

ASPEN TECHNOLOGY INC /DE/
Form 10-Q
January 28, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended December 31, 2014

or

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

For the transition period from _____ to _____

Commission file number: 001-34630

ASPEN TECHNOLOGY, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

04-2739697
(I.R.S. Employer Identification No.)

20 Crosby Drive
Bedford, Massachusetts
(Address of principal executive offices)

01730
(Zip Code)

(781) 221-6400

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

As of January 21, 2015, there were 88,222,753 shares of the registrant's common stock (par value \$0.10 per share) outstanding.

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<u>SIGNATURES</u>		

ASPENONE is one of our registered trademarks. All other trade names, trademarks and service marks appearing in this Form 10-Q are the property of their respective owners.

Our fiscal year ends on June 30, and references to a specific fiscal year are the twelve months ended June 30 of such year (for example, fiscal 2015 refers to the year ending June 30, 2015).

Table of Contents**PART I - FINANCIAL INFORMATION****Item 1. Financial Statements.***Consolidated Financial Statements (unaudited)***ASPEN TECHNOLOGY, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited)**

	Three Months Ended		Six Months Ended	
	December 31, 2014	2013	December 31, 2014	2013
	(Dollars in Thousands, Except per Share Data)			
Revenue:				
Subscription and software	\$ 98,716	\$ 88,924	\$ 197,459	\$ 167,607
Services and other	9,074	9,845	17,457	18,727
Total revenue	107,790	98,769	214,916	186,334
Cost of revenue:				
Subscription and software	5,208	5,022	10,409	9,642
Services and other	7,057	7,421	14,237	14,879
Total cost of revenue	12,265	12,443	24,646	24,521
Gross profit	95,525	86,326	190,270	161,813
Operating expenses:				
Selling and marketing	22,821	24,178	44,439	47,109
Research and development	15,957	15,016	32,225	30,850
General and administrative	10,226	11,020	22,451	22,893
Total operating expenses, net	49,004	50,214	99,115	100,852
Income from operations	46,521	36,112	91,155	60,961
Interest income	132	307	268	694
Interest expense	(4)	(8)	(7)	(26)
Other income (expense), net	(248)	(531)	(60)	(1,335)
Income before provision for income taxes	46,401	35,880	91,356	60,294
Provision for income taxes	15,937	12,617	31,924	22,032
Net income	\$ 30,464	\$ 23,263	\$ 59,432	\$ 38,262
Net income per common share:				
Basic	\$ 0.34	\$ 0.25	\$ 0.66	\$ 0.41
Diluted	\$ 0.34	\$ 0.25	\$ 0.65	\$ 0.41
Weighted average shares outstanding:				
Basic	89,942	92,839	90,562	93,124
Diluted	90,471	93,816	91,196	94,137

See accompanying Notes to these unaudited consolidated financial statements.

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ASPEN TECHNOLOGY, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	Three Months Ended		Six Months Ended	
	2014	December 31, 2013	2014	December 31, 2013
	(Dollars in Thousands)			
Net income	\$ 30,464	\$ 23,263	\$ 59,432	\$ 38,262
Other comprehensive income (loss):				
Net unrealized gains (losses) on available for sale securities, net of tax effects of \$20 and \$42 for the three and six months ended December 31, 2014, and \$6 and \$47 for the three and six months ended December 31, 2013	(39)	11	(78)	88
Foreign currency translation adjustments	(945)	(3)	(2,475)	1,333
Total other comprehensive income (loss)	(984)	8	(2,553)	1,421
Comprehensive income	\$ 29,480	\$ 23,271	\$ 56,879	\$ 39,683

See accompanying Notes to these unaudited consolidated financial statements.

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ASPEN TECHNOLOGY, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(Unaudited)

	December 31, 2014	June 30, 2014
	(Dollars in Thousands, Except Share Data)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 158,443	\$ 199,526
Short-term marketable securities	72,675	67,619
Accounts receivable, net	19,578	38,532
Current portion of installments receivable, net		640
Unbilled services	639	1,656
Prepaid expenses and other current assets	9,015	10,567
Prepaid income taxes	696	605
Current deferred tax assets	4,920	10,537
Total current assets	265,966	329,682
Long-term marketable securities	25,334	31,270
Non-current installments receivable, net	498	811
Property, equipment and leasehold improvements, net	18,327	7,588
Computer software development costs, net	1,153	1,390
Goodwill	18,045	19,276
Non-current deferred tax assets	11,265	12,765
Other non-current assets	2,766	5,190
Total assets	\$ 343,354	\$ 407,972
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 2,250	\$ 412
Accrued expenses and other current liabilities	31,984	34,984
Income taxes payable	1,983	2,168
Current deferred revenue	197,778	228,940
Total current liabilities	233,995	266,504
Non-current deferred revenue	40,634	45,942
Other non-current liabilities	31,005	11,850
Commitments and contingencies (Note 11)		
Series D redeemable convertible preferred stock, \$0.10 par value Authorized 3,636 shares as of December 31, 2014 and June 30, 2014 Issued and outstanding none as of December 31, 2014 and June 30, 2014		
Stockholders' equity:		
Common stock, \$0.10 par value Authorized 210,000,000 shares Issued 101,283,764 shares at December 31, 2014 and 101,033,740 shares at June 30, 2014 Outstanding 88,867,557 shares at December 31, 2014 and 91,661,850 shares at June 30, 2014		
	10,128	10,103
Additional paid-in capital	605,455	591,324
Accumulated deficit	(204,602)	(264,034)
Accumulated other comprehensive income	6,819	9,372
Treasury stock, at cost 12,416,207 shares of common stock at December 31, 2014 and 9,371,890 shares at June 30, 2014	(380,080)	(263,089)
Total stockholders' equity	37,720	83,676
Total liabilities and stockholders' equity	\$ 343,354	\$ 407,972

See accompanying Notes to these unaudited consolidated financial statements.

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ASPEN TECHNOLOGY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Six Months Ended	
	2014	December 31, 2013
	(Dollars in Thousands)	
Cash flows from operating activities:		
Net income	\$ 59,432	\$ 38,262
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,858	2,479
Net foreign currency (gains) losses	(1,379)	1,079
Stock-based compensation	7,666	7,538
Deferred income taxes	21,773	16,791
Provision for bad debts	338	805
Tax benefits from stock-based compensation	7,684	83
Excess tax benefits from stock-based compensation	(7,684)	(83)
Other non-cash operating activities	782	896
Changes in assets and liabilities:		
Accounts receivable	18,519	6,475
Unbilled services	990	1,171
Prepaid expenses, prepaid income taxes, and other assets	2,914	1,536
Installments receivable	980	8,345
Accounts payable, accrued expenses, and other liabilities	(5,254)	(5,651)
Deferred revenue	(35,844)	(7,470)
Net cash provided by operating activities	73,775	72,256
Cash flows from investing activities:		
Purchases of marketable securities	(39,048)	(18,992)
Maturities of marketable securities	39,012	12,424
Purchases of property, equipment and leasehold improvements	(4,328)	(1,724)
Capitalized computer software development costs	(137)	(504)
Net cash used in investing activities	(4,501)	(8,796)
Cash flows from financing activities:		
Exercises of stock options	1,515	4,430
Repurchases of common stock	(115,905)	(58,919)
Payments of tax withholding obligations related to restricted stock	(2,574)	(4,237)
Excess tax benefits from stock-based compensation	7,684	83
Net cash used in financing activities	(109,280)	(58,643)
Effect of exchange rate changes on cash and cash equivalents	(1,077)	228
(Decrease) increase in cash and cash equivalents	(41,083)	5,045
Cash and cash equivalents, beginning of period	199,526	132,432
Cash and cash equivalents, end of period	\$ 158,443	\$ 137,477
Supplemental disclosure of cash flow information:		
Income taxes paid, net	\$ 2,621	\$ 5,045
Supplemental disclosure of non-cash investing and financing activities:		
Landlord improvement allowance included in leasehold improvements and deferred rent liability	\$ 6,064	\$
Purchases of property, equipment and leasehold improvements included in accounts payable and accrued expenses	2,184	

Common stock repurchases included in accrued expenses

1,712

See accompanying Notes to these unaudited consolidated financial statements.

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ASPEN TECHNOLOGY, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. Interim Unaudited Consolidated Financial Statements

The accompanying interim unaudited consolidated financial statements of Aspen Technology, Inc. and its subsidiaries have been prepared on the same basis as our annual consolidated financial statements. We have omitted certain information and footnote disclosures normally included in our annual consolidated financial statements. Such interim unaudited consolidated financial statements have been prepared in conformity with U.S. Generally Accepted Accounting Principles (GAAP), as defined in the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 270, *Interim Reporting*, for interim financial information and with the instructions to Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. It is suggested that these unaudited consolidated financial statements be read in conjunction with the audited consolidated financial statements for the year ended June 30, 2014, which are contained in our Annual Report on Form 10-K, as previously filed with the U.S. Securities and Exchange Commission (SEC). In the opinion of management, all adjustments, consisting of normal and recurring adjustments, considered necessary for a fair presentation of the financial position, results of operations, and cash flows at the dates and for the periods presented have been included and all intercompany accounts and transactions have been eliminated in consolidation. The results of operations for the three and six months ended December 31, 2014 are not necessarily indicative of the results to be expected for any subsequent quarter or for the full fiscal year.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Unless the context requires otherwise, references to we, our and us refer to Aspen Technology, Inc. and its subsidiaries.

Reclassifications

Certain line items in prior period financial statements have been reclassified to conform to the current period presentations.

2. Significant Accounting Policies

(a) Overview of Licensing Model Changes

Transition to the aspenONE Licensing Model

Prior to fiscal 2010, we offered term or perpetual licenses to specific products, or specifically defined sets of products, which we refer to as point products. The majority of our license revenue was recognized under an upfront revenue model, in which the net present value of the aggregate license fees was recognized as revenue upon shipment of the point products. Customers typically received one year of post-contract software maintenance and support, or SMS, with their license agreements and then could elect to renew SMS annually. Revenue from SMS was recognized ratably over the period in which the SMS was delivered.

In fiscal 2010, we introduced the following changes to our licensing model:

(i) We began offering our software on a subscription basis, allowing our customers access to all products within a licensed suite (aspenONE Engineering or aspenONE Manufacturing and Supply Chain). SMS is included for the entire term of the arrangement and customers are entitled to any software products or updates introduced into the licensed suite. We refer to this license arrangement as our aspenONE licensing model.

(ii) We began to include SMS for the entire term on our point product term arrangements.

Beginning in fiscal 2012, we introduced our Premier Plus SMS offering to provide more value to our customers. As a part of this offering, customers receive 24x7 support, faster response times, dedicated technical advocates and access to web-based training modules.

Revenue related to our aspenONE licensing model and to term point product license arrangements with Premier Plus SMS is recognized over the term of the arrangement on a ratable basis. The changes to our licensing model introduced in fiscal 2010 did not change the method or timing of customer billings or cash collections.

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Impact of Licensing Model Changes

The principal accounting implications of the changes to our licensing model in fiscal 2010 are as follows:

- Prior to fiscal 2010, the majority of our license revenue was recognized on an upfront basis. Since the upfront model resulted in the net present value of multiple years of future installments being recognized at the time of shipment, the changes to our licensing model resulted in a reduction in our software license revenue for fiscal 2010, 2011 and 2012 as compared to the fiscal years preceding our licensing model changes. These changes did not impact the incurrence or timing of our expenses, and there was no corresponding expense reduction to offset the lower revenue, resulting in operating losses for fiscal 2010, 2011 and 2012. By fiscal 2013, a sufficient number of license arrangements had been renewed on the aspenONE licensing model to generate ratable revenue sufficient to support an operating profit.
- Since fiscal 2010, revenue from annually renewable SMS arrangements (legacy SMS revenue) has decreased, and been offset by a corresponding increase in subscription and software revenue as customers have transitioned to our aspenONE licensing model. Under our aspenONE licensing model and for point product arrangements with Premier Plus SMS included for the full contract term, the entire arrangement fee, including the SMS component, is included within subscription and software revenue.
- Installment payments from aspenONE agreements and from point product arrangements with SMS included for the contract term are not considered fixed or determinable, and as a result, are not included in installments receivable. Accordingly, our installments receivable balance has decreased as licenses previously executed under our upfront revenue model reached the end of their terms.
- The amount of our deferred revenue has increased as more revenue from our term license portfolio has been recognized on a ratable basis.

(b) Revenue Recognition

We generate revenue from the following sources: (1) licensing software products and SMS; and (2) providing professional services and training. We sell our software products to end users under fixed-term and perpetual licenses. As a standard business practice, we offer extended payment term options for our fixed-term license arrangements, which are generally payable on an annual basis. Many of our fixed-term license agreements include product mixing rights that allow customers the flexibility to change or alternate the use of multiple products included in the license arrangement after those products are delivered to the customer. We refer to these arrangements as token arrangements. Tokens are fixed units of measure. The amount of software usage is limited by the number of tokens purchased by the customer.

Four basic criteria must be satisfied before software license revenue can be recognized: persuasive evidence of an arrangement between us and an end user; delivery of our product has occurred; the fee for the product is fixed or determinable; and collection of the fee is probable.

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Persuasive evidence of an arrangement We use a signed contract as evidence of an arrangement for software licenses and SMS. For professional services we use a signed contract and a work proposal to evidence an arrangement. In cases where both a signed contract and a purchase order are required by the customer, we consider both taken together as evidence of the arrangement.

Delivery of our product Software and the corresponding access keys are generally delivered to customers electronically or via disk media with standard shipping terms of FOB Origin. Our software license agreements do not contain conditions for acceptance.

Fee is fixed or determinable We assess whether a fee is fixed or determinable at the outset of the arrangement. Significant judgment is involved in making this assessment.

Under our upfront revenue model, we are able to demonstrate that the fees are fixed or determinable for all arrangements, including those for our term licenses that contain extended payment terms. We have an established history of collecting under the terms of these contracts without providing concessions to customers. In addition, we also assess whether a contract modification to an existing term arrangement constitutes a concession. In making this assessment, significant analysis is performed to ensure that no concessions are given. Our software license agreements do not include a right of return or exchange. For license arrangements

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executed under the upfront revenue model, we recognize license revenue upon delivery of the software product, provided all other revenue recognition requirements are met.

We cannot assert that the fees under our aspenONE licensing model and point product arrangements with Premier Plus SMS are fixed or determinable because the rights provided to customers, and the economics of the arrangements, are not comparable to our transactions with other customers under the upfront revenue model. As a result, the amount of revenue recognized for these arrangements is limited by the amount of customer payments that become due.

Collection of fee is probable We assess the probability of collecting from each customer at the outset of the arrangement based on a number of factors, including the customer's payment history, its current creditworthiness, economic conditions in the customer's industry and geographic location, and general economic conditions. If in our judgment collection of a fee is not probable, revenue is recognized as cash is collected, provided all other conditions for revenue recognition have been met.

Vendor-Specific Objective Evidence of Fair Value

We have established VSOE for certain SMS offerings, professional services, and training, but not for our software products or our Premier Plus SMS offering. We assess VSOE for SMS, professional services, and training, based on an analysis of standalone sales of the offerings using the bell-shaped curve approach. We do not have a history of selling our Premier Plus SMS offering to customers on a standalone basis, and as a result are unable to establish VSOE for this deliverable. As of July 1, 2014, we are no longer able to establish VSOE for legacy SMS offerings sold with our perpetual license arrangements. As a result, all perpetual license agreements that include legacy SMS entered into subsequent to June 30, 2014 are being recognized ratably over the legacy SMS service period. Loss of VSOE on legacy SMS offerings sold with our perpetual license arrangements did not have a material impact on our revenue during the three and six months ended December 31, 2014.

We allocate the arrangement consideration among the elements included in our multi-element arrangements using the residual method. Under the residual method, the VSOE of the undelivered elements is deferred and the remaining portion of the arrangement fee is recognized as revenue upon delivery of the software, assuming all other revenue recognition criteria are met. If VSOE does not exist for an undelivered element in an arrangement, revenue is deferred until such evidence does exist for the undelivered elements, or until all elements are delivered, whichever is earlier. Under the upfront revenue model, the residual license fee is recognized upon delivery of the software provided all other revenue recognition criteria were met. Arrangements that qualified for upfront recognition during fiscal 2014 and prior periods included sales of perpetual licenses, amendments to existing legacy term arrangements and renewals of legacy term arrangements.

Subscription and Software Revenue

Subscription and software revenue consists of product and related revenue from our (i) aspenONE licensing model, including Premier Plus SMS; (ii) point product arrangements with our Premier Plus SMS offering included for the contract term; (iii) legacy arrangements including (a) amendments to existing legacy term arrangements, (b) renewals of legacy term arrangements and (c) legacy arrangements that are being recognized over time as a result of not previously meeting one or more of the requirements for recognition under the upfront revenue model; (iv) legacy SMS arrangements; and (v) perpetual arrangements.

When a customer elects to license our products under our aspenONE licensing model, our Premier Plus SMS offering is included for the entire term of the arrangement and the customer receives, for the term of the arrangement, the right to any new unspecified future software products and updates that may be introduced into the licensed aspenONE software suite. Due to our obligation to provide unspecified future software products and updates, we are required to recognize revenue ratably over the term of the arrangement, once the other revenue recognition criteria noted above have been met.

Our point product arrangements with Premier Plus SMS include SMS for the term of the arrangement. Since we do not have VSOE for our Premier Plus SMS offering, the SMS element of our point product arrangements is not separable. As a result, revenue associated with point product arrangements with Premier Plus SMS included for the contract term is recognized ratably over the term of the arrangement, once the other revenue recognition criteria have been met.

Perpetual and legacy term license arrangements do not include the same rights as those provided to customers under the aspenONE licensing model and point product arrangements with Premier Plus SMS. Legacy SMS revenue is generated from legacy SMS offerings provided in support of perpetual and legacy term license arrangements. Customers typically receive SMS for one year and then can elect to renew SMS annually. During fiscal 2014 and prior periods, we had VSOE for certain legacy SMS offerings sold with perpetual and term license arrangements and could therefore separate the undelivered elements. Accordingly, license fee revenue for perpetual and legacy term license arrangements was recognized upon delivery of the software products using the residual method, provided all other revenue recognition requirements were met. VSOE of fair value for the undelivered SMS component sold with our perpetual and term license arrangements was deferred and subsequently amortized into revenue ratably over the contractual term of

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the SMS arrangement. As of July 1, 2014, we are no longer able to establish VSOE for our legacy SMS offerings sold with our perpetual license arrangements. As a result, all perpetual license agreements that include legacy SMS entered into subsequent to June 30, 2014 are being recognized ratably over the legacy SMS service period. Loss of VSOE on legacy SMS offerings sold with our perpetual license arrangements did not have a material impact on revenue during the three and six months ended December 31, 2014.

Services and Other Revenue

Professional Services Revenue

Professional services are provided to customers on a time-and-materials (T&M) or fixed-price basis. We recognize professional services fees for our T&M contracts based upon hours worked and contractually agreed-upon hourly rates. Revenue from fixed-price engagements is recognized using the proportional performance method based on the ratio of costs incurred to the total estimated project costs. Project costs are typically expensed as incurred. The use of the proportional performance method is dependent upon our ability to reliably estimate the costs to complete a project. We use historical experience as a basis for future estimates to complete current projects. Additionally, we believe that costs are the best available measure of performance. Out-of-pocket expenses which are reimbursed by customers are recorded as revenue.

In certain circumstances, professional services revenue may be recognized over a time period longer than the period over which the services are performed. If the costs to complete a project are not estimable or the completion is uncertain, the revenue is recognized upon completion of the services. In circumstances in which professional services are sold as a single arrangement with, or in contemplation of, a new aspenONE license or point product arrangement with Premier Plus SMS, revenue is deferred and recognized on a ratable basis over the longer of (i) the period the services are performed or (ii) the license term. When we provide professional services considered essential to the functionality of the software, we recognize the combined revenue from the sale of the software and related services using the completed contract or percentage-of-completion method.

We have occasionally been required to commit unanticipated additional resources to complete projects, which resulted in losses on those contracts. Provisions for estimated losses on contracts are made during the period in which such losses become probable and can be reasonably estimated.

Training Revenue

We provide training services to our customers, including on-site, Internet-based and customized training. Revenue is recognized in the period in which the services are performed. In circumstances in which training services are sold as a single arrangement with, or in contemplation of, a new aspenONE license or point product arrangement with Premier Plus SMS, revenue is deferred and recognized on a ratable basis over the longer of (i) the period the services are performed or (ii) the license term.

Deferred Revenue

Deferred revenue includes amounts billed or collected in advance of revenue recognition, including arrangements under the aspenONE licensing model, point product arrangements with Premier Plus SMS, legacy SMS arrangements, professional services, and training. Under the aspenONE licensing model and for point product arrangements with Premier Plus SMS, VSOE does not exist for the undelivered elements, and as a result the arrangement fees are recognized ratably (i.e., on a subscription basis) over the term of the license. Deferred revenue is recorded as each invoice becomes due.

For arrangements under the upfront revenue model, a portion of the arrangement fee is generally recorded as deferred revenue due to the inclusion of an undelivered element, typically our legacy SMS offering or professional services. The amount of revenue allocated to undelivered elements is based on the VSOE for those elements using the residual method, and is earned and recognized as revenue as each element is delivered.

(c) Loss Contingencies

We accrue estimated liabilities for loss contingencies arising from claims, assessments, litigation and other sources when it is probable that a liability has been incurred and the amount of the claim, assessment or damages can be reasonably estimated. We believe that we have sufficient accruals to cover any obligations resulting from claims, assessments or litigation that have met these criteria. Please refer to Note 11 for discussion of these matters and related liability accruals.

(d) Foreign Currency Transactions

Foreign currency exchange gains and (losses) generated from the settlement and remeasurement of transactions denominated in

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currencies other than the functional currency of our subsidiaries are recognized in our results of operations as incurred as a component of other income (expense), net. Net foreign currency (losses) were (\$0.2) million and (\$0.1) million during the three and six months ended December 31, 2014 and (\$0.5) million and (\$1.3) million during the three and six months ended December 31, 2013, respectively.

(e) Recently Issued Accounting Pronouncements

In May 2014, FASB issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers*. ASU No. 2014-09 was issued by the FASB as a part of the joint project with the International Accounting Standards Board to clarify revenue recognition principles and develop a common revenue standard for GAAP and International Financial Reporting Standards.

ASU No. 2014-09 is effective for the fiscal years, and interim periods within those years, beginning after December 15, 2016. Early adoption of ASU No. 2014-09 is not permitted. The amendments included within ASU No. 2014-09 should be applied by using one of the following methods:

Retrospectively to each prior reporting period presented. The entity may elect any of the practical expedients described in ASU No. 2014-09 when applying this method.

Retrospectively with the cumulative effect of initially applying ASU No. 2014-09 recognized at the date of initial application. In the reporting periods that include the date of the initial application of ASU No. 2014-09, the entity should disclose the amount by which each financial statement line item is affected by the application of ASU No. 2014-09 in the current reporting period as compared to the guidance that was in effect before the change.

We expect to adopt ASU No. 2014-09 during the first quarter of fiscal 2018. We are currently evaluating the impact of ASU No. 2014-09 on our financial position, results of operations and cash flows.

(f) Other

For further information with regard to our Significant Accounting Policies, please refer to Note 2 of our Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2014.

3. Marketable Securities

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The following table summarizes the fair value, the amortized cost and unrealized holding gains (losses) on our marketable securities as of December 31, 2014 and June 30, 2014:

	Fair Value		Cost		Unrealized Gains		Unrealized Losses
(Dollars in Thousands)							
December 31, 2014:							
U.S. corporate bonds	\$ 72,675	\$	72,722	\$	5	\$	(51)
Total short-term marketable securities	\$ 72,675	\$	72,722	\$	5	\$	(51)
U.S. corporate bonds	\$ 25,334	\$	25,397	\$	5	\$	(67)
Total long-term marketable securities	\$ 25,334	\$	25,397	\$	5	\$	(67)
June 30, 2014:							
U.S. corporate bonds	\$ 67,619	\$	67,587	\$	39	\$	(7)
Total short-term marketable securities	\$ 67,619	\$	67,587	\$	39	\$	(7)
U.S. corporate bonds	\$ 31,270	\$	31,290	\$	1	\$	(21)
Total long-term marketable securities	\$ 31,270	\$	31,290	\$	1	\$	(21)

Our marketable securities are classified as available-for-sale and reported at fair value on the unaudited consolidated balance sheets. Net unrealized gains (losses) are reported as a separate component of accumulated other comprehensive income, net of tax.

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Realized gains and (losses) on investments are recognized in earnings as incurred. Our investments consist primarily of investment grade fixed income corporate debt securities with maturity dates ranging from January 2015 through August 2016 as of December 31, 2014 and from July 2014 through May 2016 as of June 30, 2014.

We review our marketable securities for impairment at each reporting period to determine if any of our securities have experienced an other-than-temporary decline in fair value in accordance with the provisions of ASC Topic 320, *Investments- Debt and Equity Securities*. We consider factors, such as the length of time and extent to which the market value has been less than the cost, the financial condition and near-term prospects of the issuer, our intent to sell, and whether it is more likely than not we will be required to sell the investment before recovery of its amortized cost basis. If we believe that an other-than-temporary decline in fair value has occurred, we write down the investment to fair value and recognize the credit loss in earnings and the non-credit loss in accumulated other comprehensive income. As of December 31, 2014 and 2013, our marketable securities were not considered other-than-temporarily impaired and, as such, we did not recognize impairment losses during the three and six months periods then ended. Unrealized losses are attributable to changes in interest rates.

4. Goodwill

During fiscal 2014, we re-aligned our reporting units to reflect our revised operating and reportable segment structure (refer to Note 12). Prior to fiscal 2014, we had three reporting units: license; SMS, training and other; and professional services. During fiscal 2014, we re-aligned our reporting units into subscription and software; and services. As a result of this re-alignment, goodwill assigned to the subscription and software reporting unit included combined goodwill of the license; and SMS, training and other reporting units. The carrying amount of goodwill of the services reporting unit was zero at December 31, 2014, June 30, 2014 and June 30, 2013 and consisted of fully impaired gross goodwill of \$5.1 million.

The changes in the carrying amount of goodwill for our subscription and software reporting unit during the six months ended December 31, 2014 and fiscal year ended June 30, 2014 were as follows:

	Amount (Dollars in Thousands)
Balance as of June 30, 2013:	
Goodwill	\$ 84,701
Accumulated impairment losses	(65,569)
	\$ 19,132
Effect of currency translation	144
Balance as of June 30, 2014:	
Goodwill	\$ 84,845
Accumulated impairment losses	(65,569)
	\$ 19,276
Effect of currency translation	(1,231)
Balance as of December 31, 2014:	
Goodwill	\$ 83,614

Accumulated impairment losses	(65,569)
	\$ 18,045

We test goodwill for impairment annually (or more often if impairment indicators arise), at the reporting unit level. We first assess qualitative factors to determine whether the existence of events or circumstances indicates that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If we determine, based on this assessment, that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, we perform the two-step goodwill impairment test. The first step requires us to determine the fair value of the reporting unit and compare it to the carrying amount, including goodwill, of such reporting unit. If the fair value exceeds the carrying amount, no impairment loss is recognized. However, if the carrying amount of the reporting unit exceeds its fair value, the goodwill of the unit may be impaired. The amount of impairment, if any, is measured based upon the implied fair value of goodwill at the valuation date.

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Fair value of a reporting unit is determined using a combined weighted average of a market-based approach (utilizing fair value multiples of comparable publicly traded companies) and an income-based approach (utilizing discounted projected cash flows). In applying the income-based approach, we would be required to make assumptions about the amount and timing of future expected cash flows, growth rates and appropriate discount rates. The amount and timing of future cash flows would be based on our most recent long-term financial projections. The discount rate we would utilize would be determined using estimates of market participant risk-adjusted weighted-average costs of capital and reflect the risks associated with achieving future cash flows.

We have elected December 31st as the annual impairment assessment date and perform additional impairment tests if triggering events occur. We performed our annual impairment test for the subscription and software reporting unit as of December 31, 2014, and, based upon the results of our qualitative assessment, determined that it was not likely that its fair value was less than its carrying amount. As such, we did not perform the two-step goodwill impairment test and did not recognize impairment losses as a result of our analysis. If an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value, goodwill will be evaluated for impairment between annual tests.

5. Income Taxes

The effective tax rate for the periods presented is primarily the result of income earned in the U.S., taxed at U.S. federal and state statutory income tax rates, income earned in foreign tax jurisdictions taxed at the applicable rates, as well as the impact of permanent differences between book and tax income.

Our effective tax rate for the three months ended December 31, 2014 was 34.3% as compared to 35.2% for the corresponding period of the prior fiscal year. Our effective tax rate for the six months ended December 31, 2014 was 34.9% as compared to 36.5% for the corresponding period of the prior fiscal year. During the three and six months ended December 31, 2014 and 2013, our income tax expense was driven primarily by pre-tax profitability in our domestic and foreign operations and the impact of permanent items, including non-deductible stock-based compensation expense, slightly offset by a benefit from a U.S. domestic production activity deduction. Our effective tax rate for the three and six months ended December 31, 2014 and 2013 differs from the U.S. federal statutory income tax rate primarily as a result of the impact of the permanent items.

We use the with and without ordering approach to calculate our tax provision. This methodology requires us to utilize all other tax attributes before recognizing excess tax benefits. Excess tax benefits are generated when the deductible value of stock-based compensation for income tax purposes exceeds the value recognized for financial statement purposes. Excess tax benefits are not included as a component of deferred tax assets. When realized, excess tax benefits reduce income taxes payable and increase additional paid in capital. During the second quarter of fiscal 2015, we recognized \$7.7 million from excess tax benefits. In our unaudited consolidated statements of cash flows, the excess tax benefits are reported as both a \$7.7 million source of cash flow from financing activities with an equivalent offsetting reduction to cash flow from operating activities.

Deferred income taxes are recognized based on temporary differences between the financial statement and tax bases of assets and liabilities. Deferred tax assets and liabilities are measured using the statutory tax rates and laws expected to apply to taxable income in the years in which the temporary differences are expected to reverse. Valuation allowances are provided against net deferred tax assets if, based upon the available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income and the timing of the temporary differences becoming deductible. Management considers, among other available information, scheduled reversals of deferred tax liabilities, projected future taxable income, limitations of

availability of net operating loss carryforwards, and other matters in making this assessment.

We do not provide deferred taxes on unremitted earnings of foreign subsidiaries since we intend to indefinitely reinvest those earnings either currently or sometime in the foreseeable future. Unrecognized provisions for taxes on undistributed earnings of foreign subsidiaries, which are considered indefinitely reinvested, are not material to our consolidated financial position or results of operations.

6. Fair Value

We determine fair value by utilizing a fair value hierarchy that ranks the quality and reliability of the information used in its determination. Fair values determined using Level 1 inputs utilize unadjusted quoted prices in active markets for identical assets or liabilities that we have the ability to access. Fair values determined using Level 2 inputs utilize data points that are observable, such as quoted prices, interest rates and yield curves for similar assets and liabilities.

Cash equivalents of \$138.8 million and \$175.9 million as of December 31, 2014 and June 30, 2014, respectively, are reported at fair value utilizing quoted market prices in identical markets, or Level 1 inputs. Our cash equivalents consist of short-term, highly liquid investments with remaining maturities of three months or less when purchased.

Marketable securities of \$98.0 million and \$98.9 million as of December 31, 2014 and June 30, 2014, respectively, are reported at fair value calculated in accordance with the market approach, utilizing market consensus pricing models with quoted prices that are directly or indirectly observable, or Level 2 inputs.

Financial instruments not measured or recorded at fair value in the accompanying unaudited consolidated financial statements consist of accounts receivable, installments receivable and accounts payable. The estimated fair value of these financial instruments

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approximates their carrying value.

7. Supplementary Balance Sheet Information

The following table summarizes our accounts receivable, net of the related allowance for doubtful accounts, as of December 31, 2014 and June 30, 2014.

	Gross	Allowance (Dollars in Thousands)	Net
December 31, 2014:			
Accounts receivable	\$ 22,042	\$ 2,464	\$ 19,578
	\$ 22,042	\$ 2,464	\$ 19,578
June 30, 2014:			
Accounts receivable	\$ 41,997	\$ 3,465	\$ 38,532
	\$ 41,997	\$ 3,465	\$ 38,532

As of December 31, 2014, one customer's receivable balance represented approximately 19% of our total receivables.

Property, equipment and leasehold improvements in the accompanying unaudited consolidated balance sheets consist of the following:

	December 31, 2014	June 30, 2014
	(Dollars in Thousands)	
Property, equipment and leasehold improvements - at cost:		
Computer equipment	\$ 11,252	\$ 11,772
Purchased software	25,405	23,720
Furniture & fixtures	5,168	4,530
Leasehold improvements	10,568	3,448
Accumulated depreciation	(34,066)	(35,882)
Property, equipment and leasehold improvements - net	\$ 18,327	\$ 7,588

Accrued expenses and other current liabilities in the accompanying unaudited consolidated balance sheets consist of the following:

December 31, 2014	June 30, 2014
(Dollars in Thousands)	

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Royalties and outside commissions	\$	3,288	\$	3,596
Payroll and payroll-related		13,574		19,347
Other		15,122		12,041
Total accrued expenses and other current liabilities	\$	31,984	\$	34,984

Other non-current liabilities in the accompanying unaudited consolidated balance sheets consist of the following:

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	December 31, 2014		June 30, 2014
	(Dollars in Thousands)		
Deferred rent (1)	\$ 4,888	\$	402
Other (2)	26,117		11,448
Total other non-current liabilities	\$ 31,005	\$	11,850

(1) During the six months ended December 31, 2014, we received \$6.1 million of landlord-funded leasehold improvements related to our new principal executive offices located in Bedford, Massachusetts. The landlord-funded leasehold improvements are recorded as property, plant and equipment and deferred rent in our unaudited consolidated balance sheets as of December 31, 2014. The landlord-funded leasehold improvements were recorded as deferred rent and will be amortized as a reduction to rent expense over the life of the lease. During fiscal 2014, we made \$1.5 million of improvements to the Bedford, Massachusetts offices that were determined to be owned by the landlord. As of June 30, 2014, the \$1.5 million of improvements were recorded within other non-current assets in our consolidated balance sheets and reclassified as a reduction to deferred rent during the second quarter of fiscal 2015. The \$1.5 million of improvements will be amortized as additional rent expense over the life of the lease. Please refer to Note 11 for further information on the lease.

(2) Other is comprised primarily of our net reserve for uncertain tax liabilities of \$23.7 million and \$9.3 million as of December 31, 2014 and June 30, 2014, respectively. We account for unrecognized tax benefits in accordance with ASU No. 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*. In accordance with ASU 2013-11, deferred tax assets should be presented net of liabilities for uncertain tax positions provided there are specific deferred tax assets available to settle the uncertain income tax liabilities. As of June 30, 2014, we had sufficient deferred tax assets available to settle a portion of our reserve for uncertain tax positions, and consequently, a only a portion of our total reserve for uncertain tax positions was reported as a non-current liability in our consolidated balance sheets. As of December 31, 2014, we no longer had deferred tax assets available to net against our reserve for uncertain tax positions and the total reserve for uncertain tax liabilities is reported as a non-current liability. Our total reserve for uncertain tax positions was approximately \$24.0 million as of December 31, 2014 and June 30, 2014.

8. Stock-Based Compensation

General Award Terms

We issue stock options and restricted stock units (RSUs) to our employees and outside directors, pursuant to stockholder-approved equity compensation plans. Option awards are granted with an exercise price equal to the market closing price of our stock on the trading day prior to the grant date; those options generally vest over four years and expire within 7 or 10 years of grant. RSUs generally vest over four years. Historically, our practice has been to settle stock option exercises and RSU vesting through newly-issued shares.

Stock-Based Compensation Accounting

We recognize stock-based compensation expense on a straight-line basis, net of forfeitures, over the requisite service period for time-vested awards. Our share-based awards are accounted for as equity instruments. Our policy is to issue new shares upon the exercise of stock awards.

We utilize the Black-Scholes option valuation model for estimating the fair value of options granted. The Black-Scholes option valuation model incorporates assumptions regarding expected stock price volatility, the expected life of the option, the risk-free interest rate, dividend yield and the market value of our common stock. The expected stock price volatility is determined based on our

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stock's historic prices over a period commensurate with the expected life of the award. The expected life of an option represents the period for which options are expected to be outstanding as determined by historic option exercises and post-vesting cancellations. The risk-free interest rate is based on the U.S. Treasury yield curve for notes with terms approximating the expected life of the options granted. The expected dividend yield is zero, based on our history and expectation of not paying dividends on common shares.

The weighted average estimated fair value of option awards granted during the three months ended December 31, 2013 was \$10.86. There were no option awards granted during the three months ended December 31, 2014. The weighted average estimated fair value of option awards granted during the six months ended December 31, 2014 and 2013 was \$13.64 and \$11.33, respectively.

We utilized the Black-Scholes option valuation model with the following weighted average assumptions:

	Six Months Ended December 31,	
	2014	2013
Risk-free interest rate	1.5%	1.3%
Expected dividend yield	0.0%	0.0%
Expected life (in years)	4.5	4.6
Expected volatility factor	35.0%	39.3%

The stock-based compensation expense and its classification in the unaudited consolidated statements of operations for the three and six months ended December 31, 2014 and 2013 are as follows:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2014	2013	2014	2013
	(Dollars in Thousands)			
Recorded as expenses:				
Cost of services and other	\$ 339	\$ 327	\$ 677	\$ 628
Selling and marketing	754	710	1,504	1,821
Research and development	973	889	1,964	1,745
General and administrative	1,396	1,225	3,521	3,344
Total stock-based compensation	\$ 3,462	\$ 3,151	\$ 7,666	\$ 7,538

A summary of stock option and RSU activity under all equity plans for the six months ended December 31, 2014 is as follows:

	Stock Options			Restricted Stock Units		
	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in 000 s)	Shares	Weighted Average Grant Date Fair Value
Outstanding at June 30, 2014	1,246,528	\$ 20.30	7.14	\$ 32,543	617,269	\$ 25.74
Granted	281,085	43.44			331,742	43.44

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Settled (RSUs)						(211,020)		27.51
Exercised	(112,417)		13.48					
Cancelled / Forfeited	(24,058)		25.22			(27,197)		25.45
Outstanding at December 31, 2014	1,391,138	\$	25.44	7.35	\$	15,754	710,794	\$ 33.49
Vested and exercisable at December 31, 2014	800,889	\$	19.50	6.43	\$	12,831		
Vested and expected to vest as of December 31, 2014	1,314,255	\$	25.00	7.28	\$	15,342	617,512	\$ 33.58

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The weighted average grant-date fair value of RSUs granted during the six months ended December 31, 2014 was \$43.44, and during the three and six months ended December 31, 2013 was \$38.10 and \$32.61, respectively. There were no RSUs granted during the three months ended December 31, 2014. During the three months ended December 31, 2014 and 2013, the total fair value of shares vested from RSU grants was \$3.5 million and \$5.0 million, respectively, and during the six months ended December 31, 2014 and 2013 was \$7.7 million and \$12.2 million, respectively.

At December 31, 2014, the total future unrecognized compensation cost related to stock options and RSUs was \$5.9 million and \$20.6 million, respectively, and is expected to be recorded over a weighted average period of 2.8 years each, respectively.

The total intrinsic value of options exercised during the three months ended December 31, 2014 and 2013 was \$0.7 million and \$2.7 million, respectively. The total intrinsic value of options exercised during the six months ended December 31, 2014 and 2013 was \$3.0 million and \$9.2 million, respectively. We received \$1.5 million and \$4.4 million in cash proceeds from option exercises during the six months ended December 31, 2014 and 2013, respectively. We paid \$2.7 million and \$4.2 million for withholding taxes on vested RSUs during the six months ended December 31, 2014 and 2013, respectively.

At December 31, 2014, common stock reserved for future issuance or settlement under equity compensation plans was 6.3 million shares.

9. Stockholders Equity

Stock Repurchases

On April 23, 2014, our Board of Directors approved a share repurchase program for up to \$200 million worth of our common stock and terminated the previous program that had been approved by the Board of Directors on April 23, 2013. The previous program had an authorized value of up to \$150 million and remaining capacity of approximately \$37.5 million when terminated. The timing and amount of any shares repurchased are based on market conditions and other factors. All share repurchases of our common stock have been recorded as treasury stock under the cost method.

We repurchased 3,044,317 shares of our common stock for \$117.0 million during the six months ended December 31, 2014. We repurchased 3,110,114 shares of our common stock for \$121.8 million during fiscal 2014. As of December 31, 2014, the remaining dollar value under the stock repurchase program approved on April 23, 2014 was \$58.1 million.

Accumulated Other Comprehensive Income

As of December 31, 2014 and 2013, accumulated other comprehensive income was comprised of foreign translation adjustments of \$6.9 million and \$8.6 million and net unrealized gains (losses) on available for sale securities of (\$0.1 million) and less than \$0.1 million, respectively. As of September 30, 2014 and 2013, accumulated other comprehensive income was comprised of foreign translation adjustments of \$7.8 million and \$8.7 million and net unrealized gains (losses) on available for sale securities of less than \$0.1 million each, respectively.

As of June 30, 2014 and 2013, accumulated other comprehensive income was comprised of foreign translation adjustments of \$9.4 million and \$7.3 million and net unrealized gains (losses) on available for sale securities of less than \$0.1 million and (\$0.1 million), respectively.

10. Net Income Per Share

Basic income per share is determined by dividing net income by the weighted average common shares outstanding during the period. Diluted income per share is determined by dividing net income by diluted weighted average shares outstanding during the period. Diluted weighted average shares reflect the dilutive effect, if any, of potential common shares. To the extent their effect is dilutive, employee equity awards and other commitments to be settled in common stock are included in the calculation of diluted net income per share based on the treasury stock method.

The calculations of basic and diluted net income per share and basic and dilutive weighted average shares outstanding for the three and six months ended December 31, 2014 and 2013 are as follows:

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	Three Months Ended December 31,		Six Months Ended December 31,	
	2014	2013	2014	2013
	(Dollars and Shares in Thousands, Except per Share Data)			
Net income	\$ 30,464	\$ 23,263	\$ 59,432	\$ 38,262
Weighted average shares outstanding	89,942	92,839	90,562	93,124
Dilutive impact from:				
Share-based payment awards	529	977	634	1,013
Dilutive weighted average shares outstanding	90,471	93,816	91,196	94,137
Income per share				
Basic	\$ 0.34	\$ 0.25	\$ 0.66	\$ 0.41
Dilutive	\$ 0.34	\$ 0.25	\$ 0.65	\$ 0.41

For the three and six months ended December 31, 2014 and 2013, certain employee equity awards were anti-dilutive based on the treasury stock method. Additionally, options to purchase 287,463 shares of our common stock were not included in the computation of dilutive weighted average shares outstanding, as of December 31, 2014, because their exercise prices ranged from \$38.71 per share to \$47.40 per share and were greater than the average market price of our common stock during the three and six months ended December 31, 2014. These options were outstanding as of December 31, 2014 and expire at various dates through July 31, 2024.

The following employee equity awards were excluded from the calculation of dilutive weighted average shares outstanding because their effect would be anti-dilutive as of December 31, 2014 and 2013:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2014	2013	2014	2013
	(Shares in Thousands)			
Employee equity awards	832	312	640	652

11. Commitments and Contingencies*Operating Leases*

We lease certain facilities under non-cancellable operating leases with terms in excess of one year. Rental expense on leased facilities under operating leases was approximately \$2.1 million and \$1.8 million during the three months ended December 31, 2014 and 2013 and \$3.8 million and \$3.6 million during the six months ended December 31, 2014 and 2013, respectively.

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During fiscal 2014, we entered into a lease agreement for our new principal executive offices located in Bedford, Massachusetts. The lease commenced on November 1, 2014, has an initial term of 10 years and five months and is for 142,673 square feet of office space. We may extend the term of the lease, subject to certain terms and conditions, for two successive terms of five years each. Base annual rent is subject to escalating payments over the term of the lease and will range between approximately \$2.2 million and \$3.9 million in addition to our proportionate share of operating expenses and real estate taxes. Future minimum non-cancelable lease payments amount to approximately \$35.7 million over the lease term. As of December 31, 2014, estimated aggregate capital expenditures related to the build out of our office space in Bedford, Massachusetts are expected to total approximately \$9.2 million, of which \$7.8 million represents binding contractual obligations. As of December 31, 2014, we have made cumulative payments of approximately \$5.0 million under these obligations and expect to make remaining payments of \$2.8 million during fiscal 2015. We occupied 105,874 square feet of the Bedford, Massachusetts facility on November 1, 2014 and expect to move into the remaining 36,799 square feet on February 1, 2015.

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Other

In the ordinary course of business, we are, from time to time, involved in lawsuits, claims, investigations, proceedings and threats of litigation, including proceedings related to intellectual property rights. These matters include an April 2004 claim by a customer that certain of our software products and implementation services failed to meet the customer's expectations. In March 2014, a judgment was issued in favor of the claimant customer against us in the amount of approximately \$2.6 million plus interest and a portion of legal fees. We have filed an appeal of the judgment.

While the outcome of the proceedings and claims referenced above cannot be predicted with certainty, there were no such matters, as of December 31, 2014 that, in the opinion of management, were reasonably possible to have a material adverse effect on our financial position, results of operations or cash flows. Liabilities, if applicable, related to the aforementioned matters discussed in this Note have been included in our accrued liabilities at December 31, 2014, and were not material to our financial position for the six months period then ended. We do not believe that, as of December 31, 2014, there is a reasonable possibility of a material loss exceeding the amounts already accrued for the proceedings or matters discussed above. However, the results of litigation (including the above-referenced appeal) and claims cannot be predicted with certainty; unfavorable resolutions are possible and could materially affect our results of operations, cash flows or financial position. In addition, regardless of the outcome, litigation could have an adverse impact on us because of attorneys' fees and costs, diversion of management resources and other factors.

12. Segment Information

Operating segments are defined as components of an enterprise that engage in business activities for which discrete financial information is available and regularly reviewed by the chief operating decision maker in deciding how to allocate resources and to assess performance. Our chief operating decision maker is our President and Chief Executive Officer.

Prior to fiscal 2014, we had three operating and reportable segments: license; SMS, training and other; and professional services. During fiscal 2014, we re-aligned our operating and reportable segments into i) subscription and software; and ii) services, in order to conform our segment structure to the manner in which our President and Chief Executive Officer manages our business.

The subscription and software segment is engaged in the licensing of process optimization software solutions and associated support services. The services segment includes professional services and training.

The accounting policies of the operating segments are the same as those described in the summary of significant accounting policies (refer to Note 2 in the financial statements of our Form 10-K for the year ended June 30, 2014). We do not track assets or capital expenditures by operating segments. Consequently, it is not practical to present assets, capital expenditures, depreciation or amortization by operating segments.

The following table presents a summary of our reportable segments' profits:

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	Subscription and software	Services (Dollars in Thousands)	Total
Three Months Ended December 31, 2014			
Segment revenue	\$ 98,716	\$ 9,074	\$ 107,790
Segment expenses (1)	(43,986)	(7,057)	(51,043)
Segment profit	\$ 54,730	\$ 2,017	\$ 56,747
Three Months Ended December 31, 2013			
Segment revenue	\$ 88,924	\$ 9,845	\$ 98,769
Segment expenses (1)	(44,216)	(7,421)	(51,637)
Segment profit	\$ 44,708	\$ 2,424	\$ 47,132
Six Months Ended December 31, 2014			
Segment revenue	\$ 197,459	\$ 17,457	\$ 214,916
Segment expenses (1)	(87,073)	(14,237)	(101,310)
Segment profit	\$ 110,386	\$ 3,220	\$ 113,606
Six Months Ended December 31, 2013			
Segment revenue	\$ 167,607	\$ 18,727	\$ 186,334
Segment expenses (1)	(87,601)	(14,879)	(102,480)
Segment profit	\$ 80,006	\$ 3,848	\$ 83,854

(1) Our reportable segments' operating expenses include expenses directly attributable to the segments. Segment expenses do not include allocations of general and administrative; restructuring; interest income, net; and other (income) expense, net. As a result of the operating and reportable segments' realignment, certain costs are more directly attributable to our new operating segments. Starting with fiscal 2014, segment expenses include selling and marketing, research and development, stock-based compensation and certain corporate expenses incurred in support of the segments. Prior to fiscal 2014, segment expenses included certain allocations of selling and marketing; general and administrative; and research and development and did not include restructuring and other corporate expenses incurred in support of these functions.

Reconciliation to Income Before Income Taxes

The following table presents a reconciliation of total segment profit to income before income taxes for the three and six months ended December 31, 2014 and 2013:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2014	2013	2014	2013
	(Dollars in Thousands)			
Total segment profit for reportable segments	\$ 56,747	\$ 47,132	\$ 113,606	\$ 83,854
General and administrative	(10,226)	(11,020)	(22,451)	(22,893)
Other income (expense), net	(248)	(531)	(60)	(1,335)
Interest income (net)	128	299	261	668

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Income before income taxes	\$	46,401	\$	35,880	\$	91,356	\$	60,294
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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

You should read the following discussion in conjunction with our unaudited consolidated financial statements and related notes beginning on page 3. In addition to historical information, this discussion contains forward-looking statements that involve risks and uncertainties. You should read Item 1A. Risk Factors, of Part II for a discussion of important factors that could cause our actual results to differ materially from our expectations.

Our fiscal year ends on June 30th, and references in this Quarterly Report to a specific fiscal year are to the twelve months ended June 30th of such year (for example, fiscal 2015 refers to the year ending on June 30, 2015). Unless the context indicates otherwise, references in this report to we, us and our refer to Aspen Technology, Inc. and its subsidiaries.

Business Overview

We are a leading global provider of mission-critical process optimization software solutions designed to manage and optimize plant and process design, operational performance, and supply chain planning. Our aspenONE software and related services have been developed specifically for companies in the process industries, including the energy, chemicals, and engineering and construction industries. Customers use our solutions to improve their competitiveness and profitability by increasing throughput and productivity, reducing operating costs, enhancing capital efficiency, and decreasing working capital requirements.

Our software incorporates our proprietary mathematical and empirical models of manufacturing and planning processes and reflects the deep domain expertise we have amassed from focusing on solutions for the process industries for over 30 years. We have developed our applications to design and optimize processes across three principal business areas: engineering, manufacturing and supply chain. We are a recognized market and technology leader in providing process optimization software for each of these business areas.

We have established sustainable competitive advantages within our industry based on the following strengths:

- Innovative products that can enhance our customers' profitability;
- Long-term customer relationships;
- Large installed base of users of our software; and
- Long-term license contracts with historically high renewal rates.

We have approximately 2,000 customers globally. Our customers in the process industries include energy, chemicals, engineering and construction, as well as consumer packaged goods, power, metals and mining, pulp and paper, pharmaceuticals and biofuels.

We license our software products primarily through a subscription offering which we refer to as our aspenONE licensing model. Our aspenONE products are organized into two suites: 1) engineering and 2) manufacturing and supply chain, or MSC. The aspenONE licensing model provides customers with access to all of the products within the aspenONE suite(s) they license. Customers can change or alternate the use of multiple products in a licensed suite through the use of exchangeable units of measurement, called tokens, licensed in quantities determined by the customer. This licensing system enables customers to use products as needed and to experiment with different products to best solve whatever critical business challenges they face. Customers can increase their usage of our software by purchasing additional tokens as business needs evolve. We believe easier access to all of the aspenONE products will lead to increased software usage and higher revenue over time.

Transition to the aspenONE Licensing Model

Prior to fiscal 2010, we offered term or perpetual licenses to specific products, or specifically defined sets of products, which we refer to as point products. The majority of our license revenue was recognized under an upfront revenue model, in which the net present value of the aggregate license fees was recognized as revenue upon shipment of the point products, provided all revenue recognition criteria were met. Customers typically received one year of post-contract software maintenance and support, or SMS, with their license agreements and then could elect to renew SMS annually. Revenue from SMS was recognized ratably over the period in which the SMS was delivered.

In fiscal 2010, we introduced the following changes to our licensing model:

- (i) We began offering our software on a subscription basis, allowing our customers access to all products within a licensed suite (aspenONE Engineering or aspenONE Manufacturing and Supply Chain). SMS is included for the entire term of the arrangement and customers are entitled to any software products or updates introduced into the licensed suite. We refer to this license arrangement as our aspenONE licensing model.

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- (ii) We began to include SMS for the entire term on our point product term arrangements.

Beginning in fiscal 2012, we introduced our Premier Plus SMS offering to provide more value to our customers. As a part of this offering, customers receive 24x7 support, faster response times, dedicated technical advocates and access to web-based training modules.

Revenue related to our aspenONE licensing model and to term point product license arrangements with Premier Plus SMS is recognized over the term of the arrangement on a ratable basis. The changes to our licensing model introduced in fiscal 2010 did not change the method or timing of customer billings or cash collections. The revenue transition will not be fully completed until the end of fiscal 2015. As of December 31, 2014, a significant percentage of our active license agreements have been transitioned to our aspenONE licensing model.

Impact of Licensing Model Changes

The principal accounting implications of the changes to our licensing model in fiscal 2010 are as follows:

- Prior to fiscal 2010, the majority of our license revenue was recognized on an upfront basis. Since the upfront model resulted in the net present value of multiple years of future installments being recognized at the time of shipment, the changes to our licensing model resulted in a reduction in our software license revenue for fiscal 2010, 2011 and 2012 as compared to the fiscal years preceding our licensing model changes. These changes did not impact the incurrence or timing of our expenses, and there was no corresponding expense reduction to offset the lower revenue, resulting in operating losses for fiscal 2010, 2011 and 2012. By fiscal 2013, a sufficient number of license arrangements had been renewed on the aspenONE licensing model to generate ratable revenue sufficient to support an operating profit. The revenue transition will not be fully completed until the end of fiscal 2015.
- The transition will not be complete until the remaining term license agreements executed under our upfront revenue model reach the end of their original term. Many of our license arrangements were five or six years in duration when the aspenONE licensing model was introduced at the start of fiscal 2010, and consequently, a number of agreements executed under the upfront revenue model will not reach the end of their original term until the end of fiscal 2015.
- Since fiscal 2010, revenue from annually renewable SMS arrangements (legacy SMS revenue) has decreased, and been offset by a corresponding increase in subscription and software revenue as customers have transitioned to our aspenONE licensing model. Under our aspenONE licensing model and for point product arrangements with Premier Plus SMS included for the full contract term, the entire arrangement fee, including the SMS component, is included within subscription and software revenue.
- Installment payments from aspenONE agreements and from point product arrangements with SMS included for the contract term are not considered fixed or determinable, and as a result, are not included in installments receivable. Accordingly, our installments receivable balance has, and is expected to continue to, decrease as licenses previously executed under our upfront revenue model reach the end of their terms.

- The amount of our deferred revenue has increased, and is expected to continue to increase, as more revenue from our term license portfolio is recognized on a ratable basis.

For additional information about the recognition of revenue under the upfront revenue model and our aspenONE licensing model, please refer to Management's Discussion and Analysis of Financial Condition and Results of Operations - Revenue contained in Part II, Item 7 of our Form 10-K for our fiscal year ended June 30, 2014. Due to the accounting implications resulting from the changes to our licensing model, we believe that a number of performance indicators based on U.S. generally accepted accounting principles, or GAAP, including revenue, gross profit, operating income and net income, should be reviewed in conjunction with certain non-GAAP and other business measures in assessing our performance, growth and financial condition. We utilize a number of non-GAAP and other key business metrics, including those described below under Key Business Metrics, to track our business performance during the transition period to our aspenONE licensing model, which we expect will be completed by the end of fiscal 2015. None of these metrics should be considered as an alternative to any measure of financial performance calculated in accordance with GAAP.

Segments Re-alignment

Prior to fiscal 2014, we had three operating and reportable segments: license; SMS, training and other; and professional services.

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During fiscal 2014, we re-aligned our operating and reportable segments into i) subscription and software; and ii) services, in order to conform our segment structure to the manner in which our chief operating decision maker manages our business.

The subscription and software segment is engaged in the licensing of process optimization software solutions and associated support services. The services segment includes professional services and training.

For additional information on segment revenues and their operating results, please refer to Note 12 Segment Information in the Notes to the Unaudited Consolidated Financial Statements.

Revenue

We generate revenue primarily from the following sources:

- *Subscription and software.* We provide integrated process optimization software solutions designed specifically for process industries. We license our software products, together with SMS, primarily on a term basis, and we offer extended payment options for our term license arrangements that generally require annual payments, which we also refer to as installments. We provide customers technical support, access to software fixes and updates and the right to any new unspecified future software products and updates that may be introduced into the licensed aspenONE software suite. Our technical support services are provided from our customer support centers throughout the world, as well as via email and through our support website.
- *Services and other.* We provide training and professional services to our customers. Our professional services are focused on implementing our technology in order to improve customers' plant performance and gain better operational data. Customers who use our professional services typically engage us to provide those services over periods of up to 24 months. We charge customers for professional services on a time-and-materials or fixed-price basis. We provide training services to our customers, including on-site, Internet-based and customized training.

Key Components of Operations

Revenue

Subscription and Software Revenue. Our subscription and software revenue consists of product and related revenue from the following sources:

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- (i) aspenONE licensing model;

- (ii) point product arrangements with our Premier Plus SMS offering included for the contract term (referred to as point product arrangements with Premier Plus SMS);

- (iii) legacy arrangements including (a) amendments to existing legacy term arrangements, (b) renewals of legacy term arrangements and (c) legacy arrangements that are being recognized over time as a result of not previously meeting one or more of the requirements for recognition under the upfront revenue model;

- (iv) legacy SMS arrangements; and

- (v) perpetual arrangements.

Services and Other Revenue. Our services and other revenue consists primarily of revenue related to professional services and training. The amount and timing of this revenue depend on a number of factors, including:

- whether the professional services arrangement was sold as a single arrangement with, or in contemplation of, a new aspenONE licensing arrangement;

- the number, value and rate per hour of service transactions booked during the current and preceding periods;

- the number and availability of service resources actively engaged on billable projects;

- the timing of milestone acceptance for engagements contractually requiring customer sign-off;

- the timing of collection of cash payments when collectability is uncertain; and

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- the size of the installed base of license contracts.

Cost of Revenue

Cost of Subscription and Software. Our cost of subscription and software revenue consists of (i) royalties, (ii) amortization of capitalized software and purchased technology intangibles, (iii) distribution fees, (iv) costs of providing Premier Plus SMS bundled with our aspenONE licensing and point product arrangements, and (v) costs of providing legacy SMS.

Cost of Services and Other. Our cost of services and other revenue consists primarily of personnel-related and external consultant costs associated with providing customers professional services and training.

Operating Expenses

Selling and Marketing Expenses. Selling expenses consist primarily of the personnel and travel expenses related to the effort expended to license our products and services to current and potential customers, as well as for overall management of customer relationships. Marketing expenses include expenses needed to promote our company and our products and to conduct market research to help us better understand our customers and their business needs.

Research and Development Expenses. Research and development expenses consist primarily of personnel expenses related to the creation of new software products, enhancements and engineering changes to existing products and costs of acquired technology prior to establishing technological feasibility.

General and Administrative Expenses. General and administrative expenses include the costs of corporate and support functions, such as executive leadership and administration groups, finance, legal, human resources and corporate communications, and other costs, such as outside professional and consultant fees, and provision for bad debts.

Restructuring Charges. Restructuring charges result from the closure or consolidation of our facilities, or from qualifying reductions in headcount. We did not incur any restructuring charges during the three and six months ended December 31, 2014. Restructuring charges amounted to less than \$0.1 million in both three and six months periods ended December 31, 2013 and are presented within general and administrative expenses in our unaudited consolidated statements of operations during the periods then ended.

Other Income and Expenses

Interest Income. Interest income is recorded for the accretion of interest on the installment payments of our term software license contracts when revenue is recognized upfront at net present value, and from the investment in marketable securities and short-term money market instruments.

Interest Expense. During the three and six months ended December 31, 2014 and 2013, interest expense was comprised of miscellaneous interest charges.

Other Income (Expense), Net. Other income (expense), net is comprised primarily of foreign currency exchange gains (losses) generated from the settlement and remeasurement of transactions denominated in currencies other than the functional currency of our operating units.

Provision for Income Taxes. Provision for income taxes is comprised of domestic and foreign taxes. We record interest and penalties related to income tax matters as a component of income tax expense. We expect the amount of income tax expense to vary each reporting period depending upon fluctuations in our taxable income by jurisdiction.

Key Business Metrics

Background

The changes to our licensing model resulted in a reduction in our product-related revenue for each period starting with fiscal 2010, as compared to the fiscal years preceding our licensing model changes. Since the upfront model resulted in the net present value of multiple years of future installments being recognized at the time of shipment, we do not expect to recognize levels of revenue reflective of the value of our active license agreements until the remaining term license agreements executed under our upfront revenue model (i) reach the end of their original terms and (ii) are renewed. As a result, we believe that a number of our performance indicators based on GAAP, including revenue, gross profit, operating income and net income, should be reviewed in conjunction with

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certain non-GAAP and other business measures in assessing our performance, growth and financial condition. We utilize the following non-GAAP and other key business metrics to track our business performance during the transition period to our aspenONE licensing model, which we expect will be completed by the end of fiscal 2015:

- Total term contract value;
- Annual spend;
- Adjusted total costs; and
- Free cash flow.

None of these metrics should be considered as an alternative to any measure of financial performance calculated in accordance with GAAP.

Total Term Contract Value

Total term contract value, or TCV, is an estimate of the renewal value, as of a specific date, of our active portfolio of term license agreements. TCV is calculated by multiplying the terminal annual payment for each active term license agreement by the original length of the existing license term, and then aggregating this amount for all active term license agreements. Accordingly, TCV represents the full renewal value of all of our current term license agreements under the hypothetical assumption that all of those agreements are simultaneously renewed for the identical license terms and at the same terminal annual payment amounts. TCV includes the value of SMS for any multi-year license agreements for which SMS is committed for the entire license term. TCV does not include any amounts for perpetual licenses, professional services, training or standalone renewal SMS. TCV is calculated using constant currency assumptions for agreements denominated in currencies other than U.S. dollars in order to remove the impact of currency fluctuations between comparison dates.

We also estimate a *license-only TCV*, which we refer to as TLCV, by removing the SMS portion of TCV using our historic estimated selling price for SMS. Our portfolio of active license agreements currently reflects a mix of (a) license agreements that include SMS for the entire license term and (b) legacy license agreements that do not include SMS. TLCV provides a consistent basis for assessing growth during the transition period as customers transition to arrangements that include SMS for the term of the arrangement.

We believe TCV and TLCV are useful metrics for analyzing our business performance while we are transitioning to our aspenONE licensing model or to point product arrangements with Premier Plus SMS included for the full term, and revenue comparisons between fiscal periods do not reflect the actual growth rate of our business. Comparing TCV and TLCV for different dates provides insight into the growth and retention rate of our business during the period between those dates.

TCV and TLCV increase as the result of:

- new term license agreements with new or existing customers;
- renewals or modifications of existing license agreements that result in higher license fees due to price escalation or an increase in the number of tokens (units of software usage) or products licensed; and
- renewals of existing license agreements that increase the length of the license term.

The renewal of an existing license agreement will not increase TCV and TLCV unless the renewal results in higher license fees or a longer license term. TCV and TLCV are adversely affected by customer non-renewals and by renewals that result in lower license fees or a shorter license term. Our standard license term historically has been between five and six years, and we do not expect this standard term to change in the future. Many of our contracts have escalating annual payments throughout the term of the arrangement. By calculating TCV and TLCV based on the terminal year annual payment, we are typically using the highest annual fee from the existing arrangement to calculate the hypothetical renewal value of our portfolio of term arrangements.

We estimate that TLCV grew by approximately 4.5% during the second quarter of fiscal 2015, from \$1.88 billion at September 30, 2014 to \$2.0 billion at December 31, 2014, and by approximately 6.2% during the first half of fiscal 2015, from \$1.85 billion at June 30, 2014.

We estimate that TCV grew by approximately 4.6% during the second quarter of fiscal 2015, from \$2.23 billion at September 30, 2014 to \$2.33 billion at December 31, 2014, and by approximately 6.4% during the first half of fiscal 2015, from \$2.19 billion at June 30, 2014. The growth was attributable primarily to a larger number of tokens or products sold.

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Annual Spend

Annual spend is a derivative metric that is closely related to TCV. TCV is an estimate of the renewal value of our active portfolio of term license agreements, as of a specific date. Annual spend is an estimate of the annualized value of our active portfolio of term agreements, as of a specific date. Annual spend is calculated by taking the most recent annual invoice value of each of our active term contracts and then aggregating this amount for all active term licenses. Annual spend also includes the annualized value of standalone SMS agreements purchased in conjunction with term license agreements. We believe that the annual spend metric may be helpful to investors attempting to analyze and model subscription and software revenue while we transition to our aspenONE licensing model. Comparing annual spend for different dates provides insight into the growth and retention rates of our business, and since annual spend represents the estimated annualized billings associated with our active term license agreements, it provides insight into a normalized value for subscription and software revenue.

Annual spend increases as a result of:

- New term license agreements with new or existing customers;

- Renewals or modifications of existing license agreements that result in higher license fees due to price escalation or an increase in the number of tokens (units of software usage) or products licensed; and

- Escalation of annual payments in our active term contracts.

Annual spend is adversely affected by term license and standalone SMS agreements that are not renewed. Unlike TCV and TLCV, the value of annual spend is not impacted by changes to contract duration.

We estimate that annual spend grew by approximately 3.9% during the second quarter of fiscal 2015, from \$384.9 million at September 30, 2014 to \$399.9 million at December 31, 2014, and by approximately 5.4% during the first half of fiscal 2015, from \$379.5 million at June 30, 2014. The growth was attributable primarily to a larger number of tokens or products sold.

Adjusted Total Costs

We use a non-GAAP measure of adjusted total costs, which excludes certain non-cash and non-recurring expenses, to supplement our presentation of total cost of revenue and total operating costs presented on a GAAP basis. Management believes that this financial measure is useful to investors because it approximates the cash operating costs of the business. The presentation of adjusted total costs is not meant to be considered as an alternative to total cost of revenue and total operating costs as a measure of our total costs.

Adjusted total costs are calculated as the sum of total cost of revenue and total operating expenses, adjusted for the net impact of (a) stock-based compensation expense; (b) restructuring charges; (c) amortization of purchased technology intangibles; and (d) expensing of non-capitalized acquired technology.

Non-capitalized acquired technology includes the cost of certain technology acquired as a part of a project to develop a commercially available product that does not meet the accounting definition of having reached technological feasibility. The cost of non-capitalized acquired technology is charged to research and development at the time of acquisition. We did not incur any charges related to non-capitalized acquired technology during the three and six months ended December 31, 2014 and 2013.

The following table presents our adjusted total costs during the three and six months ended December 31, 2014 and 2013:

	Three Months Ended December 31,		Period-to-Period Change		Six Months Ended December 31,		Period-to-Period Change	
	2014	2013	\$	%	2014	2013	\$	%
(Dollars in Thousands, Except Percentages)								
Total cost of revenue	\$ 12,265	\$ 12,443	\$ (178)	(1.4)%	\$ 24,646	\$ 24,521	\$ 125	0.5%
Total operating expenses	\$ 49,004	\$ 50,214	(1,210)	(2.4)	\$ 99,115	\$ 100,852	(1,737)	(1.7)
Total expenses	61,269	62,657	(1,388)	(2.2)	123,761	125,373	(1,612)	(1.3)
Less:								
Stock-based compensation	(3,462)	(3,151)	(311)	9.9	(7,666)	(7,538)	(128)	1.7
Restructuring charges		(7)	7	(100.0)		(4)	4	(100.0)
Amortization of purchased technology intangibles	(224)	(224)			(448)	(473)	25	(5.3)
Adjusted total costs (non-GAAP)	\$ 57,583	\$ 59,275	\$ (1,692)	(2.9)%	\$ 115,647	\$ 117,358	\$ (1,711)	(1.5)%

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Comparison of the Three Months Ended December 31, 2014 and 2013

Total expenses decreased by \$1.4 million during the three months ended December 31, 2014 as compared to the corresponding period of the prior fiscal year. Please refer to the Results of Operations section below for additional information on period-over-period expense fluctuations.

Adjusted total costs decreased by \$1.7 million during the three months ended December 31, 2014 compared to the corresponding period of the prior fiscal year. The period-over-period decrease in adjusted total costs was primarily attributable to lower bad debt expense of \$0.8 million, lower compensation-related costs of \$0.7 million, a benefit of \$0.9 million associated with collecting a business tax refund and receipt of \$0.7 million for an award in connection with a certain legal action. These decreases were partially offset by higher legal costs of \$0.6 million, higher rent and depreciation expense of \$0.6 million, and other net costs of \$0.2 million.

Stock-based compensation expense increased by \$0.3 million primarily due to the expense associated with our August 2014 annual equity awards grant program, partially offset by decreases related to certain awards reaching the end of their vesting period.

Comparison of the Six Months Ended December 31, 2014 and 2013

Total expenses decreased by \$1.6 million during the six months ended December 31, 2014 as compared to the corresponding period of the prior fiscal year. Please refer to the Results of Operations section below for additional information on period-over-period expense fluctuations.

Adjusted total costs during the six months ended December 31, 2014 decreased by \$1.7 million compared to the corresponding period of the prior fiscal year. The period-over-period decrease in adjusted total costs was primarily attributable to lower bad debt expense of \$1.1 million, lower compensation-related costs of \$0.9 million, a benefit of \$0.9 million associated with collecting a business tax refund and receipt of \$0.7 million for an award in connection with a certain legal action. These decreases were partially offset by higher legal costs of \$0.9 million, higher depreciation expense of \$0.5 million and higher rent expense of \$0.3 million, and other net costs of \$0.2 million.

Stock-based compensation expense during the six months ended December 31, 2014 was consistent with the same period of the prior fiscal year.

Free Cash Flow

We use a non-GAAP measure of free cash flow to analyze cash flows generated from our operations. Management believes that this financial measure is useful to investors because it permits investors to view our performance using the same tools that management uses to gauge progress in achieving our goals. We believe this measure is also useful to investors because it is an indication of cash flow that may be available to fund investments in future growth initiatives and a basis for comparing our performance with that of our competitors. The presentation of free cash flow is not meant to be considered in isolation or as an alternative to cash flows from operating activities as a measure of liquidity.

Free cash flow is calculated as net cash provided by operating activities adjusted for the net impact of (a) purchases of property, equipment and leasehold improvements; (b) capitalized computer software development costs; (c) excess tax benefits from stock-based compensation; and (d) non-capitalized acquired technology.

Excess tax benefits are generated when the deductible value of stock-based compensation for income tax purposes exceeds the value recognized for financial statement purposes. When realized, excess tax benefits reduce income taxes payable and increase additional paid in capital. In our unaudited consolidated statements of cash flows, excess tax benefits are considered a source of cash flow from financing activities. Utilization of deferred tax assets are treated as a source of cash from operating activities. We include excess tax benefits as a component of free cash flow to present consistent treatment of all tax expenses and benefits, irrespective of their source.

Non-capitalized acquired technology includes the cost of certain technology acquired as a part of a project to develop a commercially available product that does not meet the accounting definition of having reached technological feasibility. The cost of non-capitalized acquired technology is charged to research and development at the time of acquisition. We exclude the payment for the acquired technology from free cash flow to be consistent with the treatment of other transactions where acquired assets are capitalized. During the six months ended December 31, 2014, we did not make any payments for non-capitalized acquired technology.

We do not expect to recognize levels of revenue reflective of the value of our active license agreements until the remaining term license agreements executed under our upfront revenue model (i) reach the end of their original terms; and (ii) are renewed. As a result, we believe that our income statement profitability measures based on GAAP, such as total revenue, gross profit, operating income and net income, should be reviewed in conjunction with free cash flow to measure of our financial performance. Customer collections and, consequently, cash flows from operating activities and free cash flow are primarily driven by license and services billings, rather than the timing of revenue. The introduction of our aspenONE licensing model has not had an impact on cash receipts.

The following table provides a reconciliation of net cash flows provided by operating activities to free cash flow for the indicated periods:

	Six Months Ended	
	December 31,	
	2014	2013
	(Dollars in Thousands)	
Net cash provided by operating activities	\$ 73,775	\$ 72,256
Purchases of property, equipment, and leasehold improvements	(4,328)	\$ (1,724)
Capitalized computer software development costs	(137)	\$ (504)
Excess tax benefits from stock-based compensation	7,684	\$ 83
Free cash flow (non-GAAP)	\$ 76,994	\$ 70,111

Total free cash flow increased \$6.9 million during the six months ended December 31, 2014 as compared to the same period of the prior fiscal year.

We have realized steadily improving free cash flow due to growth of our portfolio of term license contracts as well as from the renewal of customer contracts on an installment basis that were previously paid upfront.

Critical Accounting Estimates and Judgments

Our unaudited consolidated financial statements are prepared in accordance with GAAP. The preparation of our interim financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue, expenses and related disclosures. We base our estimates on historical experience and various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily

apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe that the assumptions and estimates associated with the following critical accounting policies have the greatest potential impact on our unaudited consolidated financial statements:

- revenue recognition;
- accounting for income taxes; and
- loss contingencies.

Revenue Recognition

Four basic criteria must be satisfied before software license revenue can be recognized: persuasive evidence of an arrangement between us and an end user; delivery of our product has occurred; the fee for the product is fixed or determinable; and collection of the fee is probable.

Persuasive evidence of an arrangement We use a signed contract as evidence of an arrangement for software licenses and SMS. For professional services we use a signed contract and a work proposal to evidence an arrangement. In cases where both a signed contract and a purchase order are required by the customer, we consider both taken together as evidence of the arrangement.

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Delivery of our product Software and the corresponding access keys are generally delivered to customers via disk media with standard shipping terms of Free Carrier, our warehouse (i.e., FCA, named place). Our software license agreements do not contain conditions for acceptance.

Fee is fixed or determinable We assess whether a fee is fixed or determinable at the outset of the arrangement. Significant judgment is involved in making this assessment.

Under our upfront revenue model, we are able to demonstrate that the fees are fixed or determinable for all arrangements, including those for our term licenses that contain extended payment terms. We have an established history of collecting under the terms of these contracts without providing concessions to customers. In addition, we also assess whether a contract modification to an existing term arrangement constitutes a concession. In making this assessment, significant analysis is performed to ensure that no concessions are given. Our software license agreements do not include a right of return or exchange. For license arrangements executed under the upfront revenue model, we recognize license revenue upon delivery of the software product, provided all other revenue recognition requirements are met.

We cannot assert that the fees under our aspenONE licensing model and point product arrangements with Premier Plus SMS are fixed or determinable because the rights provided to customers, and the economics of the arrangements, are not comparable to our transactions with other customers under the upfront revenue model. As a result, the amount of revenue recognized for these arrangements is limited by the amount of customer payments that become due.

Collection of fee is probable We assess the probability of collecting from each customer at the outset of the arrangement based on a number of factors, including the customer's payment history, its current creditworthiness, economic conditions in the customer's industry and geographic location, and general economic conditions. If in our judgment collection of a fee is not probable, revenue is recognized as cash is collected, provided all other conditions for revenue recognition have been met.

Vendor-Specific Objective Evidence of Fair Value

We have established VSOE for certain SMS offerings, professional services, and training, but not for our software products or our Premier Plus SMS offering. We assess VSOE for SMS, professional services, and training based on an analysis of standalone sales of these offerings using the bell-shaped curve approach. We do not have a history of selling our Premier Plus SMS offering to customers on a standalone basis, and as a result are unable to establish VSOE for this deliverable. As of July 1, 2014, we are no longer able to establish VSOE for legacy SMS offerings sold with our perpetual license arrangements. As a result, all perpetual license agreements that include legacy SMS entered into subsequent to June 30, 2014 are being recognized ratably over the legacy SMS service period. Loss of VSOE on legacy SMS offerings sold with our perpetual license arrangements did not have a material impact on our revenue during the three and six months ended December 31, 2014.

We allocate the arrangement consideration among the elements included in our multi-element arrangements using the residual method. Under the residual method, the VSOE of the undelivered elements is deferred and the remaining portion of the arrangement fee is recognized as revenue upon delivery of the software, assuming all other revenue recognition criteria are met. If VSOE does not exist for an undelivered element in an arrangement, revenue is deferred until such evidence does exist for the undelivered elements, or until all elements are delivered, whichever is earlier. Under the upfront revenue model, the residual license fee is recognized upon delivery of the software provided all other revenue recognition criteria were met. Arrangements that qualified for upfront recognition during fiscal 2014 and prior periods included sales of

perpetual licenses, amendments to existing legacy term arrangements and renewals of legacy term arrangements.

Subscription and Software Revenue

Subscription and software revenue consists of product and related revenue from our (i) aspenONE licensing model; (ii) point product arrangements with our Premier Plus SMS offering included for the contract term; (iii) legacy arrangements including (a) amendments to existing legacy term arrangements, (b) renewals of legacy term arrangements and (c) legacy arrangements that are being recognized over time as a result of not previously meeting one or more of the requirements for recognition under the upfront revenue model; (iv) legacy SMS arrangements; and (v) perpetual arrangements.

When a customer elects to license our products under our aspenONE licensing model, our Premier Plus SMS offering is included for the entire term of the arrangement and the customer receives, for the term of the arrangement, the right to any new unspecified future software products and updates that may be introduced into the licensed aspenONE software suite. Due to our obligation to provide unspecified future software products and updates, we are required to recognize revenue ratably over the term of the arrangement, once the other revenue recognition criteria noted above have been met.

Our point product arrangements with Premier Plus SMS include SMS for the term of the arrangement. Since we do not have VSOE for our Premier Plus SMS offering, the SMS element of our point product arrangements is not separable. As a result, revenue

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associated with point product arrangements with Premier Plus SMS included for the contract term is recognized ratably over the term of the arrangement, once all other revenue recognition criteria have been met.

Perpetual and legacy term license arrangements do not include the same rights as those provided to customers under the aspenONE licensing model and point product arrangements with Premier Plus SMS. Legacy SMS revenue is generated from legacy SMS offerings provided in support of perpetual and legacy term license arrangements. Customers typically receive SMS for one year and then can elect to renew SMS annually. During fiscal 2014 and prior periods, we had VSOE for certain legacy SMS offerings sold with perpetual and term license arrangements and could therefore separate the undelivered elements. Accordingly, license fee revenue for perpetual and legacy term license arrangements was recognized upon delivery of the software products using the residual method, provided all other revenue recognition requirements were met. VSOE of fair value for the undelivered SMS component sold with our perpetual and term license arrangements was deferred and subsequently amortized into revenue ratably over the contractual term of the SMS arrangement. As of July 1, 2014, we are no longer able to establish VSOE for legacy SMS offerings sold with our perpetual license arrangements. As a result, all perpetual license agreements that include legacy SMS entered into subsequent to June 30, 2014 are being recognized ratably over the legacy SMS service period. Loss of VSOE on legacy SMS offerings sold with our perpetual license arrangements did not have a material impact on our revenue during the three and six months ended December 31, 2014.

Services and Other Revenue

Professional Services Revenue

Professional services are provided to customers on a time-and-materials (T&M) or fixed-price basis. We recognize professional services fees for our T&M contracts based upon hours worked and contractually agreed-upon hourly rates. Revenue from fixed-price engagements is recognized using the proportional performance method based on the ratio of costs incurred to the total estimated project costs. Project costs are typically expensed as incurred. The use of the proportional performance method is dependent upon our ability to reliably estimate the costs to complete a project. We use historical experience as a basis for future estimates to complete current projects. Additionally, we believe that costs are the best available measure of performance. Out-of-pocket expenses which are reimbursed by customers are recorded as revenue.

In certain circumstances, professional services revenue may be recognized over a time period longer than the period over which the services are performed. If the costs to complete a project are not estimable or the completion is uncertain, the revenue is recognized upon completion of the services. In circumstances in which professional services are sold as a single arrangement with, or in contemplation of, a new aspenONE license or point product arrangement with Premier Plus SMS, revenue is deferred and recognized on a ratably basis over the longer of (i) the period the services are performed, or (ii) the license term. When we provide professional services considered essential to the functionality of the software, we recognize the combined revenue from the sale of the software and related services using the completed contract or percentage-of-completion method.

We have occasionally been required to commit unanticipated additional resources to complete projects, which resulted in losses on those contracts. Provisions for estimated losses on contracts are made during the period in which such losses become probable and can be reasonably estimated.

Training Revenue

We provide training services to our customers, including on-site, Internet-based, public and customized training. Revenue is recognized in the period in which the services are performed. In circumstances in which training services are sold as a single arrangement with, or in contemplation of, a new aspenONE license or point product arrangement with Premier Plus SMS, revenue is deferred and recognized on a ratable basis over the longer of (i) the period the services are performed or (ii) the license term.

Accounting for Income Taxes and Loss Contingencies

Please refer to Management's Discussion and Analysis of Financial Condition and Result of Operations contained in Part II, Item 7 of our Annual Report on Form 10-K for our fiscal year ended June 30, 2014 for a discussion of our critical accounting policies and estimates related to accounting for income taxes and loss contingencies.

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The following table sets forth the results of operations and the period-over-period percentage change in certain financial data for the three and six months ended December 31, 2014 and 2013:

	Three Months Ended December 31,		Increase / (Decrease) Change %	Six Months Ended December 31,		Increase / (Decrease) Change %
	2014	2013		2014	2013	
Revenue:						
Subscription and software	\$ 98,716	\$ 88,924	11.0%	\$ 197,459	\$ 167,607	17.8%
Services and other	9,074	9,845	(7.8)	17,457	18,727	(6.8)
Total revenue	107,790	98,769	9.1	214,916	186,334	15.3
Cost of revenue:						
Subscription and software	5,208	5,022	3.7	10,409	9,642	8.0
Services and other	7,057	7,421	(4.9)	14,237	14,879	(4.3)
Total cost of revenue	12,265	12,443	(1.4)	24,646	24,521	0.5
Gross profit	95,525	86,326	10.7	190,270	161,813	17.6
Operating expenses:						
Selling and marketing	22,821	24,178	(5.6)	44,439	47,109	(5.7)
Research and development	15,957	15,016	6.3	32,225	30,850	4.5
General and administrative	10,226	11,020	(7.2)	22,451	22,893	(1.9)
Total operating expenses, net	49,004	50,214	(2.4)	99,115	100,852	(1.7)
Income from operations	46,521	36,112	28.8	91,155	60,961	49.5
Interest income	132	307	(57.0)	268	694	(61.4)
Interest expense	(4)	(8)	(50.0)	(7)	(26)	(73.1)
Other income (expense), net	(248)	(531)	(53.3)	(60)	(1,335)	(95.5)
Income before provision for income taxes	46,401	35,880	29.3	91,356	60,294	51.5
Provision for income taxes	15,937	12,617	26.3	31,924	22,032	44.9
Net income	\$ 30,464	\$ 23,263	31.0%	\$ 59,432	\$ 38,262	55.3%

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The following table sets forth the results of operations as a percentage of net revenue for certain financial data for the three and six months ended December 31, 2014 and 2013:

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	Three Months Ended December 31,		Six Months Ended December 31,	
Revenue:				
Subscription and software	91.6%	90.0%	91.9%	89.9%
Services and other	8.4	10.0	8.1	10.1
Total revenue	100.0	100.0	100.0	100.0
Cost of revenue:				
Subscription and software	4.8	5.1	4.8	5.2
Services and other	6.5	7.5	6.6	8.0
Total cost of revenue	11.4	12.6	11.5	13.2
Gross profit	88.6	87.4	88.5	86.8
Operating expenses:				
Selling and marketing	21.2	24.4	20.7	25.2
Research and development	14.8	15.2	15.0	16.6
General and administrative	9.5	11.2	10.4	12.3
Total operating expenses, net	45.5	50.8	46.1	54.1
Income from operations	43.2	36.6	42.4	32.7
Interest income	0.1	0.2	0.1	0.4
Interest expense				
Other (expense) income, net	(0.2)	(0.5)		(0.7)
Income before provision for income taxes	43.0	36.3	42.5	32.4
Provision for income taxes	14.8	12.7	14.9	11.9
Net income	28.3%	23.6%	27.7%	20.5%

Revenue

Total revenue increased by \$9.0 million and \$28.6 million during the three and six months ended December 31, 2014 as compared to the corresponding periods of the prior fiscal year. The increase was attributable to higher subscription and software revenue of \$9.8 million and \$29.9 million, partially offset by lower services and other revenue of \$0.8 million and \$1.3 million, respectively.

Subscription and Software Revenue

	Three Months Ended December 31,		Period-to-Period Change		Six Months Ended December 31,		Period-to-Period Change	
	2014	2013	\$	%	2014	2013	\$	%
	(Dollars in Thousands)							
Subscription and software revenue	\$ 98,716	\$ 88,924	\$ 9,792	11.0%	\$ 197,459	\$ 167,607	\$ 29,852	17.8%
As a percent of revenue	91.6%	90.0%			91.9%	89.9%		

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The increase in subscription and software revenue during the three and six months ended December 31, 2014 as compared to the corresponding periods of the prior fiscal year was primarily the result of a larger base of license arrangements being recognized on a ratable basis.

We expect subscription and software revenue to continue to increase during fiscal 2015 as a result of: (i) having a larger base of license arrangements recognized on a ratable basis, (ii) increased customer usage of our software; (iii) adding new customers; and (iv) escalating annual payments. Please refer to [Transition to the aspenONE licensing model](#) and [Impact of Licensing Model Changes](#) sections above for additional information on the transition.

Table of Contents**Services and Other Revenue**

	Three Months Ended December 31,		Period-to-Period Change		Six Months Ended December 31,		Period-to-Period Change	
	2014	2013	\$	%	2014	2013	\$	%
Services and other revenue	\$ 9,074	\$ 9,845	\$ (771)	-7.8%	\$ 17,457	\$ 18,727	\$ (1,270)	-6.8%
As a percent of revenue	8.4%	10.0%			8.1%	10.1%		

(Dollars in Thousands)

Services and other revenue consists primarily of revenue related to professional services and training.

The decrease in services and other revenue of \$0.8 million during the three months ended December 31, 2014 as compared to the corresponding period of the prior fiscal year was attributable primarily to lower professional services revenue.

The period-over-period decrease in professional services revenue of \$0.8 million during the three months ended December 31, 2014 was primarily attributable to a decrease of \$1.3 million due to lower level of customer activity, partially offset by a revenue increase of \$0.5 million due to the timing of recognition of previously deferred revenue primarily related to professional service arrangements bundled with aspenONE transactions.

The decrease in services and other revenue of \$1.3 million during the six months ended December 31, 2014 as compared to the corresponding period of the prior fiscal year was primarily attributable to lower professional services revenue.

The period-over-period decrease in professional services revenue of \$1.4 million during the six months ended December 31, 2014 was primarily attributable to a decrease of \$2.4 million due to lower level of customer activity, partially offset by a revenue increase of \$1.0 million due to the timing of recognition of previously deferred revenue primarily related to professional service arrangements bundled with aspenONE transactions.

Under the aspenONE licensing model, revenue from committed professional service arrangements that are sold as a single arrangement with, or in contemplation of, a new aspenONE licensing transaction is deferred and recognized on a ratable basis over the longer of (a) the period the services are performed or (b) the term of the related software arrangement. As our typical contract term approximates five years, professional services revenue on these types of arrangements will usually be recognized over a longer period than the period over which the services are performed.

Gross Profit

Gross profit increased from \$86.3 million during the three months ended December 31, 2013 to \$95.5 million during the corresponding period of the current fiscal year. The period-over-period increase in gross profit was primarily attributable to the growth of our subscription and software revenue of \$9.8 million and consistent cost of subscription and software revenue.

Gross profit increased from \$161.8 million during the six months ended December 31, 2013 to \$190.3 million during the corresponding period of the current fiscal year. The period-over-period increase in gross profit was primarily attributable to the growth of our subscription and software revenue of \$29.9 million, offset by an increase of \$0.8 million in cost of subscription and software revenue.

Gross profit margin increased from 87.4% and 86.8% during the three and six months ended December 31, 2013 to 88.6% and 88.5% during each of the corresponding periods of the current fiscal year. For further discussion of subscription and software gross profit and services and other gross profit, please refer to the *Cost of Subscription and Software Revenue* and *Cost of Services and Other Revenue* sections below.

Table of Contents*Expenses***Cost of Subscription and Software Revenue**

	Three Months Ended December 31,		Period-to-Period Change		Six Months Ended December 31,		Period-to-Period Change	
	2014	2013	\$	%	2014	2013	\$	%
	(Dollars in Thousands)							
Cost of subscription and software revenue	\$ 5,208	\$ 5,022	\$ 186	3.7%	10,409	9,642	\$ 767	8.0%
As a percent of revenue	4.8%	5.1%			4.8%	5.2%		

Cost of subscription and software revenue during the three months ended December 31, 2014 was consistent with the corresponding period of the prior fiscal year.

Subscription and software gross profit margin was approximately 94% during the three months ended December 31, 2014 and remained consistent with the corresponding period of the prior fiscal year.

Cost of subscription and software revenue increased by \$0.8 million during the six months ended December 31, 2014 as compared to the corresponding period of the prior fiscal year. The increase was primarily attributable to higher personnel-related costs of \$0.4 million and other net costs of \$0.4 million.

Subscription and software gross profit margin was approximately 94% during the six months ended December 31, 2014 and remained consistent with the corresponding period of the prior fiscal year.

Cost of Services and Other Revenue

	Three Months Ended December 31,		Period-to-Period Change		Six Months Ended December 31,		Period-to-Period Change	
	2014	2013	\$	%	2014	2013	\$	%
	(Dollars in Thousands)							
Cost of services and other revenue	\$ 7,057	\$ 7,421	\$ (364)	-4.9%	\$ 14,237	\$ 14,879	\$ (642)	-4.3%
As a percent of revenue	6.5%	7.5%			6.6%	8.0%		

Cost of services and other revenue includes the cost of providing professional services and training.

Cost of services and other revenue during the three and six months ended December 31, 2014 was consistent with the corresponding period of the prior fiscal year.

Gross profit margin on services and other revenue decreased from 24.6% during the three months ended December 31, 2013 to 22.0% during the corresponding period of the current fiscal year primarily due to lower revenue of \$0.8 million, partially offset by lower net costs of \$0.4 million.

Gross profit margin on services and other revenue decreased from 20.5% during the six months ended December 31, 2013 to 18.4% during the corresponding period of the current fiscal year primarily due to lower revenue of \$1.3 million, partially offset by lower net costs of \$0.6 million.

Selling and Marketing Expense

	Three Months Ended December 31,		Period-to-Period Change		Six Months Ended December 31,		Period-to-Period Change	
	2014	2013	\$	%	2014	2013	\$	%
	(Dollars in Thousands)							
Selling and marketing expense	\$ 22,821	\$ 24,178	\$ (1,357)	-5.6%	\$ 44,439	\$ 47,109	\$ (2,670)	-5.7%
As a percent of revenue	21.2%	24.4%			20.7%	25.2%		

The period-over-period decrease of \$1.4 million in selling and marketing expense during the three months ended December 31, 2014 was primarily attributable to lower compensation-related costs of \$1.1 million, lower third-party commissions of \$0.5 million and other net costs of \$0.2 million. These decreases were partially offset by higher overhead allocations of \$0.4 million.

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The period-over-period decrease of \$2.7 million in selling and marketing expense during the six months ended December 31, 2014 was primarily attributable to lower compensation-related costs of \$2.1 million, lower third-party commissions of \$0.6 million, and lower other net costs of \$0.6 million. These decreases were partially offset by higher overhead allocations of \$0.6 million.

Research and Development Expense

	Three Months Ended December 31,		Period-to-Period Change		Six Months Ended December 31,		Period-to-Period Change	
	2014	2013	\$	%	2014	2013	\$	%
	(Dollars in Thousands)							
Research and development expense	\$ 15,957	\$ 15,016	\$ 941	6.3%	\$ 32,225	\$ 30,850	\$ 1,375	4.5%
As a percent of revenue	14.8%	15.2%			15.0%	16.6%		

The period-over-period increase of \$0.9 million in research and development expense during the three months ended December 31, 2014 was primarily attributable to higher overhead allocations of \$0.4 million and other net items of \$0.5 million.

The period-over-period increase of \$1.4 million in research and development expense during the six months ended December 31, 2014 was primarily attributable to higher overhead allocations of \$0.6 million and other net items of \$0.8 million.

General and Administrative Expense

	Three Months Ended December 31,		Period-to-Period Change		Six Months Ended December 31,		Period-to-Period Change	
	2014	2013	\$	%	2014	2013	\$	%
	(Dollars in Thousands)							
General and administrative expense	\$ 10,226	\$ 11,020	\$ (794)	-7.2%	\$ 22,451	\$ 22,893	\$ (442)	-1.9%
As a percent of revenue	9.5%	11.2%			10.4%	12.3%		

The period-over-period decrease of \$0.8 million in general and administrative expense during the three months ended December 31, 2014 was primarily attributable to lower bad debt expense of \$0.8 million, a benefit of \$0.9 million associated with collecting a business tax refund and receipt of \$0.7 million for an award in connection with a certain legal action. These decreases were partially offset by higher legal costs of \$0.5 million, and other net costs of \$1.1 million.

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The period-over-period decrease of \$0.4 million in general and administrative expense during the six months ended December 31, 2014 was primarily attributable to lower bad debt expense of \$1.1 million, a benefit of \$0.9 million associated with collecting a business tax refund and receipt of \$0.7 million for an award in connection with a certain legal action. These decreases were partially offset by higher legal costs of \$0.9 million, higher consultant costs of \$0.5 million and other net costs of \$0.9 million.

Interest Income

	Three Months Ended December 31,		Period-to-Period Change		Six Months Ended December 31,		Period-to-Period Change	
	2014	2013	\$	%	2014	2013	\$	%
	(Dollars in Thousands)							
Interest income	\$ 132	\$ 307	\$ (175)	-57.0%	\$ 268	\$ 694	\$ (426)	-61.4%
As a percent of revenue	0.1%	0.2%			0.1%	0.4%		

The period-over-period decrease in interest income during the three and six months ended December 31, 2014 was attributable to the decrease of our installments receivable portfolio.

Table of Contents**Other Income (Expense), Net**

	Three Months Ended December 31,		Period-to-Period Change		Six Months Ended December 31,		Period-to-Period Change	
	2014	2013	\$	%	2014	2013	\$	%
	(Dollars in Thousands)							
Other income (expense), net	\$ (248)	\$ (531)	\$ 283	-53.3%	\$ (60)	\$ (1,335)	\$ 1,275	-95.5%
As a percent of revenue	-0.2%	-0.5%			0.0%	-0.7%		

Other income (expense), net is comprised primarily of unrealized and realized foreign currency exchange gains and (losses) generated from the settlement and remeasurement of transactions denominated in currencies other than the functional currency of our operating units. Other income (expense), net also includes miscellaneous non-operating gains and (losses).

During the three months ended December 31, 2014 and 2013, other income (expense), net was comprised of (\$0.2) million and (\$0.5) million of net currency losses, respectively.

During the six months ended December 31, 2014 and 2013, other income (expense), net was comprised of (\$0.1) million and (\$1.3) million of net currency losses, respectively.

Provision for Income Taxes

	Three Months Ended December 31,		Period-to-Period Change		Six Months Ended December 31,		Period-to-Period Change	
	2014	2013	\$	%	2014	2013	\$	%
	(Dollars in Thousands)							
Provision for income taxes	\$ 15,937	\$ 12,617	\$ 3,320	26.3%	\$ 31,924	\$ 22,032	\$ 9,892	44.9%
Effective tax rate	34.3%	35.2%			34.9%	36.5%		

The effective tax rate for the periods presented is primarily the result of income earned in the U.S. taxed at U.S. federal and state statutory income tax rates, income earned in foreign tax jurisdictions taxed at the applicable rates, as well as the impact of permanent differences between book and tax income.

Our effective tax rate for the three months ended December 31, 2014 was 34.3% as compared to 35.2% for the corresponding period of the prior fiscal year. Our effective tax rate for the six months ended December 31, 2014 was 34.9% as compared to 36.5% for the corresponding period of the prior fiscal year.

We recognized an income tax expense of \$15.9 million and \$31.9 million during the three and six months ended December 31, 2014 compared to \$12.6 million and \$22.0 million during the corresponding periods of the prior fiscal year. The period-over-period increases of \$3.3 million and \$9.9 million were primarily attributable to higher U.S. pre-tax profit.

Liquidity and Capital Resources

Resources

In recent years, we have financed our operations with cash generated from operating activities. As of December 31, 2014, our principal sources of liquidity consisted of \$158.4 million in cash and cash equivalents and \$98.0 million of marketable securities. As of December 31, 2013, our principal sources of liquidity consisted of \$137.5 million in cash and cash equivalents and \$98.2 million of marketable securities.

We believe our existing cash and cash equivalents and marketable securities, together with our cash flows from operating activities will be sufficient to meet our anticipated cash needs for at least the next twelve months. We may need to raise additional funds in the event we decide to make one or more acquisitions of businesses, technologies or products. If additional funding is required, we may not be able to effect a receivable, equity or debt financing on terms acceptable to us or at all.

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Our cash equivalents of \$138.8 million and \$106.3 million consist primarily of money market funds as of December 31, 2014 and 2013, respectively. Our investments in marketable securities of \$98.0 million and \$98.2 million as of December 31, 2014 and 2013 consist primarily of investment grade fixed income corporate debt securities with maturities ranging from less than 1 month to 20 months and from less than 1 month to 21 months, respectively. The fair value of our portfolio is affected by interest rate movements, credit and liquidity risks. The objective of our investment policy is to manage our cash and investments to preserve principal and maintain liquidity, while earning a return on our investment portfolio by investing available funds. We diversify our investment portfolio by investing in multiple types of investment-grade securities and attempt to mitigate a risk of loss by using a third-party investment manager.

The following table summarizes our cash flow activities for the periods indicated:

	Six Months Ended	
	December 31,	
	2014	2013
	(Dollars in Thousands)	
Cash flow provided by (used in):		
Operating activities	\$ 73,775	\$ 72,256
Investing activities	(4,501)	(8,796)
Financing activities	(109,280)	(58,643)
Effect of exchange rates on cash balances	(1,077)	228
(Decrease) increase in cash and cash equivalents	\$ (41,083)	\$ 5,045

Operating Activities

Our primary source of cash is from the annual installments associated with our software license arrangements and related software support services, and to a lesser extent from professional services and training. We believe that cash inflows from our term license business will grow as we benefit from the continued growth of our portfolio of term license contracts.

Due to our increased profitability during fiscal 2014 and 2013, we have been utilizing our tax credits and net operating losses to offset U.S. corporate income taxes payable. We anticipate fully utilizing our tax credits and net operating losses due to continued expected profitability and becoming a U.S. corporate tax payer by the end of fiscal 2016.

Cash from operating activities provided \$73.8 million during the six months ended December 31, 2014. This amount resulted from net income of \$59.4 million, adjusted for non-cash items of \$32.0 million and net uses of cash of \$17.7 million related to changes in working capital.

Non-cash items consisted primarily of deferred income tax expense of \$21.8 million, stock-based compensation expense of \$7.7 million, depreciation and amortization expense of \$2.9 million and other net items of \$1.0 million, partially offset by net foreign currency gains of \$1.4 million.

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Cash used by working capital of \$17.7 million was primarily attributable to cash outflows related to decreases in deferred revenue of \$35.8 million, decreases in accounts payable, accrued expenses and other current liabilities of \$5.3 million, partially offset by cash inflows related to decreases in accounts receivable of \$18.5 million, decreases in prepaid expenses, prepaid income taxes and other assets of \$2.9 million and other net items of \$2.0 million. Please refer to Note 11 Commitments and Contingencies in the Notes to the Unaudited Consolidated Financial Statements for further information on the lease.

Our installments receivable balance continues to decrease as a result of collecting payments on our term software license contracts for which revenue was recognized upfront. Cash inflows generated from collections of installments receivable are expected to continue to decrease. Please refer to Transition to the aspenONE Licensing Model and Impact of Licensing Model Changes sections above for additional information on the transition.

Cash flows related to deferred revenue vary due to the timing of invoicing, in particular the anniversary dates of annual installments associated with multi-year software license arrangements.

During the second quarter of fiscal 2015, we recognized \$7.7 million of excess tax benefits in our unaudited consolidated balance sheets. Excess tax benefits are generated when the deductible value of stock-based compensation for income tax purposes exceeds the value recognized for financial statement purposes. Excess tax benefits reduced our income tax liabilities and increased our additional paid in capital by \$7.7 million and \$0.1 million during the six months ended December 31, 2014 and 2013, respectively. Excess tax benefits are considered a source of cash flows from financing activities.

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Investing Activities

During the six months ended December 31, 2014, we used \$4.5 million of cash for investing activities. The uses of cash consisted primarily of \$39.0 million for purchases of marketable securities, capital expenditures of \$4.3 million primarily related to our new principal executive offices located in Bedford, Massachusetts and other items of \$0.1 million, partially offset by \$39.0 million resulting from the maturities of marketable securities.

Please refer to the **Contractual Obligations** section below for further information on capital expenditures related to our new principal executive offices.

Financing Activities

During the six months ended December 31, 2014, we used \$109.3 million of cash for financing activities. We used \$115.9 million for repurchases of our common stock and \$2.6 million for withholding taxes on vested and settled restricted stock units. Sources of cash during the period included proceeds of \$1.5 million from the exercise of employee stock options. Cash used for financing activities during the six months ended December 31, 2014 includes realized benefits of \$7.7 million from stock-based compensation tax deductions in excess of stock-based compensation expense recognized in our financial statements. These benefits reduced our income tax liabilities and increased our additional paid in capital during the six months ended December 31, 2014.

Contractual Obligations

During fiscal 2014, we entered into a lease agreement for our new principal executive offices located in Bedford, Massachusetts. The lease commenced on November 1, 2014, has an initial term of 10 years and five months and is for 142,673 square feet of office space. Subject to the terms and conditions of the lease, we may extend the term of the lease for two successive terms of five years each. We have a one-time option to terminate the lease on the last day of the eighth year following the lease term commencement date, subject to a termination penalty of \$4.1 million. Base annual rent is subject to escalating payments over the term of the lease and will range between approximately \$2.2 million and \$3.9 million in addition to our proportionate share of operating expenses and real estate taxes. Future minimum non-cancelable lease payments amount to approximately \$35.7 million over the lease term, including payments of \$0.9 million due in fiscal 2015. We occupied 105,874 square feet of the Bedford, Massachusetts facility on November 1, 2014 and expect to move into the remaining 36,799 square feet on February 1, 2015.

As of December 31, 2014, estimated aggregate capital expenditures related to the build out of our office space in Bedford, Massachusetts are expected to total approximately \$9.2 million, of which \$7.8 million represents binding contractual obligations. As of December 31, 2014, we have made cumulative payments of approximately \$5.0 million under these obligations and expect to make remaining payments of \$2.8 million during fiscal 2015, funded from our cash flows from operating activities.

Except for the commitments under the aforementioned lease agreement, we are not currently a party to any other material purchase contracts related to future capital expenditures, and we do not expect our future investment in capital expenditures to be materially different from recent

levels.

Recently Issued and Adopted Accounting Pronouncements

In May 2014, FASB issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers*. ASU No. 2014-09 was issued by the FASB as a part of the joint project with the International Accounting Standards Board to clarify revenue recognition principles and develop a common revenue standard for GAAP and International Financial Reporting Standards.

ASU No. 2014-09 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. Early adoption of ASU No. 2014-09 is not permitted. The amendments included within ASU No. 2014-09 should be applied by using one of the following methods:

Retrospectively to each prior reporting period presented. The entity may elect any of the practical expedients described in ASU No. 2014-09 when applying this method.

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Retrospectively with the cumulative effect of initially applying ASU No. 2014-09 recognized at the date of initial application. In the reporting periods that include the date of the initial application of ASU No. 2014-09, the entity should disclose the amount by which each financial statement line item is affected by the application of ASU No. 2014-09 in the current reporting period as compared to the guidance that was in effect before the change.

We will adopt ASU No. 2014-09 during the first quarter of fiscal 2018. We are currently evaluating the impact of ASU No. 2014-09 on our financial position, results of operations and cash flows.

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Item 3. Quantitative and Qualitative Disclosures About Market Risk.

In the ordinary course of conducting business, we are exposed to certain risks associated with potential changes in market conditions. These market risks include changes in currency exchange rates and interest rates which could affect operating results, financial position and cash flows. We manage our exposure to these market risks through our regular operating and financing activities and, if considered appropriate, we may enter into derivative financial instruments, such as forward currency exchange contracts.

Foreign Currency Risk

During the three months ended December 31, 2014 and 2013, 15.0% and 15.4% of our total revenue was denominated in a currency other than the U.S. dollar, respectively. During the six months ended December 31, 2014 and 2013, 15.0% and 16.2% of our total revenue was denominated in a currency other than the U.S. dollar, respectively. In addition, certain of our operating costs incurred outside the United States are denominated in currencies other than the U.S. dollar. We conduct business on a worldwide basis and as a result, a portion of our revenue, earnings, net assets and net investments in foreign affiliates is exposed to changes in foreign currency exchange rates. We measure our net exposure for cash balance positions and for cash inflows and outflows in order to evaluate the need to mitigate our foreign exchange risk. We may enter into foreign currency forward contracts to minimize the impact related to unfavorable exchange rate movements, although we have not done so during the three and six months ended December 31, 2014 and 2013. Our largest exposures to foreign currency exchange rates exist primarily with the Euro, Pound Sterling, Canadian Dollar, and Japanese Yen.

During the three months ended December 31, 2014 and 2013, we recorded (\$0.2) million and (\$0.5) million of net foreign currency exchange (losses) related to the settlement and remeasurement of transactions denominated in currencies other than the functional currency of our operating units. Our analysis of operating results transacted in various foreign currencies indicated that a hypothetical 10% change in the foreign currency exchange rates could have increased or decreased the consolidated results of operations by approximately \$1.5 million and \$1.4 million for the three months ended December 31, 2014 and 2013, respectively.

During the six months ended December 31, 2014 and 2013, we recorded (\$0.1) million and (\$1.3) million of net foreign currency exchange (losses) related to the settlement and remeasurement of transactions denominated in currencies other than the functional currency of our operating units. Our analysis of operating results transacted in various foreign currencies indicated that a hypothetical 10% change in the foreign currency exchange rates could have increased or decreased the consolidated results of operations by approximately \$2.9 million and \$3.0 million for the six months ended December 31, 2014 and 2013, respectively.

Interest Rate Risk

We place our investments in money market instruments and high quality, investment grade, fixed-income corporate debt securities that meet high credit quality standards, as specified in our investment guidelines.

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We attempt to mitigate the risks by diversifying our investment portfolio, limiting the amount of investments in debt securities of any single issuer and using a third-party investment manager. Our debt securities are short- to intermediate- term investments with maturities ranging from less than one month to 20 months as of December 31, 2014 and from less than one month to 21 months as of December 31, 2013, respectively. We do not use derivative financial instruments in our investment portfolio.

Our analysis of our investment portfolio and interest rates at December 31, 2014 and 2013 indicated that a 100 basis point increase or decrease in interest rates would result in a decrease or increase of approximately \$0.6 million during each period in the fair value of our investment portfolio determined in accordance with income-based approach utilizing portfolio future cash flows discounted at the appropriate rates.

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Item 4. Controls and Procedures

a) Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2014. The term disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Securities Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Securities Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of December 31, 2014, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were effective.

b) Changes in Internal Controls Over Financial Reporting

During the three months ended December 31, 2014, no changes were identified in our internal controls over financial reporting that materially affected, or were reasonably likely to materially affect, our internal controls over financial reporting.

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PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

Refer to Note 11, Commitments and Contingencies, in the Notes to the Unaudited Consolidated Financial Statements for information regarding certain legal proceedings, the contents of which are herein incorporated by reference.

Item 1A. Risk Factors.

The risks described in Item 1A. Risk Factors, in our Annual Report on Form 10-K for the year ended June 30, 2014, could materially and adversely affect our business, financial condition and results of operations. These risk factors do not identify all risks that we face our operations could also be affected by factors that are not presently known to us or that we currently consider to be immaterial to our operations. The Risk Factors section of our 2014 Annual Report on Form 10-K remains current in material respects, with the exception of the revised risk factors below.

The majority of our revenue is attributable to operations outside the United States, and our operating results therefore may be materially affected by the economic, political, military, regulatory and other risks of foreign operations or of transacting business with customers outside the United States.

As of December 31, 2014, we operated in 32 countries. We sell our products primarily through a direct sales force located throughout the world. In the event that we are unable adequately to staff and maintain our foreign operations, we could face difficulties managing our international operations.

Customers outside the United States accounted for the majority of our total revenue during the three and six months ended December 31, 2014 and 2013. We anticipate that revenue from customers outside the United States will continue to account for a significant portion of our total revenue for the foreseeable future. Our operating results attributable to operations outside the United States are subject to additional risks, including:

- unexpected changes in regulatory requirements, tariffs and other barriers, including, for example, sanctions or other regulatory restrictions imposed by the United States or foreign governments;
- less effective protection of intellectual property;

- requirements of foreign laws and other governmental controls;
- delays in the execution of license agreement renewals in the same quarter in which the original agreements expire;
- difficulties in collecting trade accounts receivable in other countries;
- adverse tax consequences; and
- the challenges of managing legal disputes in foreign jurisdictions.

Fluctuations in foreign currency exchange rates could result in declines in our reported revenue and operating results.

During the three months ended December 31, 2014 and 2013, 15.0% and 15.4% of our total revenue was denominated in a currency other than the U.S. dollar, respectively. During the six months ended December 31, 2014 and 2013, 15.0% and 16.2% of our total revenue was denominated in a currency other than the U.S. dollar, respectively. In addition, certain of our operating expenses incurred outside the United States are denominated in currencies other than the U.S. dollar. Our reported revenue and operating results are subject to fluctuations in foreign exchange rates. Foreign currency risk arises primarily from the net difference between non-U.S. dollar receipts from customers outside the United States and non-U.S. dollar operating expenses for subsidiaries in foreign countries. Currently, our largest exposures to foreign exchange rates exist primarily with the Euro, Pound Sterling, Canadian dollar and Japanese Yen against the U.S. dollar. During the three and six months ended December 31, 2014 and 2013, we did not enter into, and were not a party to, any derivative financial instruments, such as forward currency exchange contracts, intended to manage the volatility of these market risks. We cannot predict the impact of foreign currency fluctuations, and foreign currency fluctuations in the future may adversely affect our revenue and operating results. Any hedging policies we may implement in the future may not be successful, and the cost of those hedging techniques may have a significant negative impact on our operating results.

Table of Contents**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

The following table provides information about purchases by us during the three months ended December 31, 2014 of shares of our common stock.

ISSUER PURCHASES OF EQUITY SECURITIES

Period	(a) Total Number of Shares Purchased (2)	(b) Average Price Paid per Share (3)	(c) Total Number of Shares Purchased as Part of Publicly Announced Program (1)	(d) Approximate Dollar Value of Shares that May Yet Be Purchased Under the Program
October 1 to 31, 2014	454,525	\$ 36.45	454,525	
November 1 to 30, 2014	533,495	\$ 37.71	533,495	
December 1 to 31, 2014	1,005,582	\$ 35.11	1,005,582	
Total	1,993,602	\$ 36.11	1,993,602	\$ 58,000,000

(1) On April 23, 2014, our Board of Directors approved a share repurchase program for up to \$200 million worth of our common stock. This share repurchase program replaced and terminated the prior program approved by the Board of Directors on April 23, 2013 that provided for repurchases of up to \$150 million.

(2) As of December 31, 2014, the total number of shares of common stock repurchased under all programs approved by the Board of Directors was 12,416,207 shares.

(3) The total average price paid per share is calculated as the total amount paid for the repurchase of our common stock during the period divided by the total number of shares repurchased.

Table of Contents**Item 6. Exhibits.**

Exhibit Number	Description	Filed with this Form 10-Q	Incorporated by Reference Form	Filing Date with SEC	Exhibit Number
31.1	Certification of Principal Executive Officer pursuant to Exchange Act Rules 13a-14 and 15d-14, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	X			
31.2	Certification of Principal Financial Officer pursuant to Exchange Act Rules 13a-14 and 15d-14, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	X			
32.1	Certification of President and Chief Executive Officer and Executive Vice President and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	X			
101.INS	Instance Document	X			
101.SCH	XBRL Taxonomy Extension Schema Document	X			
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document	X			
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document	X			
101.LAB	XBRL Taxonomy Extension Label Linkbase Document	X			
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document	X			

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SIGNATURES

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.

Aspen Technology, Inc.

Date: January 28, 2015

By: */s/ ANTONIO J. PIETRI*
Antonio J. Pietri
President and Chief Executive Officer
(Principal Executive Officer)

Date: January 28, 2015

By: */s/ MARK P. SULLIVAN*
Mark P. Sullivan
Executive Vice President and Chief Financial Officer
(Principal Financial and Accounting Officer)

Table of Contents**EXHIBIT INDEX**

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