NORTHWEST NATURAL GAS CO
Form 8-K
February 12, 2009

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 8-K

CURRENT REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

February 12, 2009

Date of Report (Date of earliest event reported)

NORTHWEST NATURAL GAS COMPANY

(Exact name of registrant as specified in its charter)

Commission File No. 1-15973

Oregon	**93-0256722**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

220 N.W. Second Avenue, Portland, Oregon 97209

(Address of principal executive offices) (Zip Code)

Registrant s Telephone Number, including area code: (503) 226-4211

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

¨ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

¨ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

¨ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

¨ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 2.02 Results of Operation and Financial Condition

On February 12, 2009, Northwest Natural Gas Company issued a press release announcing its earnings for the quarter and year ended December 31, 2009. A copy of the press release is attached as Exhibit 99.1.

The information contained herein and in the accompanying exhibit shall not be incorporated by reference into any filing of NW Natural, whether made before or after the date hereof, regardless of any general incorporation language in such filing, unless expressly incorporated by specific reference to such filing. The information in this report, including the exhibit hereto, shall not be deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liabilities of that section or Sections 11 and 12(a)(2) of the Securities Act of 1933, as amended.

Forward Looking Statements

This report and other presentations made by NW Natural from time to time may contain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements include statements concerning plans, objectives, goals, strategies, future events or performance, and other statements that are other than statements of historical facts. The company s expectations, beliefs and projections are expressed in good faith and are believed to have a reasonable basis. However, each such forward-looking statement involves uncertainties and is qualified in its entirety by reference to the factors described in Part I, Item 1A Risk Factors, and Forward-Looking Statements following Part II, and Item 7A Quantitative and Qualitative Disclosure about Market Risk in the company s 2007 Annual Report on Form 10-K; Part I, Forward-Looking Statements, Item 1A Risk Factors, and Part II, Item 7A, Quantitative and Qualitative Disclosures about Market Risk, in the company s most recent Annual Report on Form 10-K; and in Part I, Item 3 Quantitative and Qualitative Disclosures about Market Risk, Forward-Looking Statements following Part I, Item 2, and Part II, Item 1A Risk Factors in the company s most recent quarterly financial statements that could cause the actual results of the company to differ materially from those projected in such forward-looking statements.

All subsequent forward-looking statements, whether written or oral and whether made by or on behalf of the company, also are expressly qualified by these cautionary statements. Any forward-looking statement speaks only as of the date on which such statement is made, and the company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time and it is not possible for the company to predict all such factors, nor can it assess the impact of each such factor or the extent to which any factor, or combination of factors, may cause results to differ materially from those contained in any forward-looking statement.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

NORTHWEST NATURAL GAS COMPANY

(Registrant)

Dated: February 12, 2009

/s/ David H. Anderson
Senior Vice President and

Chief Financial Officer

EXHIBIT INDEX

Exhibits	**Description**
99.1	Press Release of Northwest Natural Gas Company issued February 12, 2009 (furnished and not filed).

e="2" face="Times New Roman" style="font-size:10.0pt;">)

(280

)

(8,715

)

Impairment of assets

(1,776

)

(1,776

)

Accrued expenses, June 30, 2004

12,049

911

12,960

Restructuring charge

9,132

4,349

968

14,449

Impairment of assets

(968

)

(968

)

Fiscal 2005 payments

(12,915

)

(4,534

)

(17,449

)

Restructuring charge Accretion

446

3

449

Change in estimate Revised assumptions

(287

)

(497

)

(784

)

Accrued expenses, June 30, 2005

8,425

232

8,657

Change in estimate Revised assumptions

643

27

670

Restructuring charge Accretion

432

432

Fiscal 2006 payments

(2,645

)

(67

)

(2,712

)

Accrued expenses, June 30, 2006

$

6,855

$

192

$

$

7,047

Expected final payment date

September 2012

December 2006

Closure/consolidation of facilities: Approximately $20.5 million and $9.1 million of the fiscal 2004 and 2005 restructuring charges, respectively, related to the termination of facility leases and other lease related costs. The costs recorded in fiscal 2005 related to termination activities did not qualify for accrual as of June 30, 2004. The facility leases had remaining terms ranging from several months to eight years. The amount accrued is an estimate of the remaining obligation under the lease or actual costs to buy-out leases, reduced by expected income from the sublease of the underlying properties.

Employee severance, benefits and related costs: Approximately $1.2 million and $4.4 million of the fiscal 2004 and 2005 restructuring charges, respectively, related to the reduction in headcount. In the aggregate, approximately 147 employees, or 9% of the workforce, were eliminated under the restructuring plan implemented by management. The fiscal 2005 restructuring charge related to employees had not been notified in a manner that would allow for accrual as of June 30, 2004. Such notification occurred in Q1, 2005. A majority of the employees were located in North America, although Europe was affected as well. All business units were affected, including services, sales and marketing, research and development, and general and administrative.

Impairment of assets: Approximately $1.8 million and $1.0 million of the fiscal 2004 and 2005 restructuring charges, respectively, related to charges associated with the impairment of fixed assets associated with the closed and consolidated facilities. These assets were reviewed for impairment in accordance with SFAS No. 144, and were considered to be impaired because their carrying values were in excess of their fair values.

(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 June 30, 2006, there was $10.0 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**	**Employee Severance, Benefits, and Related Costs**	**Impairment of Assets and Disposition Costs**	**Total**
Restructuring charge	$ 17,347	$ 10,028	$ 1,278	$ 28,653
Additional impairment of assets			302	302
Fiscal 2003 payments	(3,548)	(7,297)		(10,845)
Accrued expenses, June 30, 2003	13,799	2,731	1,580	18,110
Fiscal 2004 payments	(2,567)	(2,170)	(770)	(5,507)
Change in estimate Revised assumptions	(4,507)	(269)	(134)	(4,910)
Accrued expenses, June 30, 2004	6,725	292	676	7,693
Fiscal 2005 payments	(2,266)	(63)	(403)	(2,732)
Change in estimate Revised assumptions.	7,239	(69)	(195)	6,975
Accrued expenses, June 30, 2005	11,698	160	78	11,936
Change in estimate Revised assumptions.	1,116	(95)		1,021
Fiscal 2006 payments	(2,848)	(65)	(78)	(2,991)
Accrued expenses, June 30, 2006	$ 9,966	$	$	$ 9,966
Expected final payment date	September 2012			

Closure/consolidation of facilities: Approximately $17.4 million of the restructuring charge related to the termination of facility leases and other lease related costs. Of this amount, approximately $8.7 million was recorded in the three months ended December 31, 2002 and approximately $8.7 million was recorded as a result of the June 2003 increase to the accrual. The facility leases had remaining terms ranging from several months to eight years. The amount accrued is an estimate of the remaining obligation under the lease or actual costs to buy-out leases, reduced by expected income from the sublease of the underlying properties. The June 2003 increase to the accrual is primarily due to revised estimates related to sublease assumptions, as actual sublease rates have been significantly less than originally estimated and the Company has experienced delays contracting with sublessors. The revisions to the accrual that occurred in fiscal 2004 relate to revisions made to sublease assumptions and to the buyout of a remaining lease obligation and the revisions to the accrual that occurred in fiscal 2005 relate to revised estimates with respect to the facility vacancy term.

Employee severance, benefits and related costs: Approximately $10.0 million of the restructuring charge related to the reduction in headcount. Of this amount, approximately $8.2 million was recorded in the three months ended December 31, 2002 and approximately $1.8 million was recorded as a result of the June 2003 increase to the accrual. Approximately 400 employees, or 20% of the workforce, were eliminated under the restructuring plan implemented by management. All geographic regions and business units were affected, including services, sales and marketing, research and development, and general and administrative. The revisions to the accrual that occurred in fiscal 2004 relate to revisions of estimates of severance terms and benefit levels.

Impairment of assets and disposition costs: Approximately $1.3 million of the restructuring charge related to charges associated disposing of certain products and assets. This consisted of costs related to preparing certain development groups for divestment or closure, offset by a gain related to the cancellation of a note payable to a European government. The note payable was related to the research and development group that was divested as part of the restructuring plan. The revisions to the accrual that occurred in fiscal 2004 relate to changes in estimates of ongoing costs of disposal activities.

(d) Restructuring charges originally arising in Q4 FY02

In the fourth quarter of fiscal 2002, management initiated a plan to reduce operating expenses and to restructure operations around the Company s two primary product lines, engineering software and manufacturing/supply chain software. The Company reduced worldwide headcount by approximately 10%, or 200 employees, closed and consolidated facilities, and disposed of certain assets, resulting in an aggregate restructuring charge of $13.2 million. During fiscal 2004, the Company recorded a $1.5 million decrease to the accrual related to revised assumptions associated with lease exit costs, particularly the buyout of a remaining lease obligation, and severance obligations. During fiscal 2005, the Company recorded a $0.2 million increase to the accrual due to changes in estimates of sublease assumptions and severance settlements. During fiscal 2006, the Company recorded a $0.1 million increase to the accrual due to changes in sublease assumptions.

As of June 30, 2006, there was $0.5 million remaining in accrued expenses relating to the remaining severance obligations and lease payments. The components of the restructuring plan are as follows (in thousands):

Fiscal 2002 Restructuring Plan	**Closure/ Consolidation of Facilities**	**Employee Severance, Benefits, and Related Costs**	**Total**
Restructuring charge	$ 4,901	$ 8,285	$ 13,186
Fiscal 2002 payments		(1,849)	(1,849)
Accrued expenses, June 30, 2002	4,901	6,436	11,337
Fiscal 2003 payments	(695)	(4,748)	(5,443)
Accrued expenses, June 30, 2003	4,206	1,688	5,894
Fiscal 2004 payments	(1,302)	(1,060)	(2,362)
Change in estimate Revised assumptions	(1,221)	(320)	(1,541)
Accrued expenses, June 30, 2004	1,683	308	1,991
Fiscal 2005 payments	(994)	(284)	(1,278)
Change in estimate Revised assumptions	93	87	180
Accrued expenses, June 30, 2005	782	111	893
Change in estimate Revised assumptions	75		75
Fiscal 2006 payments	(375)	(66)	(441)
Accrued expenses, June 30, 2006	$ 482	$ 45	$ 527
Expected final payment date	September 2012	December 2006	

Closure/consolidation of facilities: Approximately $4.9 million of the restructuring charge related to the termination of facility leases and other lease-related costs. The facility leases had remaining terms ranging from several months to nine years. The amount accrued is an estimate of the actual costs to buy-out leases or to sublease the underlying properties. The revisions to the accrual that occurred in fiscal 2004 relate to revisions made to sublease assumptions, as actual sublease rates have been significantly less than originally estimated and the Company has experienced delays contracting with sub-lessors, and to the buyout of a remaining lease obligation.

Employee severance, benefits and related costs: Approximately $8.3 million of the restructuring charge related to the reduction in headcount. Approximately 200 employees, or 10% of the workforce, were eliminated under the changes to the business plan implemented by management. Business units impacted included sales and marketing, services, research and development, and general and administrative, across all geographic areas. The revisions to the accrual that occurred in fiscal 2004 relate to revisions of estimates of severance terms and benefit levels.

Write-off of assets: Approximately $1.2 million of the restructuring charge related to the write-off of prepaid royalties related to third-party software products that the Company will no longer support and sell.

(4) Line of Credit

In January 2003, the Company executed a Loan Arrangement with Silicon Valley Bank. This arrangement provides a line of credit of up to the lesser of (i) $15.0 million or (ii) 70% of eligible domestic receivables, and a line of credit of up to the lesser of (i) $10.0 million or (ii) 80% of eligible foreign receivables. The lines of credit bear interest at the bank s prime rate (8.25% at June 30, 2006). The Company needs to maintain a $4.0 million compensating cash balance with the bank, or it is subject to an unused line fee and collateral handling fees. The lines of credit initially were collateralized by nearly all of the assets of the Company, and upon the Company s achieving certain net income targets, the collateral would be reduced to a lien on the accounts receivable. The Company is required to meet certain financial covenants, including minimum tangible net worth, minimum cash balances and an adjusted quick ratio.

As of June 30, 2006, there were $8.5 million in letters of credit outstanding under the line of credit, and there was $11.8 million available for future borrowing. On September 15, 2006, the Company executed an amendment to the Loan Arrangement that adjusted the terms of certain financial covenants. The Loan Arrangement expires in January 2007.

(5) Accrued Expenses and Other Liabilities

Accrued expenses in the accompanying consolidated balance sheets consist of the following (in thousands):

	June 30,	
	2005	**2006**
Royalties and outside commissions	$ 12,777	$ 10,288
Payroll and payroll-related	13,047	21,784
Restructuring accruals	8,833	4,965
Payable to financing companies	16,662	11,407
Income and other taxes	12,009	11,918
Other	17,392	17,354
	$ 80,720	$ 77,716

Other liabilities in the accompanying consolidated balance sheets consist of the following (in thousands):

	June 30,	
	2005	**2006**
Restructuring accruals	$ 15,197	$ 13,191
Deferred rent	5,255	4,321
Royalties and outside commissions	2,691	2,534
Other		400
	$ 23,143	$ 20,446

F-20

(6) Long-Term Obligations

Long-term obligations consist of the following at June 30, 2005 and 2006 (in thousands):

	2005	2006
Note payable incurred in connection with an acquisition, payable in quarterly installments of approximately $273, plus interest at 6% per year through January 2006	$ 803	
Note payable of a UK subsidiary due in monthly installments of approximately $50 plus interest at 9% per year, through March 2008	577	396
	1,380	396
Less Current portion	1,042	247
	$ 338	$ 149

Maturities of these long-term obligations are as follows (in thousands):

Years Ending June 30,	Amount
2007	$ 247
2008	149
	$ 396

In June 1998, the Company sold $86.3 million of debentures to qualified institutional buyers. During fiscal 2004, the Company used a portion of the proceeds from the Series D-1 and Series D-2 redeemable convertible preferred stock financing to repurchase and retire $29.5 million of the Debentures. In June 2005, the Company paid $58.2 million to retire the entire outstanding principal amount of the Debentures, together with interest accrued thereon.

The Company recorded interest expense associated with these debentures of $4.5 million and $2.9 million in the years ended June 30, 2004 and 2005, respectively.

(7) Preferred Stock

The Company s Board of Directors is authorized, subject to any limitations prescribed by law, without further stockholder approval, to issue, from time to time, up to an aggregate of 10,000,000 shares of preferred stock in one or more series. Each such series of preferred stock shall have such number of shares, designations, preferences, voting powers, qualifications and special or relative rights or privileges, which may include, among others, dividend rights, voting rights, redemption and sinking fund provisions, liquidation preferences and conversion rights, as shall be determined by the Board of Directors in a resolution or resolutions providing for the issuance of such series. Any such series of preferred stock, if so determined by the Board of Directors, may have full voting rights with the common stock or limited voting rights and may be convertible into common stock or another security of the Company.

Series B redeemable convertible preferred stock

In February and March 2002, the Company sold 40,000 shares of Series B-I convertible preferred stock (Series B-I Preferred), and 20,000 shares of Series B-II convertible preferred stock (Series B-II Preferred and, collectively with Series B-I Preferred, the Series B Preferred) together with (i) warrants to purchase 507,584 shares of common stock at an initial exercise price of $23.99 per share and (ii) warrants to purchase 283,460 shares of common stock at an initial exercise price of $20.64 per share, to three institutional investors for an aggregate purchase price of $60.0 million. The Company received approximately $56.6 million in net cash proceeds after closing costs.

In June 2003, the Company amended the terms of the Series B Preferred in conjunction with the Series D-1 and Series D-2 redeemable convertible preferred stock financing. This amendment gave the holders of the Series B Preferred the right to redeem their Series B Preferred shares for cash in certain circumstances that were outside of the Company s control. As a result of this redemption feature, the carrying value of the Series B Preferred was reclassified outside of stockholders equity on the accompanying consolidated balance sheet. In August 2003, the Company repurchased all of the outstanding shares of Series B Preferred.

Series D redeemable convertible preferred stock

In August 2003, the Company issued and sold 300,300 shares of Series D-1 redeemable 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. 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 Preferred. 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 holders of the Series B Preferred, for new warrants to purchase 791,044 shares of common stock at an exercise price of $4.08. These transactions are referred to collectively as the Series D Preferred financing.

The Company incurred $10.7 million in costs related to the issuance of the Series D-1 and D-2 Preferred (together, the Series D Preferred) and allocated the net proceeds received between the Series D Preferred and the warrants on the basis of the relative fair values at the date of issuance, allocating $15.5 million of proceeds to the warrants. The warrants are exercisable at any time prior to the seventh anniversary of their issue date. The remaining discount on the Series D Preferred is being accreted to its redemption value over the earliest period of redemption.

The value of total consideration paid to the holders of the Series B Preferred, consisting of cash, Series D-2 Preferred and warrants, was less than the carrying value of the Series B Preferred at the time of retirement. This resulted in a gain of $6.5 million, which the Company recorded in the accretion of preferred stock discount and dividend line of the accompanying consolidated statement of operations.

Each share of Series D Preferred is entitled to vote on all matters in which holders of common stock are entitled to vote, receiving a number of votes equal to the number of shares of common stock into which it is then convertible. In addition, holders of Series D-1 Preferred, as a separate class, are entitled to elect a certain number of directors, based on a formula as defined in the Series D Preferred Certificate of Designations. The holders of the Series D-1 Preferred are entitled to elect a number of the Company s directors calculated as a ratio of the Series D-1 Preferred voting power as compared to the total voting power of the Company s common stock. The Series D-1 Preferred holders have elected three of the Company s current directors.

The Series D Preferred earns cumulative dividends at an annual rate of 8%, which are payable when and if declared by the Board of Directors, in cash or, subject to certain conditions, common stock. As of June 30, 2006, the Company has accrued $28.5 million in dividends on the Series D Preferred.

Each share of Series D Preferred is convertible at any time into a number of shares of common stock equal to its stated value divided by the then-effective conversion price. The stated value is currently $333.00 per share and is subject to adjustment in the event of any stock dividend, stock split, reverse stock split, recapitalization, or like occurrences. The current conversion price is $3.33 per share. Each share of Series D Preferred currently is convertible into 100 shares of common stock. The Series D Preferred have anti-dilution rights that will adjust the conversion ratio downwards in the event that the Company issues certain additional securities at a price per share less than the conversion price then in effect.

The Series D Preferred is subject to redemption at the option of the holders as follows: 50% on or after August 14, 2009 and 50% on or after August 14, 2010. The shares will be redeemed for cash at a price of $333.00 per share, plus accumulated but unpaid dividends.

The Series D Preferred is subject to redemption at the option of the Company, at any time after August 2006 at a price of $416.25 per share plus any accumulated and unpaid dividends if, among other things, the average trading price of the Company s common stock exceeds $7.60 per share for 45 consecutive days. If the Company makes such an election, the holders of the Series D Preferred may elect to convert their Series D Preferred shares into shares of common stock rather than have them redeemed.

On May 16, 2006, the Holders of the Series D Preferred converted 30,000 shares into 3,000,000 shares of common stock. At the time of the conversion the Company also paid $2.4 million in dividends on the converted shares. As of June 30, 2006, the Series D Preferred is convertible into 33,336,400 shares of common stock.

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

	Years Ended June 30,		
	2004	**2005**	**2006**
Accrual of dividend on Series B preferred	(296)		
Accretion of discount on Series B preferred	(643)		
Gain on retirement of Series B preferred, net of warrant modification charge	6,452		
Accrual of dividend on Series D preferred	(8,690)	(10,692)	(11,518)
Accretion of discount on Series D preferred	(3,181)	(3,758)	(3,865)
	$ (6,358)	$ (14,450)	$ (15,383)

(8) Stock-Based Compensation

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 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(R), 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. 123(R), 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 s policy is to issue new shares upon exercise of stock options.

The Company has elected the modified prospective transition method for adopting SFAS 123(R), and consequently prior periods have not been modified. Under this method, the provisions of SFAS 123(R) 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 123(R), the Company recorded $8.4 million of stock-based compensation for the year ended June 30, 2006, respectively, included in the following categories (in thousands):

Recorded as expense:	
Cost of service and other	$ 1,442
Selling and marketing	2,534
Research and development	1,239
General and administrative	3,015
	8,230
Capitalized computer software development costs:.	148
Total stock-based compensation	$ 8,378

The Company utilized the Black-Scholes valuation model for estimating the fair value of the stock compensation granted after the adoption of SFAS 123(R). The weighted-average fair values of the options granted under the stock option plans and shares subject to purchase under the employee stock purchase plan were $4.20 and $4.73, respectively, for the year ended June 30, 2006 using the following assumptions:

	Year Ended June 30, 2006	
	Stock Option Plans	**Stock Purchase Plan**
Average risk-free interest rate	4.56 %	4.02 %
Expected dividend yield	None	None
Expected life	6.0 Years	0.5 Years
Expected volatility	85 %	42 %

The dividend yield of zero is based on the fact that the Company has never paid cash dividends on common stock and has no present intention 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 over a period commensurate with the expected life of the options 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.

A summary of option activity under all stock option plans in fiscal 2004, 2005 and 2006 follows:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value ($000)
Outstanding, June 30, 2003	8,414,382	$ 11.35		
Options granted	6,278,204	3.04		
Options exercised	(1,321,997)	3.12		
Options forfeited	(101,435)	4.74		
Options expired	(904,061)	16.55		
Outstanding, June 30, 2004	12,365,093	7.52		
Options granted	4,076,825	6.18		
Options exercised	(1,271,047)	2.84		
Options forfeited	(2,681,580)	3.54		
Options expired	(1,451,575)	14.78		
Outstanding at June 30, 2005	11,037,716	8.56		
Options granted	3,147,500	5.74		
Options exercised	(2,602,564)	4.22		
Options forfeited.	(1,177,311)	4.99		
Options expired.	(944,892)	15.11		
Outstanding at June 30, 2006	9,460,449	$ 7.37	7.0	$ 52,820
Exercisable at June 30, 2006	5,402,058	$ 8.76	5.7	$ 22,648

The following tables summarize information about stock options outstanding and exercisable under the 1995 Plan, the 1995 Directors Plan, the 1996 Plan, the Petrolsoft Plan, the 2001 Plan and the 2005 Plan at June 30, 2006:

Range of Exercise Prices	Options Outstanding at June 30, 2006	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Options Exercisable at June 30, 2006	Weighted Average Exercise Price
$2.21-$4.33	1,932,900	6.4	$ 2.81	1,430,466	$ 2.82
4.33-8.67	5,658,956	8.3	5.93	2,251,252	6.33
8.67-13.00	245,845	7.5	10.80	97,592	10.29
13.00-17.34	1,279,868	3.0	14.05	1,279,868	14.05
17.34-21.67	15,438	3.9	20.63	15,438	20.63
21.67-26.01	88,500	3.2	23.69	88,500	23.69
26.01-30.34	150,540	1.5	28.94	150,540	28.94
30.34-34.68	27,386	2.6	31.28	27,386	31.28
34.68-39.01	24,000	4.0	38.50	24,000	38.50
39.01-43.34	37,016	3.5	40.04	37,016	40.04
June 30, 2006	9,460,449	7.0	$ 7.37	5,402,058	$ 8.76
Exercisable, June 30, 2005				7,094,332	$ 10.37
Exercisable, June 30, 2004				7,464,123	$ 10.48

As of June 30, 2006, the total compensation cost related to unvested awards not yet recognized was $16.7 million. The weighted average period over which this will be recognized is approximately three years. The total intrinsic value of options exercised during the year ended June 30, 2006 was $14.9 million. The

F-25

Company received $11.0 million from option exercises during the year ended June 30, 2006; a $0.1 million tax benefit was realized for tax deductions from option exercises during the year ended June 30, 2006.

Prior to July 1, 2005, the Company s employee stock compensation plans were accounted for in accordance with Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees (APB 25) and related interpretations. The Company elected the disclosure-only alternative permitted under SFAS No. 123 for fixed stock-based awards to employees.

Under APB 25, compensation expense was measured as of the date the number of shares and exercise price become fixed. Generally, this occurred on the grant date, in which case the stock option was accounted for as a fixed award as of the date of grant. Compensation expense associated with fixed awards was measured as the difference between the fair market value of our stock on the date of grant and the grant recipient s exercise price, which was the intrinsic value of the award on that date. Stock compensation expense was recognized over the vesting period using the ratable method, whereby an equal amount of expense was recognized for each year of vesting. The Company recognized stock-based compensation charges of $6.7 million and $0.4 million in the years ended June 30, 2004 and 2005 associated with the amortization to compensation expense related to stock option awards that had an intrinsic value on the date of grant.

SFAS 123(R) requires the presentation of pro forma information for the comparative period prior to the adoption as if all of the Company s employee stock options had been accounted for under the fair value method of the original SFAS 123. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS 123 to stock-based employee compensation to the prior-year periods (in thousands, except per share data).

	2004	**2005**
Income (loss) attributable to common shareholders (in thousands)		
As reported	$ (32,542)	$ (88,020)
Less: Stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(21,949)	(9,344)
Add: Stock-based compensation expense included in reported net income (loss).	6,703	1,524
Pro forma	$ (47,788)	$ (95,840)
Income (loss) attributable to common shareholders per share		
Basic and diluted		
As reported	$ (0.80)	$ (2.08)
Pro forma	(1.18)	(2.26)

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions used for grants during the applicable period:

	2004	**2005**
Risk free interest rates	3.27 3.50%	3.49 4.17%
Expected dividend yield	None	None
Expected life	5-7 Years	5 Years
Expected volatility	99%	100%

The weighted average fair value per option granted was $2.51 and $4.74 for the years ended June 30, 2004 and 2005, respectively.

F-26

The fair value of the shares issued under the employee stock purchase plan is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions used for grants during the applicable period:

	2004	**2005**
Risk free interest rates	3.49 3.50%	3.49 4.17%
Expected dividend yield	None	None
Expected life	6 months	6 months
Expected volatility	42%	42%

The weighted average fair value of shares issued under the employee stock purchase plan was $4.46 and $1.96 for the years ended June 30, 2004 and 2005, respectively

In May 2005, the shareholders approved the establishment of the 2005 Stock Incentive Plan (the 2005 Plan), which provides for the reservation of up to 4,000,000 shares of common stock for issuance under the 2005 Plan. The 2005 Plan provides for the grant of incentive and nonqualified stock options and other stock-based awards, including the grant of shares based upon certain conditions, the grant of securities convertible into common stock and the grant of stock appreciation rights. Restricted stock and other stock-based awards granted under the 2005 Plan may not exceed, in the aggregate, 2,000,000 shares of common stock. As of June 30, 2006, there were 3,925,000 shares of common stock available for issuance subject to awards under the 2005 Plan.

In December 2000, the shareholders approved the establishment of the 2001 Stock Option Plan (the 2001 Plan), which provides for the issuance of incentive stock options and nonqualified options. Under the 2001 Plan, the Board of Directors may grant stock options to purchase up to an aggregate of 4,000,000 shares of common stock. At July 1, 2002, July 1, 2003 and July 1, 2004, the 2001 Plan was expanded to cover an additional 5% of the outstanding shares on the preceding June 30, rounded down to the nearest number divisible by 10,000. In no event, however, may the number of shares subject to incentive options under the 2001 Option Plan exceed 8,000,000 unless the 2001 Plan is amended and approved by the shareholders. As of June 30, 2006, there were 786,950 shares of common stock available for grant under the 2001 Plan.

In December 1996, the shareholders of the Company approved the establishment of the 1996 Special Stock Option Plan (the 1996 Plan). This plan provides for the issuance of incentive stock options and nonqualified options to purchase up to 500,000 shares of common stock. Stock options become exercisable over varying periods and expire no later than 10 years from the date of grant. As of June 30, 2006, there were 119,252 shares available for grant under the 1996 Plan.

In October 1997, the Company s Board of Directors approved the 1998 Employee Stock Purchase Plan, under which the Board of Directors may grant stock purchase rights for a maximum of 1,000,000 shares through September 30, 2007. In December 2000 and 2003, the shareholders voted to increase the number of shares eligible under the 1998 Employee Stock Purchase Plan by 2,000,000 and 3,000,000 shares, respectively.

Participants are granted options to purchase shares of common stock on the last business day of each semi-annual payment period for 85% of the market price of the common stock on the first or last business day of such payment period, whichever is less. The purchase price for such shares is paid through payroll deductions, and the current maximum allowable payroll deduction is 10% of each eligible employee s compensation. Under the plan, the Company issued 976,960 shares in 2003, 315,751 shares in 2005, and 188,119 shares in 2006. As of June 30, 2006, there were 2,645,939 shares available for future issuance under the 1998 Employee Stock Purchase Plan as amended. In addition, on July 1, 2006, the Company issued 61,395 shares under the 1998 Employee Stock Purchase Plan.

(9) Common Stock

(a) *Warrants*

In connection with the August 1997 acquisition of NeuralWare, Inc., the Company converted warrants to purchase NeuralWare common stock into warrants to purchase 10,980 shares of the Company s common stock. Warrants to purchase 1,260 shares expired unexercised through June 30, 2005 and the remaining warrants expired unexercised in April 2006.

In connection with the February and March 2002 sales of Series B Preferred, the Company issued warrants with five-year lives to purchase 791,044 shares of common stock at an exercise price ranging from $20.64 to $23.99 per share, as noted previously in Note 7. In August 2003, in conjunction with the Series D Preferred financing, these warrants were exchanged for new warrants to purchase 791,044 shares of common stock at an exercise price of $4.08 per share. As of June 30, 2006, none of these warrants had been exercised. Such warrants will expire in fiscal 2007.

In connection with the May 2002 sale of common stock to private investors, the Company issued warrants to purchase up to 3,208,333 shares of common stock at a price of $13.20 per share. In August 2003, the warrants were canceled, and new warrants were issued to purchase 1,152,665 shares at an exercise price of $9.76 per share, due to the impact of the Series D Preferred financing on the warrants anti-dilution provisions. In January 2004, warrants to purchase 129,191 shares of common stock were exercised in a cashless exercise, resulting in the issuance of 17,922 shares of common stock. As of June 30, 2006, warrants to purchase 1,023,474 shares of common stock at an exercise price of $9.76 were exercisable.

In connection with the August 2003 Series D Preferred financing, the Company issued warrants with seven-year lives to purchase 7,267,286 shares of common stock at an exercise price of $3.33 per share. As of June 30, 2006, none of these warrants had been exercised. 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.

A summary of the Company s outstanding common stock warrants at June 30, 2006 is as follows:

Warrant:	Outstanding	Exercise Price	Expiration Date
Series B warrants	791,044	$ 4.08	Feb Mar 2007
Private placement warrants	1,023,474	$ 9.76	May 2007
Series D warrants(1)	7,267,286	$ 3.33	Aug 2010
Total outstanding at June 30, 2006	9,081,804		

(1) After the exercise of 6,006,006 Series D warrants in July 2006, 1,261,280 Series D warrants and 3,075,798 total warrants were outstanding.

(b) Stockholder Rights Plan

During fiscal 1998, the Board of Directors of the Company adopted a Stockholder Rights Agreement (the Rights Plan) and distributed one Right for each outstanding share of Common Stock. The Rights were issued to holders of record of Common Stock outstanding on March 12, 1998. Each share of Common Stock issued after March 12, 1998 will also include one Right, subject to certain limitations. Each Right when it becomes exercisable will initially entitle the registered holder to purchase from the Company one one-hundredth (1/100th) of a share of Series A Preferred Stock at a price of $175.00 (the Purchase Price).

The Rights will become exercisable and separately transferable when the Company learns that any person or group has acquired beneficial ownership of 15% or more of the outstanding Common Stock or on such other date as may be designated by the Board of Directors following the commencement of, or first public disclosure of an intent to commence, a tender or exchange offer for outstanding Common Stock that could result in the offeror becoming the beneficial owner of 15% or more of the outstanding Common Stock. In such circumstances, holders of the Rights will be entitled to purchase, for the Purchase Price, a number of hundredths of a share of Series A Preferred Stock equivalent to the number of shares of Common Stock (or, in certain circumstances, other equity securities) having a market value of twice the Purchase Price. Beneficial holders of 15% or more of the outstanding Common Stock, however, would not be entitled to exercise their Rights in such circumstances. As a result, their voting and equity interests in the Company would be substantially diluted if the Rights were to be exercised.

The Rights expire in March 2008, but may be redeemed earlier by the Company at a price of $.01 per Right, in accordance with the provisions of the Rights Plan.

The Company amended the Rights Plan in June 2003 so that the terms of the Rights Plan would not be applicable to the securities issued as part of the Series D preferred financing or to any securities issued in the future pursuant to the preemptive rights granted as part of this financing.

(10) Income Taxes

The Company accounts for income taxes under the provisions of SFAS No. 109, Accounting for Income Taxes. Under the liability method specified by SFAS No. 109, a deferred tax asset or liability is measured based on the difference between the financial statement and tax bases of assets and liabilities, as measured by the enacted tax rates.

Income (loss) before provision for income taxes consists of the following (in thousands):

	Years Ended June 30, 2004	2005	2006
Domestic	$ (9,999)	$ (66,270)	$ 15,505
Foreign	4,405	(5,269)	4,031
Total	$ (5,594)	$ (71,539)	$ 19,536

The provisions for income taxes shown in the accompanying consolidated statements of operations are composed of the following (in thousands):

	Years Ended June 30, 2004	2005	2006
Federal			
Current	$	$	$
Deferred	20,333	45	
State			
Current	739	778	990
Deferred	1,823		
Foreign			
Current	14,205	4,028	8,718
Deferred	(16,861)	(2,820)	(2,995)
	$ 20,239	$ 2,031	$ 6,713

The provision for income taxes differs from that based on the federal statutory rate due to the following (in thousands):

	Years Ended June 30, 2004	2005	2006
Federal tax at statutory rate	$ (1,958)	$ (25,038)	$ 6,837
State income tax, net of federal tax benefit	1,688	541	566
Utilization of net operating loss carryforward			(5,711)
Tax effect resulting from foreign activities	(9,566)	1,423	2,365
Tax credits generated	(1,193)	(1,397)	(1,000)
Permanent differences, net	1,337	425	3,408
Expiration of tax attributes		12,410	(48)
Provision for tax contingencies	4,319		2,317
Valuation allowance	25,612	13,667	(2,021)
Provision for income taxes	$ 20,239	$ 2,031	$ 6,713

The approximate tax effect of each type of temporary difference and carry forward is as follows (in thousands):

	June 30, 2005	2006
Deferred tax assets:		
Revenue related	$ 456	$ 3,253
Federal and state tax credits	14,023	12,531
Federal and state loss carryforwards	42,288	47,014
Foreign loss carryforwards	7,150	5,087
Restructuring accruals	21,004	18,301
Other reserves and accruals	13,552	10,281
Intangible assets	5,838	4,276
Property, plant and equipment	2,089	2,467
Other temporary differences	257	2,477
	106,657	105,687
Valuation allowance	(104,611)	(102,590)
	2,046	3,097
Deferred tax liabilities:		
Revenue related	1,721	
Intangible assets	(3,416)	
	(1,695)	
Net deferred tax assets (liabilities)	$ 351	$ 3,097

Upon customer payment of certain foreign receivables, withholding taxes are withheld by customers and remitted to local tax authorities. Under current U.S. tax law, these withholding taxes may be creditable against U.S. taxes payable subject to certain limitations. The Company has recorded a full valuation allowances against these credits, and will recognize the benefit of these credits only when it is more likely than not that these deferred tax assets will be realized. The withholding taxes are included in the foreign tax provision as they are withheld and remitted. Utilization of the taxes as foreign tax credits is recorded as a reduction of the domestic tax expense in the period it is more likely than not that these deferred tax assets will be realized.

As of June 30, 2006, the Company had net operating loss (NOL) carryforwards for U.S. federal and state income tax purposes of approximately $148.6 million and $51.7 million, respectively, and foreign net operating loss carryforwards of approximately $17.1 million. The Company had federal tax credits and state tax credits of approximately $14.5 million and $3.6 million, respectively. The tax credits and NOL carryforwards expire at various dates from 2007 through 2025. The Company has determined that it underwent an ownership change (as defined under section 382 of the Internal Revenue Code of 1986, as amended) during the year ended June 30, 2004. As such, the recognition of the Company s federal NOLs and tax credits may be limited. Moreover, an ownership change might have also occurred under the laws of certain states and foreign countries in which the Company has generated NOLs and tax credits. Accordingly, it is possible that these NOL and tax credits could also be limited under rules similar to those of section 382. Due to the uncertainty surrounding the realization and timing of these tax attributes, the Company has recorded a valuation allowance of approximately $104.6 million and $102.6 million as of June 30, 2005 and 2006, respectively.

(11) Operating Leases

The Company leases its facilities and various office equipment under noncancelable operating leases with terms in excess of one year. Rent expense charged to operations was approximately $11.7 million, $9.3 million and $7.5 million for the years ended June 30, 2004, 2005 and 2006, respectively. Future minimum lease payments under these leases as of June 30, 2006, net of sub-lease income of $1.8 million, $1.8 million, $0.7 million, $0.6 million, and $0.4 million for the years ended June 30, 2007, 2008, 2009, 2010, and 2011, respectively, are as follows (in thousands):

Years ended June 30,	**Amount**
2007	$ 9,680
2008	7,437
2009	7,570
2010	7,406
2011	6,460
Thereafter	14,834
	$ 53,387

The Company has issued approximately $8.3 million of standby letters of credit in connection with certain facility leases that expire through 2016.

(12) Sale of Installments Receivable

(a) Traditional Activities

Installments receivable represent the present value of future payments related to the financing of noncancelable term and perpetual license agreements that provide for payment in installments, generally over a one- to five-year period. A portion of each installment agreement is recognized as interest income in the accompanying consolidated statements of operations. The interest rates utilized for the years ended June 30, 2004, 2005, and 2006 ranged from 7.0% to 8.0%.

The Company has arrangements to sell certain of its installments receivable to three financial institutions. The Company has sold, and treated as sales certain of its installment contracts for aggregate proceeds of $54.9 million, $97.6 million and $77.1 million during fiscal 2004, 2005 and 2006, 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 $1.5 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

Initial Transaction

On June 15, 2005, the Company securitized certain outstanding installment software license receivables (which receivables were not sold in the traditional sales described above) with a net carrying value of $71.2 million. Such securitization was structured in a manner so that the securitization qualified as a sale. The Company received $43.8 million of cash and retained an interest in the sold receivables valued at $16.6 million. It also retained certain limited recourse obligations relative to the receivables valued at approximately $1.0 million. Overall, the transaction (including $2.1 million in aggregate fees and expenses, including fees of the lenders agent and fees of the Company s outside legal counsel and financial advisors) resulted in a loss of $14.6 million in the quarter ended June 30, 2005 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 noted above, the retained interest in the sold receivables was recorded at its fair market value of $16.6 million at the time of the transaction and was (and currently 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.

The Company retained the servicing rights relative to the receivables and receives annual servicing fees of $0.1 million per year. The benefits of servicing are just adequate to compensate the servicer for its responsibilities, and thus no servicing asset or liability has been recorded.

In connection with the above transaction, the Company incurred an obligation to guaranty that the proceeds from all foreign denominated installments receivable included in the securitized pool will be equal to the U.S. dollar value on the initial contract date. The fair value of this obligation, as of the transaction date and as of June 30, 2005 and 2006 was not material and has thus been accorded no value.

Ongoing Retained Interests

The Company values its retained interest in sold receivables in accordance with the guidance of EITF No. 99-20 Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interest in Securitized Financial Assets. Accordingly, its retained interest is being accreted through interest income over the anticipated life of the retained interest. The accretion methodology is assessed quarterly and any diminution in value is recoded directly to the statement of operations.

Key economic assumptions used in subsequently measuring potential impairment in the carrying value of the Company s retained interests in the software license receivables at June 30, 2005 and 2006 and the effect on the fair value of those interests from adverse changes in those assumptions are as follows (in thousands, except for annualized rates):

	June 30, 2005	**2006**
Balance sheet carrying value of retained interest in sold receivables	$ 16,667	$ 19,010
Expected credit losses (annual rate):	0.82 %	0.82 %
Impact on fair value of 10% adverse change	$ (48)	$ (34)
Impact on fair value of 20% adverse change	$ (96)	$ (68)
Residual cash flow discount rate (annual rate):	16.0 %	16.0 %
Impact on fair value of 10% adverse change	$ (923)	$ (774)
Impact on fair value of 20% adverse change	$ (1,790)	$ (1,512)

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. Further, this analysis does not assume any impact resulting from management s intervention to mitigate these variations.

(13) Commitments and Contingencies

(a) FTC Settlement

On December 21, 2004, the FTC approved the Company s proposed consent decree, which constituted a complete and final settlement of the FTC s complaint against the Company relating to its acquisition of Hyprotech in May 2002. The FTC s approval also constituted approval of the transactions contemplated by the purchase and sale agreement that the Company and its subsidiaries Hyprotech Company, AspenTech Canada Ltd., AspenTech Ltd. and Hyprotech UK Ltd. entered into on October 6, 2004 with Honeywell International, Inc. and its subsidiaries Honeywell Control Systems Limited and Honeywell Limited-Honeywell Limitee. The Company previously completed the sale of its AXSYS product line to Bentley Systems Incorporated on July 21, 2004, as set forth in the FTC consent decree. The Company recorded a $0.3 million gain related to this sale.

On December 23, 2004, the Company and its subsidiaries completed the transactions with Honeywell contemplated by the October 6, 2004 purchase agreement, which relates to the sale of the Company s operator training business and ownership of rights to the intellectual property to the Hyprotech engineering products to Honeywell International. Under the terms of the transactions:

- the Company retains a perpetual, worldwide, royalty-free license to the entire Hyprotech engineering software product line and has the right to continue to develop and sell the Hyprotech engineering products, other than AXSYS which was sold to Bentley Systems;

- the Company retains its customer licenses for HYSYS and related products;

- the Company retains all rights in its Aspen RefSYS and Aspen Oil & Gas solutions;

- the Company agreed to a cash payment of approximately $6.0 million from Honeywell in consideration of the transfer of the Company s operator training services business, the Company s covenant not-to-compete in the operator training business for three years, and the transfer of ownership of the intellectual property of the Company s Hyprotech engineering products, $1.2 million of which is subject to holdback and may be released upon the resolution of any adjustments for uncollected billed accounts receivable and unbilled accounts receivable;

- the Company transferred and Honeywell assumed, as of the closing date, approximately $4 million in accounts receivable relating to the operator training business; and

- the Company entered into a two-year support agreement with Honeywell under which the Company agrees to provide Honeywell with source code to new releases of the Hyprotech products provided to customers under standard software maintenance services agreements.

The Honeywell transaction resulted in a deferred gain of $0.2 million, which is subject to a potential increase of $1.2 million upon resolution of the holdback payment and will be amortized over the two-year life of the support agreement.

(b) KBC Settlement

On October 1, 2004, the Company, together with its subsidiaries AspenTech, Inc. and Hyprotech Company, entered into a Settlement Agreement with KBC Advanced Technologies Plc, KBC Advanced Technologies Inc. and AEA Technology Plc. Pursuant to the settlement agreement, the parties agreed to settle (1) the arbitration proceedings in England relating to a contract dispute involving the parties and (2) the legal proceedings filed by KBC in state district court in Houston, Texas against the Company and Hyprotech Company.

As part of the settlement, KBC recognized the Company s right to develop, market and license Aspen RefSYS, and the Company recognized KBC s right to develop, market and license HYSYS.Refinery, their respective refinery-wide simulation products. The Company licensed commercial, object code, copies of Aspen HYSYS, Aspen PIMS, and Aspen Orion to KBC for use as part of KBC s consulting services business, without the right to sublicense. In addition, the Company paid KBC $3.75 million in lieu of costs incurred in the dispute. This charge was recorded in fiscal 2005 in general and administrative expenses.

(c) Litigation

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. On October 29, 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.

On June 9, 2006, the Company announced that it had 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, on July 7, 2006, the Company announced that three of its former executive officers had each received a Wells Notice letter regarding the same matter.

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 or results of operations.

Class Action 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 Suit

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.

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.

(d) Other

The Company has entered into an employment agreement with its president and chief executive officer providing for the payment of cash and other benefits in certain situations of his voluntary or involuntary termination, including following a change in control. Payment under this agreement would consist of a lump sum equal to approximately two times (1) his annual base salary plus (2) the average of his annual bonus for the three preceding fiscal years. The agreement also provides that the payments would be increased in the event that it would subject him to excise tax as a parachute payment under the Internal Revenue Code. The increase would be equal to the additional tax liability imposed on him as a result of the payment.

The Company has entered into agreements with two executive officers, providing for severance payments in the event that the executive is terminated by the Company other than for cause. Payments under these agreements consist of continuation of base salary for a period of 12 months. The Company has also entered into an agreement with its former chairman and founder pursuant to which, in the event of a change in control, all amounts due to him for the remainder of the term of his agreement become immediately due and payable.

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 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 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.

(14) Retirement and Profit Sharing Plans

The Company maintains a defined contribution retirement plan under Section 401(k) of the Internal Revenue Code covering all eligible employees, as defined. Under the plan, a participant may elect to defer receipt of a stated percentage of his or her compensation, subject to limitation under the Internal Revenue Code, which would otherwise be payable to the participant for any plan year. The Company may make discretionary contributions to this plan, including making matching contributions up to a maximum of 6% of an employee s pretax contribution. During the fiscal years ended June 30, 2004, 2005 and 2006, the Company made matching contributions of approximately $0.1 million, $1.0 million and $0.8 million, respectively. These contributions, which vested immediately, were expensed in each respective year.

(15) Joint Ventures and Other Investments

In November 2000, the Company invested $0.6 million in a global chemical business-to-business e-commerce company supporting major chemical companies in Asia. This investment entitles the Company to a minority interest in this company and is accounted for using the cost method and, accordingly, is being valued at cost unless a permanent impairment in its value occurs or the investment is liquidated. As of June 30, 2006, the Company has determined that an other than temporary impairment has not occurred. This investment is included in other assets in the accompanying consolidated balance sheet as of June 30, 2005 and 2006.

In the accompanying consolidated statements of operations for the year ended June 30, 2004, the Company has recognized losses of approximately $0.4 million, as its portion of the losses from a joint venture that was dissolved in 2005 and from its investment in a Cyprus-based company that was surrendered in fiscal 2005.

(16) Segment and Geographic Information

The Company follows the provisions of SFAS No. 131, Disclosures about Segments of an Enterprise and related Information, which establishes standards for reporting information about operating segments in annual financial statements and requires selected information about operating segments in interim financial reports issued to stockholders. It also established standards for disclosures about products and services, and geographic areas. 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 line 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 license line of business is engaged in the development and licensing of software. The consulting services line of business offers implementation, advanced process control, real-time optimization and other consulting services in order to provide its customers with complete solutions. The maintenance and training line of business provides customers with a wide range of support services that include on-site support, telephone support, software updates and various forms of training on how to use the Company s products.

The accounting policies of the line of business operating segments are the same as those described in the summary of significant accounting policies. 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
Year ended June 30, 2004				
Revenues from external customers	$ 158,150	$ 96,512	$ 77,784	$ 332,446
Controllable expenses	66,825	69,854	14,323	151,002
Controllable margin(1)	$ 91,325	$ 26,658	$ 63,461	$181,444
Year ended June 30, 2005				
Revenues from external customers	$ 129,621	$ 65,248	$ 75,125	$ 269,994
Controllable expenses	64,225	53,835	16,299	134,359
Controllable margin(1)	$ 65,396	$ 11,413	$ 58,826	$135,635
Year ended June 30, 2006				
Revenues from external customers	$ 152,773	$ 63,919	$ 76,456	$ 293,148
Controllable expenses	66,045	47,093	14,715	127,853
Controllable margin(1)	$ 86,728	$ 16,826	$ 61,741	$165,295

(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:

	Years Ended June 30 2004 (In thousands)	2005	2006
Total controllable margin for reportable segments	$181,444	$135,635	$165,295
Selling and marketing	(90,907)	(80,349)	(70,716)
General and administrative and overhead	(79,764)	(85,986)	(70,841)
Asset impairment charges	(4,217)		
Restructuring charges and FTC legal costs	(20,085)	(24,960)	(3,993)
Gain (loss) on sales and disposals of assets	747	(14,314)	(898)
Interest and other income and expense	7,188	$ (1,565)	689
Income (loss) before (provision for) benefit from income taxes and equity in earnings from joint ventures	$ (5,594)	$ (71,539)	$ 19,536

F-38

Geographic Information:

Domestic and export sales as a percentage of total revenues are as follows:

	Years Ended June 30, 2004	2005	2006
United States	42.8 %	39.7 %	42.9 %
Europe	33.0	37.2	30.5
Japan	4.6	5.8	5.3
Other	19.6	17.3	21.3
	100.0 %	100.0 %	100.0 %

During the years ended June 30, 2004, 2005 and 2006 there were no customers that individually represented greater than 10% of the Company s total revenue.

The Company has long-lived assets of approximately $20.6 million that reside in the United States, and $28.4 million that reside in other geographic locations as of June 30, 2006.

Revenues for the Company s North American, European and Asian operations are as follows for the years ended June 30 (in thousands). The Company has intercompany distribution arrangements with its subsidiaries. The basis for these arrangements, disclosed below as transfers between geographic locations, is cost plus a specified percentage for services and a commission rate for sales generated in the geographic region.

	North America	Europe	Asia	Eliminations	Consolidated
2004	$ 240,280	$ 83,427	$ 16,825	$ (8,086)	$ 332,446
2005	$ 180,465	$ 75,035	$ 17,916	$ (3,422)	$ 269,994
2006	$ 215,588	$ 60,201	$ 19,165	$ (1,806)	$ 293,148

(17) Restatements of Consolidated Financial Statements

First Restatement

In connection with the preparation of 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 yet been finalized, and other measurement date errors. As a result of the errors in determining measurement dates, the Company has 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 $7.2 million and $0.5 million for the years ended June 30, 2004 and 2005, and resulted in compensation charges totaling $50.1 million for the periods prior to fiscal 2004, which is reflected in the July 1, 2003 beginning accumulated deficit.

F-39

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 the fourth quarter of fiscal 2006 in connection with this contingency.

The restatement of prior year financial statements also includes the adjustments for other errors identified after the applicable period had been originally reported. Such errors were not previously recorded because the Company believed the amount of any such errors, both individually and in the aggregate, were not material to the Company s consolidated financial statements. These errors related to the timing of revenue recognition, losses on sales and disposals of assets, interest income, and the calculation of foreign currency gains and losses.

Second Restatement

Subsequent to the issuance of the consolidated financial statements for the fiscal year ended June 30, 2006, and 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. 123R, as of July 1, 2005.

In order to correct these errors, the Company has restated its financial statements for the fiscal year ended June 30, 2006 in order to reflect (a) additional stock-based compensation expense of approximately $1.4 million and (b) additional revenues of approximately $0.3 million. These errors had no effect on the fiscal year ended June 30, 2004 or 2005.

Third Restatement

Subsequent to the Company s issuance of restated consolidated financial statements for the year ended June 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 in the years ended June 30, 2002 through 2006, and the three months ended September 30, 2005 and 2006. 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 long term investments 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 properly 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 and facility leasing costs, losses on sale of assets and inappropriate gross presentation of receivables and deferred revenue for customers that did not meet revenue recognition criteria. The tax effect of correcting all of the above errors required further adjustments. The Company also added disclosure relative to reseller relationships in Note 13.

In order to correct these errors, the Company has restated its financial statements for the fiscal years ended June 30, 2004, 2005 and 2006, in order to reflect (a) foreign currency transaction gains of $3.8 million, losses of $3.1 million, and losses of $4.4 million, respectively, (b) additional amortization of technology related intangible assets of $0.7 million, $1.1 million, and $1.5 million, respectively, (c) additional facility lease costs of less than $0.1 million per fiscal year, (d) for the year ended June 30, 2006, a reduction in service revenues of $0.4 million, (e) for the year ended June 30, 2004 an increase in loss on sales and disposals of assets of $0.1 million, (f) income tax provision increase of $0.1 million and decrease of $1.5 million and of $2.0 million, respectively, and (g) the reduction of accounts receivable and offsetting reduction in deferred revenues of $6.5 million at June 30, 2006 to eliminate the gross presentation of amounts due from customers that had not met revenue recognition criteria. These errors had a cumulative effect of decreasing net loss by $2.9 million, net of income taxes, for the periods prior to fiscal 2004, which is reflected in the July 1, 2003 beginning accumulated deficit.

Effects of Restatements

As a result of the foregoing, the Company has restated its financial statements as of June 30, 2005 and 2006 and for the fiscal years ended June 30, 2004, 2005 and 2006. The first and third restatement also affected periods prior to fiscal 2004 which are reflected in the opening accumulated deficit and other comprehensive loss of the Company as of June 30, 2003.

The effect of the restatements are summarized as follows:

	Income (loss) attributable to common shareholders			Accumulated deficit
	2004	2005	2006	July 1, 2003
	(In thousands)			
Originally reported	$ (28,164)	$ (83,822)	$ 2,963	$ (286,742)
First Restatement				
Stock compensation	(7,199)	(515)		(50,051)
Other	(50)	(887)		(936)
Second Restatement				
Stock compensation forfeiture rate			(1,355)	
Other			250	
Third Restatement				
Foreign currency transaction related	3,823	(3,118)	(4,436)	2,119
Foreign currency translation related	(706)	(1,108)	(1,489)	(108)
Other	(165)	(38)	(486)	(16)
Tax effects	(81)	1,468	1,993	879
As restated	$ (32,542)	$ (88,020)	$ (2,560)	$ (334,855)

Revenue and Expense Adjustments

Set forth below are the adjustments to the Company s previously issued statements of operations for the fiscal years ended June 30, 2004, 2005 and 2006 (amounts in thousands).

	Year ended June 30, 2004				
		First Restatement		Third Restatement	
	As Previously Reported	Stock-based Compensation and Related Payroll Withholding Tax Adjustments	Other Adjustments	Adjustments	As Restated
Revenues:					
Software licenses	$ 158,661	$	$ (511)	$	$ 158,150
Service and other	174,335		(39)		174,296
Total revenues	332,996		(550)		332,446
Cost of revenues:					
Cost of software licenses	15,577				15,577
Cost of service and other	99,183	2,557	83		101,823
Amortization of technology related intangible assets	7,270			706	7,976
Impairment of technology related intangible and computer software development assets	3,250				3,250
Total cost of revenues	125,280	2,557	83	(706)	128,626
Gross profit	207,716	(2,557)	(633)	(706)	203,820
Operating costs:					
Selling and marketing	100,028	1,826	(48)		101,806
Research and development	58,955	1,204	(48)		60,111
General and administrative	32,727	1,612	8	33	34,380
Long-lived asset impairment charges	967				967
Restructuring charges and FTC legal costs	20,085				20,085
Loss (gain) on sales and disposals of assets	(879)			132	(747)
Total operating costs	211,883	4,642	(88)	165	216,602
Income (loss) from operations	(4,167)	(7,199)	(545)	(871)	(12,782)
Interest income	7,296				7,296
Interest expense	(4,940)				(4,940)
Foreign currency exchange gain (loss)	252		757	3,823	4,832
Income (loss) before provision for income taxes and equity in earnings from joint ventures	(1,559)	(7,199)	212	2,952	(5,594)
Provision for income taxes	(19,896)		(262)	(81)	(20,239)
Equity in losses from joint ventures	(351)				(351)
Net income (loss)	(21,806)	(7,199)	(50)	2,871	(26,184)
Accretion of preferred stock discount and dividend	(6,358)				(6,358)
Income (loss) attributable to common shareholders	$ (28,164)	$ (7,199)	$ (50)	$ 2,871	$ (32,542)
Basic income (loss) per share attributable to common shareholders	$ (0.69)	$ (0.18)	$ (0.00)	$ 0.07	$ (0.80)
Diluted income (loss) per share attributable to common shareholders	$ (0.69)	$ (0.18)	$ (0.00)	$ 0.07	$ (0.80)
Basic weighted average shares outstanding	40,575				40,575
Diluted weighted average shares outstanding	40,575				40,575

F-42

	Year ended June 30, 2005				
	As Previously Reported	First Restatement Stock-based Compensation and Related Payroll Withholding Tax Adjustments	Other Adjustments	Third Restatement Adjustments	As Restated
Revenues:					
Software licenses	$ 129,233	$	$ 388	$	$ 129,621
Service and other	140,334		39		140,373
Total revenues	269,567		427		269,994
Cost of revenues:					
Cost of software licenses	16,864				16,864
Cost of service and other	82,638	189	(83)		82,744
Amortization of technology related intangible assets	7,112			1,108	8,220
Impairment of technology related intangible and computer software development assets					
Total cost of revenues	106,614	189	$ (83)	1,108	107,828
Gross profit	162,953	(189)	510	(1,108)	162,166
Operating costs:					
Selling and marketing	96,187	136	(48)		96,275
Research and development	47,236	88	(48)		47,276
General and administrative	49,175	102		38	49,315
Long-lived asset impairment charges					
Restructuring charges and FTC legal costs	24,907		53		24,960
Loss (gain) on sales and disposals of assets	13,635		679		14,314
Total operating costs	231,140	326	636	38	232,140
Income (loss) from operations	(68,187)	(515)	(126)	(1,146)	(69,974)
Interest income	6,143		61		6,204
Interest expense	(4,170)				(4,170)
Foreign currency exchange gain (loss)	618		(1,099)	(3,118)	(3,599)
Income (loss) before provision for income taxes and equity in earnings from joint ventures	(65,596)	(515)	(1,164)	(4,264)	(71,539)
Provision for income taxes	(3,776)		277	1,468	(2,031)
Equity in losses from joint ventures					
Net income (loss)	(69,372)	(515)	(887)	(2,796)	(73,570)
Accretion of preferred stock discount and dividend	(14,450)				(14,450)
Income (loss) attributable to common shareholders	$ (83,822)	$ (515)	$ (887)	$ (2,796)	$ (88,020)
Basic income (loss) per share attributable to common shareholders	$ (1.98)	$ (0.01)	$ (0.02)	$ (0.07)	$ (2.08)
Diluted income (loss) per share attributable to common shareholders	$ (1.98)	$ (0.01)	$ (0.02)	$ (0.07)	$ (2.08)
Basic weighted average shares outstanding	42,381				42,381
Diluted weighted average shares outstanding	42,381				42,381

F-43

	Year ended June 30, 2006			
		Second Restatement	Third Restatement	
	As Previously Reported	Adjustments	Adjustments	As Restated
Revenues:				
Software licenses	152,686	$ 87	$	$ 152,773
Service and other	140,564	250	(439)	140,375
Total revenues	293,250	337	(439)	293,148
Cost of revenues:				
Cost of software licenses	16,805			16,805
Cost of service and other	72,492	198		72,690
Amortization of technology related intangible assets	7,070		1,489	8,559
Impairment of technology related intangible and computer software development assets				
Total cost of revenues	96,367	198	1,489	98,054
Gross profit	196,883	139	(1,928)	195,094
Operating costs:				
Selling and marketing	84,010	495		84,505
Research and development	44,139	183		44,322
General and administrative	41,916	566	47	42,529
Long-lived asset impairment charges				
Restructuring charges and FTC legal costs	3,993			3,993
Loss (gain) on sales and disposals of assets	898			898
Total operating costs	174,956	1,244	47	176,247
Income (loss) from operations	21,927	(1,105)	(1,975)	18,847
Interest income	5,034			5,034
Interest expense	(985)			(985)
Foreign currency exchange gain (loss)	1,076		(4,436)	(3,360)
Income (loss) before provision for income taxes and equity in earnings from joint ventures	27,052	(1,105)	(6,411)	19,536
Provision for income taxes	(8,706)		1,993	(6,713)
Equity in losses from joint ventures				
Net income (loss)	18,346			