

ASPEN TECHNOLOGY INC /DE/
Form 10-Q/A
March 15, 2007

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Amendment No. 1
to

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2006

OR

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

For the transition period from _____ to _____

Commission File Number: 000-24786

Aspen Technology, Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

Ten Canal Park

Cambridge, Massachusetts

(Address of Principal Executive Offices)

04-2739697

(I.R.S. Employer
Identification No.)

02141

(Zip Code)

(617) 949-1000

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act). (Check one):

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

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

As of March 9, 2007, there were 87,749,130 shares of the registrant's common stock (par value \$0.10 per share) outstanding.

TABLE OF CONTENTS

	Page
Explanatory Notes	
<u>PART I. FINANCIAL INFORMATION</u>	
<u>FINANCIAL INFORMATION</u>	
<u>Item 1. Condensed Consolidated Financial Statements</u>	4
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	23
<u>Item 4. Controls and Procedures</u>	33
PART II. OTHER INFORMATION	
OTHER INFORMATION	
<u>Item 6. Exhibits</u>	38
<u>SIGNATURES</u>	39
CERTIFICATIONS	

Purpose of this Form 10-Q/A

Subsequent to our issuance of condensed consolidated financial statements for the three months ended September 30, 2006, and in the course of preparing the condensed consolidated financial statements for the three and six months ended December 31, 2006, we identified errors in the accounting for foreign currency denominated transactions. We incorrectly accounted for transaction gains and losses on intercompany balances denominated in currencies other than the functional currency as if such balances were of a long term investment nature and included the impact as a component of accumulated other comprehensive income (loss) rather than earnings. These transaction gains and losses should have been included in earnings as the conditions for accounting for these intercompany balances as a long term investment were not met. In addition, we identified errors in the recording of purchase accounting in other than the functional currency of the acquired entity. These purchase accounting adjustments should have been denominated in the currency of the applicable subsidiary and translated to United States Dollars and were incorrectly recorded as United States Dollar denominated net assets in the consolidated financial statements. Accordingly, translation of the balance sheet position related to the purchase accounting allocations and translation impact of the amortization of intangible assets was not recorded.

In addition, we identified other errors in the course of preparing the condensed consolidated financial statements for the three and six months ended December 31, 2006. These errors related to the timing of recognition of service revenue, facility leasing costs, and professional fees. We also recognized the tax effects of these corrections and added disclosure relative to reseller relationships in footnote 8.

In total, the above adjustments are reflected in the Third Restatement described in Amendment No. 2 to our Form 10-K for the fiscal year ended June 30, 2006, and in this Amendment No. 1 on Form 10-Q, which we refer to as this Form 10-Q/A. In order to correct the errors with respect to the three months ended September 30, 2005 and 2006, we are restating our condensed consolidated financial statements for these periods, in order to reflect (a) foreign currency transaction losses of \$3.1 million and gains of \$0.3 million, respectively, (b) additional amortization of technology related intangible assets of \$0.3 million and \$0.4 million, respectively, (c) income tax provision decrease of \$1.0 million and \$0.1 million, respectively, (d) additional facility lease costs of less than \$0.1 million in each period, and (e) for the three months ended September 30, 2006, an increase in service revenues of \$0.4 million and a decrease in legal costs of \$0.1 million and related balance sheet adjustments.

See Note 12 to the condensed consolidated financial statements for a discussion of the restatement. This Form 10-Q/A updates the information provided in Part I, Items 1, 2, and 4 of the original Form 10-Q for the effects of the restatement. This Form 10-Q/A has not been updated for events occurring after the filing of the original Form 10-Q, except to reflect the restatement.

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements**
ASPEN TECHNOLOGY, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited and dollars in thousands)

	September 30, 2006	June 30, 2006
	(As restated, see Note 12)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 88,866	\$ 86,272
Accounts receivable, net	50,576	49,163
Unbilled services	8,544	8,518
Current portion of long-term installments receivable, net	5,699	12,123
Prepaid expenses and other current assets	8,438	9,179
Total current assets	162,123	165,255
Long-term installments receivable, net	10,447	35,681
Retained interest in sold receivables.	28,067	19,010
Property and leasehold improvements, at cost	45,327	44,771
Accumulated depreciation and amortization	(36,916)	(36,097)
Property and leaseholds, net.	8,411	8,674
Computer software development costs, net	16,242	15,456
Purchased intellectual property, net	24	165
Other intangible assets, net	4,805	6,711
Goodwill	18,031	18,035
Deferred tax assets	3,098	3,097
Other assets	2,466	2,552
	\$ 253,714	\$ 274,636
LIABILITIES AND STOCKHOLDERS EQUITY (DEFICIT)		
Current liabilities:		
Current portion of long-term debt	\$ 249	\$ 247
Accounts payable	3,143	4,613
Accrued expenses	67,165	77,716
Deferred revenue	52,895	57,936
Total current liabilities	123,452	140,512
Long-term debt and obligations, less current maturities	97	149
Deferred revenue, less current portion	2,851	2,609
Other liabilities	19,080	20,446
Redeemable Preferred Stock:		
Outstanding 333,364 shares as of September 30, 2006 and June 30, 2006	129,211	125,475
Stockholders' equity (deficit):		
Common stock:		
Outstanding 53,461,512 as of September 30, 2006 and 48,857,035 as of June 30, 2006	5,370	4,909
Additional paid-in capital	433,120	430,811
Accumulated deficit	(467,130)	(457,977)
Accumulated other comprehensive income (loss)	8,176	8,215
Treasury stock, at cost	(513)	(513)
Total stockholders' equity (deficit)	(20,977)	(14,555)
	\$ 253,714	\$ 274,636

The accompanying notes are an integral part of these condensed consolidated financial statements.

ASPEN TECHNOLOGY, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited and in thousands, except per share data)

	Three Months Ended	
	September 30,	
	2006	2005
	(As restated, see Note 12)	(As restated see Note 12)
Software licenses	\$ 28,076	\$ 24,037
Service and other	36,246	35,797
Total revenues	64,322	59,834
Cost of software licenses	3,149	3,875
Cost of service and other	17,481	17,343
Amortization of technology related intangible assets	1,902	2,106
Total cost of revenues	22,532	23,324
Gross profit	41,790	36,510
Operating costs:		
Selling and marketing	21,210	18,758
Research and development	8,490	10,183
General and administrative	10,084	10,469
Restructuring charges	1,446	2,199
Loss on sales and disposals of assets	5,769	61
Total operating costs	46,999	41,670
Income (loss) from operations	(5,209)	(5,160)
Foreign currency exchange loss	(94)	(3,297)
Interest income	1,248	1,047
Interest expense	(481)	(231)
Income (loss) before provision for income taxes	(4,536)	(7,641)
(Provision for) benefit from income taxes	(881)	309
Net income (loss)	(5,417)	(7,332)
Accretion of preferred stock discount and dividend	(3,736)	(3,778)
Income (loss) applicable to common shareholders	\$ (9,153)	\$ (11,110)
Basic and diluted income (loss) per share applicable to common shareholders	\$ (0.17)	\$ (0.26)
Weighted average shares outstanding basic and diluted	52,801	43,237

The accompanying notes are an integral part of these condensed consolidated financial statements.

ASPEN TECHNOLOGY, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited and in thousands)

	Three Months Ended September 30, 2006 (As restated, see Note 12)	2005 (As restated see Note 12)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	\$(5,417)	\$(7,332)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	5,271	6,337
Transaction (gain) loss on intercompany accounts	(321)	3,093
Stock-based compensation.	1,741	1,808
Loss on securitization of installments receivable	5,672	
Loss on sales and disposals of assets	97	61
Accretion of discount on retained interest in sold receivables	(766)	(757)
Changes in assets and liabilities:		
Decrease (increase) in accounts receivable	(1,426)	7,421
Decrease (increase) in unbilled services	10	(1,479)
Decrease (increase) in installments receivable, including proceeds from securitization	18,587	(3,382)
Decrease (increase) in prepaid expenses and other current assets	771	(1,078)
Decrease in accounts payable and accrued expenses	(12,745)	(19,657)
Decrease in deferred revenue	(4,783)	(4,345)
Increase (decrease) in other liabilities	(1,366)	24
Net cash provided by (used in) operating activities	5,325	(19,286)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and leasehold improvements	(957)	(395)
Decrease in other long-term assets	86	55
Capitalized computer software development costs	(2,744)	(2,105)
Net cash used in investing activities	(3,615)	(2,445)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Issuance of common stock under employee stock purchase plans	423	445
Exercise of stock options	551	1,194
Payments of long-term debt	(50)	(311)
Net cash provided by financing activities	924	1,328
EFFECTS OF EXCHANGE RATE CHANGES ON CASH	(40)	(46)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	2,594	(20,449)
CASH AND CASH EQUIVALENTS, beginning of period	86,272	68,149
CASH AND CASH EQUIVALENTS, end of period	\$ 88,866	\$ 47,700

The accompanying notes are an integral part of these condensed consolidated financial statements.

ASPEN TECHNOLOGY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Interim Condensed and Consolidated Financial Statements

In the opinion of management, the accompanying unaudited interim condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America for interim financial information and pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (the SEC) for reporting on Form 10-Q. Accordingly, certain information and footnote disclosures required for complete financial statements are not included herein. It is suggested that these unaudited interim condensed consolidated financial statements be read in conjunction with the audited consolidated financial statements for the year ended June 30, 2006, which are contained in the Annual Report on Form 10-K, as amended, of Aspen Technology, Inc. (the Company), as previously filed with the SEC. In the opinion of management, all adjustments, consisting of normal and recurring adjustments, considered necessary for a fair presentation of the financial position, results of operations, and cash flows at the dates and for the periods presented have been included. The results of operations for the three-month period ended September 30, 2006 are not necessarily indicative of the results to be expected for the full fiscal year.

2. Sale of Installments Receivable

(a) Traditional Activities

Installments receivable represent the present value of future payments related to the financing by the Company of noncancelable term and perpetual license agreements with its customers which provide for payment in installments over a one to five-year period. A portion of each installment agreement is recognized as interest income in the accompanying consolidated condensed statements of operations. The interest rate utilized for the three months ended September 30, 2006 and 2005 was 8.0%.

The Company has arrangements to sell certain of its installments receivable to three financial institutions. The Company sold certain of its installment contracts for aggregate proceeds of approximately \$9.0 million and \$8.5 million during the three months ended September 30, 2006 and 2005, respectively. Generally, no gain or loss is recognized on the sale of the receivables due to the consistency of the discount rates used by the Company and the financial institutions.

The financial institutions have certain recourse to the Company upon nonpayment by the customer under the installments receivable. The amount of recourse is determined pursuant to the provisions of the Company's contracts with the financial institutions. Collections of these receivables reduce the Company's recourse obligations, as defined in the contracts. The Company's potential recourse obligation related to these contracts is within the range of \$0.1 million to \$1.2 million. In addition, the Company is obligated to pay additional costs to the financial institutions in the event of default by the customer.

(b) Securitization of Installments Receivable

On September 29, 2006, the Company entered into a \$75.0 million three year revolving securitization facility and securitized certain outstanding installment software license receivables (which receivables were not sold in the traditional sales described above) with a net carrying value of \$32.1 million. The structure of the facility was such that the securitization qualified as a sale. The Company received \$19.4 million of cash and retained an interest in the sold receivables valued at \$8.3 million. It also retained certain limited recourse obligations relative to the receivables valued at approximately \$0.5 million. Overall, the

transaction resulted in a loss of \$5.7 million in the quarter ended September 30, 2006 and was recorded as a loss on sales and disposals of assets in the accompanying consolidated statement of operations.

The amount of the loss was based on the previous carrying amount of the financial assets involved in the transfer, allocated between the assets sold and the retained interests based on their relative fair value at the date of transfer, as well as transaction costs.

As noted above, the retained interest in the sold receivables was recorded at its fair value of \$8.3 million at the time of the transaction and is classified as a long-term asset on the Company's consolidated balance sheet. The Company estimates fair value based on the present value of future expected cash flows based on using management's best estimates of key assumptions, principally credit losses, and discount rates commensurate with the risks involved.

Key economic assumptions used in subsequently measuring the carrying value of the Company's retained interests in the license receivables sold during the quarter ended September 30, 2006 and the effect on the fair value of those interests from adverse changes in those assumptions are as follows (in thousands):

Balance sheet carrying value of retained interest in sold receivables	\$	8,291	
Expected credit losses (annual rate):		0.82	%
Impact on fair value of 10% adverse change	\$	(23))
Impact on fair value of 20% adverse change	\$	(45))
Residual cash flow discount rate (annual rate):		13.0	%
Impact on fair value of 10% adverse change	\$	(397))
Impact on fair value of 20% adverse change	\$	(773))

These sensitivities are hypothetical and presented for illustrative purposes only. Changes in fair value based on a 10% variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, the effect of a variation in a particular assumption is calculated without changing any other assumption; in reality, changes in one assumption may result in changes in another, which may magnify or counteract the sensitivities.

The Company is recognizing the accretion of its retained interest to the estimated cash flow that will be received in interest income. Total interest income from accretion was \$0.8 million for the three months ended September 30, 2006 and 2005. The Company recognizes an impairment of the carrying value of its retained interest if a decline in the fair value of the retained interest is determined to be other-than-temporary. No such impairments have been recognized through September 30, 2006.

The Company retained the servicing rights relative to the receivables and receives annual servicing fees of \$0.3 million per year. The benefits of the servicing rights approximate the costs estimated to be incurred by the Company, and thus no servicing asset or liability has been recorded.

In connection with the above transaction, the Company incurred an obligation to guarantee that the proceeds from all installments receivable denominated in currencies other than the U.S. dollar included in the securitized pool will be equal to the U.S. dollar value on the initial contract date. The Company has entered into forward foreign exchange contracts intended to mitigate the financial exposure due to changes in currency exchange rates which are further described below. The fair value of this obligation was not material and has thus been accorded no value.

3. Derivative Instruments and Hedging

The Company follows the provisions of Statement of Financial Accounting Standards (SFAS), No. 133 Accounting for Derivative Instruments and Hedging Activities. SFAS No. 133, as amended by SFAS No. 138, requires that all derivatives, including foreign currency exchange contracts, be recognized on the balance sheet at fair value. Derivatives that are not hedges must be adjusted to fair value through earnings. If a derivative is a hedge, depending on the nature of the hedge, changes in the fair value of the derivative are either offset against the change in fair value of assets, liabilities or firm commitments through earnings or recognized in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of a derivative's change in fair value is to be immediately recognized in earnings.

Forward foreign exchange contracts are used primarily by the Company to hedge certain balance sheet exposures resulting from changes in foreign currency exchange rates. Such exposures primarily result from portions of the Company's installment receivables that are denominated in currencies other than the U.S. dollar, primarily the Euro, the Japanese Yen, Canadian dollar and the British Pound Sterling. In addition, the Company incurred exposures as part of the June 2005 and September 2006 securitizations of installments receivable, in that the Company is obligated, in the form of a guarantee, to cover the exposure in the installments receivable that were transferred to its subsidiaries, resulting from changes in foreign currency exchange rates.

The foreign exchange contracts are entered into to hedge recorded installments receivable, both held and securitized, made in the normal course of business, and accordingly, are not speculative in nature. As part of its overall strategy to manage the level of exposure to the risk of foreign currency exchange rate fluctuations, the Company hedges the majority of its installments receivable denominated in foreign currencies.

The Company's guarantee to cover the exposure in the securitized installments receivable represents an embedded derivative. The Company calculates the value of this guarantee at each balance sheet date, and if the value of the guarantee represents an obligation, the fair value is recorded as a liability. As of September 30, 2006, the value of this embedded derivative represented an asset to the Company, and as such, no entry was recorded.

At September 30, 2006, the Company had effectively hedged \$29.3 million of installments receivable, either held or securitized, and accounts receivable denominated in foreign currency. The Company does not hold or transact in financial instruments for purposes other than to hedge foreign currency risk. The gross value of the installments receivable that were denominated in foreign currency was \$33.3 million and \$40.3 million at September 30, 2006 and June 30, 2006, respectively. The installments receivable held as of September 30, 2006 mature at various times through September 2011. There have been no material gains or losses recorded relating to hedge contracts for the periods presented.

The Company records its foreign currency exchange contracts at fair value in its consolidated balance sheet and the related gains or losses on these hedge contracts are recognized in earnings. During the three months ended September 30, 2006 and 2005 the net gain recognized in the consolidated statements of operations was not material.

The following table provides information about the Company's foreign currency derivative financial instruments outstanding as of September 30, 2006. The information is provided in U.S. dollar amounts (in thousands), as presented in the Company's consolidated financial statements. The table presents the notional amount (at contract exchange rates) and the weighted average contractual foreign currency rates:

	Notional Amount	Estimated Fair Value(1)	Average Contract Rate
Euro	\$ 19,329	\$ 19,676	1.26
British Pound Sterling	4,987	5,118	1.83
Canadian Dollar	2,434	2,483	1.14
Japanese Yen	2,154	2,004	112.38
Swiss Franc	394	388	1.21
	\$ 29,298	\$ 29,669	

(1) The estimated fair value is based on the estimated amount at which the contracts could be settled based on the spot rates as of September 30, 2006. The market risk associated with these instruments resulting from currency exchange rate movements is expected to offset the market risk of the underlying installments being hedged. The credit risk is that the Company's banking counterparties may be unable to meet the terms of the agreements. The Company minimizes such risk by limiting its counterparties to major financial institutions. In addition, the potential risk of loss with any one party resulting from this type of credit risk is monitored. Management does not expect any loss as a result of default by other parties. However, there can be no assurances that the Company will be able to mitigate market and credit risks described above.

4. Stock-Based Compensation Plans

The Company issues stock options to its employees and outside directors and provides employees the right to purchase stock pursuant to stockholder approved stock option and employee stock purchase programs. Option awards are generally granted with an exercise price equal to the market price of the Company's stock at the date of the grant; those options generally vest over four years and have 7 and 10-year contractual terms.

Effective July 1, 2005, the Company adopted the provisions of SFAS No. 123 (revised 2004), *Share-Based Payment* (SFAS No. 123R), using the Statement's modified prospective application method. Prior to July 1, 2005, the Company followed Accounting Principles Board Opinion 25, *Accounting for Stock Issued to Employees*, and related interpretations in accounting for its stock-based compensation. Under the provisions of SFAS No. 123R, the Company recognizes the fair value of stock-based compensation in net income, over the requisite service period of the individual grantees, which generally equals the vesting period. All of the Company's stock-based compensation is accounted for as equity instruments and there have been no liability awards granted.

The Company elected the modified prospective transition method for adopting SFAS 123R, and consequently prior periods have not been modified. Under this method, the provisions of SFAS 123R apply to all awards granted or modified after the date of adoption. The unrecognized expense of awards not yet vested at the date of adoption shall be recognized in net income in the periods after the date of adoption using the same valuation method (*i.e.*, Black-Scholes) and assumptions determined under the original provisions of SFAS 123, *Accounting for Stock-Based Compensation*, (SFAS 123) as disclosed in previous filings. Under the provisions of SFAS 123R, the Company recorded \$1.8 million of stock-based compensation for the three months ended September 30, 2006 and 2005, included in the following categories (in thousands):

	Three Months Ended September 30,	
	2006	2005
Recorded as expense:		
Cost of service and other	\$ 310	\$ 299
Selling and marketing	621	509
Research and development	199	208
General and administrative	611	792
	1,741	1,808
Capitalized computer software development costs	55	39
Total stock-based compensation.	\$ 1,796	\$ 1,847

The Company utilized the Black-Scholes valuation model for estimating the fair value of the stock compensation granted after the adoption of SFAS 123R. The weighted-average fair values of the options granted under the stock option plans were \$8.91 and \$3.88 and of the shares subject to purchase under the employee stock purchase plan were \$2.60 and \$1.99 for the three months ended September 30, 2006 and 2005, respectively, using the following assumptions:

	Three Months Ended September 30, 2006		Three Months Ended September 30, 2005	
	Stock Option Plans	Purchase Plan	Stock Option Plans	Purchase Plan
Average risk-free interest rate	4.84	%	5.10	%
Expected dividend yield	None		None	
Expected life	6.0 Years		0.5 Years	
Expected volatility	85	%	53	%
			85	%
			42	%

The dividend yield of zero is based on the Company's history of not having paid cash dividends and on its present intention not to pay cash dividends. Expected volatility is based on the historical volatility of the Company's common stock over the period commensurate with or longer than the expected life of the options. The risk-free interest rate is the U.S. Treasury STRIPS rate on the date of grant. The expected life was calculated using the method outlined in SEC Staff Accounting Bulletin Topic 14.D.2, *Expected Term*, as the Company's historical experience does not provide a reasonable basis for the expected term of the option.

5. Net Income (Loss) Per Common Share

Basic earnings per share was determined by dividing income (loss) attributable to common shareholders by the weighted average common shares outstanding during the period. Diluted earnings per share was determined by dividing income (loss) attributable to common shareholders by diluted weighted average shares outstanding. Diluted weighted average shares reflects the dilutive effect, if any, of potential common shares. To the extent their effect is dilutive, potential common shares include common stock

options and warrants, based on the treasury stock method, preferred stock, based on the if-converted method, and other commitments to be settled in common stock. The calculations of basic and diluted income (loss) attributable to common shareholders per share and basic and diluted weighted average shares outstanding are as follows (in thousands, except per share data):

	Three Months Ended September 30,	
	2006	2005
Income (loss) applicable to common shareholders	\$ (9,153)	\$ (11,110)
Basic weighted average common shares outstanding	52,801	43,237
Weighted average potential common shares		
Diluted weighted average shares outstanding	52,801	43,237
Basic and diluted income (loss) per share applicable to common shareholders	\$ (0.17)	\$ (0.26)

The following potential common shares were excluded from the calculation of diluted weighted average shares outstanding as their effect would be anti-dilutive (in thousands):

	Three Months Ended September 30,	
	2006	2005
Convertible preferred stock	33,336	36,336
Preferred stock dividend, to be settled in common stock	2,864	3,554
Options and warrants	12,213	21,911
Total	48,413	61,801

6. Comprehensive Income (Loss)

Comprehensive income (loss) is defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. The components of comprehensive income (loss) for the three months ended September 30, 2006 and 2005 are as follows (in thousands):

	Three Months Ended September 30,	
	2006	2005
Net income (loss)	\$ (5,147)	\$ (7,332)
Foreign currency translation adjustments	(39)	3,396
Comprehensive income (loss)	\$ (5,186)	\$ (3,936)

7. Restructuring Charges

During the three months ended September 30, 2006, the Company recorded \$1.4 million in restructuring charges primarily related to severance and relocation expenses under the May 2005 restructuring plan which are recognized in the period in which the affected employees were notified or the relocation expenses were incurred.

(a) Restructuring charges originally arising in Q4 FY05.

In May 2005, the Company initiated a plan to consolidate several corporate functions and to reduce its operating expenses. The plan to reduce operating expenses primarily resulted in headcount reductions, and also included the termination of a contract and the consolidation of facilities. These actions resulted in an aggregate restructuring charge of \$3.8 million, recorded in the fourth quarter of fiscal 2005. During the year ended June 30, 2006, the Company recorded an additional \$1.8 million related to headcount reductions, relocation costs and facility consolidations associated with the May 2005 plan that are recognized in the period in which the affected employees were notified, the relocation expenses were incurred, or the Company ceased use of the affected facilities. During the quarter ended September 30, 2006, the Company recorded an additional \$1.4 million in severance and relocation expenses for employees that were notified or relocation expenses that were incurred during the period.

As of September 30, 2006, there was \$1.3 million remaining in accrued expenses relating to the remaining severance obligations and lease payments. During the three months ended September 30, 2006, the following activity was recorded (in thousands):

Fiscal 2005 Restructuring Plan	Closure/ Consolidation of Facilities	Employee Severance, Benefits, and Related Costs	Total
Accrued expenses, June 30, 2006	\$ 99	\$ 513	\$ 612
Restructuring charge	26	1,369	1,395
Restructuring charge Accretion	1		1
Payments	(64)	(680)	(744)
Accrued expenses, September 30, 2006	\$ 62	\$ 1,202	\$ 1,264
Expected final payment date	May 2007	March 2007	

(b) Restructuring charges originally arising in Q4 FY04

During fiscal 2004, the Company recorded \$15.2 million in net restructuring charges. Of this amount, \$23.5 million is associated with a June 2004 restructuring plan, which is offset by \$8.3 million in adjustments to prior restructuring accruals and deferred rent balances.

In June 2004, the Company initiated a plan to reduce its operating expenses in order to better align its operating cost structure with the current economic environment and to improve operating margins. The plan to reduce operating expenses resulted in the consolidation of facilities, headcount reductions, and the termination of operating contracts. These actions resulted in an aggregate restructuring charge of \$23.5 million, recorded in the fourth quarter of fiscal 2004. During the year ended June 30, 2005, the Company recorded \$14.4 million related to headcount reductions and facility consolidations associated with the June 2004 restructuring plan, that are recognized in the period in which the affected employees were notified or the Company ceased use of the affected facilities. In addition, the Company recorded \$0.4 million in restructuring charges related to the accretion of the discounted restructuring accrual and a \$0.8 million decrease to the accrual related to changes in estimates of severance benefits and sublease terms. During the year ended June 30, 2006 the Company recorded a \$0.7 million increase to the accrual primarily due to a change in the estimate of future operating costs and sublease assumptions associated with the facilities.

As of September 30, 2006, there was \$6.5 million remaining in accrued expenses relating to the remaining severance obligations and lease payments. During the three months ended September 30, 2006, the following activity was recorded (in thousands):

Fiscal 2004 Restructuring Plan	Closure/ Consolidation of Facilities and Contract exit costs	Employee Severance, Benefits, and Related Costs	Total
Accrued expenses, June 30, 2006	\$ 6,855	\$ 192	\$ 7,047
Change in estimate Revised assumptions	21		21
Restructuring charge Accretion	65		65
Payments	(583) (79) (662)
Accrued expenses, September 30, 2006	\$ 6,358	\$ 113	\$ 6,471
Expected final payment date	September 2012	December 2006	

(c) Restructuring charges originally arising in Q2 FY03

In October 2002, management initiated a plan to further reduce operating expenses in response to first quarter revenue results that were below expectations and to general economic uncertainties. The plan to reduce operating expenses resulted in headcount reductions, consolidation of facilities, and discontinuation of development and support for certain non-critical products. These actions resulted in an aggregate restructuring charge of \$28.7 million. During fiscal 2004, the Company recorded a \$4.9 million decrease to the accrual related to revised assumptions associated with lease exit costs, particularly the buyout of a remaining lease obligation, and severance benefit obligations. During fiscal 2005 and fiscal 2006, the Company recorded \$7.0 million and \$1.0 million increases, respectively to the accrual primarily due to a change in the estimate of the facility vacancy term, extending to the term of the lease.

As of September 30, 2006, there was \$9.5 million remaining in accrued expenses relating to the remaining lease payments. The components of the restructuring plan are as follows (in thousands):

Fiscal 2003 Restructuring Plan	Closure/ Consolidation of Facilities
Accrued expenses, June 30, 2006	\$ 9,966
Change in estimate Revised assumptions.	(38)
Payments.	(387)
Accrued expenses, September 30, 2006	\$ 9,541
Expected final payment date	September 2012

8. Commitments and Contingencies

U.S. Attorney s Office Investigation and Wells Notice

In October 2004, the audit committee of the Company s board of directors commenced a detailed investigation of the accounting for certain software license and service agreement transactions entered into with certain alliance partners and other customers during fiscal years 2000 through 2002 (and later, fiscal 2000 to 2004), which investigation concluded in March 2005. In October 2004, the Company announced that it had received a subpoena from the U.S. Attorney s Office for the Southern District of New York requesting documents relating to transactions to which the Company was a party during the 2000 to 2002 time frame, associated documents dating from January 1, 1999, and additional materials.

In June 2006, the Company received a Wells Notice letter from the SEC of possible civil enforcement action regarding the Company s originally filed financial statements for fiscal years 2000 through 2004, which the Company restated in March 2005 following the conclusion of the audit

committee's review. In addition, the Company has been advised that Lawrence Evans, its former Chairman of the Board and Chief Executive Officer, David McQuillin, its former Chief Executive Officer, and Lisa Zappala, its former Chief Financial Officer, received separate Wells Notice letters in July 2006 regarding the same matter. Lawrence Evans is a current employee of the Company pursuant to an employment agreement entered into in June 2003, although he is no longer an executive officer.

The Company has cooperated fully with the subpoena requests and in the investigation by the U.S. Attorney's Office and the SEC. The investigation by the U.S. Attorney's Office is ongoing in coordination with the SEC, to which the audit committee had initially reported the initiation of the audit committee's investigation. The Company is currently unable to determine whether resolution of these matters will have a material adverse impact on its financial position or results of operations, or reasonably estimate the amount of the loss, if any, that may result from resolution of these matters. However, the ultimate outcome could have a material adverse effect on the Company's financial position and results of operations.

Class Action and Opt Out Suits

In November 2004, two putative class action lawsuits were filed against the Company in the United States District Court for the District of Massachusetts, captioned, respectively, *Fener v. Aspen Technology, Inc., et. al.*, Civil Action No. 04-12375 (D. Mass.) (filed Nov. 9, 2004) and *Stockmaster v. Aspen Technology, Inc., et. al.*, Civil Action No. 04-12387 (D. Mass.) (filed Nov. 10, 2004), (the "Class Actions"). The Class Actions allege, among other things, that the Company violated Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder in connection with various statements about its financial condition for fiscal years 2000 through 2004. On February 2, 2005, the Court consolidated the cases under the caption *Aspen Technology, Inc. Securities Litigation*, Civil Action No. 04-12375 (D. Mass.), and appointed The Operating Engineers and Construction Industry and Miscellaneous Pension Fund (Local 66) and City of Roseville Employees' Retirement System as lead plaintiff, purporting to represent a putative class of persons who purchased Aspen Technology, Inc. common stock between January 25, 2000 and October 29, 2004. On August 26, 2005, the plaintiffs filed a consolidated amended complaint containing allegations materially similar to the prior complaints and expanding the class action period.

Following mediation, on November 16, 2005, the Company and the plaintiffs on behalf of putative class members, defined to include all persons who purchased our common stock between October 29, 1999 and March 15, 2005, inclusive, (the "Class"), entered into a Stipulation and Agreement of Compromise, Settlement and Release of Securities Action, which (the "Stipulation"). The Stipulation was filed with the Court on the same date and provided, among other things, for settlement and release of all direct and indirect claims of the Class concerning matters covered by the Stipulation. On December 12, 2005, the Court granted preliminary approval of the settlement provided for in the Stipulation. After notice to the Class and after the hearing, on March 6, 2006, the Court granted final approval of the settlement, and the class action lawsuit was dismissed with prejudice. The Company entered into the Stipulation to resolve the matter and without acknowledging any fault, liability or wrongdoing of any kind. There has been no adverse determination by the Court against the Company or any of the other defendants in the case.

Members of the Class who opted out of the settlement (representing 1,457,969 shares of common stock, or less than 1% of the shares putatively purchased during the Class Action period) may bring their own individual actions, ("Opt Out Claims"). To date, state law Opt Out Claims, including claims of fraud, statutory treble damages, deceptive practices, and/or rescissory damages liability, based on the restated results of one or more fiscal periods included in the restated financial statements referenced in the Class Action, have been filed in Massachusetts Superior Court. The Company has responded by motion to dismiss on the grounds that the claims fail properly to state a claim. If not dismissed or settled on terms acceptable to us, the Company plans to defend the Opt Out Claims vigorously.

Pursuant to the terms of the Class Action settlement, the Company paid \$1.9 million and its insurance carrier paid \$3.7 million into a settlement fund for a total of \$5.6 million. The Company's \$1.9 million payment was recorded in general and administrative expenses in the quarter ended September 30, 2005. All costs of preparing and distributing notices to members of the Class and administration of the settlement, together with all fees and expenses awarded to plaintiffs' counsel and certain other expenses, will be paid out of the settlement fund, which will be maintained by an escrow agent under the Court's supervision.

On September 6, 2006, the Company also announced that, in connection with the preparation of financial statements for the fiscal year ended June 30, 2006, a subcommittee of independent directors was appointed to review the Company's accounting treatment for stock option grants for prior years. Following that announcement, the Company and certain of its officers and directors were named defendants in a purported federal securities class action lawsuits filed in Massachusetts federal district court, alleging violations of the Exchange Act and claiming material misstatements concerning its financial condition and results. In response to the Company's motion to dismiss the complaint, the parties stipulated to voluntary dismissal of the plaintiff's claims with prejudice on September 26, 2006 without any payment by the Company.

Derivative Suits

On December 1, 2004, a putative derivative action lawsuit was filed as a related action to the first filed of the Class Actions (described above) in the United States District Court for the District of Massachusetts, captioned *Caviness v. Evans, et al.*, Civil Action No. 04-12524 (D. Mass.), (the Derivative Action). The complaint, as subsequently amended, alleged, among other things, that the former and current director and officer defendants caused the Company to issue false and misleading financial statements, and brought derivative claims for the following: breach of fiduciary duty for insider trading; breach of fiduciary duty; abuse of control; gross mismanagement; waste of corporate assets; and unjust enrichment.

On August 18, 2005, the Court granted defendants' motion to dismiss the Derivative Action for failure of the plaintiff to make a pre-suit demand on the Company's board of directors to take the actions referenced in the Derivative Action complaint.

On April 12, 2005, the Company received a letter on behalf of another shareholder, demanding that the board of directors of the Company take actions substantially similar to those referenced in the Derivative Action. On February 28, 2006, the Company received a letter on behalf of Mr. Caviness, demanding that the Company take actions referenced in the Derivative Action complaint. The board of directors responded to both of the foregoing letters that the board has taken the letters under advisement pending further regulatory investigation developments, which the board continues to monitor and with which the Company continues to cooperate. In its responses, the board also requested confirmation of each person's status as a stockholder of Aspen Technology, Inc., and, with respect to the most recent letter, also referred the purported stockholder to the March 6, 2006 final approval of the settlement of direct and indirect claims of the Class in the Class Actions.

On September 27, 2006, a purported derivative action was filed in Massachusetts state court against the Company and certain present and former officers and directors captioned *Rapine v. AspenTech* (Civ. No. 06-3455). The complaint alleged that the Company breached its fiduciary duty in connection with the Company's restatement of financial statements stemming from its review of past stock option grants. On October 16, 2006, the Company removed the case to federal court and moved to dismiss it on the grounds that the plaintiff had failed to make the requisite pre-suit demand on the Company's board of directors, and because the Company was advised that the claims are largely also barred by the March 6, 2006 Class

Action settlement. The court has not ruled on the motion to dismiss. The Company cannot estimate the ultimate outcome of the case at this preliminary stage.

Other

From time to time, the Company is subject to legal proceedings, claims, and litigation arising in the ordinary course of business. The outcome of these matters is currently not determinable, and there can be no assurance that such matters will not have a material adverse effect on the Company's consolidated financial position, results of operations, or cash flows.

The Company maintains strategic alliance relationships with third parties, including resellers, agents and systems integrators (collectively Agents or Agent) that market, sell and/or integrate the Company's products and services. The cessation or termination of certain relationships, by us the Company or an Agent, may subject the Company to material liability and/or expense. This material liability and/or expense includes potential payments due upon the termination or cessation of the relationship by us the Company or an Agent, costs related to the establishment of a direct sales presence or development of a new Agent in the territory.

No such events of termination or cessation have occurred. The Company is not able to reasonably estimate the amount of any such liability and/or expense if such event were to occur, given the range of factors that could affect the ultimate determination of the liability. Actual payments could be in the range of zero to twenty million dollars. If the Company reacquires the territorial rights for an applicable sales territory and establishes a direct sales presence, future commissions otherwise payable to an Agent for existing customer maintenance contracts and other intangible assets may be assumed from the Agent. If any of the foregoing were to occur, the Company may be subject to litigation and liability such that its operating results, cash flows and financial condition could be materially and adversely affected.

9. Preferred Stock Financing

In August 2003, the Company issued and sold 300,300 shares of Series D-1 convertible preferred stock (Series D-1 Preferred), along with warrants to purchase up to 6,006,006 shares of common stock at a price of \$3.33 per share, in a private placement to several investment partnerships managed by Advent International Corporation for an aggregate purchase price of \$100.0 million and incurred issuance costs of \$10.7 million. Concurrently, the Company paid cash of \$30.0 million and issued 63,064 shares of Series D-2 convertible preferred stock (Series D-2 Preferred), along with warrants to purchase up to 1,261,280 shares of common stock at a price of \$3.33 per share, to repurchase all of the outstanding Series B-I and B-II convertible preferred stock. In addition the Company exchanged existing warrants to purchase 791,044 shares of common stock at an exercise price ranging from \$20.64 to \$23.99 held by the Series B Preferred holders, for new warrants to purchase 791,044 shares of common stock at an exercise price of \$4.08.

In May 2006, holders of the Series D-1 Preferred converted 30,000 shares into 3,000,000 shares of common stock so that as of September 30, 2006 the Series D Preferred is convertible into 33,336,400 shares of common stock. In July 2006, 6,006,006 warrants were exercised in a cashless exercise, resulting in the issuance of 4,369,336 shares of the Company's common stock.

In the accompanying consolidated condensed statements of operations, the accretion of preferred stock discount and dividend consist of the following (in thousands):

	Three Months Ended	
	September 30,	
	2006	2005
Accrual of dividend on Series D preferred stock	\$ (2,812)	\$ (2,808)
Accretion of discount on Series D preferred stock	(924)	(970)
Total	\$ (3,736)	\$ (3,778)

10. Segment Information

SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, establishes standards for reporting information about operating segments in companies' financial statements. Operating segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance. The Company's chief operating decision maker is the Chief Executive Officer of the Company.

The Company is organized geographically and by line of business. The Company has three major lines of business operating segments: license, consulting services and maintenance and training. The Company also evaluates certain subsets of business segments by vertical industries as well as by product categories. While the Executive Management Committee evaluates results in a number of different ways, the line of business management structure is the primary basis for which it assesses financial performance and allocates resources.

The accounting policies of the line of business operating segments are the same as those described in the Company's Annual Report on Form 10-K, as amended, for the fiscal year ended June 30, 2006. The Company does not track assets or capital expenditures by operating segments. Consequently, it is not practical to show assets, capital expenditures, depreciation or amortization by operating segments. The following table presents a summary of operating segments (in thousands):

	License	Consulting Services	Maintenance and Training	Total
Three Months Ended September 30, 2006				
Revenues from external customers	\$ 28,076	\$ 16,544	\$ 19,702	\$ 64,322
Controllable expenses	12,698	10,767	3,784	27,249
Controllable margin(1)	\$ 15,378	\$ 5,777	\$ 15,918	\$ 37,073
Three Months Ended September 30, 2005				
Revenues from external customers	\$ 24,037	\$ 16,946	\$ 18,851	\$ 59,834
Controllable expenses	14,927	11,273	3,441	29,641
Controllable margin(1)	\$ 9,110	\$ 5,673	\$ 15,410	\$ 30,193

(1) The controllable margins reported reflect only the expenses of the line of business and do not represent the actual margins for each operating segment since they do not contain an allocation for selling and marketing, general and administrative, development and other corporate expenses incurred in support of the line of business.

Profit Reconciliation (in thousands):

	Three Months Ended September 30,	
	2006	2005
Total controllable margin for reportable segments	\$ 37,073	\$ 30,193
Selling and marketing	(17,629)	(15,335)
General and administrative and overhead	(17,438)	(17,758)
Restructuring charges	(1,446)	(2,199)
Loss on sales and disposals of assets	(5,769)	(61)
Interest and other income and expense, net	673	(2,481)
Income (loss) before provision for from income taxes	\$ (4,536)	\$ (7,641)

11. Recent Accounting Pronouncements

In July 2006, the FASB issued Interpretation No. 48, Accounting for Uncertain Tax Positions, an Interpretation of FAS 109 (FIN 48), which clarifies the criteria for recognition and measurement of benefits from uncertain tax positions. Under FIN 48, an entity should recognize a tax benefit when it is more-likely-than-not, based on the technical merits, that the position would be sustained upon examination by a taxing authority. The amount to be recognized should be measured as the largest amount of tax benefit that is greater than 50 percent likely of being realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information. Furthermore, any change in the recognition, derecognition or measurement of a tax position should be recognized in the interim period in which the change occurs. The Company expects to adopt FIN 48 as of July 1, 2007, and any change in net assets as a result of applying the Interpretation will be recognized as an adjustment to retained earnings on that date. The Company is in the process of evaluating its uncertain tax positions in accordance with FIN 48.

In September 2006, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements (SAB 108), which provides guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of materiality. SAB 108 is effective for fiscal years beginning after November 15, 2006. The Company believes that the initial adoption of SAB 108 will not have a material impact on its consolidated financial statements.

In September 2006, the FASB issued Statement of Financial Standard No. 157, Fair Value Measurements (SFAS 157). SFAS 157 establishes a framework for measuring fair value in generally accepted accounting principles (GAAP), and expands disclosures about fair value measurements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. The Company has not yet determined the effect, if any, that the application of SFAS No. 157 will have on its consolidated financial statements.

12. Restatement of Condensed Consolidated Financial Statements

Subsequent to the issuance of condensed consolidated financial statements for the three months ended September 30, 2006, and in the course of preparing the condensed consolidated financial statements for the three and six months ended December 31, 2006, the Company identified errors in the accounting for foreign currency denominated transactions. The Company incorrectly accounted for transaction gains and losses on intercompany balances denominated in currencies other than the functional currency as if such balances were of a long term investment nature and included the impact as a component of accumulated other comprehensive income (loss) rather than earnings. These transaction gains and losses should have been included in earnings as the conditions for accounting for these intercompany balances as a long term investment were not met. In addition, the Company identified errors in the recording of purchase accounting in other than the functional currency of the acquired entity. These purchase accounting adjustments should have been denominated in the currency of the applicable subsidiary and translated to United States Dollars and were incorrectly recorded as United States Dollar denominated net assets in the consolidated financial statements. Accordingly, translation of the balance sheet position related to the purchase accounting allocations and translation impact of the amortization of intangible assets was not recorded.

In addition, the Company identified other errors in the course of preparing the condensed consolidated financial statements for the three and six months ended December 31, 2006. These errors related to the timing of recognition of service revenue, facility leasing costs, and professional fees in the three months ended September 30, 2006. The tax effect of correcting all of the above errors required further adjustments. The Company also added disclosure related to reseller relationships in Note 8.

In order to correct these errors, the Company has restated its financial statements for the three months ended September 30, 2005 and 2006, in order to reflect (a) foreign currency transaction losses of \$3.1 million and gains of \$0.3 million, respectively, (b) additional amortization of technology related intangible assets of \$0.3 million and \$0.4 million, respectively, (c) income tax provision decrease of \$1.0 million and \$0.1 million, respectively, (d) additional facility lease costs of less than \$0.1 million in each period, and (e) for the three months ended September 30, 2006, an increase in service revenues of \$0.4 million and a decrease in legal costs of \$0.1 million, and related balance sheet adjustments.

In connection with the preparation of the consolidated financial statements for the fiscal year ended June 30, 2006, a subcommittee of independent members of the board of directors reviewed the Company's accounting treatment for all stock options granted since the Company completed its initial public offering in fiscal 1995. Based upon the subcommittee's review, the Audit Committee and Company management determined that certain option grants during fiscal years 1995 through 2004 were accounted for improperly, and concluded that stock-based compensation associated with certain grants was misstated in fiscal years 1995 through 2005, and in the nine months ended March 31, 2006. The subcommittee identified errors related to the determination of the measurement dates for grants of options allocated among a pool of employees when the specific number of options to be awarded to specific employees had not been finalized, and other measurement date errors. As a result of the errors in determining measurement dates, the Company also recorded payroll withholding tax-related adjustments for certain options formerly classified as Incentive Stock Option (ISO) grants under Internal Revenue Service regulations. These options were determined to have been granted with an exercise price below the fair market value of the Company's stock on the actual grant date, so do not qualify for ISO tax treatment. The disqualification of ISO classification and the resulting conversion to non-qualified status results in additional withholding taxes on exercise of those options. The Company recorded estimated payroll withholding tax charges of \$0.5 million, \$0.2 million, and \$1.2 million for the years ended June 30, 2004, 2005, and 2006, respectively, in connection with the disqualification of such ISO tax treatment. The stock-based compensation charges, including the aforementioned withholding tax adjustments, increased the net loss by \$0.2 million for the three months ended September 30, 2005 relative to amounts previously reported for that quarter.

In addition, as a result of the errors in determining measurement dates, certain options were determined to have been granted with an exercise price below the fair market value of the Company's stock on the actual grant date. These discounted options vesting subsequent to December 2004 result in nonqualified deferred compensation for purposes of Section 409A of the Internal Revenue Code, and holders are subject to an excise tax on the value of the options in the year in which they vest. Management has concluded that it is probable the Company will either implement a plan to assist the affected employees for the amount of this tax, or adjust the terms of the original option grant which would also have financial statement ramifications. As such, the Company recorded an estimated liability of approximately \$1.0 million in June 2006 in connection with this contingency.

In the course of preparing the condensed consolidated financial statements for the three months ended September 30, 2006, the Company identified errors in the accounting for stock-based compensation and certain revenue transactions in the fiscal year ended June 30, 2006. The stock-based compensation error was due to a calculation error associated with forfeiture rates upon the adoption of SFAS No. 123(R), *Share-Based Payment* (SFAS No. 123R), as of July 1, 2005. The effect of correcting this error increased the net loss by \$0.3 million during the three months ended September 30, 2005 relative to amounts previously reported for that quarter.

The restatement of the condensed consolidated financial statements for the quarter ended September 30, 2005 also included adjustments for other errors identified after that quarter had originally been reported. These errors primarily related to the timing of revenue recognition, interest income, and the calculation of foreign currency gains and losses.

Effects of the Restatements

As a result of the foregoing, the Company has restated its condensed consolidated financial statements for the three months ended September 30, 2005 and 2006.

Impact of the Financial Statement Adjustments on the Condensed Consolidated Statement of Operations

The following table presents the impact of the financial statement adjustments on the Company's previously reported condensed consolidated statement of operations (in thousands, except per share data).

Condensed Consolidated Statement of Operations

	Three Months Ended September 30, 2006			Three Months Ended September 30, 2005		
	As Previously Reported	Restatement Adjustments	As Restated	As Previously Reported	Restatement Adjustments	As Restated
Software licenses	\$ 28,076	\$	\$ 28,076	\$ 24,317	\$ (280)	\$ 24,037
Service and other	35,878	368	36,246	35,736	61	35,797
Total revenues	63,954	368	64,322	60,053	(219)	59,834
Cost of software licenses	3,149		3,149	3,782	93	3,875
Cost of service and other	17,481		17,481	17,244	99	17,343
Amortization of technology related intangible assets	1,472	430	1,902	1,782	324	2,106
Total cost of revenues	22,102	430	22,532	22,808	516	23,324
Gross profit	41,852	(62)	41,790	37,245	(735)	36,510
Operating costs:						
Selling and marketing	21,210		21,210	18,647	111	18,758
Research and development	8,490		8,490	10,134	49	10,183
General and administrative	10,145	(61)	10,084	10,185	284	10,469
Restructuring charges	1,446		1,446	2,199		2,199
Loss on sales and disposals of assets	5,769		5,769	61		61
Total operating costs	47,060	(61)	46,999	41,226	444	41,670
Income (loss) from operations	(5,208)	(1)	(5,209)	(3,981)	(1,179)	(5,160)
Foreign currency exchange gain (loss)	(415)	321	(94)	(663)	(2,364)	(3,297)
Interest income, net	767		767	151	665	816
Income before provision for income taxes	(4,856)	320	(4,536)	(4,493)	(3,148)	(7,641)
Provision for income taxes	(932)	51	(881)	(640)	949	309
Net income (loss)	(5,788)	371	(5,417)	(5,133)	(2,199)	(7,332)
Accretion of preferred stock discount and dividend	(3,736)		(3,736)	(3,778)		(3,778)
Income applicable to common shareholders	\$ (9,524)	\$ 371	\$ (9,153)	\$ (8,911)	\$ (2,199)	\$ (11,110)
Basic and diluted income (loss) per share applicable to common shareholders	\$ (0.18)	\$ 0.01	\$ (0.17)	\$ (0.21)	\$ (0.05)	\$ (0.26)
Weighted average shares outstanding basic and diluted	52,801		52,801	43,237		43,237

Impact of the Financial Statement Adjustments on the Condensed Consolidated Balance Sheet

The following table presents the impact of the financial statement adjustments on the Company's previously reported condensed consolidated balance sheet as of September 30, 2006 (in thousands).

	As Previously Reported	Restatement Adjustments	As Restated
Prepaid expenses and other current assets	\$ 8,439	\$ (1)	\$ 8,438
Total current assets	162,124	(1)	162,123
Property and leasehold improvements, net	8,093	318	8,411
Other intangible assets, net	3,658	1,147	4,805
Goodwill	14,901	3,130	18,031
Deferred tax assets	1,595	1,503	3,098
Total assets	247,617	6,097	253,714
Accrued expenses	66,961	204	67,165
Deferred revenue	52,824	71	52,895
Current liabilities	123,177	275	123,452
Deferred tax liability	1,309	(1,309)	
Accumulated deficit	(466,032)	(1,098)	(467,130)
Accumulated other comprehensive income (loss)	(53)	8,229	8,176
Total stockholders' equity (deficit)	(28,108)	7,131	(20,977)
Total liabilities and stockholders' equity (deficit)	247,617	6,097	253,714

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and the related notes appearing elsewhere in this Form 10-Q/A and in our annual report on Form 10-K, as amended, for the fiscal year ended June 30, 2006. This discussion contains forward-looking statements that involve risks, uncertainties and assumptions. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of a number of factors, including those set forth in Item 1A. Risk Factors in Part II of this Form 10-Q.

The following discussion gives effect to the restatements discussed in Note 12 to the consolidated financial statements included in this Form 10-Q/A. Our fiscal year ends on June 30, and references in this Form 10-Q/A to a specific fiscal year are the twelve months ended June 30 of such year (for example, fiscal 2006 refers to the year ended June 30, 2006).

Overview

We are a leading supplier of integrated software and services to the process industries, which consist of oil and gas, petroleum, chemicals, pharmaceuticals and other industries that manufacture and produce products from a chemical process. We provide a comprehensive, integrated suite of software applications that utilize proprietary empirical models of chemical manufacturing processes to improve plant and process design, economic evaluation, production, production planning and scheduling, and operational performance, and an array of services designed to optimize the utilization of these products by our customers.

Critical Accounting Estimates and Judgments

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of our financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, expenses and related disclosures. We base our estimates on historical experience and various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. The significant accounting policies that we believe are the most critical to aid in fully understanding and evaluating our reported financial results include the following:

- revenue recognition for both software licenses and fixed-fee consulting services;
- impairment of long-lived assets, goodwill and intangible assets;
- accrual of legal fees associated with outstanding litigation;
- accounting for income taxes;
- allowance for doubtful accounts;
- accounting for securitization of installments receivable and subsequent valuation;
- restructuring accruals; and
- accounting for stock-based compensation.

Revenue Recognition Software Licenses

We recognize software license revenue in accordance with SOP No. 97-2, Software Revenue Recognition, as amended by SOP No. 98-4 and SOP No. 98-9, as well as the various interpretations and clarifications of those statements. When we provide professional services considered not essential to the functionality of the software, and for which Vendor Specific Objective Evidence of fair value or VSOE, has been established, we recognize revenue for the delivered software when the basic criteria of SOP 97-2 are

met. VSOE has been established, in most instances, for Software Maintenance Services, Training and professional services rates. When we provide professional services that are considered essential to the functionality of the software, we recognize revenue when the basic criteria of SOP 97-2 are met and when the services have been completed. When we provide professional services, which involve significant production, modification or customization of the licensed software, we recognize such revenue and any related software licenses in accordance with SOP 81-1, Accounting for Performance of Construction Type and Certain Performance Type Contracts . These statements all require that four basic criteria must be satisfied before software license revenue can be recognized:

persuasive evidence of an arrangement between ourselves and a third party exists;

delivery of our product has occurred;

the sales price for the product is fixed or determinable; and

collection of the sales price is reasonably assured.

Our management uses its judgment concerning the satisfaction of these criteria, particularly the criteria relating to the determination of whether the fee is fixed and determinable and the criteria relating to the collectibility of the receivables, particularly the installments receivable, relating to such sales. These two criteria are particularly relevant to reseller transactions where, specifically, revenue is only recognized upon delivery to the end user, since the determination of whether the fee is fixed or determinable and whether collection is probable is more difficult. Should changes and conditions cause management to determine that these criteria are not met for certain future transactions, all or substantially all of the software license revenue recognized for such transactions could be deferred.

Revenue Recognition Fixed-Fee Consulting Services

We recognize revenue associated with fixed-fee service contracts in accordance with the proportional performance method, measured by the percentage of costs (primarily labor) incurred to date as compared to the estimated total costs (primarily labor) for each contract. When a loss is anticipated on a contract, the full amount of the anticipated loss is provided currently. Our management uses its judgment concerning the estimation of the total costs to complete the contract, considering a number of factors including the experience of the personnel that are performing the services and the overall complexity of the project. We have a significant amount of experience in the estimation of the total costs to complete a contract and have not typically recorded material losses related to these estimates. We do not expect the accuracy of our estimates to change significantly in the future. Should changes and conditions cause actual results to differ significantly from management's estimates, revenue recognized in future periods could be adversely affected.

Impairment of Long-lived Assets, Goodwill and Intangible Assets

In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, we review the carrying value of long-lived assets when circumstances dictate that they should be reevaluated, based upon the expected future operating cash flows of our business. These future cash flow estimates are based on historical results, adjusted to reflect our best estimate of future markets and operating conditions, and are continuously reviewed based on actual operating trends. Historically, actual results have occasionally differed from our estimated future cash flow estimates. In the future, actual results may differ materially from these estimates, and accordingly cause a full impairment of our long-lived assets.

In accordance with SFAS No. 142, Goodwill and Other Intangible Assets, we conduct at least an annual assessment on January 1st of the carrying value of our goodwill assets, which is based on either estimates of future income from the reporting units or estimates of the market value of the units, based on comparable recent transactions. These estimates of future income are based upon historical results,

adjusted to reflect our best estimate of future markets and operating conditions, and are continuously reviewed based on actual operating trends. Historically, actual results have occasionally differed from our estimated future cash flow estimates. In the future, actual results may differ materially from these estimates. In addition, the relevancy of recent transactions used to establish market value for our reporting units is based on management's judgment.

The timing and size of any future impairment charges involves the application of management's judgment and estimates and could result in the impairment of all or substantially all of our long-lived assets, intangible assets and goodwill, which totaled \$47.5 million as of September 30, 2006.

Accrual of Legal Fees Associated with Outstanding Litigation

We accrue estimated future legal fees associated with outstanding litigation for which management has determined that it is probable that a loss contingency exists. This requires management to estimate the amount of legal fees that will be incurred in the defense of the litigation. These estimates are based heavily on our expectations of the scope, length to complete and complexity of the claims. Historically, as these factors have changed after our original estimates, we have adjusted our estimates accordingly. In the future, additional adjustments may be recorded as the scope, length or complexity of outstanding litigation changes.

Accounting for Income Taxes

We estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual current tax liabilities together with the assessment of temporary differences resulting from differing treatment of items, such as deferred revenue, for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheet. Deferred tax assets also result from unused operating loss carryforwards, research and development tax credit carryforwards and foreign tax credit carryforwards. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income and to the extent we believe that recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase or decrease this allowance in a period, the impact will be included in the tax provision in our statement of operations.

Significant management judgment is required in determining any valuation allowance recorded against these deferred tax assets and liabilities. The valuation allowance is based on our estimates of taxable income by jurisdiction in which we operate and the period over which our deferred tax assets will be recoverable. In the event that actual results differ from these estimates or we adjust these estimates in future periods we may need to establish an additional valuation allowance which could result in a tax provision equal to the carrying value of our deferred tax assets. We have provided a full valuation allowance for all U.S. domiciled net deferred tax assets.

Allowance for Doubtful Accounts

We make judgments as to our ability to collect outstanding receivables and provide allowances for the portion of receivables for which collection is doubtful. Provisions are made based upon a specific review of all significant outstanding invoices. In determining these provisions, we analyze our historical collection experience and current economic trends. If the historical data we use to calculate the allowance provided for doubtful accounts do not reflect the future ability to collect outstanding receivables, additional provisions for doubtful accounts may be required for all or substantially all of certain receivable balances.

Accounting for Securitization of Installments Receivable

We made judgments with respect to several variables associated with our June 2005 and September 2006 securitization transactions that had a significant impact on the valuation of our retained

interest in the sold receivables, as well as the calculation of the loss on the transactions. These judgments include the discount rate used to value the retained interest in the sold receivables, and estimates of rates of default. In determining these factors, we consulted third parties with respect to fair market discount rates, and analyzed our historical collection experience to default rates and collection timing. If the historical collection data do not reflect the future ability to collect outstanding receivables, the value of our retained interest may fluctuate.

Accounting for Restructuring Accruals

We follow SFAS 146, Accounting for Costs Associated with Exit or Disposal Activities. In accounting for these obligations, we are required to make assumptions related to the amounts of employee severance, benefits, and related costs and to the time period over which facilities will remain vacant, sublease terms, sublease rates and discount rates. We base our estimates and assumptions on the best information available at the time the obligation has arisen. These estimates are reviewed and revised as facts and circumstances dictate; changes in these estimates could have a material effect on the amount accrued on the balance sheet.

Accounting for Stock-Based Compensation

We adopted SFAS No. 123(R), Share-Based Payment, effective July 1, 2005. Under the fair value provisions of this statement, stock-based compensation cost is measured at the grant date based on the value of the award and is recognized as expense over the vesting period. SFAS 123(R) requires significant judgment and the use of estimates, particularly for assumptions such as stock price volatility and expected option lives to value stock-based compensation in net income. If actual results differ significantly from these estimates, stock-based compensation expense and our results of operations could fluctuate significantly.

Results of Operations

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The following table sets forth the percentages of total revenues represented by certain condensed consolidated statement of operations data for the periods indicated:

	Three Months Ended	
	September 30,	
	2006	2005
Software licenses	43.6 %	40.2 %
Service and other	56.4	59.8
Total revenues	100.0	100.0
Cost of software licenses	4.9	6.5
Cost of service and other	27.2	29.0
Amortization of technology related intangible assets	2.9	3.5
Total Cost of Revenues	35.0	39.0
Gross Profit	65.0	61.0
Operating costs:		
Selling and marketing	33.0	31.3
Research and development	13.2	17.0
General and administrative	15.7	17.5
Restructuring charges	2.2	3.7
Loss on sales and disposals of assets		