Unearned Stock Compen- sation | Accumulated Other Comprehensive Loss | Retained Deficit | Total Shareholders' Equity |
|---|-----------------|--------|--------------|----------|----------------------------|----------|----------------------------------|--|---|---------------------|----------------------------------|
| | Shares | Amount | Shares | Amount | | | | | | | |
| Balance at January 1, 2002 | | \$ | 6,288,566 | \$ 6,289 | | | \$ 66,140,446 | \$ (348,021) | \$ (72,103) | \$ (58,890,310) | \$ 6,836,301 |
| Issuance of common stock and options in purchase of businesses | | | 4,210,799 | 4,211 | | | 7,213,875 | (266,173) | | | 6,951,913 |
| Issuance of Series A preferred stock, net of amount held in escrow | 1,984,000 | 1,984 | | | (1,984,000) | | 1,982,016 | | | | |
| Issuance of warrants in connection with Series A preferred stock issuance | | | | | | 426,560 | (426,560) | | | | |
| Release of preferred stock proceeds from escrow | | | | | 1,984,000 | | | | | | 1,984,000 |
| Issuance cost for Series A preferred stock | | | | | | 6,595 | (109,040) | | | | (102,445) |
| Issuance of Series B preferred stock | 1,111,000 | 1,111 | | | | | 998,889 | | | | 1,000,000 |
| Issuance cost for Series B preferred stock | | | | | | | (38,284) | | | | (38,284) |
| Issuance of warrants in connection with Series B preferred stock issuance | | | | | | 170,085 | (170,085) | | | | |

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| | Preferred Stock | | Common Stock | | Unearned Stock Compensation | | Accumulated Other Comprehensive Loss | | | | |
|---|-----------------|----------------------|--------------|------------------|-----------------------------|-------------------|--------------------------------------|--------------------|--------------------|------------------------|----------------------|
| Stock options exercised | | | | 37 | 7,580 | | | 7,617 | | | |
| Deferred stock compensation | | | 37,861 | | (208,733) | 208,733 | | | | | |
| Amortization of unearned compensation | | | | | | 240,688 | | 240,688 | | | |
| Foreign currency translation adjustment | | | | | | | 36,737 | 36,737 | | | |
| Net loss | | | | | | | (2,395,044) | (2,395,044) | | | |
| Total comprehensive loss | | | | | | | | (2,358,307) | | | |
| Balance at December 31, 2002 | 3,095,000 | \$ 3,095 | 10,537,226 | \$ 10,537 | \$ 603,240 | \$ 75,390,104 | \$ (164,773) | \$ (35,366) | \$ (61,285,354) | \$ 14,521,483 | |
| Conversion of preferred stock | (3,095,000) | (3,095) | 3,114,840 | 3,115 | | (20) | | | | | |
| Forfeiture of merger consideration | | | (44,787) | (45) | | (64,448) | | | | (64,493) | |
| Series A dividend payment | | | | | | (45,457) | | | | (45,457) | |
| Other | | | 10,327 | 10 | | 10,215 | | | | 10,225 | |
| Warrants exercised | | | 151,500 | 151 | (64,500) | 364,349 | | | | 300,000 | |
| Stock options exercised | | | 264,140 | 265 | | 133,185 | | | | 133,450 | |
| Deferred stock compensation | | | | | (2,223) | 2,223 | | | | | |
| Amortization of unearned compensation | | | | | | | 135,927 | | | 135,927 | |
| Preferred stock issuance costs | | | | | (8,665) | | | | | (8,665) | |
| Foreign currency translation adjustment | | | | | | | (16,464) | | | (16,464) | |
| Net income | | | | | | | | 1,050,032 | | 1,050,032 | |
| Total comprehensive income | | | | | | | | | | 1,033,568 | |
| Balance at December 31, 2003 | | \$ 14,033,246 | | \$ 14,033 | | \$ 538,740 | \$ 75,777,040 | \$ (26,623) | \$ (51,830) | \$ (60,235,322) | \$ 16,016,038 |

See accompanying notes.

F-5

PERFICIENT, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Year Ended December 31,

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| | 2002 | 2003 |
|--|----------------|--------------|
| OPERATING ACTIVITIES | | |
| Net income (loss) | \$ (2,395,044) | \$ 1,050,032 |
| Adjustments to reconcile net income (loss) to net cash provided by operations: | | |
| Depreciation | 687,570 | 670,436 |
| Intangibles amortization | 1,285,524 | 610,421 |
| Non-cash stock compensation | 240,688 | 135,927 |
| Non-cash interest expense | 63,295 | 72,383 |
| Non-cash interest income | (11,017) | |
| Loss on disposal of assets | 11,341 | 30,954 |
| Changes in operating assets and liabilities (net of the effect of acquisitions): | | |
| Accounts receivable | 887,275 | (1,577,259) |
| Other assets | (85,167) | 199,753 |
| Accounts payable | 149,608 | (297,185) |
| Other liabilities | (476,737) | 990,015 |
| Net cash provided by operating activities | 357,336 | 1,885,477 |
| INVESTING ACTIVITIES | | |
| Purchase of property and equipment | (167,323) | (191,207) |
| Purchase of businesses, net of cash acquired | (725,848) | |
| Payments on Javelin notes | (125,000) | (500,000) |
| Advances to Vertecon | (200,000) | |
| Proceeds from disposal of assets | 1,700 | 1,950 |
| Net cash used in investing activities | (1,216,471) | (689,257) |
| FINANCING ACTIVITIES | | |
| Payments on capital lease obligation | (352,575) | (569,695) |
| Proceeds from short-term borrowings | 533,641 | 166,282 |
| Payments on short-term borrowings | (2,089,030) | (706,293) |
| Payments on long-term debt | (6,903) | |
| Proceeds from issuance of preferred stock | 2,984,000 | |
| Preferred stock issuance costs | (130,504) | (8,665) |
| Payment of dividends | | (45,457) |
| Proceeds from stock issuances, net | 7,617 | 433,450 |
| Net cash provided by (used in) financing activities | 946,246 | (730,378) |
| Effect of exchange rate on cash and cash equivalents | 25,653 | (1,449) |
| Change in cash and cash equivalents | 112,764 | 464,393 |
| Cash and cash equivalents at beginning of period | 1,412,238 | 1,525,002 |
| Cash and cash equivalents at end of period | \$ 1,525,002 | \$ 1,989,395 |
| Supplemental disclosures: | | |
| Interest paid | \$ 176,453 | \$ 207,326 |
| Cash paid for income taxes | \$ | \$ 449,768 |
| Non cash activities: | | |
| Common stock and options issued in purchase of businesses | \$ 7,218,086 | \$ |

Year Ended December 31,

Issuance of note payable in purchase of business

| Year Ended December 31, | |
|-------------------------|-----------|
| | |
| \$ | 1,292,500 |
| \$ | |

See accompanying notes.

F-6

PERFICIENT, INC.**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****December 31, 2003****1. Business Overview**

Perficient, Inc. (the "Company") is an eBusiness solutions provider to large and major midsize companies and Internet software vendors. The Company enables its clients and partners to optimize profitability and strengthen customer relationships through reliable, quick-to-market eBusiness solutions. The Company provides a broad range of end-to-end business and technology solutions with a focus on serving the financial services, healthcare, technology and energy industries.

The Company was incorporated on September 17, 1997 in Texas. The Company began operations in 1997 and is structured as a "C" corporation. On May 3, 1999 the Company reincorporated in Delaware. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All material inter-company accounts and transactions have been eliminated in consolidation.

2. Summary of Significant Accounting Policies**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates, and such differences could be material to the financial statements.

Revenue Recognition

Revenues are primarily derived from professional services provided on a time and materials basis, with the remaining revenue derived from fixed fee engagements and software sales. For time and material contracts, revenue is recognized and billed by multiplying the number of hours expended in the performance of the contract by the established billing rates. For fixed fee projects, revenue is generally recognized using the proportionate performance method based on the ratio of hours expended to total estimated hours. Provisions for estimated losses on uncompleted contracts are made on a contract-by-contract basis and are recognized in the period in which such losses are determined. Billings in excess of costs plus earnings are classified as deferred revenues. On many projects the Company is also reimbursed for out-of-pocket expenses such as airfare, lodging and meals. These reimbursements are included as a component of revenue in accordance with the Financial Accounting Standards Board's Emerging Issues Task Force ("EITF") 01-14, *Income Statement Characterization of Reimbursements Received for "Out-of-Pocket" Expenses Incurred*. In accordance with EITF 99-19, *Reporting Revenue Gross as a Principal versus Net as an Agent*, revenue from software resales is recorded on a gross basis based on the Company's role as principal in the transaction. As provided in EITF 99-19 criteria to be considered "principal", the Company is the primary obligator and bears the associated credit risk in the transaction. In the event the Company does not meet the requirements to be considered a principal in the software resale transaction and acts as an agent, the revenue would be recorded on a net basis.

Cash Equivalents

Cash equivalents consist primarily of cash deposits and investments with original maturities of ninety days or less when purchased.

F-7

Advertising Expense

The cost of advertising is expensed as incurred. Advertising costs for the years ended December 31, 2002 and 2003 were not material.

Property and Equipment

Property and equipment are recorded at cost. Depreciation of property and equipment is computed using the straight-line method over the useful lives of the assets (generally 2 to 5 years). Leasehold improvements are amortized over the shorter of the life of the lease or the estimated useful life of the assets. Amortization of assets recorded under capital leases is computed using the straight-line method and is included in depreciation expense. The cost and accumulated amortization of assets recorded under capital leases was approximately \$412,000 and \$52,000, respectively, at December 31, 2002 and approximately \$412,000 and \$134,000, respectively, at December 31, 2003.

Intangible Assets

Intangible assets, primarily resulting from purchase business combinations, are being amortized using the straight-line method with a life of two to three years for employment and non-compete agreements and a life of three to five years for customer relationship intangibles. Intangible assets consist of the following:

| | December 31, | |
|--------------------------------------|----------------------|----------------------|
| | 2002 | 2003 |
| Cost: | | |
| Employment and noncompete agreements | \$ 550,000 | \$ 550,000 |
| Customer relationships | 3,600,000 | 3,600,000 |
| Goodwill | 36,384,000 | 36,308,000 |
| Accumulated amortization: | | |
| Employment and noncompete agreements | (370,000) | (518,000) |
| Customer relationships | (2,805,000) | (3,267,000) |
| Goodwill | (24,979,000) | (24,979,000) |
| Net Book Value: | \$ 12,380,000 | \$ 11,694,000 |

Amortization expense for employment, non-compete agreements, and customer relationships is expected to be approximately \$132,237 in 2004, \$100,000 in 2005, \$100,000 in 2006, and \$32,237 in 2007.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards ("SFAS") 141, *Business Combinations*, and SFAS No. 142, *Goodwill and Other Intangible Assets*. Under these rules, ratable amortization of intangibles assets with indefinite lives, including goodwill, has been replaced with periodic review and analysis to assess possible impairment. Intangible assets with definite lives must be amortized over their estimated useful lives. In accordance with SFAS No. 142, the Company assesses its goodwill on October 1 of each year or more frequently if events or changes in circumstances indicate that goodwill might be impaired. The goodwill impairment test is a two-step

process. The first step of the impairment analysis compares the fair value to the net book value. In determining fair value, management utilizes a blended approach and calculates fair value based on market capitalization, revenue and earnings multiples based on industry comparables, and discounted cash flow analysis. Step two of the analysis compares the implied fair value of goodwill to its carrying amount. If the carrying amount of goodwill exceeds its implied fair value, an impairment loss is recognized equal to that excess.

Business acquisitions typically result in goodwill and other intangible assets, and the recorded values of those assets may become impaired in the future. The determination of the value of such intangible assets requires us to make estimates and assumptions that affect the Company's consolidated financial statements. Management assesses potential impairments to intangible assets on an annual basis or when there is evidence that events or changes in circumstances indicate that the carrying amount of an asset may not be recovered. Management's judgments regarding the existence of impairment indicators and future cash flows related to intangible assets are based on operational performance of the acquired businesses, market conditions and other factors. Future events could cause management to conclude that impairment indicators exist and that goodwill associated with the acquired businesses is impaired. Any resulting impairment loss could have an adverse impact on the Company's results of operations by decreasing net income.

Impairment of Long-Lived Assets

The Company evaluates its long-lived assets in accordance with SFAS No. 144, *Accounting for the Impairment of Long-Lived Assets*. Long-lived assets held and used by the Company are reviewed for impairment whenever events or changes in circumstances indicate that their net book value may not be entirely recoverable. When such factors and circumstances exist, the Company compares the projected undiscounted future cash flows associated with the related asset or group of assets over their estimated useful lives against their respective carrying amounts. Impairment, if any, is based on the excess of the carrying amount over the fair value of those assets and is recorded in the period in which the determination was made. The Company adopted SFAS No. 144 as of January 1, 2002.

Income Taxes

The Company accounts for income taxes in accordance with SFAS No. 109, *Accounting for Income Taxes*. This Statement prescribes the use of the liability method whereby deferred tax asset and liability account balances are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Foreign Currency Transactions

For the Company's foreign subsidiaries, the functional currency has been determined to be the local currency, and therefore, assets and liabilities are translated at year-end or period-end exchange rates, and income statement items are translated at average exchange rates prevailing during the year or period. Such translation adjustments are recorded in aggregate as a component of stockholders' equity. Gains and losses from foreign currency denominated transactions, including a \$7,500 loss during 2002 and a \$15,800 gain in 2003, are included in other income (expense). Due to the on-going

F-9

liquidation of the United Kingdom subsidiary, a foreign currency gain of \$15,500 was transferred from cumulative translation adjustments and included as a component of net income for the year ended December 31, 2003.

Segments

The Company follows the provisions of the SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*. SFAS No. 131 requires a business enterprise, based upon a management approach, to disclose financial and descriptive information about its operating segments. Operating segments are components of an enterprise about which separate financial information is available and regularly evaluated by the chief operating decision maker(s) of an enterprise. Under this definition, the Company operates as a single segment for all periods presented. The Company's chief operating decision maker is considered to be the Chief Executive Officer and Chairman of the Board. The chief operating decision maker allocates resources and assesses performance of the business and other activities at the consolidated level.

Earnings Per Share

The Company follows the provisions of SFAS No. 128, *Earnings Per Share*. Basic earnings per share is computed by dividing net income (loss) available to common stockholders by the weighted-average number of common shares outstanding during the period. Diluted earnings per share includes the weighted average number of common shares outstanding and the number of equivalent shares which would be issued related to the stock options and warrants using the treasury method, contingently issuance shares, and convertible preferred stock using the if-converted method, unless such additional equivalent shares are anti-dilutive.

Stock-Based Compensation

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SFAS No. 123, *Accounting for Stock-Based Compensation*, prescribes accounting and reporting standards for all stock-based compensation plans, including employee stock options. As allowed by SFAS No. 123, the Company has elected to account for its employee stock-based compensation in accordance with Accounting Principles Board Opinion No. 25, *Accounting For Stock Issued To Employees*, ("APB 25"), which allows the use of the intrinsic value method. The Company's basis for electing accounting treatment under APB 25 is principally due to the satisfactory incorporation of the dilutive effect of these shares in the reported earnings per share calculation and the presence of pro forma supplemental disclosure of the estimated fair value methodology prescribed by SFAS No. 123 and SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*. The fair value of options was calculated at the date of grant using the Black-Scholes pricing model with the following weighted-average assumptions for the year ended December 31, 2002 and 2003, respectively: risk free interest rate of 3.5% and 2.98%; dividend yield of 0%; weighted-average expected life of options of 5 years; and a volatility factor of 1.066 and 1.515.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and which are fully transferable. In addition, option valuation models in general require the input of highly subjective assumptions, including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly

F-10

different than traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a single reliable measure of the fair value of its stock options.

The following table illustrates the effect on net income (loss) and earnings per share if the Company had applied the fair value recognition provisions of SFAS 123:

| | Year ended December 31, | |
|---|-------------------------|--------------|
| | 2002 | 2003 |
| Net income (loss) available to common stockholders as reported | \$ (4,230,803) | \$ 892,400 |
| Total stock-based compensation costs included in the determination of net income (loss) available to common stockholders as reported | 240,688 | 135,927 |
| The stock-based employee compensation cost that would have been included in the determination of net income (loss) available to common stockholders if the fair value based method had been applied to all awards | (2,783,044) | (1,147,235) |
| Pro forma net income (loss) | \$ (6,773,159) | \$ (118,908) |
| Earnings per share | | |
| Basic as reported | \$ (0.53) | \$ 0.08 |
| Diluted as reported | \$ (0.53) | \$ 0.06 |
| Basic and diluted pro forma | \$ (0.84) | \$ (0.01) |

Fair Value of Financial Instruments

Cash equivalents, accounts receivable, accounts payable, other accrued liabilities, and debt are stated at cost which approximates fair value due to the short-term maturity of these instruments.

Recently Issued Accounting Standards

In January 2003, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 46 ("FIN 46"), *Consolidation of Variable Interest Entities*. FIN 46 requires that if an entity has a controlling financial interest in a variable interest entity, the assets, liabilities and results of activities of the variable interest entity should be included in the consolidated financial statements of the entity. FIN 46 is effective immediately for all new variable interest entities created or acquired after January 31, 2003. For variable interest entities created or acquired

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prior to February 1, 2003, the provisions of FIN 46 must be applied for the first interim or annual period beginning after December 15, 2003. Management does not believe that the adoption of FIN 46 will have a material impact on the Company's consolidated results of operations or financial position.

In May 2003, the FASB issued SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity*. SFAS No. 150 establishes standards on the classification and measurement of certain financial instruments with characteristics of both liabilities and equity. The

F-11

provisions of SFAS No. 150 are effective for financial instruments entered into or modified after May 31, 2003, and to all other instruments that exist as of the beginning of the first interim financial reporting period beginning after June 15, 2003. The changes that resulted from the issuance of SFAS No. 150 did not have a material effect on the Company's consolidated results of operations or financial position.

In December 2003, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin (SAB) No. 104, *Revenue Recognition*, which codifies, revises and rescinds certain sections of SAB No. 101, *Revenue Recognition*, in order to make this interpretive guidance consistent with current authoritative accounting and auditing guidance and SEC rules and regulations. The changes noted in SAB No. 104 did not have a material effect on the Company's consolidated results of operations, consolidated financial position or consolidated cash flows.

3. Net Income (Loss) Per Share

Computations of the net income (loss) per share are as follows:

| | Year Ended December 31, | |
|--|-------------------------|--------------|
| | 2002 | 2003 |
| Net income (loss) | \$ (2,395,044) | \$ 1,050,032 |
| Beneficial conversion charge on preferred stock | (1,672,746) | |
| Accretion of dividends on preferred stock | (163,013) | (157,632) |
| Net income (loss) available to common stockholders | \$ (4,230,803) | \$ 892,400 |
| Basic: | | |
| Weighted-average shares of common stock outstanding | 9,173,657 | 11,364,203 |
| Weighted-average shares of common stock subject to contingency | (1,132,506) | (545,786) |
| Shares used in computing basic net income (loss) per share | 8,041,151 | 10,818,417 |
| Effect of dilutive securities: | | |
| Weighted-average shares of common stock subject to contingency | | 545,786 |
| Preferred stock | | 2,531,436 |
| Stock options | | 1,410,512 |
| Warrants | | |
| Shares used in computing diluted net income (loss) per share | 8,041,151 | 15,306,151 |

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| | <u>Year Ended December 31,</u> | |
|-----------------------------------|--------------------------------|---------|
| Basic net income (loss) per share | \$ (0.53) | \$ 0.08 |
| Diluted net income per share | \$ (0.53) | \$ 0.07 |

Diluted net loss per share is the same as basic net loss per share for the year ended December 31, 2002, as the effect of the assumed exercise of stock options and warrants, the issuance of contingently

F-12

issuable shares resulting from business combinations, and shares of common stock issuable upon the conversion of convertible preferred stock is anti-dilutive due to the Company's net loss for that period. Diluted net loss per share for the year ended December 31, 2002 excludes common stock equivalents of 4,274,225.

4. Concentration of Credit Risk and Significant Customers

Cash and accounts receivable potentially expose the Company to concentrations of credit risk. Excess cash is placed with highly rated financial institutions. The Company provides credit, in the normal course of business, to its customers. The Company generally does not require collateral or up front payments. The Company performs periodic credit evaluations of its customers and maintains allowances for potential credit losses. Customers can be denied access to services in the event of non-payment. In August 2003, the Company entered into a one-year extension of its existing services agreement with IBM under which the Company provides deployment, integration and training services to IBM's WebSphere customers which are billed on a time and materials basis. The agreement will expire on September 1, 2004. The current contract stipulates that IBM may cancel the contract prior to its expiration date of September 1, 2004 upon 5 days written notice. Revenue from IBM accounted for approximately 35% of total revenue for both 2002 and 2003, and accounts receivable from IBM accounted for approximately 35% and 37% of total accounts receivable as of December 31, 2002 and December 31, 2003, respectively. In the event that IBM is no longer a customer following the cancellation or termination of the Company's current agreement, the Company's revenue would decrease significantly and, as with the loss of any significant customer, management may need to counteract this type of revenue decrease by reducing headcount to align with the lower demand for the Company's services. Due to the Company's significant fixed operating expenses, the loss of sales to IBM could result in the Company's inability to generate net income for some time in the future.

5. Employee Benefit Plan

The Company has a qualified 401(k) profit sharing plan available to full-time employees who meet the plan's eligibility requirements. This defined contribution plan permits employees to make contributions up to maximum limits allowed by the Internal Revenue Code. The Company, at its discretion, matches a portion of the employee's contribution under a predetermined formula based on the level of contribution and years of vesting services. The Company made matching contributions equal to 25% of the first 6% of employee contributions totaling \$130,000 and \$143,000 during 2002 and 2003, respectively, which vest over a three year period of service. The Company's related costs for the plan were approximately \$32,000 and \$19,000 during 2002 and 2003, respectively.

6. Stockholders' Equity

Preferred Stock

The Company entered into a Convertible Preferred Stock Purchase Agreement, dated as of June 26, 2002, with 2M Technology Ventures, L.P. ("2M") under which the Company sold 1,111,000 shares of Series B Convertible Preferred Stock, par value \$0.001 per share ("Series B Preferred Stock"), to 2M for a purchase price of approximately \$0.90 per share. The Company used the proceeds from the sale of the Series B Preferred Stock to strengthen its working capital position and for other

F-13

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corporate purposes. Each share of Series B Preferred Stock was initially convertible into one share of Perficient common stock at the election of the holder. The agreement also stipulated criteria for the automatic conversion of Series B preferred shares into common shares in the event that the closing price for Perficient's common stock is greater than \$3 per share for 20 consecutive days with an average trading volume greater than 50,000 shares over that same period. As of November 11, 2003, the criteria for automatic conversion were met, and accordingly, all outstanding shares of Series B preferred stock were converted to 1,111,000 shares of common stock. The Company has also issued to 2M a Warrant to purchase up to 555,500 shares of Perficient common stock in connection with this sale of Series B Preferred Stock.

2M was given the option to purchase up to an additional 1,666,500 shares of Series B Preferred Stock on the same terms as described above, however, this option was not exercised and expired on June 26, 2003.

Simultaneously with the sale of shares to 2M by the Company, 2M purchased from Steven Papermaster, Robert Anderson and Bryan Menell, 300,000, 100,000 and 100,000 shares of Perficient common stock, respectively, for \$0.75 per share. Mr. Papermaster was a member of the Company's Board of Directors at the time of the transaction and each of Messrs. Papermaster, Menell and Anderson are or had been significant holders of Perficient common stock.

In addition, the Company entered into Registration Rights Agreements with 2M pursuant to which the Company filed on October 10, 2002 a preliminary registration statement with the Securities and Exchange Commission covering the resale of the shares of common stock issuable upon the conversion of the Series B preferred stock (and exercise of the Warrants) sold in the private placement. Each share of Series B preferred stock had voting rights equal to the number of shares of common stock into which the preferred stock could then be converted. The Series B preferred stock accrued dividends payable in our common stock at an annual rate per share equal to \$0.90 multiplied by an 8% interest rate. Accrued dividends on the Series B preferred stock totaled approximately \$41,205 as of December 31, 2002 and \$110,027 as of November 10, 2003, the date of the automatic conversion. The accrued dividends on the Series B preferred stock were forfeited under the terms of the automatic conversion.

In connection with Series B preferred stock issuance, the Company recognized a beneficial conversion charge equal to approximately \$459,000, which represents the intrinsic value of the feature using a fair market value of common stock of \$1.16 and an exchange ratio of 1.34:1, in accordance with EITF 98-5, *Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios*, and EITF 00-27, *Application of EITF Issue 98-5, Accounting for Convertible Securities with Beneficial Conversion Features, or Contingently Adjustable Conversion Ratios, to Certain Convertible Instruments*. The beneficial conversion charge was calculated by first deducting the value of the warrants issued from the proceeds to compute an effective conversion ratio. The warrants were valued at approximately \$170,000 using the Black-Scholes valuation model, an assumed volatility of 50%, a risk-free interest rate of 3.5%, a weighted-average expected life of 4 years, and a dividend rate of 0%.

The Company entered into a Convertible Preferred Stock Purchase Agreement, dated as of December 21, 2001, with a limited number of investors under which the Company sold 1,984,000 shares

F-14

of Series A Convertible Preferred Stock ("Series A") to such investors for a purchase price of \$1.00 per share, for gross proceeds of \$1,984,000. The Company used the proceeds from the sale of the Series A Preferred Stock to strengthen its working capital position and for other corporate purposes. Each share of Series A preferred stock was initially convertible into one share of Perficient common stock at the election of the holder, based on a conversion ratio as defined in the agreement, initially set at \$1 and adjusted from time to time based on certain anti-dilution provisions. The Company has also issued warrants to purchase 992,000 shares of Perficient common stock in connection with this sale of Series A preferred stock. For every two shares of Series A preferred stock purchased by an investor, such investor received a Warrant to purchase one share of Perficient common stock at an initial exercise price of \$2.00 per share of common stock. In addition, the Company entered into Registration Rights Agreements with each of the purchasers pursuant to which the Company filed a registration statement with the Securities and Exchange Commission covering the resale of the shares of common stock issuable upon the conversion of the Series A preferred stock (and exercise of the Warrants) sold in the private placement which registration statement was declared effective by the Securities and Exchange Commission on October 10, 2002. Each share of Series A preferred stock had voting rights equal to the number of shares of common stock into which the preferred stock could then be converted. The Series A preferred stock accrues dividends at an annual rate per share equal to \$1.00 multiplied by the prime rate plus 150 basis points. Accrued dividends on the Series A preferred stock totaled approximately \$121,808 as of December 31, 2002 and \$210,617 on November 10, 2003, the automatic conversion date. The company paid cash dividends totaling \$45,457 to certain holders of Series A Preferred Stock who had voluntarily elected to convert their holdings to common stock prior to the automatic conversion date. The accrued dividends on the Series A preferred stock that was not voluntarily converted prior to November 10, 2003 were forfeited under the terms of the automatic conversion.

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In connection with Series A preferred stock issuance, the Company recognized a beneficial conversion charge equal to approximately \$1,180,000, which represents the intrinsic value of the feature using a fair market value of common stock of \$1.38 and an exchange ratio of 1.27:1, in accordance with EITF 98-5, *Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios*, and EITF 00-27, *Application of EITF Issue 98-5, Accounting for Convertible Securities with Beneficial Conversion Features, or Contingently Adjustable Conversion Ratios, to Certain Convertible Instruments*. The beneficial conversion charge was calculated by first deducting the value of the warrants issued from the proceeds to compute an effective conversion ratio. The warrants were valued at approximately \$427,000 using the Black Scholes valuation model, an assumed volatility of 50%, a risk-free interest rate of 3.5%, a weighted-average expected life of 4 years, and a dividend rate of 0%.

The Company obtained access to \$825,000 of the proceeds from the Series A preferred stock issuance in January 2002. The remainder of the funds remained in escrow subject to the completion of the acquisitions of Javelin Solutions, Inc. and Primary Webworks, Inc. d/b/a Vertecon, Inc.. The Company obtained access to the remaining \$1,159,000 in May 2002.

As a result of the Series B issuance discussed above, the conversion ratio for the Series A preferred stock decreased to approximately \$0.99. Additionally, as a result of the Series B preferred stock issuance, the number of warrants issued to the Series A investors increased to 1,001,920 and the

F-15

exercise price was adjusted to approximately \$1.98 per share. A beneficial conversion charge of \$22,000 related to the change in the Series A preferred stock conversion ratio and a beneficial conversion charge of \$11,000 related to the increase in the number of common shares issuable upon the exercise of the warrants was recognized during the second quarter of 2002.

Common Stock

In May 1999, the Company's Board of Directors and stockholders approved the 1999 Stock Option/Stock Issuance Plan (the "1999 Plan"). The 1999 Plan contains programs for (i) the discretionary granting of stock options to employees, non-employee board members and consultants for the purchase of shares of the Company's common stock, (ii) the discretionary issuance of common stock directly to eligible individuals, and (iii) the automatic issuance of stock options to non-employee board members. The Compensation Committee of the Board of Directors administers the 1999 Plan, and determines the exercise price and vesting period for each grant. Options granted under the 1999 Plan have a maximum term of 10 years. In the event that the Company is acquired, whether by merger or asset sale or board-approved sale by the stockholders of more than 50% of the Company's voting stock, each outstanding option under the discretionary option grant program which is not to be assumed by the successor corporation or otherwise continued will automatically accelerate in full, and all unvested shares under the discretionary option grant and stock issuance programs will immediately vest, except to the extent the Company's repurchase rights with respect to those shares are to be assigned to the successor corporation or otherwise continued in effect. The compensation committee may grant options under the discretionary option grant program that will accelerate in the acquisition even if the options are assumed or that will accelerate if the optionee's service is subsequently terminated. The compensation committee may grant options and issue shares that accelerate in connection with a hostile change in control effected through a successful tender offer for more than 50% of the Company's outstanding voting stock or by proxy contest for the election of board members, or the options and shares may accelerate upon a subsequent termination of the individual's service.

The Company has granted stock options to various employees under the terms of the respective employee agreements. The stock options generally vest over three years. The term of each option is ten years from the date of grant.

The Company recognized \$240,688 and \$135,927 of stock compensation expense during 2002 and 2003, respectively, as a result of options granted to employees with exercise prices below the fair market value of the underlying common stock on the date of grant, certain modifications to existing options, and the grant of options to certain non-employees. During 2002, the Company recognized deferred compensation totaling \$266,173 related to the acquisition of Javelin that is being amortized over the vesting period of the related options. Stock-compensation expense is recognized on a straight-line basis over the related vesting periods. Stock compensation expense for option grants to non-employees was determined using a Black-Scholes pricing model.

F-16

A summary of changes in common stock options during 2002 and 2003 is as follows:

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| | Shares | Range of Exercise Prices | Weighted- Average Exercise Price |
|--|-----------|--------------------------------|---|
| Options outstanding at January 1, 2002 | 3,290,278 | \$0.02 - \$26.00 | \$ 4.06 |
| Options granted | 1,997,825 | \$ 0.3 - \$ 8.62 | \$ 1.20 |
| Options exercised | (37,861) | \$0.03 - \$ 0.74 | \$ 0.20 |
| Options canceled | (859,516) | \$0.03 - \$26.00 | \$ 3.91 |
| Options outstanding at December 31, 2002 | 4,390,726 | \$0.02 - \$26.00 | \$ 2.82 |
| Options granted | 2,416,373 | \$0.50 - \$ 2.81 | \$ 1.53 |
| Options exercised | (264,140) | \$0.03 - \$ 1.39 | \$ 0.51 |
| Options canceled | (816,767) | \$0.03 - \$26.00 | \$ 2.66 |
| Options outstanding at December 31, 2003 | 5,726,192 | \$0.02 - \$26.00 | \$ 2.42 |
| Options vested, December 31, 2002 | 2,374,956 | \$0.02 - \$16.94 | \$ 3.61 |
| Options vested, December 31, 2003 | 2,684,572 | \$0.02 - \$16.94 | \$ 3.46 |

The following is additional information related to stock options outstanding at December 31, 2003:

| Range of Exercise Prices | Options Outstanding | | | Options Exercisable | |
|--------------------------------|---------------------|--|---|---------------------|--|
| | Options | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life (Years) | Options | Weighted Average Exercise Price |
| \$ 0.02 - \$ 0.50 | 1,224,262 | \$ 0.40 | 8.33 | 341,624 | \$ 0.16 |
| \$ 0.60 - \$ 1.41 | 1,634,600 | \$ 1.15 | 8.34 | 848,418 | \$ 1.14 |
| \$ 2.28 - \$ 4.50 | 2,531,277 | \$ 2.93 | 8.54 | 1,160,202 | \$ 3.64 |
| \$ 5.07 - \$12.97 | 211,375 | \$ 10.26 | 6.35 | 209,650 | \$ 10.28 |
| \$13.25 - \$26.00 | 124,678 | \$ 15.18 | 6.18 | 124,678 | \$ 15.18 |
| \$ 0.02 - \$26.00 | 5,726,192 | \$ 2.42 | 8.31 | 2,684,572 | \$ 3.46 |

At December 31, 2002 and 2003, the weighted-average remaining contractual life of outstanding options was 8.27 and 8.31 years, respectively. The weighted-average grant-date fair value per share of options granted during 2002 and 2003 at market prices was approximately \$0.90 and \$1.53, respectively. The weighted-average grant-date fair value per share of options granted during 2002 at below market prices was approximately \$1.31. During 2003 there were no option grants at below market prices. The weighted-average grant-date fair value per share of options granted during 2002 and 2003 at above market prices was approximately \$0.95 and \$1.15, respectively.

At December 31, 2002 and 2003, 11,500,177 and 9,065,879 shares of common stock were reserved for future issuance (at December 31, 2002 6,695,003 shares were reserved for options, 3,114,207 shares

were reserved for preferred stock, and 1,690,967 shares were reserved for warrants and at December 31, 2003 7,526,045 shares were reserved for options and 1,539,834 shares were reserved for warrants), and 2,304,276 and 1,799,852 options were available for future grants, respectively.

The following table summarizes information regarding warrants outstanding and exercisable as of December 31, 2003:

| Warrants Outstanding and Exercisable | |
|---|------------------|
| Exercise Price | Warrants |
| \$21.00 | 25,000 |
| \$12.00 | 100,000 |
| \$8.00 | 3,750 |
| \$2.00 | 555,500 |
| \$1.98 | 855,584 |
| \$1.98-\$21.00 | 1,539,834 |

7. Line of Credit and Long Term Debt

The Company has a line of credit facility providing for a borrowing capacity of up to \$6,000,000 or 80% of the eligible receivables, subject to certain borrowing base calculations as defined. Borrowings under this agreement, which expires December 2004, bear interest at the bank's prime rate plus 1.00% (5.00% at December 31, 2003). The Company is required to maintain certain financial covenants under this agreement. The line of credit is collateralized by substantially all the assets of the Company. The Company must pay unused line fee charges equal to 0.12%. The amount available for borrowing at December 31, 2003 was \$3,072,591.

Notes payable to related party at December 31, 2002 and 2003 consisted of a non interest-bearing note issued to the shareholders of Javelin Solutions, Inc. ("Javelin") in April 2002 in connection with the Company's acquisition of Javelin. The note provides for payments totaling \$1,500,000, of which \$875,000 remained outstanding on December 31, 2003. The Company made payments totaling \$62,500 in January 2004 and expects to make subsequent payments as follows: \$312,500 in April 2004, \$250,000 in April 2005, and \$250,000 in April 2006. For financial reporting purposes, an imputed interest rate of 7.5% was used to compute the net present value of the note payments. These notes are subordinate to the Company's line of credit.

Future minimum debt repayments as of December 31, 2003 are as follows:

| | Note Payable to Related Party |
|-----------------------------------|--------------------------------------|
| 2004 | \$ 375,000 |
| 2005 | 250,000 |
| 2006 | 250,000 |
| Thereafter | 875,000 |
| Less amount representing interest | (71,822) |
| Present value of debt commitments | 803,178 |
| Less current portion | (366,920) |

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| | December 31, | |
|---|------------------|------------------|
| | 2002 | 2003 |
| Deferred tax assets: | | |
| Depreciable assets | 57,128 | 134,648 |
| Tax loss carryforwards | 1,252,402 | 887,232 |
| Bad debt | 210,521 | 198,189 |
| Stock compensation | 145,297 | 4,111 |
| Accrued liabilities and other | 92,489 | 68,603 |
| | <u>1,757,837</u> | <u>1,292,783</u> |
| Total deferred tax assets | 1,757,837 | 1,292,783 |
| Valuation allowance for deferred tax assets | (1,386,936) | (1,056,604) |
| | <u>370,901</u> | <u>236,179</u> |
| Net deferred tax assets | 370,901 | 236,179 |
| | <u>\$</u> | <u>\$</u> |
| Net deferred taxes | \$ | \$ |

The Company has established a valuation allowance equal to the net deferred tax assets due to uncertainties regarding the realization of deferred tax assets based on the Company's lack of earnings history. The valuation allowance increased by approximately \$1,152,000 during 2002 and decreased by approximately \$330,000 during 2003. The 2003 decrease is primarily due to the use of tax attributes that were not previously benefited. As of December 31, 2003, approximately \$693,000 of the valuation allowance relates to acquired entities, and as such, if realized, will reduce goodwill or other noncurrent intangible assets prior to resulting in an income tax benefit.

Undistributed earnings of the Company's foreign subsidiary are considered to be permanently reinvested and, accordingly, no provision for US federal and/or state income taxes has been provided thereon.

F-20

The Company's provision for income taxes differs from the expected tax expense (benefit) amount computed by applying the statutory federal income tax rate of 34% to income before income taxes as a result of the following:

| | Year Ended December 31, | |
|-------------------------------------|-------------------------|------------|
| | 2002 | 2003 |
| Tax at statutory rate of 34% | \$ (814,315) | \$ 613,849 |
| State taxes, net of federal benefit | (37,385) | 125,494 |
| Goodwill | 414,040 | 207,542 |
| Effect of foreign operations | (12,143) | 75,739 |
| Change in valuation allowance | 459,685 | (330,332) |
| Other | (9,882) | 63,113 |
| | <u>\$</u> | <u>\$</u> |
| | 755,405 | 755,405 |

9. Commitments And Contingencies

The Company leases its office facilities and certain equipment under various operating and capital lease agreements. The Company has the option to extend the term of certain of its office facilities leases. Future minimum commitments under these lease agreements are as follows:

Operating
Leases

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| | Operating Leases |
|-------------------------------------|-----------------------------|
| 2004 | \$ 1,183,158 |
| 2005 | 1,236,920 |
| 2006 | 574,126 |
| 2007 | 242,639 |
| 2008 | 86,610 |
| Thereafter | 34,671 |
| Total minimum lease payments | \$ 3,358,124 |

Rent expense for the years ended December 31, 2002 and 2003 was \$1,281,000 and \$1,322,000, respectively. The Company expects to receive sublease income of \$220,000 during 2004, \$27,000 during 2005 and 2006, and \$11,000 during 2005. The expected sublease amounts are reflected as a reduction of the lease commitments presented above.

As required by certain of the Company's office and equipment leases, the Company has established letters of credit totaling \$550,000 to serve as collateral for these certain leases. These letters of credit reduce the amount of borrowing available under the Company's line of credit.

The Company signed a new employment agreement with its CEO, effective January 1, 2004.

F-21

10. Segments of Business and Geographic Area Information

The Company considers its business activities to constitute a single segment of business. A summary of the Company's operations by geographic area follows:

| | Year ended December 31, | |
|--------------------------------|--------------------------------|----------------------|
| | 2002 | 2003 |
| Revenue: | | |
| United States | \$ 20,309,905 | \$ 29,169,721 |
| Canada | 748,943 | 905,905 |
| United Kingdom | 1,391,436 | 116,296 |
| Total revenue | \$ 22,450,284 | \$ 30,191,922 |
| Net income (loss): | | |
| United States | \$ (2,506,025) | \$ 863,929 |
| Canada | 42,125 | 3,630 |
| United Kingdom | 68,856 | 182,473 |
| Total net income (loss) | \$ (2,395,044) | \$ 1,050,032 |
| Identifiable assets: | | |
| United States | \$ 18,898,766 | \$ 19,935,222 |
| Canada | 256,737 | 243,379 |
| United Kingdom | 437,600 | 81,382 |

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| | Year ended December 31, | |
|---------------------------|-------------------------|---------------|
| | 2002 | 2003 |
| Total identifiable assets | \$ 19,593,103 | \$ 20,259,983 |

11. Restructuring

During 2002, the Company implemented certain workforce reductions and office closures resulting in charges of approximately \$579,000, consisting of severance pay and related benefits for former employees as well as costs associated with the closure of the London office. The Company recognized \$118,000 of costs during 2002 related to the closure of the London office, which consisted of severance and benefits, lease commitments, as well as expected losses on the disposal of fixed assets, attorney and accounting fees, and other costs. As part of these restructurings, the Company reduced its workforce by a total of 30 employees, of which 17 were technology professionals and 13 were involved in selling, general administration and marketing. As of December 31, 2002, approximately \$228,000 of restructuring costs was included in other current liabilities, all of which was paid during 2003.

There was no such restructuring during 2003.

F-22

12. Balance Sheet Components

| | December 31, | |
|---|---------------------|---------------------|
| | 2002 | 2003 |
| Accounts receivable: | | |
| Accounts receivable | \$ 3,878,380 | \$ 4,932,165 |
| Unbilled revenue | 721,241 | 1,225,437 |
| Allowance for doubtful accounts | (661,248) | (622,995) |
| Total | \$ 3,938,373 | \$ 5,534,607 |
| Other current liabilities: | | |
| Accrued bonus | \$ 634,286 | \$ 1,150,614 |
| Accrued restructuring and severance costs | 228,145 | |
| Accrued vacation | 241,857 | 220,443 |
| Other payroll liabilities | 268,630 | 30,934 |
| Sales and use taxes | 45,792 | 85,187 |
| Accrued income taxes | 136,486 | 425,977 |
| Other accrued expenses | 455,344 | 484,524 |
| Software cost of sales | | 646,085 |
| Accrued medical claims | 17,705 | 5,000 |
| Deferred revenue | 276,188 | 262,107 |
| Total | \$ 2,304,433 | \$ 3,310,872 |

13. Related Party Transaction

During 2002, the Company executed an amendment to a non-compete agreement with a former employee, and as consideration, the Company required this individual to sell a portion of his holdings totaling 400,000 shares of Perficient common stock. With the consent of the Company, John T. McDonald, the Chairman and Chief Executive Officer of the Company, purchased 133,333 shares from this individual at a price of \$0.375 per share.

14. Business Combinations

On April 26, 2002, the Company consummated the acquisition of Primary Webworks, Inc. d/b/a Vertecon, Inc. ("Vertecon"), a Missouri corporation, through the merger of Vertecon with and into a wholly-owned subsidiary, Perficient Vertecon, Inc., a Delaware corporation. Perficient Vertecon, Inc. is the surviving corporation to the merger. Vertecon was a St. Louis based eBusiness Solutions provider that used advanced technology solutions to create competitive business advantages for its clients. Vertecon provided its customers with comprehensive solutions across the e-Business life cycle, including strategy, architecture, design, development and implementation services. The Company acquired Vertecon for an aggregate purchase price of approximately \$3,247,000, subject to certain post-closing adjustments. The purchase price consisted of 1,994,586 shares of Perficient common stock, of which approximately 551,985 shares were held in escrow until April 2003 at which time 44,787 shares of common stock were forfeited and canceled in accordance with the escrow agreement, the assumption of outstanding Vertecon options and direct acquisition costs. The common stock issued in the Vertecon

F-23

acquisition was valued at \$1.44 per share, which represents the average close price of the Company's common stock at the announcement of the acquisition in October 2001. The acquisition of Vertecon was consummated in order to increase and diversify Perficient's revenue base, add significant and longstanding customer relationships, provide geographic expansion into the St. Louis market, increase the number of qualified information technology consultants, and add experienced members of management among other factors. The majority of the excess cost over fair value of assets is attributed to the at-will workforce and, accordingly, is recorded as goodwill.

On April 26, 2002, the Company consummated the acquisition of Javelin Solutions, Inc. ("Javelin"), a Minnesota "S" corporation, through the merger of Javelin with and into a wholly-owned subsidiary, Perficient Javelin, Inc., a Delaware corporation. Perficient Javelin, Inc. is the surviving corporation to the merger. Javelin Solutions, Inc. was a Minneapolis-based professional services firm providing eBusiness strategy consulting, application design, implementation and integration services to large and major midsize companies. Javelin helped its clients define eBusiness strategies to improve their competitive position and business efficiency and would then design, architect, develop and implement solutions to execute those strategies. Javelin would seek to solve complex eBusiness challenges and create solutions that provided its clients with significant competitive advantages. Javelin offered a full range of integrated services consisting of strategic consulting, design of information architectures, and the creation, customization and implementation of software applications. Javelin also provided consulting services to help clients address security issues and web hosting decisions. As part of these services, Javelin provided application management services for its clients. The Company acquired Javelin for an aggregate purchase price of approximately \$5,951,000, subject to certain post-closing adjustments. The purchase price consists of 2,216,255 shares of Perficient common stock, of which approximately 1,108,127 shares were held in escrow until released in April 2003, \$1,500,000 in non-interest bearing promissory notes, the assumption of outstanding Javelin options and direct acquisition costs. The notes issued consist of \$1,000,000 that are payable in four equal annual installments, and \$500,000 (all unpaid installments of these notes issued to certain employee shareholders are subject to forfeiture upon the termination of such employee shareholder for any reason during the two year period following the closing) that are payable in eight quarterly installments. The common stock issued in the Javelin acquisition was valued at \$1.70 per share, which represents the average close price of the Company's common stock at the announcement of the acquisition in October 2001. The note payable was discounted using an assumed interest rate of 7.5%. The acquisition of Javelin was consummated in order to increase and diversify Perficient's revenue base, add significant and longstanding customer relationships, provide geographic expansion into the Minneapolis market, increase the number of qualified information technology consultants, and add experienced members of management among other factors. The majority of the excess cost over fair value of assets is attributed to the at-will workforce and, accordingly, is recorded as goodwill.

F-24

The aggregate purchase price for the acquisitions of Vertecon and Javelin is as follows:

| | <u>Vertecon</u> | <u>Javelin</u> |
|---|---------------------|---------------------|
| Common stock | \$ 2,874,997 | \$ 3,777,127 |
| Note (less imputed interest of \$210,000) | | 1,292,500 |
| Assumption of existing option plan | 16,053 | 549,909 |
| Transaction broker fee | 105,500 | 131,000 |
| Direct acquisition costs | 250,479 | 200,249 |
| | <u>\$ 3,247,029</u> | <u>\$ 5,950,785</u> |

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| <u>Vertecon</u> | <u>Javelin</u> |
|-----------------|----------------|
|-----------------|----------------|

The allocation of the purchase price for the acquisitions of Ver-tecon and Javelin is as follows:

| | <u>Vertecon</u> | <u>Javelin</u> |
|---|---------------------|---------------------|
| Cash | \$ | \$ 178,950 |
| Accounts receivable, net | 647,522 | 1,568,958 |
| Other current assets | 26,767 | 55,794 |
| Other long term assets | 53,323 | |
| Fixed assets | 472,267 | 534,715 |
| Intangibles | 4,860,087 | 5,256,373 |
| Accounts payable | (322,451) | (138,765) |
| Other current liabilities | (647,029) | (687,219) |
| Line of credit | (795,400) | (600,000) |
| Note and interest payable to Perficient | (814,487) | |
| Capital lease obligation | (193,288) | (484,194) |
| Accrued severance | (40,282) | |
| Deferred stock compensation | | 266,173 |
| | <u>\$ 3,247,029</u> | <u>\$ 5,950,785</u> |

Intangible assets recorded in connection with the acquisitions of Ver-tecon and Javelin are as follows:

| | <u>Vertecon</u> | <u>Javelin</u> |
|---------------------------------------|---------------------|---------------------|
| Customer relationships | \$ 250,000 | \$ 250,000 |
| Employment and non-compete agreements | 100,000 | 100,000 |
| Goodwill | 4,510,087 | 4,906,373 |
| | <u>\$ 4,860,087</u> | <u>\$ 5,256,373</u> |

The customer relationship intangibles are being amortized over a five-year life and the employment and non-compete agreement intangibles are being amortized over a two-year life.

The acquisitions of Ver-tecon and Javelin were recorded under the purchase method of accounting. Accordingly, the results of operations of Ver-tecon and Javelin have been included with those of the Company for periods subsequent to April 26, 2002.

F-25

In connection with the acquisitions of Ver-tecon and Javelin, we paid a broker fee to WWC Capital Group, LLC of approximately \$236,500. Michael J. Cromwell, III, a director of Perficient at the time of the transaction, is a partner of WWC Capital Group, LLC.

15. Subsequent Event (unaudited)

During the period January 1, 2004 through March 29, 2004 the Company issued 984,750 shares of common stock pursuant to the exercise of warrants, with exercise prices ranging from \$1.98 to \$2.00, that have been previously issued in connection with its Series A Preferred Stock and Series B Preferred Stock financings.

F-26

QuickLinks

PERFICIENT, INC. FORM 10-KSB ANNUAL REPORT FOR THE YEAR ENDED DECEMBER 31, 2003

TABLE OF CONTENTS

PART I

ITEM 1 DESCRIPTION OF BUSINESS

RISK FACTORS

SPECIAL NOTE REGARDING FORWARD LOOKING STATEMENTS

ITEM 2 DESCRIPTION OF PROPERTY

ITEM 3 LEGAL PROCEEDINGS

ITEM 4 SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

PART II

ITEM 5 MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

ITEM 6 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

ITEM 7 CONSOLIDATED FINANCIAL STATEMENTS

ITEM 8 CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURES

ITEM 8A CONTROLS AND PROCEDURES

PART III

ITEM 9 DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS OF REGISTRANT

ITEM 10 EXECUTIVE COMPENSATION

ITEM 11 SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

ITEM 12 CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

ITEM 13 EXHIBITS, FINANCIAL STATEMENTS AND REPORTS ON FORM 8-K

ITEM 14 PRINCIPAL ACCOUNTANT FEES AND SERVICES

SIGNATURES

PERFICIENT, INC. INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

REPORT OF INDEPENDENT AUDITORS

PERFICIENT, INC. CONSOLIDATED BALANCE SHEETS

PERFICIENT, INC. CONSOLIDATED STATEMENTS OF OPERATIONS

PERFICIENT, INC. CONSOLIDATED STATEMENTS OF CASH FLOWS

PERFICIENT, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS December 31, 2003