Schulte Roth&Zabel LLP

Alert

Selectica Activates Poison Pill, Seeks Declaratory Judgment of Pill's Validity

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Triggering of Rights
Selectica Inc. ("Selectica" or the "Company") announced in a press release on the evening of Saturday, Jan. 3, 2009, that the Board of Directors of the Company ordered the exchange of each outstanding right under its poison pill Rights Agreement (the "Rights Agreement") for one share of the Company's common stock, thereby activating its pill. It was announced that the exchange would not apply to rights formerly held by Versata Enterprises Inc. ("Versata"), Trilogy Inc. ("Trilogy") and Joseph A. Liemandt ("Liemandt" and collectively with Versata and Trilogy, the "Versata Parties"), as the Company claims that the Versata Parties' rights became void under the Rights Agreement when, on Dec. 19, 2008, the Versata Parties collectively became an "Acquiring Person" under the Rights Agreement by virtue of their having acquired shares resulting in an aggregate holding of 6.7% of the Company's common stock, exceeding the Rights Agreement's threshold. The Company also announced that it has amended the Rights Agreement to declare a new replacement preferred stock poison pill after the exchange, again utilizing a 4.99% ownership threshold, stating that such rights were being issued to protect the value of the Company's net operating loss carry-forwards (the "NOLs") and other tax credits.

Background: Amendment of the Rights Agreement; Filing of a Complaint by the Company
On Nov. 14, 2008, Versata, a subsidiary of Trilogy, acquired 5.1% of the Company and made a verbal proposal to acquire the Company. On Nov. 16, 2008, the Company's Board of Directors met to discuss amending the Rights Agreement, supposedly in an effort to protect the value of the Company's NOLs in light of the ownership level of the Versata Parties. According to a complaint subsequently filed by the Company in the Delaware Court of Chancery, the Company's losses over the last eight or more years have generated at least $140 million worth of such NOLs, which the Company asserts could be used to reduce the Company's or a potential acquiror's future tax liability. Another source has estimated the Company's federal and state NOLs as amounting to approximately $250 million as of March 31, 2008.

The Company ultimately approved an amendment to the Rights Agreement, effective Nov. 17, 2008, which reduced the threshold at which a beneficial owner became a so-called "Acquiring Person", thus triggering the operation of the Rights Agreement, from 15% to 4.99%. The amended Rights Agreement included a grandfathering provision such that beneficial owners who held in excess of the threshold amount at the time of the amendment would not trigger the pill unless they increased their holdings by .5% or more. In a Schedule 13D/A filed on Dec. 22, 2008, the Versata Parties announced that on Dec. 18, 2008, and Dec. 19, 2008, that they had purchased an additional 154,051 shares of the Company, bringing their total ownership to 6.7%. On Dec. 21, 2008, the Company filed a complaint, *Selectica, Inc. vs. Versata Enterprises, Inc. and Trilogy, Inc.*, in the Delaware Court of Chancery (the "Complaint"), seeking a declaratory judgment regarding the validity of the Rights Agreement. The Complaint outlined the history of the Rights Agreement, including the announcement on Nov. 17, 2008 to reduce the pill threshold to 4.99%. Selectica asserted in the Complaint that the trigger reduction was required to protect the value of its NOLs in light of, among other things, Section

382 or the Internal Revenue Code of 1986, as amended ("Section 382"), which limits the ability of a company to utilize such assets upon the occurrence of an "ownership change." Under Section 382, such an "ownership change" generally occurs when there is a greater than 50 percentage point increase in ownership by 5% stockholders in any three-year period. In the case of such an occurrence, the Company alleged the value of the NOLs would be significantly lost due to the operation of certain provisions of Section 382. The Company further alleged that certain acquisitions by 5% or greater Company shareholders, including Trilogy, had resulted in those stockholders making a cumulative change of beneficial ownership of approximately 40% of the Company's stock during the preceding three years, thus putting the Company in a position whereby the acquisition of an additional 10% by any 5% or greater stockholder would trigger the operation of the restrictive provisions of Section 382. On Dec. 23, 2008, Selectica filed a Motion to Expedite the proceedings. Versata and Trilogy have not yet filed an answer or any counter- or cross-claims in response to the Complaint.

Significance

This represents a rare instance of a poison pill being triggered. Selectica's amended triggering threshold of 4.99% is extraordinarily low, with the norm generally being at a 15% or 20% level, and was adopted only after an activist investor surfaced. Whether the court accepts Selectica's purported justification for the low threshold of protecting NOLs will be a significant development, as other companies would be encouraged to find a basis to lower their pill thresholds as well.

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