SYNOPSYS INC
Form 10-Q
June 10, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(MARK ONE)

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

FOR THE QUARTERLY PERIOD ENDED APRIL 30, 2008

OR

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NUMBER: 0-19807

SYNOPSYS, INC.

(Exact name of registrant as specified in its charter)

DELAWARE	**56-1546236**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

700 EAST MIDDLEFIELD ROAD
MOUNTAIN VIEW, CA 94043

(Address of principal executive offices, including zip code)

(650) 584-5000

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant (l) 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 x No o

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

142,702,930 shares of Common Stock as of June 6, 2008

SYNOPSYS, INC.
QUARTERLY REPORT ON FORM 10-Q
APRIL 30, 2008
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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SYNOPSYS, INC.
UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except par value amounts)

	April 30, 2008	October 31, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	$ 574,889	$ 579,327
Short-term investments	242,609	405,126
Total cash, cash equivalents and short-term investments	817,498	984,453
Accounts receivable, net	171,993	123,900
Deferred income taxes	127,345	123,165
Income taxes receivable	42,724	42,525
Prepaid expenses and other current assets	57,337	53,496
Total current assets	1,216,897	1,327,539
Property and equipment, net	127,223	131,866
Goodwill	765,576	767,087
Intangible assets, net	54,778	78,792
Long-term deferred income taxes	168,056	216,642
Other assets	97,629	95,411
Total assets	$ 2,430,159	$ 2,617,337
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	$ 176,746	$ 246,209
Accrued income taxes	10,280	207,572
Deferred revenue	522,078	577,295
Total current liabilities	709,104	1,031,076
Deferred compensation and other liabilities	83,322	84,648
Long-term accrued income taxes	137,597	
Long-term deferred revenue	65,310	65,220
Total liabilities	995,333	1,180,944
Stockholders equity:		
Preferred Stock, $0.01 par value: 2,000 shares authorized; none outstanding		
Common Stock, $0.01 par value: 400,000 shares authorized; 141,756 and 146,365 shares outstanding, respectively	1,417	1,464
Capital in excess of par value	1,435,900	1,401,965
Retained earnings	342,424	263,977
Treasury stock, at cost: 15,512 and 10,867 shares, respectively	(348,332)	(234,918)
Accumulated other comprehensive income	3,417	3,905
Total stockholders equity	1,434,826	1,436,393
Total liabilities and stockholders equity	$ 2,430,159	$ 2,617,337

See accompanying notes to unaudited condensed consolidated financial statements.

SYNOPSYS, INC.
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

	Three Months Ended April 30,		Six Months Ended April 30,	
	2008	**2007**	**2008**	**2007**
Revenue:				
Time-based license	$ 278,220	$ 243,096	$ 546,080	$ 494,702
Upfront license	12,214	14,624	24,735	28,127
Maintenance and service	34,119	35,208	69,203	70,309
Total revenue	324,553	292,928	640,018	593,138
Cost of revenue:				
License	41,709	34,657	82,107	70,177
Maintenance and service	16,167	15,550	32,046	31,696
Amortization of intangible assets	5,816	5,210	10,849	11,919
Total cost of revenue	63,692	55,417	125,002	113,792
Gross margin	260,861	237,511	515,016	479,346
Operating expenses:				
Research and development	95,275	91,956	187,789	187,840
Sales and marketing	82,887	79,012	160,257	168,820
General and administrative	26,171	22,551	50,012	52,228
Amortization of intangible assets	6,591	6,644	13,182	13,288
Total operating expenses	210,924	200,163	411,240	422,176
Operating income	49,937	37,348	103,776	57,170
Other income, net	151	19,668	6,481	27,602
Income before income taxes	50,088	57,016	110,257	84,772
Provision for income taxes	10,701	15,751	24,425	20,150
Net income	$ 39,387	$ 41,265	$ 85,832	$ 64,622
Net income per share:				
Basic	$ 0.28	$ 0.29	$ 0.60	$ 0.45
Diluted	$ 0.27	$ 0.28	$ 0.58	$ 0.43
Shares used in computing per share amounts:				
Basic	141,844	144,370	143,926	143,527
Diluted	145,271	149,783	147,801	148,782

See accompanying notes to unaudited condensed consolidated financial statements.

SYNOPSYS, INC.
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Six Months Ended April 30, 2008	Six Months Ended April 30, 2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 85,832	$ 64,622
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Amortization and depreciation	50,244	52,676
Share-based compensation	33,486	30,565
Deferred income taxes	3,523	10,677
Provision for doubtful accounts	429	(330)
Net change in deferred gains and losses on cash flow hedges	7,495	2,990
Gain on sale of land		(4,284)
Gain on sale of short and long-term investments	(1,192)	(1)
Net changes in operating assets and liabilities, net of acquired assets and liabilities:		
Accounts receivable	(46,982)	(43,935)
Prepaid expenses and other current assets	(10,300)	(11,272)
Other assets	26	487
Accounts payable and accrued liabilities	(69,502)	(59,642)
Accrued income taxes	(2,873)	(4,592)
Deferred revenue	(67,309)	107,196
Deferred compensation and other liabilities	980	(926)
Net cash (used in) provided by operating activities	(16,143)	144,231
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sales and maturities of short-term investments	419,181	113,351
Purchases of short-term investments	(253,699)	(178,782)
Purchases of long-term investments	(6,694)	
Sales of long-term investments	77	
Purchase of property and equipment	(19,498)	(24,520)
Proceeds from sale of land		26,298
Capitalization of software development costs	(1,408)	(1,592)
Net cash provided by (used in) investing activities	137,959	(65,245)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments on lease obligations	(1,452)	
Issuances of common stock	36,949	130,240
Purchases of treasury stock	(170,052)	(81,394)
Net cash (used in) provided by financing activities	(134,555)	48,846
Effect of exchange rate changes on cash and cash equivalents	8,301	2,483
Net (decrease) increase in cash and cash equivalents	(4,438)	130,315
Cash and cash equivalents, beginning of period	579,327	330,759
Cash and cash equivalents, end of period	$ 574,889	$ 461,074

See accompanying notes to unaudited condensed consolidated financial statements.

SYNOPSYS, INC.
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Description of Business

Synopsys, Inc. (Synopsys or the Company) is a world leader in electronic design automation (EDA), supplying the global electronics market with the software, intellectual property (IP) and services used in semiconductor design and manufacturing. The Company delivers technology-leading semiconductor design and verification platforms and integrated circuit (IC) manufacturing products to the global electronics market, enabling the development and production of complex systems-on-chips (SoCs). In addition, the Company provides: (1) IP and design services to simplify the design process and accelerate time-to-market for our customers; and (2) software and services that help customers prepare and optimize their designs for manufacturing.

Note 2. Summary of Significant Accounting Policies

The Company has prepared the accompanying unaudited condensed consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission (the Commission). Pursuant to these rules and regulations, the Company has condensed or omitted certain information and footnote disclosures it normally includes in its annual consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP). In management s opinion, the Company has made all adjustments (consisting only of normal, recurring adjustments, except as otherwise indicated) necessary to fairly present its financial position, results of operations and cash flows. The Company s interim period operating results do not necessarily indicate the results that may be expected for any other interim period or for the full fiscal year. These financial statements and accompanying notes should be read in conjunction with the consolidated financial statements and notes thereto in Synopsys Annual Report on Form 10-K for the fiscal year ended October 31, 2007 on file with the Commission.

To prepare financial statements in conformity with GAAP, management must make estimates and assumptions that affect the amounts reported in the unaudited condensed consolidated financial statements and accompanying notes. Actual results could differ from these estimates and may result in material effects on the Company s operating results and financial position. There have been no significant changes in accounting policies since the filing of the Company s Annual Report on Form 10-K for the fiscal year ended October 31, 2007, other than the impact of the adoption of Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes, (FIN 48) which is disclosed in Note 12 Taxes.

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

Fiscal Year End. The Company has adopted a fiscal year ending on the Saturday nearest to October 31. The Company s second fiscal quarter ended on May 3, 2008 and May 5, 2007. Fiscal 2008 is a 52-week fiscal year and as a result, the three and six months ended April 30, 2008 had 13 weeks and 26 weeks, respectively. Fiscal 2007 was a 53-week year and the three and six months ended April 30, 2007 had 13 weeks and 27 weeks, respectively. For presentation purposes, the unaudited condensed consolidated financial statements and accompanying notes refer to the applicable calendar month end.

Note 3. Share-based Compensation

Accounting for Share-based Compensation

The Company uses the Black-Scholes option-pricing model to determine the fair value of stock options and awards under the employee stock purchase plans in accordance with Statement of Financial Accounting Standards (SFAS) No. 123 (Revised 2004), *Share-Based Payment*, (SFAS123 (R)). The Black-Scholes option-pricing model incorporates various subjective assumptions including expected volatility, expected term and interest rates. The expected volatility for both stock options and the employee stock purchase plans (ESPP) is estimated by a combination of implied volatility for publicly traded options of the Company s stock with a term of six months or longer and the historical stock price volatility over the estimated expected term of the Company s share-based awards. The expected term of the Company s share-based awards is based on historical experience.

The assumptions used to estimate the fair value of stock options granted and employee stock purchase rights granted under the Company s stock option plans and ESPP for the three and six months ended April 30, 2008 and 2007 are as follows:

	Three Months Ended April 30, 2008	**2007**	**Six Months Ended April 30, 2008**	**2007**
Options				
Volatility	32.81% - 34.61%	30.27% - 30.77%	32.81% - 34.61%	30.27% - 32.11%
Expected term (years)	4.5	4.3	4.5	4.3
Risk-free interest rate	2.40% - 2.85%	4.47% - 4.62%	2.40% - 3.55%	4.35% - 4.73%
Expected dividend yield	0%	0%	0%	0%
Weighted average grant date fair value	$7.77	$8.50	$8.26	$8.57
ESPP				
Volatility	19.61% - 32.06%	19.61% - 44.85%	19.61% - 32.06%	19.61% - 44.85%
Expected term (years)	0.5 - 2.0	0.5 - 2.0	0.5 - 2.0	0.5 - 2.0
Risk-free interest rate	1.62% - 5.09%	3.58% - 5.09%	1.62% - 5.09%	3.58% - 5.09%
Expected dividend yield	0%	0%	0%	0%
Weighted average grant date fair value	$5.93	$6.43	$5.93	$6.43

The Company also granted restricted stock units as part of the Company s new hire and annual incentive compensation program starting in fiscal 2007. Restricted stock units are valued based on the closing price of the Company s common stock on the grant date. In general, restricted stock units vest over three to four years and are subject to the employees continuing service to the Company. During the three and six months ended April 30, 2008, the weighted average grant date fair values were $24.22 and $27.07 per share, respectively. During the three and six months ended April 30, 2007, the weighted average grant date fair values were $27.01 and $26.85 per share, respectively.

As of April 30, 2008, there was $96.6 million of unamortized share-based compensation expense which is expected to be amortized over a weighted-average period of approximately 3.6 years. The intrinsic values of options exercised during the three and six months ended April 30, 2008 were $3.6 million and $8.7 million, respectively. The intrinsic values of options exercised during the three and six months ended April 30, 2007 were $14.9 million and $47.6 million, respectively.

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

	Three Months Ended April 30,				**Six Months Ended April 30,**			
(in thousands)		**2008**		**2007**		**2008**		**2007**
Cost of license	$	2,296	$	1,621	$	3,624	$	3,473
Cost of maintenance and service		810		572		2,152		1,353
Research and development expense		7,444		5,875		13,863		10,602
Sales and marketing expense		4,351		3,645		8,051		9,311
General and administrative expense		2,940		2,636		5,796		5,826
Share-based compensation expense before taxes		17,841		14,349		33,486		30,565
Income tax benefit		(4,184)		(3,428)		(7,852)		(7,323)
Share-based compensation expense after taxes	$	13,657	$	10,921	$	25,634	$	23,242

Note 4. Stock Repurchase Program

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

During the three and six months ended April 30, 2008, the Company purchased 3.8 million shares at an average price of $23.06 per share, and 7.2 million shares at an average price of $23.64 per share, respectively. During the three and six months ended April 30, 2007, the Company purchased 2.4 million shares at an average price of $26.38 per share, and 3.1 million shares at an average price of $26.45 per share, respectively. The aggregate purchase prices were $170.1 million and $81.4 million in the six months ended April 30, 2008 and 2007, respectively. During the three and six months ended April 30, 2008, approximately 1.8 million and 2.5 million shares were reissued, respectively, for employee share-based compensation requirements. During the three and six months ended April 30, 2007, approximately 2.8 million and 7.2 million shares were reissued, respectively, for employee share-based compensation requirements. On March 22, 2007 the Board replenished the stock repurchase program to $500.0 million. As of April 30, 2008, $259.7 million remained available for further purchases under the program.

Note 5. Goodwill and Intangible Assets

Goodwill as of April 30, 2008 consisted of the following:

		(in thousands)
Balance at October 31, 2007	$	767,087
Adjustments (1)		(1,511)
Balance at April 30, 2008	$	765,576

(1) Related to income taxes and payment of a contingent consideration.

Intangible assets as of April 30, 2008 consisted of the following:

	Gross Assets	Accumulated Amortization (in thousands)	Net Assets
Core/developed technology	$ 112,655	$ 77,004	$ 35,651
Customer relationships	144,950	130,865	14,085
Contract rights intangible	8,000	6,638	1,362
Covenants not to compete	3,690	3,387	303
Trademarks and tradenames	200	70	130
Capitalized software development costs	17,879	14,632	3,247
Total (1)	$ 287,374	$ 232,596	$ 54,778

(1) Balance does not include intangible assets that were fully amortized prior to fiscal 2008.

Intangible assets as of October 31, 2007 consisted of the following:

	Gross Assets	Accumulated Amortization (in thousands)	Net Assets
Core/developed technology	$ 112,655	$ 67,088	$ 45,567
Customer relationships	144,950	118,471	26,479
Contract rights intangible	8,000	5,271	2,729
Covenants not to compete	3,690	3,054	636
Trademarks and tradenames	200	50	150
Other intangibles	8,383	8,383	
Capitalized software development costs	16,414	13,183	3,231
Total	$ 294,292	$ 215,500	$ 78,792

Total amortization expense related to intangible assets consisted of the following:

	Three Months Ended April 30,		Six Months Ended April 30,	
	2008	2007	2008	2007
		(in thousands)		
Core/developed technology	$ 5,354	$ 4,170	$ 9,916	$ 9,840
Customer relationships	6,197	6,134	12,394	12,268
Contract rights intangible	679	517	1,367	1,033
Covenant not to compete	166	283	333	565
Trademarks and tradenames	10	10	20	20
Other intangibles		740		1,480
Capitalized software development costs	721	832	1,449	1,642
Total	$ 13,127	$ 12,686	$ 25,479	$ 26,848

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

		(in thousands)
Fiscal Years:		
Remainder of fiscal 2008	$	15,665
2009		22,822
2010		9,847
2011		3,866
2012		1,671
2013 and thereafter		907
Total	$	54,778

Note 6. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities consist of:

		April 30, 2008		October 31, 2007
		(in thousands)		
Accounts payable	$	8,506	$	11,611
Payroll and related benefits		130,383		192,773
Acquisition related costs		2,463		3,221
Other accrued liabilities		35,394		38,604
Total	$	176,746	$	246,209

Note 7. Credit Facility

On October 20, 2006, the Company entered into a five-year, $300.0 million senior unsecured revolving credit facility providing for loans to the Company and certain of its foreign subsidiaries. The amount of the facility may be increased by up to an additional $150.0 million through the fourth year of the facility. The facility contains financial covenants requiring the Company to maintain a minimum leverage ratio and specified levels of cash, as well as other non-financial covenants. The facility terminates on October 20, 2011. Borrowings under the facility bear interest at the greater of the administrative agent s prime rate or the federal funds rate plus 0.50%; however, the Company has the option to pay interest based on the outstanding amount at Eurodollar rates plus a spread between 0.50% and 0.70% based on a pricing grid tied to a financial covenant. In addition, commitment fees are payable on the facility at rates between 0.125% and 0.175% per year based on a pricing grid tied to a financial covenant. As of April 30, 2008, the Company had no outstanding borrowings under this credit facility and was in compliance with all the covenants.

Note 8. Comprehensive Income

The following table sets forth the components of comprehensive income, net of tax:

	Three Months Ended April 30,				Six Months Ended April 30,			
	2008		2007		2008		2007	
	(in thousands)							
Net income	$	39,387	$	41,265	$	85,832	$	64,622
Change in unrealized (losses) gains on investments, net of tax of $1,275 and $598 for three and six months ended April 30, 2008, respectively, and of ($111) and ($49) for each of the same periods in fiscal 2007, respectively		(1,932)		165		(906)		73
Deferred gains on cash flow hedges, net of tax of ($758) and ($1,537), for three and six months ended April 30, 2008, respectively, and of ($37) and ($507) for each of the same periods in fiscal 2007, respectively		3,854		1,648		5,958		2,483
Reclassification adjustment on deferred (gains) losses on cash flow hedges, net of tax of $921 and $1,109, for three and six months ended April 30, 2008, respectively, and of ($64) and ($165) for each of the same periods in fiscal 2007, respectively		(3,010)		118		(4,110)		295
Foreign currency translation adjustment		943		3,286		(1,431)		3,800
Total	$	39,242	$	46,482	$	85,343	$	71,273

Note 9. Net Income per Share

In accordance with SFAS No. 128, *Earnings per Share* (SFAS 128), the Company computes basic income per share by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted net income per share reflects the dilution of potential common shares outstanding such as stock options and unvested restricted stock units and awards during the period using the treasury stock method.

The table below reconciles the weighted-average common shares used to calculate basic net income per share with the weighted-average common shares used to calculate diluted net income per share.

	Three Months Ended April 30,				Six Months Ended April 30,			
	2008		2007		2008		2007	
	(in thousands)							
Numerator:								
Net income	$	39,387	$	41,265	$	85,832	$	64,622

	Three Months Ended April 30, 2008	Three Months Ended April 30, 2007	Six Months Ended April 30, 2008	Six Months Ended April 30, 2007
	(in thousands)			
Denominator:				
Weighted-average common shares for basic net income per share	141,844	144,370	143,926	143,527
Dilutive effect of common share equivalents from equity-based compensation	3,427	5,413	3,875	5,255
Weighted-average common shares for diluted net income per share	145,271	149,783	147,801	148,782

	Three Months Ended April 30, 2008	Three Months Ended April 30, 2007	Six Months Ended April 30, 2008	Six Months Ended April 30, 2007
Net income per share:				
Basic	$ 0.28	$ 0.29	$ 0.60	$ 0.45
Diluted	$ 0.27	$ 0.28	$ 0.58	$ 0.43

Diluted net income per share excludes 13.0 million and 6.3 million of anti-dilutive stock options and unvested restricted stock units and awards for the three months ended April 30, 2008 and 2007, respectively; and 9.8 million and 8.9 million of anti-dilutive options and unvested restricted stock units and awards for the six months ended April 30, 2008 and 2007, respectively. While these stock options and unvested restricted stock units and awards were anti-dilutive for the respective periods, they could be dilutive in the future.

Note 10. Segment Disclosure

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

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

Revenues related to operations in the United States and other geographic areas were:

	Three Months Ended April 30,		Six Months Ended April 30,	
	2008	**2007**	**2008**	**2007**
	(in thousands)			
Revenue:				