

ASPEN TECHNOLOGY INC /DE/  
Form 10-Q  
October 26, 2017  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2017

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 001-34630

ASPEN TECHNOLOGY, INC.

(Exact name of registrant as specified in its charter)

Delaware 04-2739697

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

20 Crosby Drive

Bedford, Massachusetts 01730

(Address of principal executive offices) (Zip Code)

(781) 221-6400

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

filer  (Do not check if

a smaller reporting  
company)

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act): Yes o No   
As of October 19, 2017, there were 72,535,428 shares of the registrant's common stock (par value \$0.10 per share) outstanding.

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

Our fiscal year ends on June 30<sup>th</sup>, and references to a specific fiscal year are to the twelve months ended June 30<sup>th</sup> of such year (for example, "fiscal 2018" refers to the year ending June 30, 2018).

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## PART I - FINANCIAL INFORMATION

## Item 1. Financial Statements.

## Consolidated Financial Statements (unaudited)

ASPEN TECHNOLOGY, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS  
(Unaudited)

|  | Three Months Ended |            |
|--|--------------------|------------|
|  | September 30,      |            |
|  | 2017               | 2016       |
|  | (Dollars in        |            |
|  | Thousands, Except  |            |
|  | per Share Data)    |            |
| Revenue:                                 |                    |            |
| Subscription and software                | \$ 115,756         | \$ 113,444 |
| Services and other                       | 7,025              | 6,606      |
| Total revenue                            | 122,781            | 120,050    |
| Cost of revenue:                         |                    |            |
| Subscription and software                | 5,783              | 5,069      |
| Services and other                       | 6,949              | 6,437      |
| Total cost of revenue                    | 12,732             | 11,506     |
| Gross profit                             | 110,049            | 108,544    |
| Operating expenses:                      |                    |            |
| Selling and marketing                    | 23,571             | 22,025     |
| Research and development                 | 19,489             | 18,632     |
| General and administrative               | 13,676             | 13,157     |
| Total operating expenses                 | 56,736             | 53,814     |
| Income from operations                   | 53,313             | 54,730     |
| Interest income                          | 141                | 272        |
| Interest (expense)                       | (1,206 )           | (869 )     |
| Other (expense) income, net              | (616 )             | 646        |
| Income before provision for income taxes | 51,632             | 54,779     |
| Provision for income taxes               | 16,877             | 19,779     |
| Net income                               | \$34,755           | \$35,000   |
| Net income per common share:             |                    |            |
| Basic                                    | \$0.48             | \$0.44     |
| Diluted                                  | \$0.47             | \$0.44     |
| Weighted average shares outstanding:     |                    |            |
| Basic                                    | 73,024             | 79,048     |
| Diluted                                  | 73,609             | 79,385     |

See accompanying Notes to these unaudited consolidated financial statements.

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

|  | Three Months Ended<br>September 30, |           |
|--|-------------------------------------|-----------|
|  | 2017                                | 2016      |
|  | (Dollars in Thousands)              |           |
| Net income   | \$ 34,755                           | \$ 35,000 |
| Other comprehensive income (loss):   |                                     |           |
| Net unrealized losses on available for sale securities, net of tax effects of \$15 for the three months ended September 30, 2016 | —                                   | (26 )     |
| Foreign currency translation adjustments   | 1,401                               | (904 )    |
| Total other comprehensive income (loss)  | 1,401                               | (930 )    |
| Comprehensive income   | \$ 36,156                           | \$ 34,070 |

See accompanying Notes to these unaudited consolidated financial statements.

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ASPEN TECHNOLOGY, INC. AND SUBSIDIARIES  
 CONSOLIDATED BALANCE SHEETS  
 (Unaudited)

|  | September 30,<br>2017                           | June 30,<br>2017 |
|--|---|------------------|
|  | (Dollars in<br>Thousands, Except<br>Share Data) |                  |
| <b>ASSETS</b>  |   |                  |
| Current assets:  |   |                  |
| Cash and cash equivalents  | \$58,983  | \$101,954        |
| Accounts receivable, net   | 28,284  | 27,670           |
| Prepaid expenses and other current assets  | 11,336  | 12,061           |
| Prepaid income taxes   | 3,334   | 4,501            |
| Total current assets   | 101,937   | 146,186          |
| Property, equipment and leasehold improvements, net  | 12,360  | 13,400           |
| Computer software development costs, net   | 706   | 667              |
| Goodwill   | 51,738  | 51,248           |
| Intangible assets, net   | 20,263  | 20,789           |
| Non-current deferred tax assets  | 14,404  | 14,352           |
| Other non-current assets   | 1,315   | 1,300            |
| Total assets   | \$202,723                                       | \$247,942        |
| <b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>   |   |                  |
| Current liabilities:   |   |                  |
| Accounts payable   | \$3,522   | \$5,467          |
| Accrued expenses and other current liabilities   | 36,761  | 48,149           |
| Income taxes payable   | 15,913  | 1,603            |
| Borrowings under credit agreement  | 140,000   | 140,000          |
| Current deferred revenue   | 233,476   | 272,024          |
| Total current liabilities  | 429,672   | 467,243          |
| Non-current deferred revenue   | 26,754  | 28,335           |
| Other non-current liabilities  | 13,754  | 13,148           |
| Commitments and contingencies (Note 15)  |   |                  |
| Series D redeemable convertible preferred stock, \$0.10 par value—   |   |                  |
| Authorized— 3,636 shares as of September 30, 2017 and June 30, 2017  | —   | —                |
| Issued and outstanding— none as of September 30, 2017 and June 30, 2017  |   |                  |
| Stockholders' deficit:   |   |                  |
| Common stock, \$0.10 par value— Authorized—210,000,000 shares  |   |                  |
| Issued— 102,692,094 shares at September 30, 2017 and 102,567,129 shares at June 30, 2017                               | 10,269  | 10,257           |
| Outstanding— 72,706,959 shares at September 30, 2017 and 73,421,153 shares at June 30, 2017                            |   |                  |
| Additional paid-in capital   | 694,638   | 687,479          |
| Retained earnings  | 191,275   | 156,520          |
| Accumulated other comprehensive income   | 2,860   | 1,459            |
| Treasury stock, at cost—29,985,135 shares of common stock at September 30, 2017 and 29,145,976 shares at June 30, 2017 | (1,166,499)                                     | (1,116,499)      |
| Total stockholders' deficit  | (267,457)                                       | (260,784)        |
| Total liabilities and stockholders' deficit  | \$202,723                                       | \$247,942        |

See accompanying Notes to these unaudited consolidated financial statements.

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ASPEN TECHNOLOGY, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited)

|   | Three Months Ended<br>September 30, |            |
|---|-------------------------------------|------------|
|   | 2017                                | 2016       |
|   | (Dollars in Thousands)              |            |
| Cash flows from operating activities:   |                                     |            |
| Net income  | \$ 34,755                           | \$ 35,000  |
| Adjustments to reconcile net income to net cash provided by operating activities:                                       |                                     |            |
| Depreciation and amortization   | 1,753                               | 1,791      |
| Net foreign currency (gains) losses   | 936                                 | (745 )     |
| Stock-based compensation  | 6,414                               | 4,958      |
| Deferred income taxes   | (33 )                               | (46 )      |
| Provision for (recovery from) bad debts   | 20                                  | (7 )       |
| Tax benefits from stock-based compensation  | —                                   | 584        |
| Excess tax benefits from stock-based compensation   | —                                   | (584 )     |
| Other non-cash operating activities   | —                                   | 90         |
| Changes in assets and liabilities:  |                                     |            |
| Accounts receivable   | (504 )                              | (1,355 )   |
| Prepaid expenses, prepaid income taxes, and other assets  | 2,292                               | 1,885      |
| Accounts payable, accrued expenses, income taxes payable and other liabilities  | 6,764                               | 12,520     |
| Deferred revenue  | (40,037 )                           | (27,841 )  |
| Net cash provided by operating activities   | 12,360                              | 26,250     |
| Cash flows from investing activities:   |                                     |            |
| Purchases of marketable securities  | —                                   | (193,748 ) |
| Maturities of marketable securities   | —                                   | 53,184     |
| Purchases of property, equipment and leasehold improvements   | (123 )                              | (898 )     |
| Payments for business acquisitions  | —                                   | (5,400 )   |
| Payments for capitalized computer software costs  | (65 )                               | (51 )      |
| Net cash used in investing activities   | (188 )                              | (146,913 ) |
| Cash flows from financing activities:   |                                     |            |
| Exercises of stock options  | 2,411                               | 3,089      |
| Repurchases of common stock   | (55,109 )                           | (151,621 ) |
| Payments of tax withholding obligations related to restricted stock   | (1,650 )                            | (1,297 )   |
| Deferred business acquisition payment   | (600 )                              | —          |
| Excess tax benefits from stock-based compensation   | —                                   | 584        |
| Payments of credit agreement issuance costs   | (351 )                              | —          |
| Net cash used in financing activities   | (55,299 )                           | (149,245 ) |
| Effect of exchange rate changes on cash and cash equivalents  | 156                                 | (51 )      |
| Decrease in cash and cash equivalents   | (42,971 )                           | (269,959 ) |
| Cash and cash equivalents, beginning of period  | 101,954                             | 318,336    |
| Cash and cash equivalents, end of period  | \$ 58,983                           | \$ 48,377  |
| Supplemental disclosure of cash flow information:   |                                     |            |
| Income taxes paid, net  | \$ 1,243                            | \$ 1,239   |
| Interest paid   | 968                                 | 850        |
| Supplemental disclosure of non-cash investing and financing activities:   |                                     |            |
| Change in purchases of property, equipment and leasehold improvements included in accounts payable and accrued expenses | \$ (70 )                            | \$ 506     |

Change in common stock repurchases included in accrued expenses (5,109 ) (1,621 )

See accompanying Notes to these unaudited consolidated financial statements.

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ASPEN TECHNOLOGY, INC. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. Interim Unaudited Consolidated Financial Statements

The accompanying interim unaudited consolidated financial statements of Aspen Technology, Inc. and its subsidiaries have been prepared on the same basis as our annual consolidated financial statements. We have omitted certain information and footnote disclosures normally included in our annual consolidated financial statements. Such interim unaudited consolidated financial statements have been prepared in conformity with U.S. Generally Accepted Accounting Principles (GAAP), as defined in the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 270, Interim Reporting, for interim financial information and with the instructions to Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. It is suggested that these unaudited consolidated financial statements be read in conjunction with the audited consolidated financial statements for the year ended June 30, 2017, which are contained in our Annual Report on Form 10-K, as previously filed with the U.S. Securities and Exchange Commission (SEC). In the opinion of management, all adjustments, consisting of normal and recurring adjustments, considered necessary for a fair presentation of the financial position, results of operations, and cash flows at the dates and for the periods presented have been included and all intercompany accounts and transactions have been eliminated in consolidation. The results of operations for the three months ended September 30, 2017 are not necessarily indicative of the results to be expected for the subsequent quarter or for the full fiscal year.

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

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

2. Significant Accounting Policies

(a) Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Aspen Technology, Inc. and our wholly owned subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

(b) Significant Accounting Policies

Our significant accounting policies are described in Note 2 to the consolidated financial statements included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2017. We adopted Accounting Standards Update (ASU) No. 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (“ASU No. 2016-09”) effective July 1, 2017. Refer to Note 2 (g), “Recently Issued Accounting Pronouncements,” for further information regarding the adoption of ASU No. 2016-09. There were no other significant changes to our significant accounting policies during the three months ended September 30, 2017.

(c) Revenue Recognition

We generate revenue from the following sources: (1) Subscription and software revenue; and (2) Services and other revenue. We sell our software products to end users primarily under fixed-term licenses. We license our software products primarily through a subscription offering which we refer to as our aspenONE licensing model, which

includes software maintenance and support, known as our Premier Plus SMS offering, for the entire term. Our aspenONE products are organized into three suites: 1) engineering; 2) manufacturing and supply chain; and 3) asset performance management. The aspenONE licensing model provides customers with access to all of the products within the aspenONE suite(s) they license. We refer to these arrangements as token arrangements. Tokens are fixed units of measure. The amount of software usage is limited by the number of tokens purchased by the customer.

We also license our software through point product term arrangements, which include our Premier Plus SMS offering for the entire term, as well as perpetual license arrangements.

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

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

Delivery of our product—Software and the corresponding access keys are generally delivered to customers via electronic delivery or via physical medium with standard shipping terms of Free Carrier, our warehouse (i.e., FCA, AspenTech). Our software license agreements do not contain conditions for acceptance.

Fee is fixed or determinable—We assess whether a fee is fixed or determinable at the outset of the arrangement.

Significant judgment is involved in making this assessment.

As a standard business practice, we offer fixed-term license arrangements, which are generally payable on an annual basis.

We cannot assert that the fees under our aspenONE licensing model and point product arrangements with Premier Plus SMS are fixed or determinable because of the rights provided to customers, economics of the arrangements, and because we do not have an established history of our arrangements going to term end date without providing concessions to customers. As a result, the amount of revenue recognized for these arrangements is limited by the amount of customer payments that become due.

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

Vendor-Specific Objective Evidence of Fair Value (VSOE)

We have established VSOE for professional services and certain training offerings, but not for our software products or our SMS offerings. We assess VSOE for SMS, professional services, and training, based on an analysis of standalone sales of the offerings using the bell-shaped curve approach. We do not have a history of selling our Premier Plus SMS offering to customers on a standalone basis, and as a result are unable to establish VSOE for this deliverable.

## Subscription and Software Revenue

Subscription and software revenue consists primarily of product and related revenue from our (i) aspenONE licensing model; (ii) point product arrangements with our Premier Plus SMS offering included for the contract term; and (iii) perpetual arrangements.

When a customer elects to license our products under our aspenONE licensing model, our Premier Plus SMS offering is included for the entire term of the arrangement and the customer receives, for the term of the arrangement, the right to any new unspecified future software products and updates that may be introduced into the licensed aspenONE software suite. Due to our obligation to provide unspecified future software products and updates and because we do not have VSOE for our Premier Plus SMS offering, we are required to recognize revenue ratably over the term of the arrangement, once the other revenue recognition criteria noted above have been met.

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



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### Services and Other Revenue

#### Professional Services Revenue

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

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

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

#### Training Revenue

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

#### Deferred Revenue

Deferred revenue includes amounts billed or collected in advance of revenue recognition, including arrangements under the aspenONE licensing model, point product arrangements with Premier Plus SMS, professional services, and training. Deferred revenue is recorded as each invoice becomes due.

#### Other Licensing Matters

Our standard licensing agreements include a product warranty provision. We have not experienced significant claims related to software warranties beyond the scope of SMS support, which we are already obligated to provide, and consequently, we have not established reserves for warranty obligations.

Our agreements with our customers generally require us to indemnify the customer against claims that our software infringes third-party patent, copyright, trademark or other proprietary rights. Such indemnification obligations are generally limited in a variety of industry-standard respects, including our right to replace an infringing product. As of

September 30, 2017 and June 30, 2017, we had not experienced any material losses related to these indemnification obligations and no claims with respect thereto were outstanding. We do not expect significant claims related to these indemnification obligations, and consequently, have not established any related reserves.

(d) Loss Contingencies

We accrue estimated liabilities for loss contingencies arising from claims, assessments, litigation and other sources when it is probable that a liability has been incurred and the amount of the claim, assessment or damages can be reasonably estimated. We believe that we have sufficient accruals to cover any obligations resulting from claims, assessments or litigation that have met these criteria. Please refer to Note 15 for discussion of these matters and related liability accruals.



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(e) Foreign Currency Transactions

Foreign currency exchange gains and losses generated from the settlement and remeasurement of transactions denominated in currencies other than the functional currency of our subsidiaries are recognized in our results of operations as incurred as a component of other income (expense), net. Net foreign currency (losses) gains were \$(0.6) million and \$0.6 million during the three months ended September 30, 2017 and 2016, respectively.

(f) Research and Development Expense

We charge research and development expenditures to expense as the costs are incurred. Research and development expenses consist primarily of personnel expenses related to the creation of new products, enhancements and engineering changes to existing products and costs of acquired technology prior to establishing technological feasibility.

We acquired no technology during the three months ended September 30, 2017 and \$0.4 million during the three months ended September 30, 2016. At the time we acquired the technology, the projects to develop commercially available products did not meet the accounting definition of having reached technological feasibility and therefore the cost of the acquired technology was expensed as a research and development expense.

(g) Recently Issued Accounting Pronouncements

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606). ASU No. 2014-09 supersedes the revenue recognition requirements in Revenue Recognition (Topic 605), and requires entities to recognize revenue when they transfer promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. As currently issued and amended, ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period, though early adoption is permitted for annual reporting periods beginning after December 15, 2016. We will adopt ASU No. 2014-09 during the first quarter of fiscal 2019. Based on our preliminary assessment, the adoption of ASU No. 2014-09 will impact the timing of a portion of the revenue recognized from our term contracts. We are continuing to evaluate the impact of ASU No. 2014-09 on our consolidated financial statements and implementing accounting system changes related to the adoption.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842). Under the amendment, lessees will be required to recognize virtually all of their leases on the balance sheet, by recording a right-of-use asset and lease liability. The ASU is effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2018. Early adoption is permitted. We are currently evaluating the impact of ASU No. 2016-02 on our consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting. The amendment identifies several areas for simplification applicable to entities that issue share-based payment awards to their employees, including income tax consequences, the option to recognize gross stock compensation expense with actual forfeitures recognized when they occur, and certain classifications on the statements of cash flows. The ASU is effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2016. We adopted ASU No. 2016-09 effective July 1, 2017.

As a result of adopting the new standard, excess tax benefits from stock-based compensation are now reflected in the consolidated statements of operations as a component of the provision for income taxes, whereas they were previously a component of stockholders' deficit. The adoption of ASU No. 2016-09 resulted in a decrease in our provision for income taxes of \$0.5 million for the three months ended September 30, 2017. This represents a decrease in our effective tax rate of approximately 1.0 percentage point for the three months ended September 30, 2017, due to the recognition of excess tax benefits for options exercised and the vesting of equity awards. There was no change as a result of how we account for forfeitures for financial statement reporting purposes. We adopted the cash flow presentation prospectively, and accordingly, excess tax benefits from stock-based compensation of \$0.5 million is

presented as a cash inflow from operating activity included within the change in income tax payable for the three months ended September 30, 2017, while \$0.6 million of excess tax benefits from equity-based compensation is presented as a financing activity for the three months ended September 30, 2016. We prospectively excluded the excess tax benefits from the assumed proceeds available to repurchase shares in the computation of diluted earnings per share under the treasury stock method, which did not have a material impact on our diluted earnings per share for the three months ended September 30, 2017.

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments - Credit Losses (Topic 326). The amendment changes the impairment model for most financial assets and certain other instruments. Entities will be required to use a model that will result in the earlier recognition of allowances for losses for trade and other receivables, held-to-maturity debt securities, loans, and other instruments. For available-for-sale debt securities with unrealized losses, the losses will be

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recognized as allowances rather than as reductions in the amortized cost of the securities. The ASU is effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2019. Early adoption is permitted. We are currently evaluating the impact of ASU No. 2016-13 on our consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230). The amendment updates the guidance as to how certain cash receipts and cash payments should be presented and classified, and is intended to reduce the existing diversity in practice. The ASU is effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2017. Early adoption is permitted. We are currently evaluating the impact of ASU No. 2016-15 on our consolidated financial statements.

In January 2017, the FASB issued ASU No. 2017-01, Business Combinations (Topic 805) - Clarifying the Definition of a Business. The amendment changes the definition of a business to assist entities in evaluating when a set of transferred assets and activities constitutes a business. The ASU is effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2017. Early adoption is permitted. We do not anticipate the adoption of ASU No. 2017-01 will have a material effect on the consolidated financial statements or related disclosures.

In January 2017, the FASB issued ASU No. 2017-04, Intangibles - Goodwill and Other Topics (Topic 350) - Simplifying the Test for Goodwill Impairment. The amendment eliminates Step 2 of the goodwill impairment test and requires goodwill impairment to be measured as the amount by which a reporting unit's carrying amount exceeds its fair value, not to exceed the carrying amount of its goodwill. The ASU is effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2017. Early adoption is permitted. We do not anticipate the adoption of ASU No. 2017-04 will have a material effect on the consolidated financial statements or related disclosures.

### 3. Fair Value

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

Cash equivalents of \$43.9 million and \$79.7 million as of September 30, 2017 and June 30, 2017, respectively, were reported at fair value utilizing quoted market prices in identical markets, or "Level 1 inputs." Our cash equivalents consist of short-term, highly liquid investments with remaining maturities of three months or less when purchased.

Financial instruments not measured or recorded at fair value in the accompanying unaudited consolidated financial statements consist of accounts receivable, accounts payable and accrued liabilities. The estimated fair value of these financial instruments approximates their carrying value. The estimated fair value of the borrowings under the Credit Agreement (described below in Note 10, Credit Agreement) approximates its carrying value due to the floating interest rate.

### 4. Accounts Receivable

Our accounts receivable, net of the related allowance for doubtful accounts, were as follows as of September 30, 2017 and June 30, 2017:

|                     | Gross                  | Allowance | Net      |
|---------------------|------------------------|-----------|----------|
|                     | (Dollars in Thousands) |           |          |
| September 30, 2017: |                        |           |          |
| Accounts receivable | \$29,479               | \$ 1,195  | \$28,284 |

June 30, 2017:

Accounts receivable \$28,955 \$ 1,285 \$27,670

As of September 30, 2017, we had one customer receivable balance that individually represented approximately 18% of our total receivables.

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## 5. Property and Equipment

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

|  | September 30,<br>2017  | June 30,<br>2017 |
|--|------------------------|------------------|
|  | (Dollars in Thousands) |                  |
| Property, equipment and leasehold improvements, at cost: |                        |                  |
| Computer equipment                                       | \$ 8,313               | \$ 8,262         |
| Purchased software                                       | 24,135                 | 24,091           |
| Furniture & fixtures                                     | 6,825                  | 6,805            |
| Leasehold improvements                                   | 12,059                 | 12,025           |
| Property, equipment and leasehold improvements, at cost  | 51,332                 | 51,183           |
| Accumulated depreciation                                 | (38,972 )              | (37,783 )        |
| Property, equipment and leasehold improvements, net      | \$ 12,360              | \$ 13,400        |

## 6. Acquisitions

## Mtelligence Corporation

On October 26, 2016, we completed the acquisition of all the outstanding shares of Mtelligence Corporation (“Mtell”), a provider of predictive and prescriptive maintenance software and related services used to optimize asset performance, for total cash consideration of \$37.4 million. The purchase price consisted of \$31.9 million of cash paid at closing and an additional \$5.5 million to be held back until April 2018 as security for certain representations, warranties, and obligations of the sellers. The holdback was recorded at its fair value as of the acquisition date of \$5.3 million, and is recorded in other non-current liabilities in our consolidated balance sheet.

An allocation of the purchase price is as follows:

|                                 | Amount<br>(Dollars in<br>Thousands) |
|---------------------------------|-------------------------------------|
| Tangible assets acquired, net   | \$ 779                              |
| Identifiable intangible assets: |                                     |
| Developed technology            | 11,385                              |
| Customer relationships          | 679                                 |
| Non-compete agreements          | 553                                 |
| Goodwill                        | 25,888                              |
| Deferred tax liabilities, net   | (2,099 )                            |
| Total assets acquired           | \$ 37,185                           |

We used the income approach to determine the values of the identifiable intangible assets. The weighted-average discount rate (or rate of return) used to determine the value of the Mtell intangible assets was 19% and the effective tax rate used was 34%. The values of the developed technology, customer relationships and non-compete agreements are being amortized on a straight-line basis, except technology, which is being amortized on a proportional use basis, over their estimated useful lives of 12 years, 6 years and 3 years, respectively.

The goodwill, which is not deductible for tax purposes, reflects the value of the assembled workforce and the company-specific synergies we expect to realize by selling Mtell products and services to our existing customers. The results of operations of Mtell have been included prospectively in our results of operations since the date of acquisition.



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## 7. Intangible Assets

We include in our amortizable intangible assets those intangible assets acquired in our business and asset acquisitions. We amortize acquired intangible assets with finite lives over their estimated economic lives, generally using the straight-line method. Each period, we evaluate the estimated remaining useful lives of acquired intangible assets to determine whether events or changes in circumstances warrant a revision to the remaining period of amortization. Acquired intangibles are removed from the accounts when fully amortized and no longer in use.

Intangible assets consisted of the following as of September 30, 2017 and June 30, 2017:

|                        | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Net<br>Carrying<br>Amount |
|------------------------|-----------------------------|-----------------------------|---------------------------|
| (Dollars in Thousands) |                             |                             |                           |
| September 30, 2017:    |                             |                             |                           |
| Technology and patents | \$22,443                    | \$ (3,775 )                 | \$ 18,668                 |
| Customer relationships | 1,432                       | (221 )                      | 1,211                     |
| Non-compete agreements | 553                         | (169 )                      | 384                       |
| Total                  | \$24,428                    | \$ (4,165 )                 | \$ 20,263                 |
| June 30, 2017:         |                             |                             |                           |
| Technology and patents | \$22,350                    | \$ (3,254 )                 | \$ 19,096                 |
| Customer relationships | 1,432                       | (169 )                      | 1,263                     |
| Non-compete agreements | 553                         | (123 )                      | 430                       |
| Total                  | \$24,335                    | \$ (3,546 )                 | \$ 20,789                 |

Total amortization expense related to intangible assets is included in operating expenses and amounted to approximately \$0.5 million and less than \$0.1 million for the three months ended September 30, 2017 and 2016, respectively.

Future amortization expense as of September 30, 2017 is expected to be as follows:

| Year Ended June 30,       | Amortization<br>Expense |
|---------------------------|-------------------------|
| (Dollars in<br>Thousands) |                         |
| 2018                      | \$ 1,578                |
| 2019                      | 2,063                   |
| 2020                      | 2,134                   |
| 2021                      | 2,206                   |
| 2022                      | 2,451                   |
| Thereafter                | 9,831                   |
| Total                     | \$ 20,263               |

## 8. Goodwill

The changes in the carrying amount of goodwill for our subscription and software reporting unit during the three months ended September 30, 2017 was as follows:

|                              | Gross<br>Carrying<br>Amount | Accumulated<br>Impairment<br>Losses | Effect of<br>Currency<br>Translation | Net<br>Carrying<br>Amount |
|------------------------------|-----------------------------|-------------------------------------|--------------------------------------|---------------------------|
| (Dollars in Thousands)       |                             |                                     |                                      |                           |
| June 30, 2017:               | \$ 116,817                  | \$ (65,569 )                        | \$ —                                 | \$ 51,248                 |
| Foreign currency translation | —                           | —                                   | 490                                  | 490                       |
| September 30, 2017:          | \$ 116,817                  | \$ (65,569 )                        | \$ 490                               | \$ 51,738                 |

No triggering events indicating goodwill impairment occurred during the three months ended September 30, 2017.



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## 9. Accrued Expenses and Other Liabilities

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

|  | September 30,<br>2017  | June 30,<br>2017 |
|--|------------------------|------------------|
|  | (Dollars in Thousands) |                  |
| Payroll and payroll-related                          | \$ 12,896              | \$ 20,864        |
| Royalties and outside commissions                    | 2,706                  | 2,733            |
| Professional fees                                    | 2,382                  | 2,216            |
| Deferred acquisition payments                        | 7,932                  | 8,548            |
| Other  | 10,845                 | 13,788           |
| Total accrued expenses and other current liabilities | \$ 36,761              | \$ 48,149        |

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

|                                     | September 30,<br>2017  | June 30,<br>2017 |
|-------------------------------------|------------------------|------------------|
|                                     | (Dollars in Thousands) |                  |
| Deferred rent                       | \$ 7,045               | \$ 6,916         |
| Uncertain tax positions             | 4,307                  | 3,921            |
| Other                               | 2,402                  | 2,311            |
| Total other non-current liabilities | \$ 13,754              | \$ 13,148        |

## 10. Credit Agreement

On February 26, 2016, we entered into a \$250.0 million Credit Agreement (the "Credit Agreement") with JPMorgan Chase Bank, N.A., as administrative agent, Silicon Valley Bank, as syndication agent, and the lenders and other parties named therein (the "Lenders"). On August 9, 2017, we entered into an Amendment to increase the Credit Agreement to \$350.0 million. The indebtedness evidenced by the Credit Agreement matures on February 26, 2021. Prior to the maturity of the Credit Agreement, any amounts borrowed may be repaid and, subject to the terms and conditions of the Credit Agreement, borrowed again in whole or in part without penalty. As of September 30, 2017 and June 30, 2017, we had \$140.0 million in outstanding borrowings under the Credit Agreement.

Borrowings under the Credit Agreement bear interest at a rate equal to either, at our option, the sum of (a) the highest of (1) the rate of interest publicly announced by JPMorgan Chase Bank, N.A. as its prime rate in effect, (2) the Federal Funds Effective Rate plus 0.5%, and (3) the one-month Adjusted LIBO Rate plus 1.0%, plus (b) a margin initially of 0.5% for the first full fiscal quarter ending after the date of the Credit Agreement and thereafter based on our Leverage Ratio; or the Adjusted LIBO Rate plus a margin initially of 1.5% for the first full fiscal quarter ending after the date of the Credit Agreement and thereafter based on our Leverage Ratio. We must also pay, on a quarterly basis, an unused commitment fee at a rate of between 0.2% and 0.3% per annum, based on our Leverage Ratio. The interest rate as of September 30, 2017 was 2.74%.

All borrowings under the Credit Agreement are secured by liens on substantially all of our assets. The Credit Agreement contains affirmative and negative covenants customary for facilities of this type, including restrictions on: incurrence of additional debt; liens; fundamental changes; asset sales; restricted payments; and transactions with affiliates. The Credit Agreement contains financial covenants regarding maintenance as of the end of each fiscal

quarter, commencing with the quarter ending June 30, 2016, of a maximum Leverage Ratio of 3.0 to 1.0 and a minimum Interest Coverage Ratio of 3.0 to 1.0. As of September 30, 2017 we were in compliance with these covenants.

#### 11. Stock-Based Compensation

The weighted average estimated fair value of option awards granted was \$16.91 and \$12.96 during the three months ended September 30, 2017 and 2016, respectively.

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

|                            | Three Months Ended<br>September 30,<br>2017 |        | 2016 |  |
|----------------------------|---|--------|------|--|
| Risk-free interest rate    | 1.7 %                                       | 1.1 %  |      |  |
| Expected dividend yield    | 0.0 %                                       | 0.0 %  |      |  |
| Expected life (in years)   | 4.6   | 4.6    |      |  |
| Expected volatility factor | 28.1 %                                      | 31.5 % |      |  |

The stock-based compensation expense under all equity plans and its classification in the unaudited consolidated statements of operations for the three months ended September 30, 2017 and 2016 are as follows:

|                                | Three Months Ended<br>September 30,<br>2017 |          | 2016 |  |
|--------------------------------|---|----------|------|--|
|                                | (Dollars in Thousands)                      |          |      |  |
| Recorded as expenses:          |   |          |      |  |
| Cost of services and other     | \$ 450                                      | \$ 369   |      |  |
| Selling and marketing          | 885   | 955      |      |  |
| Research and development       | 1,896                                       | 1,062    |      |  |
| General and administrative     | 3,183                                       | 2,572    |      |  |
| Total stock-based compensation | \$ 6,414                                    | \$ 4,958 |      |  |

A summary of stock option and RSU activity under all equity plans for the three months ended September 30, 2017 is as follows:

|  | Stock Options |                                 |   | Restricted Stock Units               |           |  |
|--|---------------|---------------------------------|---|--------------------------------------|-----------|--|
|  | Shares        | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (Years) | Aggregate Intrinsic Value (in 000's) | Shares    | Weighted Average Grant Date Fair Value |
| Outstanding at June 30, 2017                         | 1,353,558     | \$ 37.98                        | 7.30  | \$ 23,535                            | 615,998   | \$ 45.62                               |
| Granted  | 375,330       | 63.14                           |   |                                      | 310,303   | 63.14                                  |
| Settled (RSUs)                                       | —             |                                 |   |                                      | (84,927 ) | 50.43                                  |
| Exercised  | (66,567 )     | 36.21                           |   |                                      | —         |  |
| Cancelled / Forfeited                                | (26,747 )     | 50.72                           |   |                                      | (21,478 ) | 56.10                                  |
| Outstanding at September 30, 2017                    | 1,635,574     | \$ 43.62                        | 7.73  | \$ 31,553                            | 819,896   | \$ 51.48                               |
| Vested and exercisable at September 30, 2017         | 836,448       | \$ 35.08                        | 6.45  | \$ 23,214                            | —         |  |
| Vested and expected to vest as of September 30, 2017 | 1,556,485     | \$ 43.16                        | 7.66  | \$ 30,741                            | 736,841   | \$ 51.50                               |

The weighted average grant-date fair value of RSUs granted was \$63.14 and \$45.44 during the three months ended September 30, 2017 and 2016, respectively. The total fair value of shares vested from RSU grants was \$5.3 million and \$4.0 million during the three months ended September 30, 2017 and 2016, respectively.

At September 30, 2017, the total future unrecognized compensation cost related to stock options was \$10.6 million and is expected to be recorded over a weighted average period of 3.0 years. At September 30, 2017, the total future unrecognized compensation cost related to RSUs was \$36.7 million and is expected to be recorded over a weighted average period of 3.0 years.

The total intrinsic value of options exercised was \$1.7 million and \$2.7 million during the three months ended September 30, 2017 and 2016, respectively. We received cash proceeds from option exercises of \$2.4 million and \$3.1 million

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during the three months ended September 30, 2017 and 2016, respectively. We withheld withholding taxes on vested RSUs of \$1.7 million and \$1.3 million during the three months ended September 30, 2017 and 2016, respectively.

At September 30, 2017, common stock reserved for future issuance or settlement under equity compensation plans was 10.6 million shares.

## 12. Stockholders' Deficit

## Stock Repurchases

On January 22, 2015, our Board of Directors approved a share repurchase program (the "Share Repurchase Program") for up to \$450.0 million worth of our common stock. On April 26, 2016 and June 8, 2017, the Board of Directors approved a \$400.0 million and \$200.0 million increase to the Share Repurchase Program, respectively. The timing and amount of any shares repurchased are based on market conditions and other factors. All shares of our common stock repurchased have been recorded as treasury stock under the cost method.

During the three months ended September 30, 2017, we repurchased 839,159 shares of our common stock in the open market for \$50.0 million. As of September 30, 2017, the total remaining value under the Share Repurchase Program was approximately \$296.3 million.

## Accumulated Other Comprehensive Income

As of September 30, 2017, accumulated other comprehensive income was comprised of foreign currency translation adjustments of \$2.9 million. As of June 30, 2017, accumulated other comprehensive income was comprised of foreign currency translation adjustments of \$1.5 million and net unrealized gains on available for sale securities of less than \$0.1 million.

## 13. Net Income Per Share

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

The calculations of basic and diluted net income per share and basic and dilutive weighted average shares outstanding for the three months ended September 30, 2017 and 2016 are as follows:

|  | Three Months Ended                                       |           |
|--|--|-----------|
|  | September 30,  |           |
|  | 2017   | 2016      |
|  | (Dollars and Shares in Thousands, Except per Share Data) |           |
| Net income                                   | \$ 34,755  | \$ 35,000 |
| Weighted average shares outstanding          | 73,024   | 79,048    |
| Dilutive impact from:                        |  |           |
| Share-based payment awards                   | 585  | 337       |
| Dilutive weighted average shares outstanding | 73,609   | 79,385    |

Income per share

|          |         |         |
|----------|---------|---------|
| Basic    | \$ 0.48 | \$ 0.44 |
| Dilutive | \$ 0.47 | \$ 0.44 |

For the three months ended September 30, 2017 and 2016, certain employee equity awards were anti-dilutive based on the treasury stock method. Additionally, during the three months ended September 30, 2017, options to purchase 372,305 shares

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and of our common stock were not included in the computation of dilutive weighted average shares outstanding, because their exercise prices ranged from \$60.05 per share to \$63.77 per share and were greater than the average market price of our common stock during the period then ended. These options were outstanding as of September 30, 2017 and expire at various dates through August 31, 2027.

The following employee equity awards were excluded from the calculation of dilutive weighted average shares outstanding because their effect would be anti-dilutive as of September 30, 2017 and 2016:

|                        | Three Months Ended    |       |
|------------------------|-----------------------|-------|
|                        | September 30,         |       |
|                        | 2017                  | 2016  |
|                        | (Shares in Thousands) |       |
| Employee equity awards | 674                   | 1,535 |

#### 14. Income Taxes

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

Our effective tax rate was 32.6% and 36.1% for the three months ended September 30, 2017 and 2016, respectively. Our effective tax rate decreased for the three months ended September 30, 2017 compared to the same period in 2016 due to discrete items, primarily related to lower interest expense on uncertain tax positions. During the three months ended September 30, 2017 and 2016, our income tax expense was driven primarily by pre-tax profitability in our domestic and foreign operations and the impact of permanent items. The permanent items are predominantly a U.S. domestic production activity deduction and tax credits for research expenditures, slightly offset by non-deductible stock-based compensation expense.

During the three months ended September 30, 2017, we adopted ASU No. 2016-09. As a result of adopting the new standard, excess tax benefits from stock-based compensation are now reflected in the consolidated statements of operations as a component of the provision for income taxes, whereas they were previously a component of stockholders' deficit. The adoption of ASU 2016-09 resulted in a decrease in our provision for income taxes of \$0.5 million for the three months ended September 30, 2017. This represents a decrease in our effective tax rate of approximately 1.0 percentage point for the three months ended September 30, 2017, due to the recognition of excess tax benefits for options exercised and the vesting of equity awards.

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

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

consolidated financial position or results of operations.

## 15. Commitments and Contingencies

### Operating Leases

We lease certain facilities under non-cancellable operating leases with terms in excess of one year. Rental expense on leased facilities under operating leases was approximately \$2.0 million and \$2.2 million during the three months ended September 30, 2017 and September 30, 2016, respectively.

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Standby letters of credit for \$3.0 million and \$2.9 million secure our performance on professional services contracts, certain facility leases and potential liabilities as of September 30, 2017 and June 30, 2017, respectively. The letters of credit expire at various dates through fiscal 2025.

## Legal Matters

In the ordinary course of business, we are, from time to time, involved in lawsuits, claims, investigations, proceedings and threats of litigation. These matters include an April 2004 claim by a customer that certain of our software products and implementation services failed to meet the customer's expectations. In March 2014, a judgment was issued by the trial court against us in the amount of approximately 1.9 million Euro ("€") plus interest and a portion of legal fees. We subsequently filed an appeal of that judgment. In March 2016, the appellate court determined that we are liable for damages in the amount of approximately €1.7 million plus interest, with the possibility of additional damages to be determined in further proceedings by the appellate court. As of September 30, 2017, there has been no change to the appellate court's determination.

While the outcome of the proceedings and claims referenced above cannot be predicted with certainty, there were no such matters, as of September 30, 2017 that, in the opinion of management, are reasonably possible to have a material adverse effect on our financial position, results of operations or cash flows. Liabilities, if applicable, related to the aforementioned matters discussed in this Note have been included in our accrued liabilities at September 30, 2017, and are not material to our financial position for the period then ended. As of September 30, 2017, we do not believe that there is a reasonable possibility of a material loss exceeding the amounts already accrued for the proceedings or matters discussed above. However, the results of litigation (including the above-referenced appeal) and claims cannot be predicted with certainty; unfavorable resolutions are possible and could materially affect our results of operations, cash flows or financial position. In addition, regardless of the outcome, litigation could have an adverse impact on us because of attorneys' fees and costs, diversion of management resources and other factors.

## 16. Segment Information

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

The subscription and software segment is engaged in the licensing of process optimization and asset performance management software solutions and associated support services. The services segment includes professional services and training. We do not track assets or capital expenditures by operating segments. Consequently, it is not practical to present assets, capital expenditures, depreciation or amortization by operating segments.

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

|                                       | Subscription<br>and Software | Services | Total     |
|---------------------------------------|------------------------------|----------|-----------|
|                                       | (Dollars in Thousands)       |          |           |
| Three Months Ended September 30, 2017 |                              |          |           |
| Segment revenue                       | \$115,756                    | \$7,025  | \$122,781 |
| Segment expenses (1)                  | (48,843 )                    | (6,949 ) | (55,792 ) |
| Segment profit                        | \$66,913                     | \$76     | \$66,989  |
| Three Months Ended September 30, 2016 |                              |          |           |
| Segment revenue                       | \$113,444                    | \$6,606  | \$120,050 |

|                      |           |          |           |
|----------------------|-----------|----------|-----------|
| Segment expenses (1) | (45,726 ) | (6,437 ) | (52,163 ) |
| Segment profit       | \$67,718  | \$169    | \$67,887  |

(1) Our reportable segments' operating expenses include expenses directly attributable to the segments. Segment expenses include selling and marketing, research and development, stock-based compensation and certain corporate expenses incurred in support of the segments. Segment expenses do not include allocations of general and administrative; interest income, net; and other income, net.

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## Reconciliation to Income before Income Taxes

The following table presents a reconciliation of total segment profit to income before income taxes for the three months ended September 30, 2017 and 2016:

|  | Three Months Ended<br>September 30, |           |
|--|-------------------------------------|-----------|
|  | 2017                                | 2016      |
|  | (Dollars in Thousands)              |           |
| Total segment profit for reportable segments | \$ 66,989                           | \$ 67,887 |
| General and administrative                   | (13,676 )                           | (13,157 ) |
| Other (expense) income, net                  | (616 )                              | 646       |
| Interest (expense) income, net               | (1,065 )                            | (597 )    |
| Income before income taxes                   | \$ 51,632                           | \$ 54,779 |

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

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

Our fiscal year ends on June 30<sup>th</sup>, and references in this Quarterly Report to a specific fiscal year are to the twelve months ended June 30<sup>th</sup> of such year (for example, "fiscal 2018" refers to the year ending on June 30, 2018).

#### Business Overview

We are a leading global supplier of asset optimization solutions that optimize asset design, operations and maintenance in complex, industrial environments. We combine decades of process modeling and operations expertise with big data machine-learning and analytics. Our purpose-built software solutions improve the competitiveness and profitability of our customers by increasing throughput, energy efficiency, and production, reducing unplanned downtime, enhancing capital efficiency, and decreasing working capital requirements over the entire asset lifecycle to support operational excellence.

Our software incorporates our proprietary mathematical and empirical models of manufacturing and planning processes and reflects the deep domain expertise we have amassed from focusing on solutions for the process and other capital-intensive industries for over 35 years. We have developed our applications to design and optimize processes across three principal business areas: engineering, manufacturing and supply chain, and asset performance management. We are a recognized market and technology leader in providing process optimization and asset performance management software solutions for each of these business areas.

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

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

We have approximately 2,100 customers globally. Our customers consist of companies engaged in the process and other capital-intensive industries such as energy, chemicals, engineering and construction, as well as pharmaceuticals, transportation, power, metals and mining, pulp and paper, and consumer packaged goods.

#### Business Segments

We have two operating and reportable segments: i) subscription and software and ii) services. The subscription and software segment is engaged in the licensing of asset optimization software solutions and associated support services. The services segment includes professional services and training.

#### Key Components of Operations

##### Revenue

We generate revenue primarily from the following sources:

**Subscription and Software Revenue.** We sell our software products to end users primarily under fixed-term licenses. We license our software products primarily through a subscription offering which we refer to as our aspenONE licensing model, which includes software maintenance and support, known as our Premier Plus SMS offering, for the entire term. Our aspenONE products are organized into three suites: 1) engineering; 2) manufacturing and supply chain; and 3) asset performance management. The aspenONE licensing model provides customers with access to all of the products within the aspenONE suite(s) they license. Customers can change or alternate the use of multiple products in a licensed suite through the use of exchangeable units of measurement, called tokens, licensed in quantities determined by the customer. This licensing system enables customers to use products as needed and to experiment with different products to best solve whatever critical business challenges they face. Customers can increase their usage of our software by purchasing additional tokens as business needs evolve.



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We provide customers technical support, access to software fixes and updates and the right to any new unspecified future software products and updates that may be introduced into the licensed aspenONE software suite. Our technical support services are provided from our customer support centers throughout the world, as well as via email and through our support website.

We also license our software through point product arrangements with our Premier Plus SMS offering included for the contract term, as well as perpetual license arrangements.

**Services and Other Revenue.** We provide training and professional services to our customers. Our professional services are focused on implementing our technology in order to improve customers' plant performance and gain better operational data. Customers who use our professional services typically engage us to provide those services over periods of up to 24 months. We charge customers for professional services on a time-and-materials or fixed-price basis. We provide training services to our customers, including on-site, Internet-based and customized training.

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

- whether the professional services arrangement was sold as a single arrangement with, or in contemplation of, a new aspenONE licensing arrangement;
- the number, value and rate per hour of service transactions booked during the current and preceding periods;
- the number and availability of service resources actively engaged on billable projects;
- the timing of milestone acceptance for engagements contractually requiring customer sign-off;
- the timing of collection of cash payments when collectability is uncertain;
- and
- the size of the installed base of license contracts.

### Cost of Revenue

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

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

### Operating Expenses

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

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

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

### Other Income and Expenses

**Interest Income.** Interest income is recorded for the accretion of interest on the investment in marketable securities and short-term money market instruments.

**Interest Expense.** During the three months ended September 30, 2017 and 2016, interest expense was primarily related to the Credit Agreement we entered into with various lenders on February 26, 2016, as amended August 9, 2017 (the "Credit Agreement").

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

Provision for Income Taxes. Provision for income taxes is comprised of domestic and foreign taxes. We record interest and penalties related to income tax matters as a component of income tax expense. Our effective income tax rate may fluctuate between fiscal years and from quarter to quarter due to items arising from discrete events, such as tax benefits from the disposition of employee equity awards, settlements of tax audits and assessments and tax law changes. Our effective income tax rate is also impacted by, and may fluctuate in any given period because of, the composition of income in foreign jurisdictions where tax rates differ.

### Key Business Metrics

We utilize certain key non-GAAP and other business measures to track and assess the performance of our business and we make these measures available to investors. We have refined the set of appropriate business metrics in the context of our evolving business and use the following non-GAAP business metrics in addition to GAAP measures to track our business performance:

• Annual spend;

• Free cash flow; and

• Non-GAAP operating income.

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

### Annual Spend

Annual spend is an estimate of the annualized value of our portfolio of term license arrangements, as of a specific date. Management believes that this financial measure is a useful metric to investors as it provides insight into the growth component of license bookings during a fiscal period. Annual spend is calculated by summing the most recent annual invoice value of each of our active term license contracts. Annual spend also includes the annualized value of standalone SMS agreements purchased in conjunction with term license agreements. Comparing annual spend for different dates can provide insight into the growth and retention rates of our business, and since annual spend represents the estimated annualized billings associated with our active term license agreements, it provides insight into the future value of subscription and software revenue.

Annual spend increases as a result of:

• New term license agreements with new or existing customers;

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

• Escalation of annual payments in our active term license contracts.

Annual spend is adversely affected by term license and standalone SMS agreements that are renewed at a lower entitlement level or not renewed and, to a lesser extent, by customer contracts that are terminated during the contract term due to the customer's business ceasing operations.

We estimate that annual spend grew by approximately 0.3% during the first quarter of fiscal 2018, from \$459.6 million at June 30, 2017 to \$460.9 million at September 30, 2017.



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## Free Cash Flow

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

Free cash flow is calculated as net cash provided by operating activities adjusted for the net impact of: purchases of property, equipment and leasehold improvements; capitalized computer software development costs; excess tax benefits from stock-based compensation; non-capitalized acquired technology; and other nonrecurring items, such as acquisition related payments.

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

|  | Three Months Ended     |           |
|--|------------------------|-----------|
|  | September 30,          |           |
|  | 2017                   | 2016      |
|  | (Dollars in Thousands) |           |
| Net cash provided by operating activities                    | \$ 12,360              | \$ 26,250 |
| Purchases of property, equipment, and leasehold improvements | (123 )                 | (898 )    |
| Capitalized computer software development costs              | (65 )                  | (51 )     |
| Non-capitalized acquired technology                          | 75                     | 846       |
| Excess tax benefits from stock-based compensation            | —                      | 584       |
| Free cash flows (non-GAAP)                                   | \$ 12,247              | \$ 26,731 |

Total free cash flow on a non-GAAP basis decreased by \$14.5 million during the three months ended September 30, 2017 as compared to the same period of the prior fiscal year primarily due to changes in working capital.

In the three months ended September 30, 2016, we acquired technology that did not meet the accounting requirements for capitalization and therefore the cost of the acquired technology was expensed as research and development. We have excluded the payment for the acquired technology from free cash flow to be consistent with transactions where the acquired technology assets were capitalized.

## Non-GAAP Operating Income

Non-GAAP operating income excludes certain non-cash and non-recurring expenses, and is used as a supplement to operating income presented on a GAAP basis. We believe that non-GAAP operating income is a useful financial measure because removing certain non-cash and other items provides additional insight into recurring profitability and cash flow from operations.

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The following table presents our net income, as adjusted for stock-based compensation expense, non-capitalized acquired technology and amortization of purchased technology intangibles, and other items, such as acquisition related expenses, for the indicated periods:

|                                     | Three Months Ended                      |          | 2017 Compared to 2016 |           |  |
|-------------------------------------|---|----------|-----------------------|-----------|--|
|                                     | 2017                                    | 2016     | \$                    | %         |  |
|                                     | September 30,<br>(Dollars in Thousands) |          |                       |           |  |
| GAAP income from operations         | \$53,313                                | \$54,730 | \$ (1,417 )           | (2.6 )%   |  |
| Plus:                               |   |          |                       |           |  |
| Stock-based compensation            | 6,414                                   | 4,958    | 1,456                 | 29.4 %    |  |
| Non-capitalized acquired technology | —                                       | 350      | (350 )                | (100.0 )% |  |
| Amortization of intangibles         | 526                                     | 55       | 471                   | 856.4 %   |  |
| Acquisition related fees            | 130                                     | 362      | (232 )                | (64.1 )%  |  |
| Non-GAAP income from operations     | \$60,383                                | \$60,455 | \$ (72 )              | (0.1 )%   |  |

In the three months ended September 30, 2016, we acquired technology that did not meet the accounting requirements for capitalization and therefore the cost of the acquired technology was expensed as research and development. We have excluded the expense of the acquired technology from non-GAAP operating income to be consistent with transactions where the acquired assets were capitalized.

## Critical Accounting Estimates and Judgments

Note 2, "Significant Accounting Policies" to the audited consolidated financial statements in our Annual Report on Form 10-K for the fiscal year ended June 30, 2017 describes the significant accounting policies and methods used in the preparation of the consolidated financial statements appearing in this report. The accounting policies that reflect our more significant estimates, judgments and assumptions in the preparation of our consolidated financial statements are described in "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7 of our Annual Report on Form 10-K for the fiscal year ended June 30, 2017, and include the following:

• revenue recognition;

• accounting for income taxes; and

• loss contingencies.

There were no significant changes to our critical accounting policies and estimates during the three months ended September 30, 2017.

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## Results of Operations

## Comparison of the Three Months Ended September 30, 2017

The following table sets forth the results of operations and the period-over-period percentage change in certain financial data for the three months ended September 30, 2017:

|  | Three Months Ended     |           | Increase / |   |
|--|------------------------|-----------|------------|---|
|  | September 30,          |           | (Decrease) |   |
|  | 2017                   | 2016      | Change     |   |
|  | (Dollars in Thousands) |           | %          |   |
| Revenue:                                 |                        |           |            |   |
| Subscription and software                | \$115,756              | \$113,444 | 2.0        | % |
| Services and other                       | 7,025                  | 6,606     | 6.3        | % |
| Total revenue                            | 122,781                | 120,050   | 2.3        | % |
| Cost of revenue:                         |                        |           |            |   |
| Subscription and software                | 5,783                  | 5,069     | 14.1       | % |
| Services and other                       | 6,949                  | 6,437     | 8.0        | % |
| Total cost of revenue                    | 12,732                 | 11,506    | 10.7       | % |
| Gross profit                             | 110,049                | 108,544   | 1.4        | % |
| Operating expenses:                      |                        |           |            |   |
| Selling and marketing                    | 23,571                 | 22,025    | 7.0        | % |
| Research and development                 | 19,489                 | 18,632    | 4.6        | % |
| General and administrative               | 13,676                 | 13,157    | 3.9        | % |
| Total operating expenses, net            | 56,736                 | 53,814    | 5.4        | % |
| Income from operations                   | 53,313                 | 54,730    | (2.6)      | % |
| Interest income                          | 141                    | 272       | (48.2)     | % |
| Interest (expense)                       | (1,206)                | (869)     | 38.8       | % |
| Other (expense) income, net              | (616)                  | 646       | (195.4)    | % |
| Income before provision for income taxes | 51,632                 | 54,779    | (5.7)      | % |
| Provision for income taxes               | 16,877                 | 19,779    | (14.7)     | % |
| Net income                               | \$34,755               | \$35,000  | (0.7)      | % |

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The following table sets forth the results of operations as a percentage of net revenue for certain financial data for the three months ended September 30, 2017:

|  | Three Months<br>Ended<br>September 30,<br>2017 |   | 2016<br>(% of Revenue) |   |
|--|--|---|------------------------|---|
| Revenue:                                 |  |   |                        |   |
| Subscription and software                | 94.3   | % | 94.5                   | % |
| Services and other                       | 5.7  |   | 5.5                    |   |
| Total revenue                            | 100.0  |   | 100.0                  |   |
| Cost of revenue:                         |  |   |                        |   |
| Subscription and software                | 4.7  |   | 4.2                    |   |
| Services and other                       | 5.7  |   | 5.4                    |   |
| Total cost of revenue                    | 10.4   |   | 9.6                    |   |
| Gross profit                             | 89.6   |   | 90.4                   |   |
| Operating expenses:                      |  |   |                        |   |
| Selling and marketing                    | 19.2   |   | 18.3                   |   |
| Research and development                 | 15.9   |   | 15.5                   |   |
| General and administrative               | 11.1   |   | 11.0                   |   |
| Total operating expenses, net            | 46.2   |   | 44.8                   |   |
| Income from operations                   | 43.4   |   | 45.6                   |   |
| Interest income                          | 0.1  |   | 0.2                    |   |
| Interest (expense)                       | (1.0   | ) | (0.7                   | ) |
| Other (expense) income, net              | (0.5   | ) | 0.5                    |   |
| Income before provision for income taxes | 42.1   |   | 45.6                   |   |
| Provision for income taxes               | 13.7   |   | 16.5                   |   |
| Net income                               | 28.3   | % | 29.2                   | % |

## Revenue

Total revenue increased by \$2.7 million during the three months ended September 30, 2017 as compared to the corresponding period of the prior fiscal year. The increase was comprised of an increase in subscription and software revenue of \$2.3 million and an increase in services and other revenue of \$0.4 million, as compared to the corresponding periods of the prior fiscal year.

## Subscription and Software Revenue

|                                   | Three Months Ended<br>September 30, |           | Period-to-Period<br>Change |       |
|-----------------------------------|-------------------------------------|-----------|----------------------------|-------|
|                                   | 2017                                | 2016      | \$                         | %     |
|                                   | (Dollars in Thousands)              |           |                            |       |
| Subscription and software revenue | \$115,756                           | \$113,444 | \$ 2,312                   | 2.0 % |
| As a percent of total revenue     | 94.3                                | % 94.5    | %                          |       |

The period-over-period increase of \$2.3 million in subscription and software revenue during the three months ended September 30, 2017 was primarily attributable to the growth of our base of license arrangements being recognized on a ratable basis.

We expect subscription and software revenue to continue to increase as a result of: (i) having a larger base of license arrangements recognized on a ratable basis; (ii) increased customer usage of our software; (iii) adding new customers; and (iv) escalating annual payments.

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## Services and Other Revenue

|                               | Three Months<br>Ended<br>September 30,<br>2017 |         | 2016   |  | Period-to-Period<br>Change |   |
|-------------------------------|--|---------|--------|--|----------------------------|---|
|                               |  |         | \$     |  | %                          |   |
|                               | (Dollars in Thousands)                         |         |        |  |                            |   |
| Services and other revenue    | \$7,025  | \$6,606 | \$ 419 |  | 6.3                        | % |
| As a percent of total revenue | 5.7  | % 5.5   |        |  |                            | % |

The period-over-period increase of \$0.4 million in services and other revenue during the three months ended September 30, 2017 was primarily attributable to higher professional services revenue of \$0.6 million and lower training revenue of \$0.2 million.

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

## Cost of Revenue

## Cost of Subscription and Software Revenue

|   | Three Months<br>Ended<br>September 30,<br>2017 |         | 2016   |  | Period-to-Period<br>Change |   |
|---|--|---------|--------|--|----------------------------|---|
|   |  |         | \$     |  | %                          |   |
|   | (Dollars in Thousands)                         |         |        |  |                            |   |
| Cost of subscription and software revenue         | \$5,783  | \$5,069 | \$ 714 |  | 14.1                       | % |
| As a percent of subscription and software revenue | 5.0  | % 4.5   |        |  |                            | % |

Cost of subscription and software revenue increased \$0.7 million for the three months ended September 30, 2017 as compared to the corresponding period of the prior fiscal year primarily due to increased amortization expense related to acquired technology.

Subscription and software gross profit margin was consistent at 95.0% and 95.5% during the three months ended September 30, 2017 and 2016, respectively.

## Cost of Services and Other Revenue

|  | Three Months<br>Ended<br>September 30,<br>2017 |         | 2016   |  | Period-to-Period<br>Change |   |
|--|--|---------|--------|--|----------------------------|---|
|  |  |         | \$     |  | %                          |   |
|  | (Dollars in Thousands)                         |         |        |  |                            |   |
| Cost of services and other revenue         | \$6,949  | \$6,437 | \$ 512 |  | 8.0                        | % |
| As a percent of services and other revenue | 98.9   | % 97.4  |        |  |                            | % |

Cost of services and other revenue increased \$0.5 million for the three months ended September 30, 2017 as compared to the corresponding period of the prior fiscal year.

The timing of revenue and expense recognition on professional service arrangements can impact the comparability of cost and gross profit margin of professional services revenue from year to year.

Gross profit margin on services and other revenue of 1.1% for the three months ended September 30, 2017 decreased from 2.6% for the corresponding period of the prior fiscal year, primarily due to higher costs of \$0.5 million.

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## Gross Profit

Gross profit increased from \$108.5 million during the three months ended September 30, 2016 to \$110.0 million during the corresponding period of the current fiscal year.

Gross profit margin decreased from 90.4% during the three months ended September 30, 2016 to 89.6% during the corresponding period of the current fiscal year. For further discussion of subscription and software gross profit and services and other gross profit, please refer to the “Cost of Subscription and Software Revenue” and “Cost of Services and Other Revenue” sections above.

## Operating Expenses

## Selling and Marketing Expense

|                               | Three Months Ended<br>September 30, |          | Period-to-Period<br>Change |       |
|-------------------------------|-------------------------------------|----------|----------------------------|-------|
|                               | 2017                                | 2016     | \$                         | %     |
|                               | (Dollars in Thousands)              |          |                            |       |
| Selling and marketing expense | \$23,571                            | \$22,025 | \$ 1,546                   | 7.0 % |
| As a percent of total revenue | 19.2 %                              | 18.3 %   |                            |       |

The period-over-period increase of \$1.5 million in selling and marketing expense during the three months ended September 30, 2017 was primarily attributable to higher compensation costs of \$0.9 million related to an increase in headcount and higher commissions of \$0.5 million.

## Research and Development Expense

|                                  | Three Months Ended<br>September 30, |          | Period-to-Period<br>Change |       |
|----------------------------------|-------------------------------------|----------|----------------------------|-------|
|                                  | 2017                                | 2016     | \$                         | %     |
|                                  | (Dollars in Thousands)              |          |                            |       |
| Research and development expense | \$19,489                            | \$18,632 | \$ 857                     | 4.6 % |
| As a percent of total revenue    | 15.9 %                              | 15.5 %   |                            |       |

The period-over-period increase of \$0.9 million in research and development expense during the three months ended September 30, 2017 was primarily attributable to higher compensation costs of \$0.9 million related to an increase in headcount and higher stock-based compensation of \$0.8 million, partially offset by lower overhead allocations of \$0.5 million and lower costs of acquired technology of \$0.4 million.

Overhead allocations consist of information systems costs, facility costs and certain benefit costs. The overhead expenses are allocated to departments based on relative headcount, geographic location and total salary.

In the three months ended September 30, 2016, we acquired technology for \$0.4 million. At the time we acquired the technology, the projects to develop commercially available products did not meet the accounting definition of having reached technological feasibility and therefore the cost of the acquired technology was expensed as a research and development expense.

## General and Administrative Expense

|  | Three Months Ended<br>September 30, | Period-to-Period<br>Change |
|--|-------------------------------------|----------------------------|
|--|-------------------------------------|----------------------------|



|                                    | 2017                   | 2016     | \$     | %     |
|------------------------------------|------------------------|----------|--------|-------|
|                                    | (Dollars in Thousands) |          |        |       |
| General and administrative expense | \$13,676               | \$13,157 | \$ 519 | 3.9 % |
| As a percent of total revenue      | 11.1                   | % 11.0   | %      |       |

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The period-over-period increase of \$0.5 million in general and administrative expense during the three months ended September 30, 2017 was primarily attributable to higher overhead allocations of \$1.1 million, higher stock-based compensation of \$0.6 million and higher compensation costs of \$0.5 million related to an increase in headcount, partially offset by lower professional services fees of \$0.9 million, lower office-related costs of \$0.6 million and lower amortization expense of \$0.2 million.

## Interest Income

|                               | Three Months Ended     |       | Period-to-Period |         |
|-------------------------------|------------------------|-------|------------------|---------|
|                               | September 30,          |       | Change           |         |
|                               | 2017                   | 2016  | \$               | %       |
|                               | (Dollars in Thousands) |       |                  |         |
| Interest income               | \$141                  | \$272 | \$(131)          | (48.2)% |
| As a percent of total revenue | 0.1                    | % 0.2 | %                |         |

The period-over-period decrease of \$0.1 million in interest income during the three months ended September 30, 2017 was attributable to a lower level of interest income from investments.

## Interest Expense

|                               | Three Months Ended     |         | Period-to-Period |        |
|-------------------------------|------------------------|---------|------------------|--------|
|                               | September 30,          |         | Change           |        |
|                               | 2017                   | 2016    | \$               | %      |
|                               | (Dollars in Thousands) |         |                  |        |
| Interest expense              | \$(1,206)              | \$(869) | \$(337)          | 38.8 % |
| As a percent of total revenue | (1.0                   | )% (0.7 | )%               |        |

The period-over-period increase of \$0.3 million in interest expense during the three months ended September 30, 2017 was attributable to an increase in the interest rate compared to the prior fiscal year related to our outstanding borrowings, which we entered into in February 2016, as described in the "Liquidity and Capital Resources" section below.

## Other (Expense) Income, net

|                               | Three Months Ended     |        | Period-to-Period |          |
|-------------------------------|------------------------|--------|------------------|----------|
|                               | September 30,          |        | Change           |          |
|                               | 2017                   | 2016   | \$               | %        |
|                               | (Dollars in Thousands) |        |                  |          |
| Other (expense) income, net   | \$(616)                | \$646  | \$(1,262)        | (195.4)% |
| As a percent of total revenue | (0.5                   | )% 0.5 | %                |          |

During the three months ended September 30, 2017 and 2016, other (expense) income, net was comprised of \$(0.6) million and \$0.6 million of currency (losses) gains, respectively.

## Provision for Income Taxes

|                            | Three Months Ended     |           | Period-to-Period |         |
|----------------------------|------------------------|-----------|------------------|---------|
|                            | September 30,          |           | Change           |         |
|                            | 2017                   | 2016      | \$               | %       |
|                            | (Dollars in Thousands) |           |                  |         |
| Provision for income taxes | \$ 16,877              | \$ 19,779 | \$(2,902)        | (14.7)% |
| Effective tax rate         | 32.6                   | % 36.1    | %                |         |

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

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permanent differences between book and tax income. Our effective tax rate decreased to 32.6% for the three months ended September 30, 2017 compared to 36.1% for the corresponding period of the prior fiscal year due to discrete items, primarily related to lower interest expense on uncertain tax positions. The adoption of ASU 2016-09 resulted in a decrease in our provision for income taxes of \$0.5 million for the three months ended September 30, 2017. This represents a decrease in our effective tax rate of approximately 1.0 percentage point for the three months ended September 30, 2017, due to the recognition of excess tax benefits for options exercised and the vesting of equity awards.

## Liquidity and Capital Resources

## Resources

In recent years, we have financed our operations with cash generated from operating activities. As of September 30, 2017, our principal capital resources consisted of \$59.0 million in cash and cash equivalents.

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

## Credit Agreement

On February 26, 2016, we entered into the \$250.0 million Credit Agreement with various lenders. On August 9, 2017, we entered into an amendment to increase the Credit Agreement to \$350.0 million. The Credit Agreement matures on February 26, 2021. Prior to the maturity of the Credit Agreement, any amounts borrowed may be repaid and, subject to the terms and conditions of the Credit Agreement, borrowed again whole or in part without penalty. As of September 30, 2017, we had \$140.0 million in outstanding borrowings under the Credit Agreement.

For a more detailed description of the Credit Agreement, see Note 10, Credit Agreement, to our Unaudited Consolidated Financial Statements in Item 1 of this Form 10-Q.

## Cash Equivalents and Cash Flows

Our cash equivalents of \$43.9 million consisted of money market funds as of September 30, 2017. The objective of our investment policy is to manage our cash and investments to preserve principal and maintain liquidity.

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

|   | Three Months Ended     |              |
|---|------------------------|--------------|
|   | September 30,          |              |
|   | 2017                   | 2016         |
|   | (Dollars in Thousands) |              |
| Cash flow provided by (used in):          |                        |              |
| Operating activities                      | \$12,360               | \$26,250     |
| Investing activities                      | (188 )                 | (146,913 )   |
| Financing activities                      | (55,299 )              | (149,245 )   |
| Effect of exchange rates on cash balances | 156                    | (51 )        |
| Decrease in cash and cash equivalents     | \$(42,971 )            | \$(269,959 ) |

### Operating Activities

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

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Cash from operating activities provided \$12.4 million during the three months ended September 30, 2017. This amount resulted from net income of \$34.8 million, adjusted for non-cash items of \$9.0 million and net uses of cash of \$31.4 million related to changes in working capital.

Non-cash items during the three months ended September 30, 2017 consisted primarily of stock-based compensation expense of \$6.4 million and depreciation and amortization expense of \$1.8 million.

Cash used by working capital of \$31.4 million during the three months ended September 30, 2017 was primarily attributable to cash outflows related to decreases in deferred revenue of \$40.0 million (cash flows related to deferred revenue vary due to the timing of invoicing, in particular the anniversary dates of annual installments associated with multi-year software license arrangements) and increases in accounts receivable of \$0.5 million, partially offset by increases in accounts payable, accrued expenses and other current liabilities of \$6.8 million and decreases in prepaid expenses, prepaid income taxes, and other assets of \$2.3 million.

### Investing Activities

During the three months ended September 30, 2017, we used \$0.2 million of cash for investing activities. We used \$0.1 million for capital expenditures and \$0.1 million for capitalized computer software development costs.

### Financing Activities

During the three months ended September 30, 2017, we used \$55.3 million of cash for financing activities. We used \$55.1 million for repurchases of our common stock, \$1.7 million for withholding taxes on vested and settled restricted stock units, \$0.6 million for business acquisitions and \$0.4 million for issuance costs in connection with the Credit Agreement, partially offset by proceeds of \$2.4 million from the exercise of employee stock options.

### Contractual Obligations

Standby letters of credit for \$3.0 million and \$2.9 million secure our performance on professional services contracts, certain facility leases and potential liabilities as of September 30, 2017 and June 30, 2017, respectively. The letters of credit expire at various dates through fiscal 2025.

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Item 3. Quantitative and Qualitative Disclosures About Market Risk.

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

Foreign Currency Risk

During the three months ended September 30, 2017 and 2016, 9.5% and 9.9% of our total revenue was denominated in a currency other than the U.S. dollar, respectively. In addition, certain of our operating costs incurred outside the United States are denominated in currencies other than the U.S. dollar. We conduct business on a worldwide basis and as a result, a portion of our revenue, earnings, net assets, and net investments in foreign affiliates is exposed to changes in foreign currency exchange rates. We measure our net exposure for cash balance positions and for cash inflows and outflows in order to evaluate the need to mitigate our foreign exchange risk. We may enter into foreign currency forward contracts to minimize the impact related to unfavorable exchange rate movements, although we have not done so during the three months ended September 30, 2017 and 2016. Our largest exposures to foreign currency exchange rates exist primarily with the Euro, Pound Sterling, Canadian Dollar, and Japanese Yen.

During the three months ended September 30, 2017 and 2016, we recorded \$(0.6) million and \$0.6 million of net foreign currency exchange (losses) gains related to the settlement and remeasurement of transactions denominated in currencies other than the functional currency of our operating units. Our analysis of operating results transacted in various foreign currencies indicated that a hypothetical 10% change in the foreign currency exchange rates could have increased or decreased the consolidated results of operations by approximately \$0.9 million and \$1.2 million for the three months ended September 30, 2017 and 2016, respectively.

Interest Rate Risk

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

We mitigate the risks by diversifying our investment portfolio, limiting the amount of investments in debt securities of any single issuer and using a third-party investment manager. Our debt securities are short- to intermediate- term investments with maturities ranging from less than 1 month to 8 months as of September 30, 2016. We held no investments in marketable securities as of September 30, 2017. We do not use derivative financial instruments in our investment portfolio.

Our analysis of our investment portfolio and interest rates at September 30, 2016 indicated that a hypothetical 100 basis point increase or decrease in interest rates would not have a material impact on the fair value of our investment portfolio determined in accordance with an income-based approach utilizing portfolio future cash flows discounted at the appropriate rates.

We had \$140.0 million in outstanding borrowings under our Credit Agreement as of September 30, 2017. A hypothetical 10% increase or decrease in interest rates paid on outstanding borrowings under the Credit Agreement would not have a material impact on our financial position, results of operations or cash flows.





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Item 4. Controls and Procedures.

a) Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of September 30, 2017. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Securities Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Securities Exchange Act is accumulated and communicated to the Company’s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives, and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of September 30, 2017, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were effective.

b) Changes in Internal Controls Over Financial Reporting

During the three months ended September 30, 2017, no changes were identified in our internal controls over financial reporting that materially affected, or were reasonably likely to materially affect, our internal controls over financial reporting.

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## PART II - OTHER INFORMATION

## Item 1. Legal Proceedings.

Refer to Note 15, "Commitments and Contingencies," in the Notes to the Unaudited Consolidated Financial Statements for information regarding certain legal proceedings, the contents of which are herein incorporated by reference.

## Item 1A. Risk Factors.

The risks described in "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended June 30, 2017, could materially and adversely affect our business, financial condition and results of operations. These risk factors do not identify all risks that we face—our operations could also be affected by factors that are not presently known to us or that we currently consider to be immaterial to our operations. The Risk Factors section of our 2017 Annual Report on Form 10-K remains current in all material respects, with the exception of the revised risk factors below.

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

During the three months ended September 30, 2017 and 2016, 9.5% and 9.9% of our total revenue was denominated in a currency other than the U.S. dollar, respectively. In addition, certain of our operating expenses incurred outside the United States are denominated in currencies other than the U.S. dollar. Our reported revenue and operating results are subject to fluctuations in foreign exchange rates. Foreign currency risk arises primarily from the net difference between non-U.S. dollar receipts from customers outside the United States and non-U.S. dollar operating expenses for subsidiaries in foreign countries. Currently, our largest exposures to foreign exchange rates exist primarily with the Euro, Pound Sterling, Canadian dollar and Japanese Yen against the U.S. dollar. During the three months ended September 30, 2017 and 2016, we did not enter into, and were not a party to any, derivative financial instruments, such as forward currency exchange contracts, intended to manage the volatility of these market risks. We cannot predict the impact of foreign currency fluctuations, and foreign currency fluctuations in the future may adversely affect our revenue and operating results. Any hedging policies we may implement in the future may not be successful, and the cost of those hedging techniques may have a significant negative impact on our operating results.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

The following table provides information about purchases by us during the three months ended September 30, 2017 of shares of our common stock:

| Period                  | Total Number of Shares Purchased (2) | Average Price Paid per Share (3) | Total Number of Shares Purchased as Part of Publicly Announced Program (1) | Approximate Dollar Value of Shares that May Yet Be Purchased Under the Program (4) |
|-------------------------|--------------------------------------|----------------------------------|--|--|
| July 1 to 31, 2017      | 280,929                              | \$ 56.49                         | 280,929  |  |
| August 1 to 31, 2017    | 308,775                              | \$ 59.14                         | 308,775  |  |
| September 1 to 30, 2017 | 249,455                              | \$ 63.62                         | 249,455  |  |
| Total                   | 839,159                              | \$ 59.58                         | 839,159  | \$ 296,292,703   |

(1) On January 22, 2015, our Board of Directors approved a share repurchase program (the "Share Repurchase Program") for up to \$450.0 million worth of our common stock. On April 26, 2016 and June 8, 2017, the Board of Directors approved a \$400.0 million and \$200.0 million increase to the Share Repurchase Program, respectively.

(2) As of September 30, 2017, the total number of shares of common stock repurchased under all programs approved by the Board of Directors was 29,985,135.

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

(4) As of September 30, 2017, the total remaining value under the Share Repurchase Program was approximately \$296.3 million.

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## Item 6. Exhibits.

| Exhibit Number | Description   | Filed with this Form 10-Q | Incorporated by Reference |                      |                |
|----------------|---|---------------------------|---------------------------|----------------------|----------------|
|                |   |                           | Form                      | Filing Date with SEC | Exhibit Number |
| 10.7           | <u>Incremental Facility Amendment, dated as of August 9, 2017, to the Credit Agreement dated as of February 26, 2016 among Aspen Technology, Inc. as borrower, the lenders, JPMorgan Chase Bank, N.A. as administrative agent and issuing bank, and certain other Lenders acting in such capacity from time to time, as issuing banks</u> | X                         |                           |                      |                |
| 31.1           | <u>Certification of Principal Executive Officer pursuant to Exchange Act Rules 13a-14 and 15d-14, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>  | X                         |                           |                      |                |
| 31.2           | <u>Certification of Principal Financial Officer pursuant to Exchange Act Rules 13a-14 and 15d-14, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>  | X                         |                           |                      |                |
| 32.1           | <u>Certification of President and Chief Executive Officer and Executive Vice President and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u>   | X                         |                           |                      |                |
| 101.INS        | Instance Document   | X                         |                           |                      |                |
| 101.SCH        | XBRL Taxonomy Extension Schema Document   | X                         |                           |                      |                |
| 101.CAL        | XBRL Taxonomy Extension Calculation Linkbase Document   | X                         |                           |                      |                |
| 101.DEF        | XBRL Taxonomy Extension Definition Linkbase Document  | X                         |                           |                      |                |
| 101.LAB        | XBRL Taxonomy Extension Label Linkbase Document   | X                         |                           |                      |                |
| 101.PRE        | XBRL Taxonomy Extension Presentation Linkbase Document  | X                         |                           |                      |                |

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SIGNATURES

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

Aspen Technology, Inc.

Date: October 26, 2017 By: /s/ ANTONIO J. PIETRI

Antonio J. Pietri  
President and Chief Executive Officer  
(Principal Executive Officer)

Date: October 26, 2017 By: /s/ KARL E. JOHNSEN

Karl E. Johnsen  
Senior Vice President and Chief Financial Officer  
(Principal Financial and Accounting Officer)

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## EXHIBIT INDEX

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