

SYNOPSYS INC
Form 10-Q
June 10, 2009
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(MARK ONE)

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

FOR THE QUARTERLY PERIOD ENDED APRIL 30, 2009

OR

- o 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: 0-19807

SYNOPSYS, INC.

(Exact name of registrant as specified in its charter)

DELAWARE

(State or other jurisdiction of
incorporation or organization)

56-1546236

(I.R.S. Employer
Identification Number)

**700 EAST MIDDLEFIELD ROAD
MOUNTAIN VIEW, CA 94043**

(Address of principal executive offices, including zip code)

(650) 584-5000

(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. (Check one):

Large accelerated filer ☒

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☐

(Do not check if a smaller reporting company)

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

As of June 5, 2009, there were 144,164,393 shares of the registrant's common stock outstanding.

Table of Contents

SYNOPSYS, INC.
QUARTERLY REPORT ON FORM 10-Q
FOR THE FISCAL QUARTER ENDED APRIL 30, 2009

TABLE OF CONTENTS

	Page
<u>PART I.</u>	1
<u>ITEM 1.</u>	1
	1
	2
	3
	4
<u>ITEM 2.</u>	15
<u>ITEM 3.</u>	26
<u>ITEM 4.</u>	26
<u>PART II</u>	27
<u>ITEM 1</u>	27
<u>ITEM 1A.</u>	27
<u>ITEM 2.</u>	35
<u>ITEM 3.</u>	35
<u>ITEM 4.</u>	35
<u>ITEM 5.</u>	36
<u>ITEM 6.</u>	36
<u>Signatures</u>	37

[Table of Contents](#)**PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****SYNOPSYS, INC.****UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS***(in thousands, except par value amounts)*

	April 30, 2009	October 31, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 506,399	\$ 577,632
Short-term investments	370,448	373,669
Total cash, cash equivalents and short-term investments	876,847	951,301
Accounts receivable, net of allowances of \$4,354 and \$2,338, respectively	189,115	147,365
Deferred income taxes	131,290	133,609
Income taxes receivable	47,651	49,859
Other current assets	50,094	40,156
Total current assets	1,294,997	1,322,290
Property and equipment, net	136,799	145,087
Goodwill	917,287	899,640
Intangible assets, net	99,343	114,760
Long-term deferred income taxes	165,600	177,386
Other long-term assets	82,025	83,315
Total assets	\$ 2,696,051	\$ 2,742,478
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 176,233	\$ 289,769
Accrued income taxes	9,256	14,496
Deferred revenue	540,609	604,718
Total current liabilities	726,098	908,983
Long-term accrued income taxes	151,816	152,745
Deferred compensation and other liabilities	76,335	76,970
Long-term deferred revenue	47,856	75,409
Total liabilities	1,002,105	1,214,107
Stockholders' equity:		
Preferred stock, \$0.01 par value: 2,000 shares authorized; none outstanding		
Common stock, \$0.01 par value: 400,000 shares authorized; 144,122 and 141,786 shares outstanding, respectively	1,441	1,418
Capital in excess of par value	1,487,096	1,471,031
Retained earnings	522,129	434,057
Treasury stock, at cost: 13,149 and 15,485 shares, respectively	(291,129)	(342,856)
Accumulated other comprehensive loss	(25,591)	(35,279)
Total stockholders' equity	1,693,946	1,528,371
Total liabilities and stockholders' equity	\$ 2,696,051	\$ 2,742,478

Edgar Filing: SYNOPSYS INC - Form 10-Q

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

SYNOPSYS, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
Revenue:				
Time-based license	\$ 283,996	\$ 278,220	\$ 569,048	\$ 546,080
Upfront license	15,994	12,214	34,321	24,735
Maintenance and service	36,845	34,119	73,221	69,203
Total revenue	336,835	324,553	676,590	640,018
Cost of revenue:				
License	42,292	41,709	84,115	82,107
Maintenance and service	15,048	16,167	30,627	32,046
Amortization of intangible assets	7,679	5,816	15,701	10,849
Total cost of revenue	65,019	63,692	130,443	125,002
Gross margin	271,816	260,861	546,147	515,016
Operating expenses:				
Research and development	102,996	95,275	200,803	187,789
Sales and marketing	82,520	82,887	159,904	160,257
General and administrative	28,691	26,171	55,873	50,012
In-process research and development			600	
Amortization of intangible assets	2,941	6,591	6,727	13,182
Total operating expenses	217,148	210,924	423,907	411,240
Operating income	54,668	49,937	122,240	103,776
Other income, net	10,445	151	12,544	6,481
Income before provision for income taxes	65,113	50,088	134,784	110,257
Provision for income taxes	16,825	10,701	34,067	24,425
Net income	\$ 48,288	\$ 39,387	\$ 100,717	\$ 85,832
Net income per share:				
Basic	\$ 0.34	\$ 0.28	\$ 0.71	\$ 0.60
Diluted	\$ 0.33	\$ 0.27	\$ 0.70	\$ 0.58
Shares used in computing per share amounts:				
Basic	143,275	141,844	142,562	143,926
Diluted	145,421	145,271	144,024	147,801

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

SYNOPSYS, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Six Months Ended April 30,,	
	2009	2008
Cash flow from operating activities:		
Net income	\$ 100,717	\$ 85,832
Adjustments to reconcile net income to net cash used in operating activities:		
Amortization and depreciation	49,728	50,244
Share-based compensation	28,803	33,486
Allowance for doubtful accounts	2,723	429
Write-down of long-term investments	2,960	
(Gain) on sale of investments	(324)	(1,192)
Deferred income taxes	7,612	3,523
Net change in deferred gains and losses on cash flow hedges	2,664	7,495
In-process research and development	600	
Net changes in operating assets and liabilities, net of acquired assets and liabilities:		
Accounts receivable	(46,707)	(46,982)
Other current assets	(7,521)	(10,300)
Other long-term assets	248	26
Accounts payable and accrued liabilities	(104,225)	(69,502)
Accrued income taxes	(5,959)	(2,873)
Deferred revenue	(88,065)	(67,309)
Deferred compensation and other liabilities	(469)	980
Net cash used in operating activities	(57,215)	(16,143)
Cash flows from investing activities:		
Proceeds from sales and maturities of short-term investments	123,041	419,181
Purchases of short-term investments	(119,227)	(253,699)
Purchases of long-term investments		(6,694)
Sales of long-term investments		77
Purchases of property and equipment	(14,734)	(19,498)
Cash paid for acquisitions	(27,333)	
Capitalization of software development costs	(1,485)	(1,408)
Net cash (used in) provided by investing activities	(39,738)	137,959
Cash flows from financing activities:		
Principal payments on capital leases	(984)	(1,452)
Issuances of common stock	26,652	36,949
Purchases of treasury stock		(170,052)
Net cash provided by (used in) financing activities	25,668	(134,555)
Effect of exchange rate changes on cash and cash equivalents	52	8,301
Net change in cash and cash equivalents	(71,233)	(4,438)
Cash and cash equivalents, beginning of year	577,632	579,327
Cash and cash equivalents, end of period	\$ 506,399	\$ 574,889

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents

SYNOPSYS, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Description of Business

Edgar Filing: SYNOPSYS INC - Form 10-Q

Synopsys, Inc. (Synopsys or the Company) is a world leader in electronic design automation (EDA), supplying the global electronics market with software, intellectual property (IP) and services used in semiconductor design and manufacturing. The Company delivers technology-leading semiconductor design and verification platforms and integrated circuit (IC) manufacturing related products to the global electronics market, enabling the development and production of complex systems-on-chips (SoCs). In addition, the Company provides IP, system-level solutions and design services to simplify the design process and accelerate time-to-market for its customers, and software and services that help customers prepare and optimize their designs for manufacturing.

Note 2. Summary of Significant Accounting Policies

The Company has prepared the accompanying unaudited condensed consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Pursuant to these rules and regulations, the Company has condensed or omitted certain information and footnote disclosures it normally includes in its annual consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP). In management's opinion, the Company has made all adjustments (consisting only of normal, recurring adjustments, except as otherwise indicated) necessary to fairly present its financial position, results of operations and cash flows. The Company's interim period operating results do not necessarily indicate the results that may be expected for any other interim period or for the full fiscal year. These financial statements and accompanying notes should be read in conjunction with the consolidated financial statements and notes thereto in Synopsys' Annual Report on Form 10-K for the fiscal year ended October 31, 2008 filed with the SEC on December 22, 2008.

To prepare financial statements in conformity with GAAP, management must make estimates and assumptions that affect the amounts reported in the unaudited condensed consolidated financial statements and accompanying notes. Actual results could differ from these estimates and may result in material effects on the Company's operating results and financial position.

Principles of Consolidation. The consolidated financial statements include the accounts of the Company and all of its subsidiaries. All significant intercompany accounts and transactions have been eliminated.

Fiscal Year End. The Company has adopted a fiscal year ending on the Saturday nearest to October 31. The Company's second quarter of fiscal 2009 ended on May 2, 2009. Fiscal 2009 and 2008 are both 52-week fiscal years. For presentation purposes, the unaudited condensed consolidated financial statements and accompanying notes refer to the applicable calendar month end.

Note 3. Fair Value Measurements of Financial Assets and Liabilities

Effective November 1, 2008, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements* (SFAS 157), which defines fair value, establishes guidelines and enhances disclosures for fair value measurements. In February 2008, the Financial Accounting Standards Board (FASB) issued Staff Position (FSP) FSP 157-2, *Effective Date of FASB Statement No. 157* (FSP 157-2). FSP 157-2 delays the effective date of SFAS 157 for all non-financial assets and liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis, until the Company's fiscal year 2010. SFAS 157 clarifies the definition of fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In addition to defining fair value, SFAS 157 establishes a three-tier fair value hierarchy that encourages the use of observable inputs but allows for unobservable inputs when observable inputs do not exist:

Edgar Filing: SYNOPSYS INC - Form 10-Q

Level 1 Observable inputs that reflect quoted prices (unadjusted) for identical instruments in active markets;

Level 2 Observable inputs other than quoted prices included in Level 1 for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-driven valuations in which all significant inputs and significant value drivers are observable in active markets; and

Level 3 Unobservable inputs to the valuation derived from fair valuation techniques in which one or more significant inputs or significant value drivers are unobservable.

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. In accordance with SFAS 157, the Company's cash equivalents, short-term investments, and marketable equity security are classified within Level 1 or Level 2. These classifications are based on the fact that cash equivalents and marketable securities are valued using quoted market prices in an active market or alternative pricing sources and models utilizing market observable inputs.

The Company's foreign currency derivative contracts are classified within Level 2 as the valuation inputs are based on quoted prices and market observable data of similar instruments.

Table of Contents

The Company's deferred compensation plan assets and liabilities are classified within Level 2 as the inputs to measure the fair value are only indirectly observable. The deferred compensation plan assets and liabilities consist of mutual funds invested in domestic and international marketable securities.

The Company's strategic investments in privately held companies are classified within Level 3 as most of the inputs used to value the investments are unobservable.

Assets/Liabilities Measured at Fair Value on a Recurring Basis

Assets and liabilities measured at fair value on a recurring basis are summarized below as of April 30, 2009:

Description	Total as of April 30, 2009	Fair Value Measurement at Reporting Date Using			
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
		(in thousands)			
Assets					
Cash equivalents:					
Money market funds	\$ 311,156	\$ 311,156	\$	\$	
Short-term investments:					
Municipal securities	370,448		370,448		
Other current assets:					
Foreign currency derivative contracts	8,160		8,160		
Other long-term assets:					
Marketable equity security(1)	565	565			
Deferred compensation plan assets	61,549	2	61,547		
Total assets	\$ 751,878	\$ 311,723	\$ 440,155	\$	
Liabilities					
Account payable and accrued liabilities:					
Foreign currency derivative contracts	\$ 13,435	\$	\$ 13,435	\$	
Deferred compensation and other liabilities:					
Deferred compensation plan liabilities	61,639		61,639		
Total liabilities	\$ 75,074	\$	\$ 75,074	\$	

(1) During the six months ended April 30, 2009, the Company recorded \$0.9 million of other-than-temporary impairment charges in other income, net, due to the decline of the stock price of a public company in its long-term investment portfolio.

Assets/Liabilities Measured at Fair Value on a Non-recurring Basis

Equity investments in privately-held companies are accounted for under the cost method of accounting. These equity investments (also called non-marketable equity investments) are classified within Level 3 as they are valued using unobservable data or data in an inactive market. The Company evaluates the fair value of each investment when an event or circumstance indicates an other-than-temporary decline in value has occurred. During the six months ended April 30, 2009, the Company determined that only one investment had impairment indicators and thus calculated the fair value of this investment by determining what a willing buyer would pay to purchase the investment using a financial model based on cash flow projections of the investment. As a result of the fair value measurement, the Company recorded \$2.1 million of other-than-temporary impairment charges on the investment in other income, net, on the unaudited condensed consolidated statement of operations in the six months ended April 30, 2009.

Table of Contents

The following table presents the equity investment subject to fair value measurement on a non-recurring basis as of April 30, 2009, and the loss recorded during the six months ended April 30, 2009:

	Total as of April 30, 2009	Significant Unobservable Inputs (Level 3)	Total gains (losses) for the three months ended April 30, 2009	Total gains (losses) for the six months ended April 30, 2009
(in thousands)				
Non-marketable equity investment	\$ 1,080	\$ 1,080	\$	\$ (2,090)

Effective January 1, 2009, the Company also adopted SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities including an Amendment of FASB Statement No. 115*. Under this statement, entities may choose to measure certain financial instruments and liabilities at fair value on a contract-by-contract basis, with changes in fair value recognized in earnings. The Company did not elect such option for its financial instruments and liabilities.

Derivatives

SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities, as amended* (SFAS 133), requires companies to recognize derivative instruments as either assets or liabilities in the statement of financial position at fair value. SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133* (SFAS 161), requires qualitative disclosures about the objectives and strategies for using derivatives and quantitative disclosures about the volume and gross fair value amounts of derivatives. The Company adopted SFAS 161 in the second quarter of fiscal 2009. Since SFAS 161 only required additional disclosure, the adoption did not impact the Company's consolidated financial position, results of operations or cash flows.

The Company operates internationally and is exposed to potentially adverse movements in foreign currency exchange rates. The Company enters into hedges in the form of foreign currency forward contracts to reduce its exposure to foreign currency rate changes on non-functional currency denominated forecasted transactions and balance sheet positions including: (1) certain assets and liabilities, (2) shipments forecasted to occur within approximately one month, (3) future billings and revenue on previously shipped orders, and (4) certain future intercompany invoices denominated in foreign currencies.

The duration of forward contracts ranges from one month to 19 months. The Company does not use foreign currency forward contracts for speculative or trading purposes. The Company enters into foreign exchange forward contracts with high credit quality financial institutions that are rated A or above and to date has not experienced nonperformance by counterparties. Further, the Company anticipates continued performance by all counterparties to such agreements.

The assets or liabilities associated with the forward contracts are recorded at fair value in other current assets or other current liabilities in the unaudited condensed consolidated balance sheet in accordance with SFAS 133. The accounting for gains and losses resulting from changes in fair value depends on the use of the foreign currency forward contract and whether it is designated and qualifies for hedge accounting.

Cash Flow Hedging Activities

Certain foreign exchange forward contracts are designated and qualify as cash flow hedges under SFAS 133. To receive hedge accounting treatment, all hedging relationships are formally documented at inception of the hedge and the hedges must be highly effective in offsetting changes to future cash flows on hedged transactions. The effective portion of gains or losses resulting from changes in fair value of these hedges is initially reported, net of tax, as a component of accumulated other comprehensive income (loss) in stockholders' equity and reclassified into revenue or operating expenses, as appropriate, at the time the forecasted transactions affect earnings. The maximum length of time over which the Company is hedging its exposure to the variability in future cash flows for forecasted transactions is approximately three years. The duration of the forward contracts is generally approximately one year or less, except for forward contracts denominated in Canadian dollar, Chinese yuan, British pound, Euro, Indian rupee and Taiwan dollar, which can have durations as long as 19 months.

Hedging effectiveness is evaluated monthly using spot rates, with any gain or loss caused by hedging ineffectiveness recorded in earnings as other income, net. The premium/discount component of the forward contracts is recorded to other income, net and is not included in evaluating hedging effectiveness.

Non-designated Hedging Activities

The Company's foreign exchange forward contracts that are used to hedge non-functional currency denominated balance sheet assets and liabilities are not designated as hedging instruments under SFAS 133. Accordingly, any gains or losses from changes in the fair value of the forward contracts are recorded in other income, net. The gains and losses on these forward contracts generally offset the gains and losses associated with the underlying assets and liabilities, which are also recorded in other income, net. The duration of the forward contracts for hedging the Company's balance sheet exposure is approximately one month.

Edgar Filing: SYNOPSYS INC - Form 10-Q

Table of Contents

The Company also has certain foreign exchange forward contracts for hedging certain international revenue and expenses that are not designated as hedging instruments under SFAS 133. Accordingly, any gains or losses from changes in the fair value of the forward contracts are recorded in other income, net. The gains and losses on these forward contracts generally offset the gains and losses associated with the foreign currency in operating income. The duration of these forward contracts is usually less than 1 year.

The overall goal of the Company's comprehensive hedging program is to minimize the impact of currency fluctuations on its net income over its fiscal year.

During the three and six months ended April 30, 2009, \$3.9 million and \$6.1 million of gains were recorded in other income, net from changes in fair values of non-designated forward contracts.

As of April 30, 2009, the Company had a total net notional amount of \$196.2 million of short-term foreign currency forward contracts outstanding with net fair market liability of \$5.3 million.

The notional principal amounts for derivative instruments provide one measure of the transaction volume outstanding as of April 30, 2009, and do not represent the amount of the Company's exposure to market loss. The Company's exposure to market loss will vary over time as a function of currency exchange rates. The amounts ultimately realized upon settlement of these financial instruments, together with the gains and losses on the underlying exposures, will depend on actual market conditions during the remaining life of the instruments.

The following represents the balance sheet location and amount of derivative instrument fair values segregated between designated and non-designated hedge instruments under SFAS 133 as of April 30, 2009:

		Fair Values of derivative instruments designated as hedging instruments under SFAS 133		Fair Values of derivative instruments not designated as hedging instruments under SFAS 133	
		(in thousands)			
Other current assets	\$	4,868		\$	3,292
Other current liabilities	\$	13,130		\$	304

The following table represents the income statement location and amount of gains and losses on derivative instrument fair values for designated hedge instruments under SFAS 133 for the three and six months ended April 30, 2009:

	Location of gain(loss) recognized in OCI on derivatives	Amount of gain(loss) recognized in OCI on derivatives (effective portion)(1)	Location of gain(loss) reclassified from OCI	Amount of gain(loss) reclassified from OCI (effective portion)(1)
--	---	---	---	---

Edgar Filing: SYNOPSYS INC - Form 10-Q

	(in thousands)							
Three months ended								
Foreign exchange contracts	Revenue		\$	2,547	Revenue		\$	1,906
Foreign exchange contracts	Operating expenses			(2,164)	Operating expenses			(5,995)
Total			\$	383			\$	(4,089)
Six months ended								
Foreign exchange contracts	Revenue		\$	2,113	Revenue		\$	2,282
Foreign exchange contracts	Operating expenses			485	Operating expenses			(10,703)
Total			\$	2,598			\$	(8,421)

(1) Refer to Note 8.

Table of Contents

The following table represents the ineffective portions of the hedge gains (losses) for derivative instruments designated as hedging instruments under SFAS 133 during the three and six months ended April 30, 2009:

	Location of gain(loss) recognized in income on derivatives (ineffective portion and excluded from effectiveness testing)		Amount of gain(loss) recognized in income statement on derivatives (ineffective portion)(1)		Amount of gain(loss) recognized in income statement on derivatives (excluded from effectiveness testing)(2)
(in thousands)					
Three months ended					
Foreign exchange contracts	Other income, net	\$	13	\$	1,480
Six months ended					
Foreign exchange contracts	Other income, net	\$	38	\$	3,044

(1) The ineffective portion includes forecast inaccuracies.

(2) The portion excluded from effectiveness includes the discount earned or premium paid for the contracts.

Note 4. Business Combinations

On December 18, 2008, the Company acquired the assets of a business for cash and incurred acquisition related costs. The Company preliminarily allocated the total purchase consideration to the assets and liabilities acquired, including identifiable intangible assets, based on their respective fair values at the acquisition date, resulting in goodwill of \$19.8 million, in process research and development expense of \$0.6 million, and identifiable intangible assets of \$6.9 million. The intangible assets are being amortized over one to six years. Goodwill, which is deductible for tax purposes, represents the excess of the purchase price over the fair value of tangible and identifiable intangible assets acquired and will not be amortized.

Note 5. Goodwill and Intangible Assets

Goodwill as of April 30, 2009 consisted of the following:

	(in thousands)
Balance at October 31, 2008	\$ 899,640
Addition(1)	19,837
Other adjustments(2)	(2,190)

Edgar Filing: SYNOPSYS INC - Form 10-Q

Balance at April 30, 2009 \$ 917,287

-
- (1) Addition relates to an acquisition of assets of a business as described in Note 4 above.
- (2) Adjustments relate to reduction of merger costs and income tax adjustments for prior year acquisitions.

Intangible assets as of April 30, 2009 consisted of the following:

	Gross Assets	Accumulated Amortization (in thousands)	Net Assets
Core/developed technology	\$ 132,731	\$ 73,964	\$ 58,767
Customer relationships	174,620	143,023	31,597
Contract rights intangible	12,600	9,890	2,710
Covenants not to compete	3,100	2,314	786
Trademarks and trade names	2,700	618	2,082
Capitalized software development costs	10,349	6,948	3,401
Total	\$ 336,100	\$ 236,757	\$ 99,343

Table of Contents

Intangible assets as of October 31, 2008 consisted of the following:

	Gross Assets	Accumulated Amortization (in thousands)	Net Assets
Core/developed technology	\$ 128,231	\$ 59,577	\$ 68,654
Customer relationships	172,420	137,106	35,314
Contract rights intangible	12,500	8,362	4,138
Covenants not to compete	3,100	2,006	1,094
Trademarks and trade names	2,600	330	2,270
Capitalized software development costs	8,784	5,494	3,290
Total	\$ 327,635	\$ 212,875	\$ 114,760

Amortization expense related to intangible assets consisted of the following:

	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
	(in thousands)			
Core/developed technology	\$ 6,998	\$ 5,354	\$ 14,387	\$ 9,916
Customer relationships	2,554	6,197	5,917	12,394
Contract rights intangible	767	679	1,528	1,367
Covenant not to compete	154	166	308	333
Trademark and trade names	147	10	288	20
Capitalized software development costs(1)	732	721	1,454	1,449
Total	\$ 11,352	\$ 13,127	\$ 23,882	\$ 25,479

(1) Amortization of capitalized software development costs is included in cost of license revenue in the unaudited condensed consolidated statements of operations.

The following table presents the estimated future amortization of intangible assets:

Fiscal Year	(in thousands)
Remainder of fiscal 2009	\$ 22,361
2010	32,788
2011	21,307
2012	13,056
2013	5,776
2014 and thereafter	4,055
Total	\$ 99,343

Note 6. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities consisted of the following:

	April 30, 2009	(in thousands)	October 31, 2008
Payroll and related benefits	\$ 115,760	\$	188,344
Other accrued liabilities	49,377		74,297
Accounts payable	8,661		23,168
Acquisition related costs	2,435		3,960
Total	\$ 176,233	\$	289,769

Table of Contents**Note 7. Credit Facility**

On October 20, 2006, the Company entered into a five-year, \$300.0 million senior unsecured revolving credit facility providing for loans to the Company and certain of its foreign subsidiaries. The amount of the facility may be increased by up to an additional \$150.0 million through the fourth year of the facility. The facility contains financial covenants requiring the Company to maintain a minimum leverage ratio and specified levels of cash, as well as other non-financial covenants. The facility terminates on October 20, 2011. Borrowings under the facility bear interest at the greater of the administrative agent's prime rate or the federal funds rate plus 0.50%; however, the Company has the option to pay interest based on the outstanding amount at Eurodollar rates plus a spread between 0.50% and 0.70% based on a pricing grid tied to a financial covenant. In addition, commitment fees are payable on the facility at rates between 0.125% and 0.175% per year based on a pricing grid tied to a financial covenant. As of April 30, 2009, the Company had no outstanding borrowings under this credit facility and was in compliance with all the covenants.

Note 8. Comprehensive Income

The following table presents the components of comprehensive income:

	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
	(in thousands)			
Net income	\$ 48,288	\$ 39,387	\$ 100,717	\$ 85,832
Change in unrealized (losses) gains on investments, net of tax of \$289 and (\$1,336), for the three and six months ended April 30, 2009, respectively, and of \$1,275 and \$598 for each of the same periods in fiscal 2008, respectively	(438)	(1,932)	2,024	(906)
Deferred gains (losses) on cash flow hedges, net of tax of \$1,288 and (\$66), for the three and six months ended April 30, 2009, respectively, and of (\$758) and (\$1,537) for each of the same periods in fiscal 2008, respectively	383	3,854	2,598	5,958
Reclassification adjustment on deferred (gains) losses on cash flow hedges, net of tax of (\$582) and (\$1,708), for the three and six months ended April 30, 2009, respectively, and of \$921 and \$1,109 for each of the same periods in fiscal 2008, respectively	4,089	(3,010)	8,421	(4,110)
Foreign currency translation adjustment	(2,482)	943	(3,355)	(1,431)
Total	\$ 49,840	\$ 39,242	\$ 110,405	\$ 85,343

Note 9. Stock Repurchase Program

Edgar Filing: SYNOPSYS INC - Form 10-Q

The Company is authorized to purchase up to \$500.0 million of its common stock under a stock repurchase program originally established by the Company's Board of Directors (Board) in December 2004 and replenished to \$500.0 million in March 2007. The Company repurchases shares to offset dilution caused by ongoing stock issuances from existing plans for equity compensation awards, acquisitions, and when management believes it is a good use of cash. Repurchases are transacted in accordance with Rule 10b-18 under the Securities Exchange Act of 1934 (Exchange Act) through open market purchases, plans executed under Rule 10b5-1 under the Exchange Act and structured transactions.

There were no stock repurchases during the three and six months ended April 30, 2009. During the three and six months ended April 30, 2008, the Company purchased 3.8 million shares at an average price of \$23.06 per share, and 7.2 million shares at an average price of \$23.64 per share, respectively. During the three and six months ended April 30, 2009, approximately 2.1 million and 2.3 million shares were reissued from treasury stock, respectively, for employee share-based compensation requirements. During the three and six months ended April 30, 2008, approximately 1.8 million and 2.5 million shares were reissued from treasury stock, respectively, for employee share-based compensation requirements. As of April 30, 2009, \$209.7 million remained available for future purchases under the program.

Note 10. Share-based Compensation

The Company uses the Black-Scholes option-pricing model to determine the fair value of stock options and employee stock purchase plan awards under SFAS No. 123 (Revised 2004), *Share-Based Payment*, (SFAS123(R)). The Black-Scholes option-pricing model incorporates various subjective assumptions including expected volatility, expected term and interest rates. The expected

Edgar Filing: SYNOPSYS INC - Form 10-Q

Table of Contents

volatility for both stock options and employee stock purchase plan (ESPP) is estimated by a combination of implied volatility for publicly traded options of the Company's stock with a term of six months or longer and the historical stock price volatility over the estimated expected term of the Company's share-based awards. The expected term of the Company's share-based awards is based on historical experience.

As of April 30, 2009, there was \$109.0 million of unamortized share-based compensation expense which is expected to be amortized over a weighted-average period of approximately 2.4 years. The intrinsic values of options exercised during the three and six months ended April 30, 2009 were \$1.4 million and \$1.6 million, respectively. The intrinsic values of options exercised during the three and six months ended April 30, 2008 were \$3.6 million and \$8.7 million, respectively.

The compensation cost recognized in the unaudited condensed consolidated statements of operations for these share-based compensation arrangements was as follows:

	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
	(in thousands)			
Cost of license	\$ 1,729	\$ 2,296	\$ 3,373	\$ 3,624
Cost of maintenance and service	543	810	1,090	2,152
Research and development expense	6,193	7,444	12,171	13,863
Sales and marketing expense	3,139	4,351	6,260	8,051
General and administrative expense	3,057	2,940	5,909	5,796
Share-based compensation expense before taxes	14,661	17,841	28,803	33,486
Income tax benefit	(3,338)	(4,184)	(6,558)	(7,852)
Share-based compensation expense after taxes	\$ 11,323	\$ 13,657	\$ 22,245	\$ 25,634

Note 11. Net Income per Share

The Company computes basic income per share by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted net income per share reflects the dilution of potential common shares outstanding such as stock options and unvested restricted stock units and awards during the period using the treasury stock method.

The tables below illustrate the weighted-average common shares used to calculate basic net income per share with the weighted-average common shares used to calculate diluted net income per share:

	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
	(in thousands)			
Numerator:				
Net income	\$ 48,288	\$ 39,387	\$ 100,717	\$ 85,832

Edgar Filing: SYNOPSYS INC - Form 10-Q

Denominator:

Weighted-average common shares for basic net income per share	143,275	141,844	142,562	143,926
Dilutive effect of common share equivalents from equity-based compensation	2,146	3,427	1,462	3,875
Weighted-average common shares for diluted net income per share	145,421	145,271	144,024	147,801

Edgar Filing: SYNOPSYS INC - Form 10-Q

Table of Contents

	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
Net income per share:				
Basic	\$ 0.34	\$ 0.28	\$ 0.71	\$ 0.60
Diluted	\$ 0.33	\$ 0.27	\$ 0.70	\$ 0.58

Diluted net income per share excludes 18.1 million and 13.0 million of anti-dilutive stock options and unvested restricted stock units and awards for the three months ended April 30, 2009 and 2008, respectively; and 19.6 million and 9.8 million of anti-dilutive options and unvested restricted stock units and awards for the six months ended April 30, 2009 and 2008, respectively. While these stock options and unvested restricted stock units and awards were anti-dilutive for the respective periods, they could be dilutive in the future.

Note 12. Segment Disclosure

SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*, (SFAS 131) requires disclosures of certain information regarding operating segments, products and services, geographic areas of operation and major customers. SFAS 131 reporting is based upon the management approach, i.e., how management organizes the Company's operating segments for which separate financial information is (1) available and (2) evaluated regularly by the Chief Operating Decision Maker (CODM) in deciding how to allocate resources and in assessing performance. Synopsys' CODMs are the Company's Chief Executive Officer and Chief Operating Officer.

The Company provides software and hardware products and consulting services in the electronic design automation software industry. The Company operates in a single segment. In making operating decisions, the CODMs primarily consider consolidated financial information, accompanied by disaggregated information about revenues by geographic region. Specifically, the CODMs consider where individual seats or licenses to the Company's products are used in allocating revenue to particular geographic areas. Revenue is defined as revenues from external customers. Goodwill is not allocated since the Company operates in one reportable operating segment.

The following table presents the revenues related to operations by geographic areas:

	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
	(in thousands)			
Revenue:				
United States	\$ 160,601	\$ 160,330	\$ 326,058	\$ 321,040
Europe	51,351	48,750	100,436	98,045
Japan	67,231	60,052	137,178	112,525
Asia-Pacific and other	57,652	55,421	112,918	108,408
Consolidated	\$ 336,835	\$ 324,553	\$ 676,590	\$ 640,018

Geographic revenue data for multi-region, multi-product transactions reflect internal allocations and is therefore subject to certain assumptions and to the Company's methodology.

Edgar Filing: SYNOPSYS INC - Form 10-Q

One customer accounted for more than ten percent of the Company's consolidated revenue in the three and six months ended April 30, 2009 and 2008.

Note 13. Other Income, net

The following table presents the components of other income, net:

	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
	(in thousands)			
Interest income	\$ 2,782	\$ 5,268	\$ 6,425	\$ 12,284
Gain (loss) on assets related to executive deferred compensation plan assets	3,499	(5,010)	(519)	(5,503)
Foreign currency exchange gain (loss)	2,311	(81)	5,712	714
Other, net	1,853	(26)	926	(1,014)
Total	\$ 10,445	\$ 151	\$ 12,544	\$ 6,481

Table of Contents**Note 14. Taxes**

The Company estimates its annual effective tax rate at the end of each fiscal quarter. The Company's estimate takes into account estimations of annual pre-tax income, the geographic mix of pre-tax income and the Company's interpretations of tax laws and possible outcomes of audits.

The following table presents the provision for income taxes and the effective tax rates for the three and six months ended April 30, 2009 and 2008:

	Three Months Ended April 30,		Six Months Ended April 30,	
	2009	2008	2009	2008
	(dollars in thousands)			
Income before income taxes	\$ 65,113	\$ 50,088	\$ 134,784	\$ 110,257
Provision for income tax	\$ 16,825	\$ 10,701	\$ 34,067	\$ 24,425
Effective tax rate	26%	21%	25%	22%

The Company's effective tax rate for the three and six months ended April 30, 2009 is lower than the statutory federal income tax rate of 35% primarily due to the tax impact of non-U.S. operations, which are taxed at lower rates, and research and development credits, partially offset by state taxes and non-deductible share-based compensation recorded under SFAS 123(R). The effective tax rate increased in the three and six months ended April 30, 2009, as compared to the same periods in fiscal 2008, primarily due to a decrease in tax exempt investment income and changes in mix of geographical earnings.

The timing of the resolution of income tax examinations is highly uncertain as well as the amounts and timing of various tax payments that are part of the settlement process. This could cause large fluctuations in the balance sheet classification of current and non-current assets and liabilities. The Company believes that in the next twelve months it is reasonably possible that the statute of limitations will expire on income and withholding tax filings in various jurisdictions, and that certain federal and foreign transfer pricing issues could be effectively settled. Given the uncertainty as to ultimate settlement terms, the timing of payment and the impact of such settlements on other uncertain tax positions, the range of the estimated potential decrease in underlying unrecognized tax benefits is between \$0 and \$76 million, of which approximately \$50 million would decrease goodwill as a result of the settlement of the IRS examination for fiscal 2002 through 2004. See *IRS Examinations* below for the status of current federal income tax audits.

On February 17, 2009, the President of the United States signed into law the American Recovery and Reinvestment Act of 2009 (the "Recovery Act"), which has significant tax implications for certain businesses and individuals. The Company has not yet fully analyzed all provisions of the Recovery Act but does not anticipate it having a material impact on its effective tax rate for fiscal 2009.

On May 27, 2009, the 9th Circuit Court of Appeals issued its ruling in the case of *Xilinx, Inc. v. Commissioner*, holding that stock based compensation was required to be included in certain transfer pricing arrangements between a U.S. company and its offshore subsidiary. As a result of the ruling in this case, the Company expects to increase its liability for unrecognized tax benefits and decrease shareholders' equity by approximately \$8 to \$10 million mostly in the third quarter of 2009.

IRS Examinations

The Company is regularly audited by the IRS.

On June 30, 2008, the Appeals Office of the IRS and the Company executed a final Closing Agreement with respect to a Revenue Agent's Report (RAR) received for the audit of fiscal years 2000 and 2001, in connection with a transfer pricing dispute. As a result of the Closing Agreement and the Company's concurrent evaluation of its ability to use certain foreign tax credits, the Company's provision for income taxes in its third fiscal quarter of 2008 included a net income tax benefit (net of decreases in related deferred tax assets) of \$17.3 million.

In July 2008, the IRS completed its field examination of fiscal years 2002-2004 and issued an RAR in which the IRS proposed an adjustment that would result in an aggregate tax deficiency for the three year period of approximately \$236.2 million, \$130.5 million of which would be a reduction of certain tax losses and credits that would otherwise be available either as refund claims or to offset taxes due in future periods. The IRS is contesting the Company's tax deduction for payments made in connection with litigation between Avant! Corporation and Cadence Design Systems, Inc. In addition, the IRS has asserted that the Company is required to make an additional transfer pricing adjustment with a wholly owned non-U.S. subsidiary as a result of the Company's acquisition of Avant! in 2002. The IRS also proposed adjustments to the Company's transfer pricing arrangements with its foreign subsidiaries, deductions for foreign trade income and certain temporary differences. The Company has agreed to additional taxes of approximately

Table of Contents

\$20.0 million for these proposed adjustments, which have been fully provided for in prior years. The total adjustments proposed by the IRS, if sustained, would also result in additional state taxes (net of the federal tax benefit for state taxes paid) of approximately \$17 million. On August 9, 2008, the Company timely filed a protest with the IRS.

In the second quarter of fiscal 2009, the Company reached a tentative settlement with the Examination Division of the IRS that would resolve this matter. The settlement is subject to further review and approval within the federal government, including the Joint Committee on Taxation of the U.S. Congress (Joint Committee), which could take at least several more months, but the Company believes that settlement is likely. If the settlement becomes final on the tentative terms agreed upon, the Company has already adequately provided for this matter. As a result of the settlement, the Company would owe additional taxes of approximately \$53 million (including interest) which would likely be payable within the next 12 months and would be fully offset by future tax benefits over the next 8 years. Upon Joint Committee approval, certain refund claims of approximately \$35 million (including interest) would be disbursed to the Company as a result of the settlement. The net impact of the tentative settlement on the Company's tax expense is not expected to be material. Final resolution of this matter could take considerable time or may not be finally approved by the federal government, in which case, while the Company believes it is still adequately provided for regarding this matter, there is still a possibility that an adverse outcome of the matter could have a material effect on the Company's results of operations and financial condition.

Note 15. Contingencies

See Note 14 above regarding the IRS Examinations.

Other Proceedings

The Company is also subject to other routine legal proceedings, as well as demands, claims and threatened litigation, that arise in the normal course of its business. The ultimate outcome of any litigation is uncertain and unfavorable outcomes could have a negative impact on the Company's financial position and results of operations.

Note 16. Effect of New Accounting Pronouncements

In May 2009, the FASB issued FASB Statement No. 165, *Subsequent Events* (SFAS 165). SFAS 165 intends to establish general standards of accounting for and disclosures of subsequent events that occurred after the balance sheet date but prior to the issuance of financial statements. SFAS 165 is effective for financial statements issued for interim or fiscal years ending after June 15, 2009. The requirements of SFAS 165 will be effective for the Company in the third fiscal quarter of fiscal 2009. The adoption of SFAS 165 will not have significant impacts on its consolidated financial position, results of operations or cash flows.

With the exception of the discussion above, the effect of recent accounting pronouncements has not changed from the Company's Annual Report on Form 10-K for the fiscal year ended October 31, 2008.

Table of Contents

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Quarterly Report on Form 10-Q, and in particular the following discussion, includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 (the Securities Act) and Section 21E of the Securities Exchange Act of 1934 (the Exchange Act). These statements include but are not limited to statements concerning: our business, product and platform strategies, expectations regarding previous and future acquisitions; completion of development of our unfinished products, or further development or integration of our existing products; continuation of current industry trends towards vendor consolidation; expectations regarding our license mix; expectations regarding customer interest in more highly integrated tools and design flows; expectations of the success of our intellectual property and design for manufacturing initiatives; expectations concerning recent completed acquisitions; expectations regarding the likely outcome of the Internal Revenue Service's proposed net tax deficiencies for fiscal years 2000 through 2004 and other outstanding litigation; expectations that our cash, cash equivalents and short-term investments and cash generated from operations will satisfy our business requirements for the next 12 months; and our expectations of our future liquidity requirements. Our actual results could differ materially from those projected in the forward-looking statements as a result of a number of factors, risks and uncertainties, including, without limitation, those identified below in Part II, Item 1A of this Form 10-Q. The words may, will, could, would, anticipate, expect, intend, believe, continue, or the negatives of these terms, or other comparable terminology and similar expressions identify these forward-looking statements. However, these words are not the only means of identifying such statements. In addition, any statements that refer to expectations, projections or other characterizations of future events or circumstances are forward-looking statements. The information included herein is given as of the filing date of this Form 10-Q with the Securities and Exchange Commission (SEC) and future events or circumstances could differ significantly from these forward-looking statements. Accordingly, we caution readers not to place undue reliance on these statements. Unless required by law, we undertake no obligation to update publicly any forward-looking statements. All subsequent written or oral forward-looking statements attributable to our company or persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. Readers are urged to carefully review and consider the various disclosures made in this report and in other documents we file from time to time with the SEC that attempt to advise interested parties of the risks and factors that may affect our business.

The following summary of our financial condition and results of operations should be read together with our unaudited condensed consolidated financial statements and the related notes thereto contained in Part I, Item 1 of this report and with our audited consolidated financial statements and the related notes thereto contained in our Annual Report on Form 10-K for the fiscal year ended October 31, 2008, filed with the SEC on December 22, 2008.

Fiscal Year End. Our fiscal year ends on the Saturday nearest to October 31. Our second fiscal quarter ended on May 2, 2009. Fiscal 2009 and 2008 are both 52-week fiscal years. For presentation purposes, the unaudited condensed consolidated financial statements and accompanying notes refer to the applicable calendar month end.

Overview

Business Summary

We are a world leader in electronic design automation (EDA) software and related services for semiconductor design companies. We offer a broad portfolio of solutions that are highly integrated to solve our customers' needs at each stage of the semiconductor chip design process. We deliver technology-leading semiconductor design and verification software platforms and integrated circuit (IC) manufacturing software products to the global electronics market, enabling the development and production of complex systems-on-chips (SoCs). In addition, we provide intellectual property (IP), system-level design hardware and software products, and design services to simplify the design process and

Edgar Filing: SYNOPSYS INC - Form 10-Q

accelerate time-to-market for our customers. Finally, we provide software and services that help customers prepare and optimize their designs for manufacturing.

We generate a substantial majority of our revenue from large customers in the semiconductor and electronics industries. Our customers typically fund purchases of our software and services largely out of their research and development (R&D) budgets and, to a lesser extent, their manufacturing and capital budgets. Our customers continually face the competing challenges of developing increasingly advanced electronics products while reducing their design and manufacturing costs in order to meet ongoing consumer demand for lower prices. Our customers business outlook and willingness to invest in new and increasingly complex chip designs affect their spending decisions and vendor selections. The current crisis in the financial markets and the ongoing weakness of the global economy have exacerbated these challenges.

Our customers bargain on various aspects of the contractual arrangements they make with us. Our customers often demand a broader portfolio of solutions, support and services and seek more favorable terms such as expanded license usage, future purchase rights and other unique rights at an overall lower total cost of design. Our customer arrangements are complex, involving hundreds of products and various license rights. No one factor drives our customers buying decisions and we compete on all fronts to capture a higher portion of our customers budgets in a highly competitive EDA market. Customers generally negotiate the total value of the

Table of Contents

arrangement rather than just unit pricing or volumes. Collectively, the increase in the value of all of our customer contracts is the primary driver of our overall growth in revenue over time. As further described below, the effect of an increase in value for a particular customer is typically recognized over the life of the customer contract rather than in one particular period.

Our business model allows a substantial majority of our customers to pay for licenses over a period of time and generates recurring revenue for us over a period of time, generally three years. We continue to target achieving greater than 90% of our total revenue as recurring revenue, which we refer to in our financial statements as time-based license and maintenance and service revenue. Accordingly, most of the revenue we recognize in any particular quarter results from our selling efforts in each of the prior periods during the last three or so years rather than from efforts or changes in the current period. The timing of orders is less important to us in the short term and we have historically been able to resist typical software industry quarter-end pressures and minimize the closing of contracts with terms, including pricing terms, which may be less favorable to us.

Short-term fluctuations in industry or general economic conditions or in orders generally do not immediately affect our financial results due to our business model. While the electronics, semiconductor and EDA industries are currently experiencing severe uncertainty and weakness due to the downturn in the global economy, to date our business model has substantially protected our financial results.

Nevertheless, our business model and longer-term financial results are not immune from sustained economic downturns. The turmoil and uncertainty caused by current economic conditions have caused some of our customers to postpone their decision-making, decrease their spending and/or delay their payments to us. We experienced a slight decrease in the committed average annual revenue from customers that renewed their contracts with us during the second quarter of fiscal 2009 and we currently expect such committed average annual revenue to also be down slightly at the end of fiscal 2009 compared to the end of fiscal 2008. Continued periods of decreased committed average annual revenue, additional customer bankruptcies, or consolidation among our customers, could adversely affect our year-over-year revenue growth and could decrease our backlog. The economic downturn has also negatively affected several of our principal competitors, and a few have recently announced lower revenues than they had previously expected. We will continue to monitor market conditions and may make adjustments to our business in order to reduce the adverse impact that the prolonged economic downturn could have on our business. We believe that the combination of our solid financials, leading technology and strong customer relationships will help us implement our strategies successfully.

Financial Performance Summary for the Three Months Ended April 30, 2009

- Total revenue of \$336.8 million was up 4% from \$324.6 million in the same quarter in fiscal 2008. The increase was primarily attributable to revenue recognized from term licenses booked in prior periods which were recognized as time-based licenses under our accounting policy, as well as the impact of Synplicity sales from our acquisition in May 2008.
- Time-based license revenue of \$284.0 million was up 2% from \$278.2 million in the same quarter in fiscal 2008. The increase was primarily attributable to revenue recognized from term licenses booked in prior periods which were recognized as time-based licenses in the current quarter.
- Upfront license revenue of \$16.0 million was up 31% from \$12.2 million in the same quarter in fiscal 2008. The increase reflected the impact of Synplicity product sales.

- We derived approximately 95% of our total revenue from time-based, maintenance and services revenues, and 5% from upfront revenue, compared to approximately 96% and 4%, respectively, in the same quarter in fiscal 2008. This reflects our adherence to our current business model.
- Maintenance revenue of \$21.6 million was up 38% from \$15.7 million in the same quarter in fiscal 2008. The increase was primarily attributable to the maintenance contracts associated with the impact of Synplicity product sales. Professional services and other revenue of \$15.2 million were down 17% from \$18.4 million in the same quarter in fiscal 2008. The decrease was primarily driven by the decrease in customer demand as a result of the economic downturn and the timing of customer acceptance of services performed under ongoing contracts.
- Net income of \$48.3 million was up 23% from \$39.4 million in the same quarter in fiscal 2008. The increase was primarily due to slight increases in revenues and cost control efforts.

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial results under the heading *Result of Operations* below are based on our unaudited condensed consolidated financial statements, which we have prepared in accordance with U.S. generally accepted accounting principles. In preparing these financial statements, we make assumptions, judgments and estimates that can affect the reported amounts of assets, liabilities, revenues and expenses and net income. On an on-going basis, we evaluate our estimates based on

Table of Contents

historical experience and various other assumptions we believe are reasonable under the circumstances. Our actual results may differ from these estimates.

We describe our revenue recognition and income taxes policies below. Our remaining critical accounting policies and estimates are discussed in Part II, Item 7 *Management's Discussion and Analysis of Financial Condition and Results of Operations* of our Annual Report on Form 10-K for the fiscal year ended October 31, 2008, filed with the SEC on December 22, 2008.

Revenue Recognition

We recognize revenue from software licenses and related maintenance and service revenue and, to a lesser extent, from hardware sales. Software license revenue consists of fees associated with the licensing of our software. Maintenance and service revenue consists of maintenance fees associated with perpetual and term licenses and professional service fees.

We have designed and implemented revenue recognition policies in accordance with Statement of Position (SOP) 97-2, *Software Revenue Recognition*, as amended, and EITF 00-21, *Revenue Arrangements with Multiple Deliverables*.

With respect to software licenses, we utilize three license types:

- *Technology Subscription Licenses (TSLs)* are time-based licenses for a finite term, and generally provide the customer limited rights to receive, or to exchange certain quantities of licensed software for, unspecified future technology. We bundle and do not charge separately for post-contract customer support (maintenance) for the term of the license.
- *Term Licenses* are also for a finite term, but do not provide the customer any rights to receive, or to exchange licensed software for, unspecified future technology. Customers purchase maintenance separately for the first year and may renew annually for the balance of the term. The annual maintenance fee is typically calculated as a percentage of the net license fee.
- *Perpetual Licenses* continue as long as the customer renews maintenance plus an additional 20 years. Perpetual licenses do not provide the customer any rights to receive, or to exchange licensed software for, unspecified future technology. Customers purchase maintenance separately for the first year and may renew annually.

For the three software license types, we recognize revenue as follows:

Edgar Filing: SYNOPSYS INC - Form 10-Q

- *TSLs.* We typically recognize revenue from TSL fees (which include bundled maintenance) ratably over the term of the license period, or as customer installments become due and payable, whichever is later. Revenue attributable to TSLs is reported as time-based license revenue in the unaudited condensed consolidated statement of operations.
- *Term Licenses.* We recognize revenue from term licenses in full upon shipment of the software if payment terms require the customer to pay at least 75% of the license fee within one year from shipment and all other revenue recognition criteria are met. Revenue attributable to these term licenses is reported as upfront license revenue in the unaudited condensed consolidated statement of operations. For term licenses in which less than 75% of the license fee is due within one year from shipment, we recognize revenue as customer installments become due and payable. Such revenue is reported as time-based license revenue in the unaudited condensed consolidated statement of operations.
- *Perpetual Licenses.* We recognize revenue from perpetual licenses in full upon shipment of the software if payment terms require the customer to pay at least 75% of the license fee within one year from shipment and all other revenue recognition criteria are met. Revenue attributable to these perpetual licenses is reported as upfront license revenue in the unaudited condensed consolidated statement of operations. For perpetual licenses in which less than 75% of the license fee is payable within one year from shipment, we recognize the revenue as customer installments become due and payable. Revenue attributable to these perpetual licenses is reported as time-based license revenue in the unaudited condensed consolidated statement of operations.

We generally recognize revenue from hardware sales in full upon shipment if all other revenue recognition criteria are met. Revenue attributable to these hardware sales is reported as upfront license revenue in the unaudited condensed consolidated statement of operations. If a technology subscription license is sold together with the hardware, we recognize revenue ratably over the term of the software license period, or as customer installments become due and payable, whichever is later.

In addition, we recognize revenue from maintenance fees ratably over the maintenance period to the extent cash has been received or fees become due and payable, and recognize revenue from professional service and training fees as such services are performed and accepted by the customer. Revenue attributable to maintenance, professional services and training is reported as maintenance and service revenue in the unaudited condensed consolidated statement of operations.

Table of Contents

Our determination of fair value of each element in multiple element arrangements is based on vendor-specific objective evidence (VSOE). We limit our assessment of VSOE of fair value for each element to the price charged when such element is sold separately.

We have analyzed all of the elements included in our multiple-element software arrangements and have determined that we have sufficient VSOE to allocate revenue to the maintenance components of our perpetual and term license products and to professional services. Accordingly, assuming all other revenue recognition criteria are met, we recognize license revenue from perpetual and term licenses upon delivery using the residual method, we recognize revenue from maintenance ratably over the maintenance term, and we recognize revenue from professional services as milestones are performed and accepted. We recognize revenue from TSLs ratably over the term of the license, assuming all other revenue recognition criteria are met, since there is not sufficient VSOE to allocate the TSL fee between license and maintenance services.

We make significant judgments related to revenue recognition. Specifically, in connection with each transaction involving our products, we must evaluate whether: (1) persuasive evidence of an arrangement exists, (2) delivery of software or services has occurred, (3) the fee for such software or services is fixed or determinable, and (4) collectability of the full license or service fee is probable. All four of these criteria must be met in order for us to recognize revenue with respect to a particular arrangement. We apply these revenue recognition criteria as follows:

- *Persuasive Evidence of an Arrangement Exists.* Prior to recognizing revenue on an arrangement, our customary policy is to have a written contract, signed by both the customer and us or a purchase order from those customers that have previously negotiated a standard end-user license arrangement or purchase agreement.
- *Delivery Has Occurred.* We deliver our products to our customers electronically or physically. For electronic deliveries, delivery occurs when we provide access to our customers to take immediate possession of the software by downloading it to the customer's hardware. For physical deliveries, the standard transfer terms are typically FOB shipping point. We generally ship our products or license keys promptly after acceptance of customer orders. However, a number of factors can affect the timing of product shipments and, as a result, timing of revenue recognition, including the delivery dates requested by customers and our operational capacity to fulfill product orders at the end of a quarter.
- *The Fee is Fixed or Determinable.* Our determination that an arrangement fee is fixed or determinable depends principally on the arrangement's payment terms. Our standard payment terms for perpetual and term licenses require 75% or more of the license fee to be paid within one year. If the arrangement includes these terms, we regard the fee as fixed or determinable, and recognize all license revenue under the arrangement in full upon delivery (assuming all other revenue recognition criteria are met). If the arrangement does not include these terms, we do not consider the fee to be fixed or determinable and generally recognize revenue when customer installments are due and payable. In the case of a TSL, because of the right to exchange products or receive unspecified future technology and because VSOE for maintenance services does not exist for a TSL, we recognize revenue ratably over the term of the license, but not in advance of when customers' installments become due and payable, even if the fee is otherwise fixed or determinable.
- *Collectability is Probable.* We judge collectability of the arrangement fees on a customer-by-customer basis pursuant to our credit review policy. We typically sell to customers with whom we have a history of successful collection. For a new customer, or when an existing customer substantially expands its commitments to us, we evaluate the customer's financial position and ability to pay and typically assign a credit limit based on that review. We increase the credit limit only after we have established a successful collection history with the customer. If we determine at any time that collectability is not probable under a particular arrangement based upon our credit review process or the customer's payment history, we recognize revenue under that arrangement as customer payments are actually received.

Income Taxes

We calculate our current and deferred tax provisions in accordance with Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes* (SFAS 109). Our estimates and assumptions used in such provisions may differ from the actual results as reflected in our income tax returns and we record the required adjustments when they are identified and resolved.

We recognize deferred tax assets and liabilities for the temporary differences between the book and tax bases of assets and liabilities using enacted tax rates in effect for the year in which we expect the differences to reverse. We record a valuation allowance to reduce the deferred tax assets to the amount that is more likely than not to be realized. In evaluating our ability to utilize our deferred tax assets, we consider all available positive and negative evidence, including our past operating results, the existence of cumulative losses in the most recent fiscal years and our forecast of future taxable income on a jurisdiction by jurisdiction basis, as

Table of Contents

well as feasible and prudent tax planning strategies. These assumptions require significant judgment about the forecasts of future taxable income and are consistent with the plans and estimates we are using to manage the underlying businesses. We believe that the net deferred tax assets of approximately \$290 million that are recorded on our balance sheet will ultimately be realized. However, if we determine in the future that it is more likely than not we will not be able to realize a portion or the full amount of deferred tax assets, we would record an adjustment to the deferred tax asset valuation allowance as a charge to earnings in the period such determination is made.

Included in our net deferred tax assets as of October 31, 2008 are federal foreign tax credits of \$70.1 million of which \$63.9 million will expire from fiscal 2013 through 2018. The remaining \$6.2 million in foreign tax credits are from acquired companies, which have a valuation allowance of \$3.4 million, and will expire between fiscal 2009 and 2017. Foreign tax credits can only be carried forward ten years, unlike net operating loss and federal research credit carryforwards that have a twenty year carryforward period, and may only be used after foreign tax credits arising in each subsequent year have been used first. Our ability to utilize foreign tax credits is dependent upon having sufficient foreign source income during the carryforward period. We have recorded a valuation allowance of \$19.7 million with respect to our foreign tax credit carryforward, of which \$14.6 million was recorded as a result of the 2000-2001 final IRS settlement. See *Note 14 of Notes to Unaudited Condensed Consolidated Financial Statements*. The need for a valuation allowance with respect to foreign tax credits is subject to change based upon a number of factors, including the amount of foreign tax credits arising in future years, our forecasts of future foreign source income, the amount of our undistributed earnings of our foreign subsidiaries, the outcome of tax audit settlements and changes in income tax laws that may affect our ability to use such credits.

The calculation of tax liabilities involves the inherent uncertainty associated with the application of complex tax laws. We are also subject to examination by various taxing authorities. We believe we have adequately provided in our financial statements for potential additional taxes. If we ultimately determine that these amounts are not owed, we would reverse the liability and recognize the tax benefit in the period in which we determine that the liability is no longer necessary. If an ultimate tax assessment exceeds our estimate of tax liabilities, we would record an additional charge to earnings. See *Note 14 of Notes to Unaudited Condensed Consolidated Financial Statements* for a discussion of taxes and the Revenue Agent's Reports from the IRS we received in June 2005 and July 2008 asserting very large net increases to our U.S. tax arising from the audit of fiscal 2000 through 2001 and fiscal 2002 through 2004, respectively.

Results of Operations

Revenue Background

We generate our revenue from the sale of software licenses, hardware products, maintenance and professional services. Under current accounting rules and policies, we recognize revenue from orders we receive for software licenses, hardware products and services at varying times. In most instances, we recognize revenue on a TSL software license order over the license term and on a term or perpetual software license order in the quarter in which the license is shipped. Substantially all of our current time-based licenses are TSLs with an average license term of approximately three years. Maintenance orders normally bring in revenue ratably over the maintenance period (normally one year). Professional service orders generally turn into revenue upon completion and customer acceptance of contractually agreed milestones. A more complete description of our revenue recognition policy can be found above under *Critical Accounting Policies and Estimates*.

Our revenue in any fiscal quarter is equal to the sum of our time-based license, upfront license, maintenance and professional service revenue for the period. We derive time-based license revenue in any quarter largely from TSL orders received and delivered in prior quarters. We derive upfront license revenue directly from term and perpetual license and product hardware orders mostly booked and shipped during the quarter. We derive maintenance revenue in any quarter largely from maintenance orders received in prior quarters since our maintenance orders generally

Edgar Filing: SYNOPSYS INC - Form 10-Q

yield revenue ratably over a term of one year. We also derive professional service revenue primarily from orders received in prior quarters, since we recognize revenue from professional services when those services are delivered and accepted, not when they are booked.

Our license revenue is sensitive to the mix of TSLs and perpetual or term licenses delivered during a reporting period. A TSL order typically yields lower current quarter revenue but contributes to revenue in future periods. For example, a \$120,000 order for a three-year TSL shipped on the last day of a quarter typically generates no revenue in that quarter, but \$10,000 in each of the twelve succeeding quarters. Conversely, perpetual licenses and term licenses with greater than 75% of the license fee due within one year from shipment typically generate current quarter revenue but no future revenue (e.g., a \$120,000 order for a perpetual license generates \$120,000 in revenue in the quarter the product is shipped, but no future revenue).

Table of Contents

Total Revenue

	April 30,		Dollar		%
	2009	2008	Change	Change	
	(dollars in millions)				
Three months ended	\$ 336.8	\$ 324.6	\$ 12.2	4%	
Six months ended	\$ 676.6	\$ 640.0	\$ 36.6	6%	

Edgar Filing: SYNOPSYS INC - Form 10-Q

The increases in total revenue for the three and six months ended April 30, 2009 compared to the same periods in fiscal 2008 were primarily due to revenue recognized from term licenses booked in prior quarters which were recognized as time-based licenses under our accounting policy as well as the impact of Synplicity sales from our acquisition in May 2008. The increases were partially offset by the decrease in professional services revenue of \$6.2 million.

While the electronics, semiconductor and EDA industries are currently experiencing severe uncertainty and weakness due to the recent downturn in the global economy, to date, our business model has substantially protected our financial results and enabled us to achieve revenue growth compared to the same periods in the previous year. Nevertheless, our business model and longer-term financial results are not immune from sustained economic downturns. The turmoil and uncertainty caused by current economic conditions have caused some of our customers to postpone their decision-making, decrease their spending and/or delay their payments to us. We experienced a slight decrease in the committed average annual revenue from customers that renewed their contracts with us during the second quarter of fiscal 2009 and we currently expect such committed average annual revenue to also be down slightly at the end of fiscal 2009 compared to the end of fiscal 2008. Continued periods of decreased committed average annual revenue, additional customer bankruptcies, or consolidation among our customers, could adversely affect our year-over-year revenue growth and could decrease our backlog.

Time-Based License Revenue

	2009	April 30, 2008	Dollar Change	% Change
		(dollars in millions)		
Three months ended	\$ 284.0	\$ 278.2	\$ 5.8	2%
Percentage of total revenue	84%	86%		
Six months ended	\$ 569.0	\$ 546.1	\$ 22.9	4%
Percentage of total revenue	84%	85%		

Edgar Filing: SYNOPSYS INC - Form 10-Q

The increases in time-based license revenue for the three and six months ended April 30, 2009 compared to the same periods in fiscal 2008 was primarily due to revenue recognized from term licenses booked in prior periods which were recognized as time-based licenses.

Upfront License Revenue

	2009	April 30, 2008 (dollars in millions)	Dollar Change	% Change
Three months ended	\$ 16.0	\$ 12.2	\$ 3.8	31%
Percentage of total revenue	5%	4%		
Six months ended	\$ 34.3	\$ 24.7	\$ 9.6	39%
Percentage of total revenue	5%	4%		

Upfront license revenue increased for the three and six months ended April 30, 2009 compared to the same periods in fiscal 2008, primarily due to Synplicity related product sales from our acquisition in May 2008. The increases were also attributable to normal fluctuations in customer license requirements which can drive the amount of upfront orders and revenue in any particular quarter.

Table of Contents

Maintenance and Services Revenue

	2009	April 30, 2008	Dollar Change	% Change
	(dollars in millions)			
Three months ended				
Maintenance revenue	\$ 21.6	\$ 15.7	\$ 5.9	38%
Professional services and other revenue	15.2	18.4	(3.2)	(17)%
Total maintenance and services revenue	\$ 36.8	\$ 34.1	\$ 2.7	8%
Percentage of total revenue	11%	11%		
Six months ended				
Maintenance revenue	\$ 42.3	\$ 32.1	\$ 10.2	32%
Professional services and other revenue	30.9	37.1	(6.2)	(17)%
Total maintenance and services revenue	\$ 73.2	\$ 69.2	\$ 4.0	6%
Percentage of total revenue	11%	11%		

Edgar Filing: SYNOPSYS INC - Form 10-Q

Maintenance revenue increased for the three and six months ended April 30, 2009 compared with the same periods in fiscal 2008, primarily due to the maintenance revenue stream from perpetual-based products that we acquired in our acquisition of Synplicity that was completed in May 2008. We expect our fiscal 2009 to similarly reflect the impact of the Synplicity acquisition on a year-over-year comparative basis, but do not expect the acquisition-related increases to continue thereafter. In addition, some customers may in the future choose not to renew maintenance on upfront licenses for economic or other factors, which would lower our future maintenance revenue.

Professional services and other revenue decreased for the three and six months ended April 30, 2009 compared with the same periods in fiscal 2008 due to the decrease in customer demand as a result of the economic downturn and the timing of customer acceptance of services performed under ongoing contracts.

Events Affecting Cost of Revenues and Operating Expenses

Edgar Filing: SYNOPSYS INC - Form 10-Q

Functional Allocation of Operating Expenses. We allocate certain human resource programs, information technology and facility expenses among our functional income statement categories based on headcount within each functional area. Annually, or upon a significant change in headcount (such as a workforce reduction, realignment or acquisition) or other factors, management reviews the allocation methodology and expenses included in the allocation pool.

Cost of Revenue

	2009	April 30, 2008	Dollar Change	% Change
(dollars in millions)				
Three months ended				
Cost of license revenue	\$ 42.3	\$ 41.7	\$ 0.6	1%
Cost of maintenance and service revenue	15.0	16.2	(1.2)	(7)%
Amortization of intangible assets	7.7	5.8	1.9	32%
Total	\$ 65.0	\$ 63.7	\$ 1.3	2%
Percentage of total revenue	19%	20%		
Six months ended				
Cost of license revenue	\$ 84.1	\$ 82.1	\$ 2.0	2%
Cost of maintenance and service revenue	30.6	32.1	(1.5)	(5)%
Amortization of intangible assets	15.7	10.8	4.9	45%
Total	\$ 130.4	\$ 125.0	\$ 5.4	4%
Percentage of total revenue	19%	20%		

We divide cost of revenue into three categories: cost of license revenue, cost of maintenance and service revenue, and amortization of intangible assets. We segregate expenses directly associated with providing consulting and training from cost of license revenue associated with internal functions providing license delivery and post-customer contract support services. We then allocate these group costs between cost of license revenue and cost of maintenance and service revenue based on license and service revenue reported.

Cost of license revenue. Cost of license revenue includes costs related to products sold and software licensed, allocated operating costs related to product support and distributions costs, royalties paid to third party vendors, and the amortization of capitalized research and development costs associated with software products which have reached technological feasibility.

Table of Contents

Cost of maintenance and service revenue. Cost of maintenance and service revenue includes operating costs associated to maintain the infrastructure necessary to operate our services and training organization, and costs associated with the delivery of our consulting services, such as, hotline and on-site support, production services and documentation of maintenance updates.

Amortization of intangible assets. Amortization of intangible assets, which is amortized to cost of revenue and operating expenses, includes the amortization of the contract rights associated with certain executory contracts and the amortization of core/developed technology, trademarks, trade names, customer relationships, covenants not to compete and other intangibles related to acquisitions.

Cost of revenue increased slightly by \$1.3 million for the three months ended April 30, 2009 compared with the same period in fiscal 2008. The increase was primarily due to an increase of \$2.1 million in personnel costs and an increase of \$1.9 million in amortization of intangible assets, as a result of prior acquisitions. The increases were partially offset by decrease in travel and functionally allocated expenses as a result of expense control efforts in fiscal 2009.

The increase in cost of revenue of \$5.4 million for the six months ended April 30, 2009 compared with the same period in fiscal 2008 was primarily due to an increase of \$4.3 million in personnel related costs and an increase of \$4.9 million in amortization of intangible assets, as a result of prior acquisitions. The increases were partially offset by lower travel, consulting and functionally allocated expenses as a result of expense control efforts in fiscal 2009.

Operating Expenses*Research and Development*

	2009	April 30, 2008	Dollar Change	% Change
		(dollars in millions)		
Three months ended	\$ 103.0	\$ 95.3	\$ 7.7	8%
Percentage of total revenue	31%	29%		
Six months ended	\$ 200.8	\$ 187.8	\$ 13.0	7%
Percentage of total revenue	30%	29%		

The increase in research and development expense for the three months ended April 30, 2009 compared with the same period in fiscal 2008 was primarily due to an increase of \$7.0 million in personnel related costs which included the increase of \$4.6 million in the fair value of our deferred compensation plan obligation, and an increase of \$1.4 million in functionally allocated expenses, reflecting headcount increases as a result of prior acquisitions. The increase was partially offset by \$1.1 million decline in depreciation expense.

The increase in research and development expense for the six months ended April 30, 2009 compared with the same period in fiscal 2008 was primarily due to an increase of \$10.7 million in employee personnel related costs which included the increase of \$2.9 million in the fair value of our deferred compensation plan obligation and an increase of \$3.6 million in functionally allocated expenses, reflecting headcount increases as a

Edgar Filing: SYNOPSYS INC - Form 10-Q

result of prior acquisitions. The increase was partially offset by \$2.4 million decrease in depreciation expense.

Sales and Marketing

	2009	April 30, 2008	Dollar Change	% Change
		(dollars in millions)		
Three months ended	\$ 82.5	\$ 82.9	\$ (0.4)	<(1)%
Percentage of total revenue	24%	26%		
Six months ended	\$ 159.9	\$ 160.3	\$ (0.4)	<(1)%
Percentage of total revenue	24%	25%		

Sales and marketing expenses were relatively flat for the three and six months ended April 30, 2009 compared with the same periods in fiscal 2008.

Table of Contents*General and Administrative*

	2009	April 30, 2008	Dollar Change	% Change
		(dollars in millions)		
Three months ended	\$ 28.7	\$ 26.2	\$ 2.5	10%
Percentage of total revenue	9%	8%		
Six months ended	\$ 55.9	\$ 50.0	\$ 5.9	12%
Percentage of total revenue	8%	8%		

The increase in general and administrative expenses for the three months ended April 30, 2009 compared with the same period in fiscal 2008 was primarily due to an increase of \$1.2 million in personnel related costs and an increase of \$1.0 million in charitable contributions.

The increase in general and administrative expenses for the six months ended April 30, 2009 compared with the same period in fiscal 2008 was primarily due to an increase of \$1.5 million in facilities related costs, \$1.2 million in personnel related costs, \$1.5 million in charitable contributions, and \$2.3 million in bad debt reserve based on our review of customer receivables.

Amortization of Intangible Assets

	2009	April 30,	2008	Dollar	%		
			(dollars in millions)	Change	Change		
Three months ended							
Included in cost of revenue	\$	7.7	\$	5.8	\$	1.9	33%
Included in operating expenses		2.9		6.6		(3.7)	(56)%
Total	\$	10.6	\$	12.4	\$	(1.8)	(15)%
Percentage of total revenue		3%		4%			
Six months ended							
Included in cost of revenue	\$	15.7	\$	10.8	\$	4.9	45%
Included in operating expenses		6.7		13.2		(6.5)	(49)%
Total	\$	22.4	\$	24.0	\$	(1.6)	(7)%
Percentage of total revenue		3%		4%			

The decrease in amortization of intangible assets for three and six months ended April 30, 2009 is primarily due to certain intangible assets acquired in prior years becoming fully amortized offset by amortization of intangible assets from our Synplicity acquisition which occurred in May of fiscal 2008 and our recent acquisition in the first quarter of fiscal 2009. See Note 5 to *Notes to Unaudited Condensed Consolidated Financial Statements* for a schedule of future amortization amounts.

In-Process Research and Development

Edgar Filing: SYNOPSYS INC - Form 10-Q

In-process research and development (IPRD) expense is composed of in-process technologies of \$0.6 million associated with an acquisition of assets of a business completed during the first quarter of fiscal 2009. At the date of the acquisition, the project associated with the IPRD efforts had not yet reached technological feasibility and the research and development in process had no alternative future uses and therefore the amount was charged to expense.

Table of Contents**Other Income, net**

	2009	April 30, 2008	Dollar Change	% Change
		(dollars in millions)		
Three months ended				
Interest income	\$ 2.8	\$ 5.3	\$ (2.5)	(47)%
Gain (loss) on assets related to executive deferred compensation plan assets	3.5	(5.0)	8.5	170%
Foreign currency exchange gain (loss)	2.3	(0.1)	2.4	2400%
Other, net	1.8		1.8	100%
Total	\$ 10.4	\$ 0.2	\$ 10.2	5100%
Six months ended				
Interest income	\$ 6.4	\$ 12.3	\$ (5.9)	(48)%
Loss on assets related to executive deferred compensation plan assets	(0.5)	(5.5)	5.0	91%
Foreign currency exchange gain	5.7	0.7	5.0	714%
Other, net	0.9	(1.0)	1.9	190%
Total	\$ 12.5	\$ 6.5	\$ 6.0	92%

Other income, net, increased during the three and six months ended April 30, 2009, compared to the same period in fiscal 2008 primarily due to the fair market value fluctuations of investments in our deferred compensation plan, and foreign currency exchange gain. These increases were partially offset by a decrease in interest income due to lower interest rates.

Effect of foreign currency fluctuations

The overall goal of our comprehensive hedging activities is to minimize the impact of currency fluctuations on our net income over our fiscal year. The success of our hedging activities depends upon the accuracy of our estimates of various balances and transactions denominated in non-functional currencies. To the extent our estimates are correct, gains and losses on our foreign currency contracts will be offset by corresponding losses and gains on the underlying transactions.

Foreign currency fluctuations, net of hedging, did not have a significant impact to expenses for the three and six months ended April 30, 2009.

Taxes

See Note 14 of the *Notes to Unaudited Condensed Consolidated Financial Statements*.

Liquidity and Capital Resources

Edgar Filing: SYNOPSYS INC - Form 10-Q

Our sources of cash, cash equivalents and short-term investments are funds generated from our business operations, issuances of common stock upon stock option exercises or employee stock purchases and funds that may be drawn down under our credit facility.

The following sections discuss changes in our balance sheet and cash flows, and other commitments on our liquidity and capital resources.

Cash and Cash Equivalents and Short-Term Investments

Edgar Filing: SYNOPSYS INC - Form 10-Q

	April 30, 2009	October 31, 2008	\$ Change	% Change
		(dollars in millions)		
Cash and cash equivalents	\$ 506.4	\$ 577.6	\$ (71.2)	(12)%
Short-term investments	370.4	373.7	(3.3)	<(1)%
Total	\$ 876.8	\$ 951.3	\$ (74.5)	(8)%

Edgar Filing: SYNOPSYS INC - Form 10-Q

During the six months ended April 30, 2009, our primary sources and uses of cash consisted of (1) cash used in operating activities of \$57.2 million, (2) proceeds from sales and maturities of short-term investments of \$123.0 million, (3) proceeds from issuances of common stock of \$26.7 million, (4) purchases of investments of \$119.2 million, and (5) cash paid for acquisitions of \$27.3 million.

Table of Contents

Cash Flows

	2009	April 30, 2008	\$ Change	% Change
		(dollars in millions)		
Six months ended				
Cash used in operating activities	\$ (57.2)	\$ (16.1)	\$ (41.1)	255%
Cash (used in) provided by investing activities	(39.7)	138.0	(177.7)	(129)%
Cash provided by (used in) financing activities	25.7	(134.6)	160.3	(119)%

Edgar Filing: SYNOPSYS INC - Form 10-Q

Cash used in operating activities. Cash used in operations is dependent primarily upon the payment terms of our license agreements. To be classified as upfront revenue, we require that 75% of a term or perpetual license fee be paid within the first year. Conversely, payment terms for TSLs are generally extended and the license fee is typically paid either quarterly or annually in even increments over the term of the license. Accordingly, we generally receive cash from upfront license revenue much sooner than from time-based licenses revenue.

Cash used in operating activities primarily increased as a result of a decrease in deferred revenue due to the timing of billings and cash payments from certain customers and increased payments to vendors compared to the same period in fiscal 2008.

Cash (used in) provided by investing activities. The increase in cash used primarily relates to the timing of maturities of marketable securities and cash paid for acquisitions offset by a decrease in our purchases of marketable securities as compared to the same period in fiscal 2008.

Cash provided by (used in) financing activities. The decrease in cash used primarily relates to no common stock repurchases made under our stock repurchase program and a lower number of employee option exercises compared to the same period in fiscal 2008. See Note 9 of *Notes to Unaudited Condensed Consolidated Financial Statements* for details of our stock repurchase program.

We hold our cash, cash equivalents and short-term investments in the United States and in foreign accounts worldwide. As of April 30, 2009, we held an aggregate of \$459.7 million in cash, cash equivalents and short-term investments in the United States and an aggregate of \$417.1 million in foreign accounts. Funds in foreign accounts are generated from revenue outside North America.

We expect that cash used in or provided by operating activities may fluctuate in future periods as a result of a number of factors, including timing of our billings and collections, our operating results, the timing and amount of tax and other liability payments and cash used in any future acquisitions.

Accounts Receivable, net

Edgar Filing: SYNOPSYS INC - Form 10-Q

April 30, 2009	October 31, 2008 (dollars in millions)	\$ Change	% Change
\$ 189.1	\$ 147.4	\$ 41.7	28%

Edgar Filing: SYNOPSYS INC - Form 10-Q

Our Days Sales Outstanding (DSO) was 51 days at April 30, 2009, and 38 days at October 31, 2008. The increase in DSO, along with an increase in accounts receivable balance, primarily relates to timing of billings to customers and relatively slower collections during fiscal 2009.

Net Working Capital. Working capital is composed of current assets less current liabilities, as shown on our unaudited condensed consolidated balance sheets. As of April 30, 2009, our net working capital was \$568.9 million, compared to \$413.3 million as of October 31, 2008. The increase in net working capital of \$155.6 million was primarily due to increases in accounts receivable of \$41.8 million and other current assets of \$7.7 million, along with a decrease in (1) current income taxes accrual of \$5.2 million, (2) accounts payable and accrued liabilities of \$113.6 million, and (3) deferred revenue of \$64.1 million. These increases were partially offset by a decrease in deferred taxes of \$2.3 million and our use of \$74.5 million in cash, cash equivalents and short-term investments as described above.

Other Commitments - Revolving Credit Facility. On October 20, 2006, we entered into a five-year, \$300.0 million senior unsecured revolving credit facility providing for loans to Synopsys and certain of our foreign subsidiaries. The amount of the facility may be increased by up to an additional \$150.0 million through the fourth year of the facility. The facility contains financial covenants requiring us to maintain a minimum leverage ratio and specified levels of cash, as well as other non-financial covenants. The facility terminates on October 20, 2011. Borrowings under the facility bear interest at the greater of the administrative agent's prime rate or the federal funds rate plus 0.50%; however, we have the option to pay interest based on the outstanding amount at Eurodollar rates plus a spread between 0.50% and 0.70% based on a pricing grid tied to a financial covenant. In addition, commitment fees are payable on the facility at rates between 0.125% and 0.175% per year based on a pricing grid tied to a financial covenant. As of April 30, 2009, we had no outstanding borrowings under this credit facility and were in compliance with all covenants.

Table of Contents

Other

Our cash equivalent and short-term investment portfolio as of April 30, 2009, consists of investment grade municipal bonds, tax-exempt money market mutual funds and taxable money market mutual funds. We follow an established investment policy and set of guidelines to monitor, manage and limit our exposure to interest rate and credit risk. The policy sets forth credit quality standards and limits our exposure to any one issuer. As a result of current adverse financial market conditions, some financial instruments, such as structured investment vehicles, sub-prime mortgage-backed securities and collateralized debt obligations, may pose risks arising from liquidity and credit concerns. As of April 30, 2009, we had no direct holdings in these categories of investments and no exposure to these financial instruments through our indirect holdings in money market mutual funds. During the three months ended April 30, 2009, we had no impairment charge associated with our short-term investment portfolio. While we cannot predict future market conditions or market liquidity, we have taken steps, including regularly reviewing our investments and associated risk profiles, which we believe will allow us to effectively manage the risks of our investment portfolio.

As a result of the challenging conditions in the financial markets over the last several months, we have been more proactively managing our cash and cash equivalents and investments and closely monitoring our capital and stock repurchase expenditures. Additionally, we believe the overall credit quality of our portfolio is strong, with our cash equivalents and fixed income portfolio invested in securities with a weighted-average credit rating exceeding AA. The majority of our investments are priced by pricing vendors and are classified as Level 1 or Level 2 investments, as measured under SFAS 157, as these vendors either provide a quoted market price in an active market or use observable inputs. See Note 3 of the *Notes to the Unaudited Condensed Consolidated Financial Statements*.

We believe that our current cash, cash equivalents, short-term investments, cash generated from operations, and available credit under our credit facility will satisfy our business requirements for at least the next twelve months.

Effect of New Accounting Pronouncements

See Note 16 of the *Notes to Unaudited Condensed Consolidated Financial Statements*.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our exposure to market risk has not changed materially since October 31, 2008. The average yield at purchase for our short-term investment portfolio remains approximately the same as of October 31, 2008. For more information in financial market risks related to changes in interest rates and foreign currency exchange rates, reference is made to Item 7A *Quantitative and Qualitative Disclosure About Market Risk* contained in Part II of our Annual Report on Form 10-K for the fiscal year ended October 31, 2008, filed with the SEC on December 22, 2008.

ITEM 4. CONTROLS AND PROCEDURES

Edgar Filing: SYNOPSYS INC - Form 10-Q

(a) *Evaluation of Disclosure Controls and Procedures.* As of April 30, 2009 (the Evaluation Date), Synopsys carried out an evaluation under the supervision and with the participation of Synopsys management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of Synopsys disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act). There are inherent limitations to the effectiveness of any system of disclosure controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable, not absolute, assurance of achieving their control objectives. Nonetheless, our Chief Executive Officer and Chief Financial Officer have concluded that, as of April 30, 2009, (1) Synopsys disclosure controls and procedures were designed to provide reasonable assurance of achieving their objectives, and (2) Synopsys disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed in the reports Synopsys files and submits under the Exchange Act is recorded, processed, summarized and reported as and when required, and that such information is accumulated and communicated to Synopsys management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding its required disclosure.

(b) *Changes in Internal Controls Over Financial Reporting.* There were no changes in Synopsys internal control over financial reporting during the three months ended April 30, 2009, that have materially affected, or are reasonably likely to materially affect, Synopsys internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are subject to routine legal proceedings, as well as demands, claims and threatened litigation, that arise in the normal course of our business. The ultimate outcome of any litigation is uncertain and unfavorable outcomes could have a negative impact on our results of operations and financial condition. Regardless of outcome, litigation can have an adverse impact on Synopsys because of the defense costs, diversion of management resources and other factors.

ITEM 1A. RISK FACTORS

We describe our business risk factors below.

The current severe downturn and uncertainty in the global economy in general and weakness in the semiconductor and electronics industries in particular may harm our business, operating results and financial condition.

The worldwide economy is currently undergoing unprecedented turmoil amid stock market volatility, tightening of credit markets, concerns of inflation and deflation, decreased consumer confidence, reduced corporate profits and capital spending, adverse business conditions and liquidity concerns and business insolvencies. This turmoil and the uncertainty about future economic conditions could continue to negatively impact our customers, which could in turn adversely affect our business. Uncertainty about current global economic conditions could also cause volatility of our stock price. In the event that the downturn persists or worsens for any extended period of time, we may need to restructure our operations and accordingly incur restructuring costs. We cannot predict the timing, strength or duration of this severe global economic downturn or subsequent recovery.

In addition, the semiconductor and electronics industries are cyclical in nature and are currently experiencing a severe downturn. The EDA industry has been adversely affected by many factors, including the current global downturn, ongoing efforts by semiconductor and electronics companies to reduce their spending, uncertainty regarding their long-term growth rate and underlying financial health, excess EDA tool capacity and increased competition. These factors could, among other things, limit our ability to maintain or increase our sales or recognize revenue from committed contracts and in turn adversely affect our business, operating results and financial condition.

If the general economy and the semiconductor and electronics industries do not improve, our business, financial condition and results of operations could be harmed.

Edgar Filing: SYNOPSYS INC - Form 10-Q

In the event that downward fluctuations in the semiconductor or electronics industries or general economic conditions persist or worsen for any extended period of time, our revenues and financial results will be adversely affected.

Our business model allows a substantial majority of our customers to pay for licenses over a period of time and generates recurring revenue for us over a period of time, generally three years. Pursuant to our business model, we generally target achieving greater than 90% of our total revenue as recurring revenue.

Short-term fluctuations in industry or general economic conditions or in orders generally do not immediately affect our financial results due to our business model. While the electronics, semiconductor and EDA industries are currently experiencing severe uncertainty and weakness due to the recent downturn in the global economy, to date, our business model has substantially protected our financial results. Nevertheless, our business model and longer-term financial results are not immune from sustained economic downturns. The turmoil and uncertainty caused by current economic conditions have caused some of our customers to postpone their decision-making, decrease their spending and/or delay their payments to us. We experienced a slight decrease in the committed average annual revenue from customers that renewed their contracts with us during the second quarter of fiscal 2009 and we currently expect such committed average annual revenue to also be down slightly at the end of fiscal 2009 compared to the end of fiscal 2008. Continued periods of decreased committed average annual revenue, additional customer bankruptcies, or consolidation among our customers, could adversely affect our year-over-year revenue growth and could decrease our backlog.

Accordingly, if the current economic conditions persist or worsen for any extended period of time, our future revenues and financial results would be adversely affected. Conversely, in the event of future upward fluctuations in conditions, the positive impact on our revenues and financial results may not be immediate.

Customer payment defaults or related issues could harm our operating results.

The majority of our backlog consists of customer payment obligations not yet due that are attributable to software we have already delivered. A significant portion of revenue we recognize in any period comes from backlog and is dependent upon our receipt of cash. Although customer payment obligations are not cancelable, we will not achieve expected revenue and cash flow if customers default, declare bankruptcy, or otherwise fail to pay amounts owed. Moreover, existing customers may seek to renegotiate pre-existing contractual commitments due to adverse changes in their own businesses. If the current economic downturn is prolonged, our

Table of Contents

customers' financial condition and in turn their ability or willingness to fulfill their contractual and financial obligations could be adversely affected. If payment defaults by our customers significantly increase or we experience significant reductions in existing contractual commitments, our operating results would be harmed.

If we do not successfully compete in the EDA industry our business and financial condition will be harmed.

We compete with EDA vendors that offer varying ranges of products and services, primarily Cadence Design Systems, Inc., Mentor Graphics Corporation and Magma Design Automation, Inc. We also compete with other EDA vendors, including continual new entrants to the marketplace, that offer products focused on one or more discrete phases of the IC design process, as well as with customers' internally developed design tools and capabilities. We compete principally on technology leadership, product quality and features (including ease-of-use), license terms, post contract customer support, interoperability with our own and other vendors' products, price and payment terms. Specifically, we believe the following competitive factors affect our success:

- Technology in the EDA industry evolves rapidly and in order to be successful we must maintain technology leadership. Accordingly, we must successfully anticipate and lead critical developments, innovate rapidly and efficiently, improve our existing products, and successfully develop or acquire new products.
- We believe that in order to be successful we must offer products that provide both a high level of integration into a comprehensive platform and a high level of individual product performance. We have invested significant resources into the development of our Galaxy Design Platform, integration of our Discovery Verification Platform and enhancement of our SystemVerilog and other advanced features and development of our Manufacturing Solutions and our IP and systems portfolios. Customers may not find these tool and IP configurations more attractive than our competitors' offerings and our efforts to balance the interests of integration versus individual product performance may not be successful.
- Some EDA vendors are increasingly offering discounts, which could be significant, as price continues to be a competitive consideration for our customers. If we do not match or are unable to match a competitor's pricing for a particular solution or if we are unable to otherwise enhance the value of our offering, we may lose business, which would result in lost revenue and could harm our operating results, particularly if the customer chooses to consolidate all or a substantial portion of their other EDA purchases with the competitor.
- We believe that in order to compete effectively, we need to enhance the value of our offering by providing additional rights such as multiple copies of the tools, post-contract customer support, expanded license usage related to duration, location and quantity, contractor and site access, future purchase rights and the ability to purchase pools of technology. If we do not match or are unable to match a competitor's offering, we may lose business, which would result in lost revenue and could harm our operating results.
- Payment terms are aggressively negotiated by our customers and affect our competitive position. Payment terms on time-based licenses have generally lengthened over time. Longer payment terms could continue in the future, which could negatively affect our future revenue and operating cash flow.

- The EDA industry is subject to continual consolidation. We and our competitors have historically acquired businesses and technologies to complement and expand our respective product offerings. If any of our competitors consolidate or acquire businesses and technologies which we do not offer, they may be able to exert even greater competitive pressure by offering a more complete or larger technology portfolio, a larger support and service capability, or lower prices.

- Despite the complexity of the EDA market, entry and expansion into the EDA market by new and existing companies can and does occur, and could make it more difficult to compete successfully.

In addition, new competitive factors may emerge from time to time. If we fail to successfully compete as described above or fail to address new competitive forces, our business will be harmed.

Lack of growth in new IC design starts, industry consolidation and other potentially long-term trends may adversely affect the EDA industry, including demand for our products and services.

The increasing complexities of SoCs and ICs, and customers' concerns about managing costs and risks have also led to the following potentially long-term negative trends in our industry:

- The number of IC design starts has decreased and we expect it to continue to decline. New IC design starts are one of the key drivers of demand for EDA software.

Table of Contents

- A number of mergers in the semiconductor and electronics industries have occurred and more are likely. Mergers can reduce the aggregate level of purchases of EDA software and services, and in some cases, increase customers' bargaining power in negotiations with their suppliers, including Synopsys.
- Due to factors such as increased globalization, cost controls among customers appear to have become more permanent, adversely impacting our customers' EDA spending.
- Industry changes, plus the cost and complexity of IC design, may be leading some companies in these industries to limit their design activity in general, to focus only on one discrete phase of the design process while outsourcing other aspects of the design to companies using our competitors' products.

All of these trends, if sustained, could harm the EDA industry, including the demand for our products and services, which in turn would harm our financial condition and results of operations.

Changes in, or interpretations of, accounting principles could result in unfavorable accounting charges or effects, including changes to our prior financial statements, which could cause our stock price to decline.

We prepare our consolidated financial statements in conformity with U.S. generally accepted accounting principles. These principles are subject to interpretation by the SEC and various bodies formed to interpret and create appropriate accounting principles. A change in these principles, or in our interpretations of these principles, can have a significant effect on our reported results and may retroactively affect previously reported results.

We have received a Revenue Agent's Report from the Internal Revenue Service claiming a significant increase in our U.S. taxable income. An adverse outcome could have an adverse effect on our results of operations and financial condition.

On July 11, 2008, we received a Revenue Agent's Report in which the Internal Revenue Service, or IRS, proposed an adjustment that would result in an aggregate tax deficiency for fiscal 2002 through 2004 of approximately \$236.2 million, \$130.5 million of which would be a reduction of certain tax credits that would otherwise be available either as refund claims or to offset taxes due in future periods. In August 2008, we timely filed a protest to the proposed deficiency with the IRS. In the second quarter of fiscal 2009, we reached a tentative settlement with the Examination Division of the IRS that would resolve this matter. The settlement is subject to further review and approval within the federal government, including the Joint Committee on Taxation of the U.S. Congress (Joint Committee), which could take at least several more months. Final resolution of this matter could take considerable time and may not be finally approved by the government, therefore there is still a possibility that an adverse outcome of this matter could result in significant tax expense and harm our results of operations and financial condition.

Edgar Filing: SYNOPSYS INC - Form 10-Q

Unfavorable tax law changes, an unfavorable government review of our tax returns or changes in our geographical earnings mix or forecasts of foreign source income could adversely affect our effective tax rate and our operating results.

Our operations are subject to income and transaction taxes in the United States and in multiple foreign jurisdictions. A change in the tax law in the jurisdictions in which we do business, including an increase in tax rates or an adverse change in the treatment of an item of income or expense, could result in a material increase in our tax expense. Currently, a substantial portion of our revenue is generated from customers located outside the United States, and a substantial portion of our assets, including employees, are located outside the United States. United States income taxes and foreign withholding taxes have not been provided on undistributed earnings for certain non-United States subsidiaries, because such earnings are intended to be indefinitely reinvested in the operations of those subsidiaries. On May 5, 2009, the President of the United States and the U.S. Treasury Department proposed changing certain of the U.S. tax rules for U.S. corporations doing business outside the United States. Specific legislation has not yet been proposed or enacted, but it is possible that these or other changes in the U.S. tax laws could increase our U.S. income tax liability in the future.

Our tax filings are subject to review or audit by the IRS and state, local and foreign taxing authorities. We exercise judgment in determining our worldwide provision for income taxes and, in the ordinary course of our business, there may be transactions and calculations where the ultimate tax determination is uncertain. The IRS examinations of our federal tax returns for the years 2000-2001 and 2002-2004 resulted in significant proposed adjustments. Although we believe our tax estimates are reasonable, we can provide no assurance that any final determination in an audit will not be materially different than the treatment reflected in our historical income tax provisions and accruals. An assessment of additional taxes as a result of an audit could adversely affect our income tax provision and net income in the period or periods for which that determination is made.

We have operations both in the United States and in multiple foreign jurisdictions with a wide range of statutory tax rates. Certain foreign operations are subject to temporary favorable foreign tax rates. Therefore, any changes in our geographical earning mix in various tax jurisdictions, including those resulting from transfer pricing adjustments and expiration of or amendments to foreign tax rulings, could materially increase our effective tax rate. Furthermore, we maintain deferred tax assets related to federal

Table of Contents

foreign tax credits and our ability to use these credits is dependent upon having sufficient future foreign source income in the United States. Changes in our forecasts of such future foreign source income could result in an adjustment to the deferred tax asset and a related charge to earnings which could materially affect our financial results.

Our revenue and earnings fluctuate and if our financial results fail to meet stockholder expectations our stock price could decline.

Many factors affect our revenue and earnings, including customer demand, license mix, the timing of revenue recognition on products and services sold, causing our revenue and earnings results to fluctuate. Accordingly, stockholders should not view our historical results as necessarily indicative of our future performance.

From time to time, we provide targets related to our future financial performance. In addition, financial analysts publish their own expectations of our future financial performance. Because our quarterly revenue and our operating results fluctuate, future financial performance is difficult to predict. Downward adjustments of our targets or the failure to meet our targets or the expectations of research analysts could cause the market price of our common stock to decline.

Some of the specific factors that could affect our revenue and earnings in a particular quarter or over several fiscal periods include, but are not limited to:

- The market for EDA products is dynamic and depends on a number of factors including consumer demand for our customers products, customer research and development and EDA budgets, pricing, our competitors' product offerings and customer design starts. It is difficult to predict in advance the effect of these and other factors on our customers' demand for our products on a medium or long term basis. As a result, actual future customer purchases could differ materially from our forecasts which, in turn, could cause our actual revenue to be materially different than our publicly disclosed targets.
- We base our operating expenses in part on our expectations for future revenue and generally must commit to expense levels in advance of revenue being recognized. Since only a small portion of our expenses varies with revenue, any revenue shortfall typically causes a direct reduction in net income.
- Our revenue and earnings targets over a number of fiscal periods assume a certain level of orders and a certain mix between upfront and time-based license revenue. The amount of orders received and changes in the mix due to factors such as the level of overall license orders, customer demand, customer payment terms and ship dates could result in lower revenue and harm our operating results. For example, if we ship more licenses generating upfront revenue than expected during any given fiscal period, our revenue and earnings for that period could be above our targets even if orders are below target; conversely, if we ship fewer licenses generating upfront revenue than expected, our revenue and earnings for that period could fall below our targets even if orders meet or even exceed our target. Similarly, if we receive a lower-than-expected level of license orders generating time-based revenue during a given period, our revenue in future periods could be negatively affected.

Edgar Filing: SYNOPSYS INC - Form 10-Q

- We may be required to implement a number of cost control measures in order to meet our externally-communicated financial targets, any of which could fail to result in the anticipated cost savings or could harm our business.
- We often amend our contracts with our customers to extend the term or add new products. Although these amendments can provide a longer-term payment stream from the customers, they can also result in a lower amount of revenue being recognized per year than under the original arrangement even if the total value of the extended contract is larger.
- Certain of our license agreements provide customers the right to re-mix a portion of the software initially subject to the license for other specified Synopsys products. While this practice helps assure the customer's access to the complete design flow needed to manufacture its product, use of these arrangements could result in reduced revenue compared to licensing the individual tools separately.
- In the past, we have regularly received a significant portion of our orders for a given quarter in the last one or two weeks of the quarter. The delay of one or more orders, particularly an order generating upfront revenue, could cause us to have lower revenue and/or earnings for that quarter.
- A large portion of our revenue is derived from a relatively small number of large customers. While our agreements with such customers are binding multi-year agreements, if we were to lose these customers or if they did not renew their agreements with us, over time our financial results could be adversely affected.
- We make significant judgments relating to revenue recognition, specifically determining the existence of proper documentation, establishing that the fee is fixed or determinable, verifying delivery of our products and services and assessing the creditworthiness of our customers. While we believe our judgments in these areas are reasonable, there can

Table of Contents

be no assurance that such judgments will not be challenged in the future. In such an event, we could be required to reduce the amount of revenue we have recognized in prior periods, which would have an adverse impact on our reported results of operations for those periods.

- Our customers spend a great deal of time reviewing and testing our products, either alone or against competing products, before making a purchase decision. Accordingly, our customers' evaluation and purchase cycles may not match our fiscal quarters. Further, sales of our products and services may be delayed if customers delay project approvals or starts because of budgetary constraints or their budget cycles.
- The sales cycle for our products is lengthy. The purchase of our products generally involves a significant commitment of capital and other resources by a customer. This commitment often requires significant technical review, assessment of competitive products and approval at a number of management levels within a customer's organization. While our customers are evaluating our products and services, we may incur substantial sales and marketing expenses and spend significant management effort to complete these sales. Any delay in completing sales in a particular quarter or the failure to complete a sale after expending resources during the sales cycle could cause our operating results to suffer.
- We rely on third party subcontractors to manufacture our hardware products. Our reliance on third parties subjects us to risks such as reduced control over delivery schedules and quality, a potential lack of adequate capacity during periods when demand is high and potential increases in product costs due to factors outside our control such as capacity shortages, pricing changes and the third parties' financial viability. Our outsourcing model could lead to delays in product deliveries, lost sales and increased costs which could harm our relationships with our customers resulting in lower operating results.

The failure to meet the semiconductor industry's demands for advancing EDA technology and continued cost reductions may harm our financial results.

SoC and IC functionality continues to increase while feature widths decrease, substantially increasing the complexity, cost and risk of IC design and manufacturing. To address greater complexity, semiconductor designers and manufacturers demand continuous innovation from EDA suppliers. At the same time, as a general business trend, we believe some customers and potential customers are seeking to buy more products from fewer suppliers and at reduced overall prices in an effort to reduce overall cost and risk. In order to succeed in this environment, we must successfully meet our customers' technology requirements and increase the value of our products, while also striving to reduce their overall costs and our own operating costs. If we fail to successfully manage these conflicting demands our financial condition and results of operations will be harmed.

We may have to invest more resources in research and development than anticipated, which could increase our operating expenses and negatively affect our operating results.

If new competitors, technological advances by existing competitors, our entry into new markets, or other competitive factors require us to invest significantly greater resources than anticipated in our research and development efforts, our operating expenses would increase. If we are required to invest significantly greater resources than anticipated in research and development efforts without a corresponding increase in revenue, our operating results could decline. Research and development expenses are likely to fluctuate from time to time to the extent we make periodic incremental investments in research and development and these investments may be independent of our level of revenue which could negatively impact our financial results. In order to remain competitive, we anticipate that we will continue to devote substantial resources to

research and development.

We may not be able to acquire businesses or technology and we may not be able to realize the potential financial or strategic benefits of the business acquisitions or strategic investments we complete, which could hurt our ability to grow our business, develop new products or sell our products.

We have acquired a number of companies or their assets in the past and expect to make additional acquisitions of businesses or technology in the future. We may not find suitable acquisition targets or we may not be able to consummate desired acquisitions due to unfavorable credit markets or other risks, which could harm our operating results. We have acquired a number of companies and technologies in recent years, including Synplicity, Inc. in May 2008. In addition to direct costs, acquisitions pose a number of risks, including:

- Potential negative impact on our earnings per share;
- Failure of acquired products to achieve projected sales;
- Problems in integrating the acquired products with our products;

Table of Contents

- Difficulties in retaining key employees and integrating them into Synopsys;
- Failure to realize expected synergies or cost savings;
- Regulatory delays;
- Drain on management time for acquisition-related activities;
- Assumption of unknown liabilities, including tax, and unanticipated costs;
- Diversion of resources and unanticipated expenses resulting from litigation arising from potential or actual business acquisitions or investments;
- Adverse effects on customer buying patterns or relationships; and
- Negative impact on our earnings resulting from the application of SFAS No. 141 (revised 2007), Business Combinations (SFAS 141R), which requirements are effective for fiscal years beginning on or after December 15, 2008 and will apply to our acquisitions beginning in the first quarter of our fiscal 2010.

While we review proposed acquisitions carefully and strive to negotiate terms that are favorable to us, an acquisition may not positively affect our future performance. If we later determine we cannot use or sell an acquired product or technology, we will be required to write down intangible assets associated with the product or technology which would harm our operating results.

Conditions of foreign economies, foreign exchange rate fluctuations and the increasingly global nature of our operations could adversely affect our performance.

We generally derive approximately 50% of our revenue from outside the United States. We expect our overall orders and revenue targets will continue to depend on substantial contributions from customers outside the United States. Foreign sales are vulnerable to regional or worldwide economic, political and health conditions, including the effects of international political conflict, hostilities and natural disasters. Further, any deterioration of foreign economies or foreign currency exchange rates would adversely affect our performance by reducing the amount of

revenue derived from outside the United States.

Our operating results are also affected by fluctuations in foreign currency exchange rates. Our results of operations can be adversely affected when the U.S. dollar weakens relative to other currencies, including the Euro, the Japanese yen and the Canadian dollar, as a result of the translation of expenses of our foreign operations denominated in foreign currencies into the dollar. Exchange rates are subject to significant and rapid fluctuations, and therefore we cannot predict the prospective impact of exchange rate fluctuations on our business, results of operations and financial condition. While we hedge most foreign currency exposures of our business, we are unable to hedge all of our currency exposures, and our hedging activities may not completely mitigate our foreign currency risks.

In addition, we have expanded our non-U.S. operations significantly in the past several years. While the increased international presence of our business creates the potential for cost reductions and higher international sales, this strategy also requires us to recruit and retain qualified technical and managerial employees, manage multiple, remote locations performing complex software development projects and ensure intellectual property protection outside of the United States. If we fail to effectively manage our global operations our business and results of operations will be harmed.

Our operations and sales to customers internationally subject us to a number of additional risks, including:

- international economic and political conditions, such as political tensions between countries in which we do business;
- unexpected changes in, or impositions of, legislative or regulatory requirements;
- difficulties in complying with a variety of foreign laws and regulatory requirements;
- differing legal standards with respect to protection of intellectual property and employment practices;
- difficulties in adapting to cultural differences in the conduct of business;
- inadequate local infrastructure that could result in business disruptions;

Table of Contents

- exporting or importing issues related to export or import restrictions, tariffs, quotas and other trade barriers and restrictions;
- financial risks such as longer payment cycles, difficulty in collecting accounts receivable and fluctuations in currency exchange rates;
- imposition of additional taxes and penalties; and
- other factors beyond our control such as terrorism, civil unrest, war and infectious diseases.

Our investment portfolio may be impaired by further deterioration of the capital markets.

Our cash equivalent and short-term investment portfolio as of April 30, 2009 consists of investment grade municipal bonds, tax-exempt money market mutual funds and taxable money market mutual funds. We follow an established investment policy and set of guidelines to monitor, manage and limit our exposure to interest rate and credit risk. The policy sets forth credit quality standards and limits our exposure to any one issuer. As a result of current adverse financial market conditions, some financial instruments, such as structured investment vehicles, sub-prime mortgage-backed securities and collateralized debt obligations, may pose risks arising from liquidity and credit concerns. As of April 30, 2009, we had no direct holdings in these categories of investments and no exposure to these financial instruments through our indirect holdings in money market mutual funds. As of April 30, 2009, we had no impairment charge associated with our short-term investment portfolio. However, we cannot predict future market conditions or market liquidity and our investment portfolio may suffer other than temporary impairments in future periods.

We account for our investment instruments in accordance with Statement of Financial Accounting Standards No. 115 *Accounting for Certain Investments in Debt and Equity Securities* (SFAS 115). All of our cash equivalents and marketable securities are treated as available-for-sale under SFAS 115. Investments in both fixed rate and floating rate interest earning instruments carry a degree of interest rate risk. Fixed rate debt securities may have their market value adversely impacted due to a rise in interest rates, while floating rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may fall short of expectations due to changes in interest rates or if the decline in fair value of our publicly traded debt or equity investments is judged to be other-than-temporary. We may suffer losses in principal if we are forced to sell securities that decline in market value due to changes in interest rates. However, because any debt securities we hold are classified as available-for-sale, no gains or losses are realized in our consolidated statements of income due to changes in interest rates unless such securities are sold prior to maturity or unless declines in value are determined to be other-than-temporary. These securities are reported at fair value with the related unrealized gains and losses included in accumulated other comprehensive income, a component of stockholders' equity, net of tax.

The current global financial crisis may cause our banking partners to become insolvent.

We rely on several large financial institutions to act as counterparties under our foreign currency forward contracts, provide credit under our revolving credit facility and provide banking transaction and deposit services worldwide. Should any of our banking partners declare

bankruptcy or otherwise default under our agreements, it could have a material impact on our financial results and reduce our credit availability.

From time to time we are subject to claims that our products infringe on third party intellectual property rights.

Under our customer agreements and other license agreements, we agree in many cases to indemnify our customers if our products infringe a third party's intellectual property rights. As a result, we are from time to time subject to claims that our products infringe on these third party rights. We are currently defending some of our customers against claims that their use of one of our products infringes on a patent held by a Japanese electronics company. We believe this claim is without merit and will continue to vigorously defend against it.

These types of claims can, however, result in costly and time-consuming litigation, require us to enter into royalty arrangements, subject us to damages or injunctions restricting our sale of products, invalidate a patent or family of patents, require us to refund license fees to our customers or to forgo future payments or require us to redesign certain of our products, any one of which could harm our business and operating results.

If we fail to protect our proprietary technology our business will be harmed.

Our success depends in part upon protecting our proprietary technology. We rely on agreements with customers, employees and others and on intellectual property laws worldwide to protect our proprietary technology. These agreements may be breached, and we may not have adequate remedies for any breach and our trade secrets may otherwise become known or be independently developed by competitors. Moreover, some foreign countries do not currently provide effective legal protection for intellectual property and our

Table of Contents

ability to prevent the unauthorized use of our products in those countries is therefore limited. We aggressively pursue action against companies or individuals that wrongfully appropriate or use our products and technologies. We engaged in anti-piracy efforts against certain companies located in China; but these actions may not be successful. We may need to commence litigation or other legal proceedings in order to:

- assert claims of infringement of our intellectual property;
- protect our trade secrets or know-how; or
- determine the enforceability, scope and validity of the propriety rights of others.

If we do not obtain or maintain appropriate patent, copyright or trade secret protection, for any reason, or cannot fully defend our intellectual property rights in some jurisdictions, our business and operating results would be harmed. In addition, intellectual property litigation is lengthy, expensive and uncertain and legal fees related to such litigation will increase our operating expenses and may reduce our net income.

Our business is subject to evolving corporate governance and public disclosure regulations that have increased both our costs and the risk of noncompliance, which could have an adverse effect on our stock price.

We are subject to rules and regulations promulgated by a number of governmental and self-regulated organizations, including the SEC, NASDAQ and the Public Company Accounting Oversight Board. Many of these regulations continue to evolve, making compliance more difficult and uncertain. In addition, our efforts to comply with these new regulations have resulted in, and are likely to continue to result in, increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities.

In particular, Section 404 of Sarbanes-Oxley Act of 2002 and related regulations require us to include a management assessment of our internal control over financial reporting and our auditors to render an opinion as to the effectiveness of our internal control over financial reporting in our annual reports. This effort has required, and will continue to require in the future, the commitment of significant financial and managerial resources. Any failure to complete a favorable assessment and obtain an unqualified opinion from our independent registered public accounting firm could cause our stock price to decline.

There are inherent limitations on the effectiveness of our controls.

We do not expect that our disclosure controls or control system will prevent all error and all fraud. Regardless of how well designed and operated it is, a control system can provide only reasonable assurance that its objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints and the benefits of controls must be considered relative to their costs. Because of the inherent

limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected. Failure of our control systems to prevent error or fraud could materially adversely impact us.

If we fail to timely recruit and retain key employees our business may be harmed.

To be successful, we must attract and retain key technical, sales and managerial employees, including those who join Synopsys in connection with acquisitions. There are a limited number of qualified EDA and IC design engineers, and competition for these individuals is intense. Our employees are often recruited aggressively by our competitors and our customers. Any failure to recruit and retain key technical, sales and managerial employees would harm our business, results of operations and financial condition.

We issue stock options and restricted stock units and maintain employee stock purchase plans as a key component of our overall compensation. We face pressure from stockholders, who must approve any increases in our equity pool, to limit the use of such equity based compensation and its dilutive effect on stockholders. In addition, we are required under U.S. GAAP to recognize compensation expense in our results from operations for employee share-based equity compensation under our equity grants and our employee stock purchase plan which has increased the pressure to limit share-based compensation. These factors may make it more difficult for us to grant attractive share-based packages in the future, which could adversely impact and limit our ability to attract and retain key employees.

Product errors or defects could expose us to liability and harm reputation and we could lose market share.

Despite extensive testing prior to releasing our products, software products frequently contain errors or defects, especially when first introduced, when new versions are released or when integrated with technologies developed by acquired companies. Product errors could affect the performance or interoperability of our products, could delay the development or release of new

Table of Contents

products or new versions of products and could adversely affect market acceptance or perception of our products. In addition, allegations of IC manufacturability issues resulting from use of our IP products could, even if untrue, adversely affect our reputation and our customers willingness to license IP products from us. Any such errors or delays in releasing new products or new versions of products or allegations of unsatisfactory performance could cause us to lose customers, increase our service costs, subject us to liability for damages and divert our resources from other tasks, any one of which could materially and adversely affect our business and operating results.

Catastrophic events may disrupt our business and harm our operating results.

We rely on our network infrastructure and enterprise applications, and technology systems for our development, marketing, operational, support and sales activities. A disruption or failure of these systems in the event of a major earthquake, fire, telecommunications failure, cyber-attack, terrorist attack, or other catastrophic event could cause system interruptions, delays in our product development and loss of critical data and could prevent us from fulfilling our customers' orders. Our corporate headquarters, a significant portion of our research and development activities, our data centers, and certain other critical business operations are located in California, near major earthquake faults. We believe we have developed sufficient disaster recovery plans and backup systems to reduce the potentially adverse effect of such events, but a catastrophic event that results in the destruction or disruption of any of our data centers or our critical business or information technology systems would severely affect our ability to conduct normal business operations and, as a result, our operating results would be adversely affected.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Synopsys' Board of Directors approved a \$500 million stock repurchase program on December 1, 2004, which was replenished to \$500 million on March 22, 2007. Funds are available until expended or until the program is suspended by the Chief Financial Officer or the Board of Directors. Synopsys did not repurchase any shares of common stock under the program during the three months ended April 30, 2009 and, as of such date, an aggregate of approximately \$209.7 million remained authorized for future purchases.

See Note 9 of *Notes to Unaudited Condensed Consolidated Financial Statements* for further information regarding our stock repurchase program.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Edgar Filing: SYNOPSYS INC - Form 10-Q

We held our Annual Meeting of Stockholders at our offices located in Mountain View, California on February 27, 2009. Three matters were submitted to, and approved by, stockholders, as set forth below.

1. The stockholders elected nine directors to our Board of Directors, to hold office for a one-year term and until their successors are elected. The votes regarding this matter were as follows:

	Total Votes For Each Director	Total Votes Withheld From Each Director
Aart J. de Geus	128,916,671	2,207,253
Chi-Foon Chan	129,256,155	1,867,769
Alfred Castino	130,033,448	1,090,476
Bruce R. Chizen	128,603,642	2,520,282
Deborah A. Coleman	129,329,184	1,794,740
John Schwarz	128,604,915	2,519,009
Sasson Somekh	129,441,984	1,681,940
Roy Vallee	128,341,366	2,782,558
Steven C. Walske	127,908,663	3,215,261

2. The stockholders approved an amendment to our 2006 Employee Equity Incentive Plan to, among other items, increase the number of shares of common stock reserved thereunder by 4,000,000 shares. The votes regarding this matter were as follows:

For	Against	Abstain	Broker Non-Votes
86,708,860	26,410,520	38,221	17,966,323

Table of Contents

3. The stockholders ratified the appointment of KPMG LLP as our independent registered public accounting firm for the fiscal year ending October 31, 2009. The votes regarding this matter were as follows:

For	Against	Abstain	Broker Non-Votes
129,918,281	1,169,615	36,027	0

ITEM 5. OTHER INFORMATION

Not applicable.

ITEM 6. EXHIBITS

Exhibit Number	Exhibit Description	Form	Incorporated By Reference		Filing Date	Filed Herewith
			File No.	Exhibit		
3.1	Amended and Restated Certificate of Incorporation	10-Q	000-19807	3.1	09/15/03	
3.2	Restated Bylaws	8-K	000-19807	3.2	06/03/09	
4.1	Specimen Common Stock Certificate	S-1	33-45138	4.3	02/24/92 (effective date)	
10.35*	2006 Employee Equity Incentive Plan	DEF 14A	000-19807	Appendix A	01/13/09	
31.1	Certification of Principal Executive Officer furnished pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Exchange Act					X
31.2	Certification of Principal Financial Officer furnished pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Exchange Act					X
32.1	Certification of Principal Executive Officer and Principal Financial Officer furnished pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Exchange Act and Section 1350 of Chapter 63 of Title 18 of the United States Code					X

* Indicates a management contract, compensatory plan or arrangement.

[Table of Contents](#)

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.

SYNOPSYS, INC.

Date: June 9, 2009

By: /s/ Brian M. Beattie
Brian M. Beattie
Chief Financial Officer
(Principal Financial Officer)

Table of Contents**EXHIBIT INDEX**

Exhibit Number	Exhibit Description	Form	Incorporated By Reference		Filing Date	Filed Herewith
			File No.	Exhibit		
3.1	Amended and Restated Certificate of Incorporation	10-Q	000-19807	3.1	09/15/03	
3.2	Restated Bylaws	8-K	000-19807	3.2	06/03/09	
4.1	Specimen Common Stock Certificate	S-1	33-45138	4.3	02/24/92 (effective date)	
10.35*	2006 Employee Equity Incentive Plan	DEF 14A	000-19807	Appendix A	01/13/09	
31.1	Certification of Principal Executive Officer furnished pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Exchange Act					X
31.2	Certification of Principal Financial Officer furnished pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Exchange Act					X
32.1	Certification of Principal Executive Officer and Principal Financial Officer furnished pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Exchange Act and Section 1350 of Chapter 63 of Title 18 of the United States Code					X

* Indicates a management contract, compensatory plan or arrangement.