

PARAMETRIC TECHNOLOGY CORP

Form 10-Q/A

December 11, 2007

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**AMENDMENT NO. 1  
TO  
FORM 10-Q**

**QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended March 31, 2007  
Commission File Number: 0-18059**

**Parametric Technology Corporation  
(Exact name of registrant as specified in its charter)**

**Massachusetts  
(State or other jurisdiction of  
incorporation or organization)**

**04-2866152  
(I.R.S. Employer  
Identification Number)**

**140 Kendrick Street, Needham, MA 02494  
(Address of principal executive offices, including zip code)  
(781) 370-5000**

**(Registrant's telephone number, including area code)**

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

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

Large Accelerated Filer  Accelerated Filer  Non-accelerated Filer

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

There were 114,859,675 shares of our common stock outstanding on May 4, 2007.

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**EXPLANATORY NOTE**

***Items Amended by this Form 10-Q/A***

This Amendment No. 1 ( Form 10-Q/A ) to our Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2007 as originally filed with the Securities and Exchange Commission ( SEC ) on May 10, 2007 (the Original Form 10-Q ) amends certain sections of the Original Form 10-Q to reflect the restatement of our unaudited consolidated financial statements (and related disclosures) as of March 31, 2007 and September 30, 2006 and for the three and six months ended March 31, 2007 and April 1, 2006 described below. With this Form 10-Q/A, we are amending:

Part I, Item 1 Unaudited Financial Statements;

Part I, Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations; and This Form 10-Q/A also includes updated certifications from our Chief Executive Officer and Chief Financial Officer required by Sections 302 and 906 of the Sarbanes-Oxley Act of 2002. The updated certifications are included in this Form 10-Q/A as Exhibits 31.1, 31.2 and 32.

This Form 10-Q/A makes only the changes described above and does not modify or update such items in any other respect, or any other items or disclosures presented in the Original Form 10-Q. Further, this Form 10-Q/A does not reflect any other events occurring after May 10, 2007, the date we filed the Original Form 10-Q. Accordingly, this Form 10-Q/A should be read in conjunction with our filings made with the SEC since the filing date of the Original Form 10-Q, including our Current Reports on Form 8-K, our Annual Report on Form 10-K for the year ended September 30, 2007, and the amendments to our Quarterly Reports on Form 10-Q for the quarterly periods ended December 30, 2006 and June 30, 2007.

***Restatement of Prior Period Financial Statements***

In our Annual Report on Form 10-K for fiscal 2007, filed on November 29, 2007, we restated our consolidated financial statements as of September 30, 2006 and for the years ended September 30, 2006 and 2005 as well as our consolidated financial statements (excluding footnotes) for the quarterly periods in fiscal 2007 and 2006, as included in Item 8 Financial Statements and Supplementary Data. With the filing of this Form 10-Q/A, we are concurrently filing amendments to our Quarterly Reports on Form 10-Q for the quarterly periods ended December 30, 2006 and June 30, 2007, as originally filed with the SEC, to restate our unaudited financial statements and related financial information for those periods and the comparative 2006 periods for the effects of the restatement.

We do not intend to file any other amended Annual Reports on Form 10-K or Quarterly Reports on Form 10-Q for periods affected by the restatement. For this reason, the Consolidated Financial Statements and related financial information contained in any of our filings with the SEC prior to November 29, 2007 should no longer be relied upon.

***Background of the Restatement***

As a result of an independent investigation led by the Audit Committee of our Board of Directors, the Audit Committee concluded on October 29, 2007 that we would need to restate our previously issued financial statements for the effect of certain transactions involving Toshiba Corporation of Japan ( Toshiba ), for which we recorded revenue of approximately \$41 million during fiscal 2001 through 2006. Based on its investigation, the Audit Committee concluded that the understanding of the arrangement was not fully reflected in the order paperwork for these transactions because there were additional circumstances known or knowable by one or more of our personnel in Japan. That condition required us to change our conclusion that the transactions met the revenue recognition criteria of Statement of Position 97-2, *Software Revenue Recognition*.

The results of the investigation indicate that during the period 2001 to 2006, an employee of Toshiba Corporation initiated purchases of both software and services from our subsidiary in Japan, PTC Japan K.K. ( PTC Japan ). Many of these purchases were completed through a third party trading company that procured the software and services on Toshiba's behalf. The transactions were supported by orders that were signed by employees of Toshiba

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and the third party trading company. PTC Japan delivered the items for which revenue was recorded and was paid for the orders in question. The Toshiba employee also allegedly entered into a series of financing agreements with third party leasing companies, including GE Capital Leasing Corporation of Japan ( GECL ), in the name of Toshiba to fund various purchases. As part of those transactions, the leasing companies allegedly entered into transactions with various third party trading companies to procure the purchased items on behalf of Toshiba. We were not a party to those financing agreements. Toshiba has disclaimed responsibility for repayment of these financed amounts and has alleged that the Toshiba employee who entered into the financing agreements was not authorized to do so and that Toshiba did not receive delivery of the items so financed.

Recently, the Toshiba employee involved in the transactions was arrested and charged with defrauding certain of the leasing companies. Among the allegations against him are that he forged contracts in the name of Toshiba. In addition, three individuals each employed by a different trading company involved in the transactions have been arrested for alleged involvement in a scheme to defraud the leasing companies. According to published news reports, the Toshiba employee and these other individuals are suspected of diverting some of the proceeds of the financings to a bank account controlled by one or more of them. Following these arrests, it was reported on October 23, 2007 that two former employees of PTC Japan were arrested on suspicion of demanding hush money from one of the participants in the fraudulent scheme. The press accounts indicate that the former PTC Japan employees who left employment with PTC Japan in 2003 and 2004, respectively were no longer working at PTC Japan at the time of the alleged demands. According to the press accounts, these individuals have not been charged with participating in the alleged underlying fraud.

To effect the restatement of revenue associated with the transactions placed by the Toshiba employee, we reduced previously recorded revenue by approximately \$8 million in fiscal 2006, \$15 million in fiscal 2005, \$9 million in fiscal 2004, \$2 million in fiscal 2003 and \$7 million in prior years, and recorded related income tax effects. We did not make any adjustments to the costs incurred in connection with these transactions due to the uncertainty regarding our ultimate ability to retain the advances received for these transactions and our belief that all such costs are unrecoverable. Upon restatement, the revenue reversed from those prior periods was deferred and classified as Customer Advances in our consolidated balance sheets. That liability (which totaled \$39.5 million at both March 31, 2007 and September 30, 2006, respectively, after the effects of foreign currency movements) will remain recorded until the rights and obligations of the several companies connected with the Toshiba transactions are resolved. To the extent that matters are resolved in our favor, we will reduce Customer Advances and record revenue or other income at that time.

Our restatement of prior period financial statements also includes adjustments for other previously identified errors that we had corrected in the periods they became known to us rather than in the periods in which they originated because we believed that the amounts of such errors, individually and in the aggregate, were not material to our financial statements for the affected periods. In this restatement, we have now recorded those corrections in the periods in which each error originated. Such adjustments, which have been tax effected, primarily relate to (i) recording rent expense on a straight-line basis for one of our office facilities, (ii) recording stock-based compensation expense due to the timing of approvals for certain stock options we granted, (iii) deferring or reversing revenue for certain customer orders in the Asia-Pacific region, and (iv) reversing an income tax reserve that was unwarranted when established.

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A summary of the cumulative revenue and net income effects of the restatement on our consolidated financial statements is as follows:

	<b>Year ended September 30,</b>				<b>Prior</b>
	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>	<b>Years</b>
	<b>(in thousands, except per share data)</b>				
Revenue, as previously reported	\$ 854,918	\$ 720,719	\$ 660,029	\$ 671,940	
Adjustments	(6,935)	(12,744)	(8,361)	(2,487)	\$ (10,506)
Revenue, as restated	\$ 847,983	\$ 707,975	\$ 651,668	\$ 669,453	
Net income (loss), as previously reported	\$ 60,866	\$ 83,592	\$ 34,813	\$ (98,280)	
Adjustments	(4,062)	(10,405)	(3,228)	(2,907)	\$ (12,927)
Net income (loss), as restated	\$ 56,804	\$ 73,187	\$ 31,585	\$ (101,187)	
Earnings (loss) per share Diluted, as previously reported	\$ 0.54	\$ 0.75	\$ 0.32	\$ (0.93)	
Adjustments	(0.04)	(0.10)	(0.03)	(0.03)	
Earnings (loss) per share Diluted, as restated	\$ 0.50	\$ 0.65	\$ 0.29	\$ (0.96)	

The adjustments made as a result of the restatement are more fully described in Note 2 to our consolidated financial statements included in Part I, Item 1 Unaudited Financial Statements of this Form 10-Q/A.

**PARAMETRIC TECHNOLOGY CORPORATION**  
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**For the Quarter Ended March 31, 2007**

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**PART I FINANCIAL INFORMATION**  
**ITEM 1. UNAUDITED FINANCIAL STATEMENTS**  
**PARAMETRIC TECHNOLOGY CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**  
(in thousands, except per share data)  
**(unaudited)**

	<b>March 31, 2007 Restated Note 2</b>	<b>September 30, 2006 Restated Note 2</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 238,027	\$ 183,448
Accounts receivable, net of allowance for doubtful accounts of \$3,760 and \$4,900 at March 31, 2007 and September 30, 2006, respectively	185,002	181,008
Prepaid expenses	24,779	20,495
Other current assets (Note 1)	65,907	51,824
Deferred tax assets	1,728	1,341
<b>Total current assets</b>	<b>515,443</b>	<b>438,116</b>
Property and equipment, net	52,284	51,603
Goodwill	262,936	249,252
Acquired intangible assets, net	79,256	77,870
Deferred tax assets	7,372	9,148
Other assets	68,844	75,398
<b>Total assets</b>	<b>\$ 986,135</b>	<b>\$ 901,387</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 17,965	\$ 17,109
Accrued expenses and other current liabilities	52,791	52,128
Accrued compensation and benefits	57,497	72,632
Accrued income taxes	8,954	5,761
Customer advances (Note 2)	39,510	39,475
Deferred revenue (Note 1)	240,475	197,769
<b>Total current liabilities</b>	<b>417,192</b>	<b>384,874</b>
Other liabilities (Note 3)	96,957	97,413
Deferred revenue (Note 1)	9,615	13,228
Commitments and contingencies (Note 11)		
Stockholders' equity:		
Preferred stock, \$0.01 par value; 5,000 shares authorized; none issued		
Common stock, \$0.01 par value; 500,000 shares authorized; 114,799 and 111,880 shares issued and outstanding at March 31, 2007 and September 30,	1,148	1,119

2006, respectively		
Additional paid-in capital	1,745,614	1,723,570
Accumulated deficit	(1,243,669)	(1,276,221)
Accumulated other comprehensive loss	(40,722)	(42,596)
Total stockholders' equity	462,371	405,872
Total liabilities and stockholders' equity	\$ 986,135	\$ 901,387

The accompanying notes are an integral part of the consolidated financial statements.



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**PARAMETRIC TECHNOLOGY CORPORATION**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(in thousands, except per share data)  
(unaudited)

	Three months ended		Six months ended	
	March 31, 2007	April 1, 2006 Restated Note 2	March 31, 2007	April 1, 2006 Restated Note 2
Revenue:				
License	\$ 71,336	\$ 54,172	\$ 137,924	\$ 113,152
Service	156,760	141,097	311,839	274,969
Total revenue	228,096	195,269	449,763	388,121
Costs and expenses:				
Cost of license revenue	4,211	1,889	7,771	5,192
Cost of service revenue	68,614	63,641	137,182	122,642
Sales and marketing	71,560	64,260	141,121	128,184
Research and development	40,153	35,989	78,137	70,572
General and administrative	20,711	18,039	39,634	37,668
Amortization of acquired intangible assets	1,588	1,288	3,676	2,646
Total costs and expenses	206,837	185,106	407,521	366,904
Operating income	21,259	10,163	42,242	21,217
Other income (expense), net	1,348	804	2,128	1,903
Income before income taxes	22,607	10,967	44,370	23,120
Provision for income taxes	5,208	4,409	11,818	9,209
Net income	\$ 17,399	\$ 6,558	\$ 32,552	\$ 13,911
Earnings per share Basic (Note 5)	\$ 0.15	\$ 0.06	\$ 0.29	\$ 0.13
Earnings per share Diluted (Note 5)	\$ 0.15	\$ 0.06	\$ 0.28	\$ 0.12
Weighted average shares outstanding Basic	112,845	109,739	112,337	109,560
Weighted average shares outstanding Diluted	117,486	113,403	117,384	112,985

The accompanying notes are an integral part of the consolidated financial statements.

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**PARAMETRIC TECHNOLOGY CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in thousands)  
(unaudited)

	<b>Six months ended</b>	
	<b>March</b>	<b>April 1,</b>
	<b>31,</b>	<b>2006</b>
	<b>2007</b>	<b>Restated</b>
		<b>Note 2</b>
Cash flows from operating activities:		
Net income	\$ 32,552	\$ 13,911
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	19,223	16,124
Stock-based compensation	17,477	19,204
Other non-cash costs (credits), net	1,529	264
Changes in operating assets and liabilities, net of effects of acquisitions:		
Accounts receivable	14,732	5,721
Accounts payable and accrued expenses	(3,122)	(10,304)
Customer advances		5,341
Accrued compensation and benefits	(17,932)	(17,872)
Deferred revenue	21,004	20,561
Accrued income taxes	3,072	(5,069)
Other current assets and prepaid expenses	(2,877)	(437)
Other noncurrent assets and liabilities	(9,535)	(7,970)
Net cash provided by operating activities	76,123	39,474
Cash flows from investing activities:		
Additions to property and equipment	(12,393)	(8,154)
Acquisitions of businesses, net of cash acquired	(17,639)	(10,675)
Net cash used by investing activities	(30,032)	(18,829)
Cash flows from financing activities:		
Proceeds from issuance of common stock	10,889	2,902
Payments of withholding taxes in connection with settlement of restricted stock units	(6,486)	(102)
Tax benefit from stock-based awards	194	
Credit facility origination costs		(881)
Payments of capital lease obligations	(244)	(220)
Net cash provided by financing activities	4,353	1,699
Effect of exchange rate changes on cash and cash equivalents	4,135	(2,602)
Net increase in cash and cash equivalents	54,579	19,742
Cash and cash equivalents, beginning of period	183,448	204,423

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Cash and cash equivalents, end of period	\$ 238,027	\$ 224,165
Supplemental disclosures of cash flow information:		
Property and equipment acquired under capital leases	\$	\$ 243

The accompanying notes are an integral part of the consolidated financial statements.

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**PARAMETRIC TECHNOLOGY CORPORATION**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
(in thousands)  
(unaudited)

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>March 31, 2007 Restated Note 2</b>	<b>April 1, 2006 Restated Note 2</b>	<b>March 31, 2007 Restated Note 2</b>	<b>April 1, 2006 Restated Note 2</b>
Net income	\$ 17,399	\$ 6,558	\$ 32,552	\$ 13,911
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustment, net of tax of \$0	338	446	2,554	851
Change in unrealized gain on investment securities, net of tax of \$0	(655)	(560)	(680)	(233)
Other comprehensive income (loss)	(317)	(114)	1,874	618
Comprehensive income	\$ 17,082	\$ 6,444	\$ 34,426	\$ 14,529

The accompanying notes are an integral part of the consolidated financial statements.

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**PARAMETRIC TECHNOLOGY CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. Basis of Presentation**

The accompanying unaudited consolidated financial statements include the accounts of Parametric Technology Corporation (PTC) and its wholly owned subsidiaries and have been prepared by management in accordance with accounting principles generally accepted in the United States of America and in accordance with the rules and regulations of the Securities and Exchange Commission regarding interim financial reporting. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. While we believe that the disclosures presented are adequate to make the information not misleading, these unaudited quarterly financial statements should be read in conjunction with our 2006 annual consolidated financial statements and related notes (as restated) included in our Annual Report on Form 10-K for the fiscal year ended September 30, 2007. A reclassification of \$8.4 million and \$5.7 million from accounts payable to accrued expenses and other current liabilities has been made in the March 31, 2007 and September 30, 2006 consolidated balance sheets, respectively, for consistent presentation. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments, consisting only of those of a normal recurring nature, necessary for a fair statement of our financial position, results of operations and cash flows at the dates and for the periods indicated. Unless otherwise indicated, all references to a year reflect our fiscal year, which ends on September 30. The year-end consolidated balance sheet is derived from our audited financial statements.

Deferred revenue primarily relates to software maintenance agreements billed to customers for which the services have not yet been provided. The liability associated with performing these services is included in deferred revenue and the related customer receivable, if not yet paid, is included in other current assets. Billed but uncollected maintenance-related amounts included in other current assets at March 31, 2007 and September 30, 2006 were \$63.7 million and \$50.0 million, respectively.

The results of operations for the three and six months ended March 31, 2007 are not necessarily indicative of the results expected for the remainder of the fiscal year.

**2. Restatement of Consolidated Financial Statements**

In this Form 10-Q/A, we are restating our consolidated balance sheets as of March 31, 2007 and September 30, 2006, our consolidated statement of operations for the three and six months ended April 1, 2006, our condensed consolidated statement of cash flows for the six months ended April 1, 2006, and our consolidated statements of comprehensive income for the three and six months ended March 31, 2007 and April 1, 2006, as well as all related footnotes.

As a result of an independent investigation led by the Audit Committee of our Board of Directors, the Audit Committee concluded on October 29, 2007 that we would need to restate our previously issued financial statements for the effect of certain transactions involving Toshiba Corporation of Japan ( Toshiba ), for which we recorded revenue of approximately \$41 million during fiscal 2001 through 2006. Based on its investigation, the Audit Committee concluded that the understanding of the arrangement was not fully reflected in the order paperwork for these transactions because there were additional circumstances known or knowable by one or more of our personnel in Japan. That condition required us to change our conclusion that the transactions met the revenue recognition criteria of Statement of Position 97-2, *Software Revenue Recognition*.

The results of the investigation indicate that during the period 2001 to 2006, an employee of Toshiba Corporation initiated purchases of both software and services from our subsidiary in Japan, PTC Japan K.K. ( PTC Japan ). Many of these purchases were completed through a third party trading company that procured the software and services on Toshiba's behalf. The transactions were supported by orders that were signed by employees of Toshiba and the third party trading company. PTC Japan delivered the items for which revenue was recorded and was paid for the orders in question. The Toshiba employee also allegedly entered into a series of financing agreements with third party leasing companies, including GE Capital Leasing Corporation of Japan ( GECL ), in the name of Toshiba to fund various purchases. As part of those transactions, the leasing companies allegedly entered into transactions with various third party trading companies to procure the purchased items on behalf of Toshiba. We



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were not a party to those financing agreements. Toshiba has disclaimed responsibility for repayment of these financed amounts and has alleged that the Toshiba employee who entered into the financing agreements was not authorized to do so and that Toshiba did not receive delivery of the items so financed.

Recently, the Toshiba employee involved in the transactions was arrested and charged with defrauding certain of the leasing companies. Among the allegations against him are that he forged contracts in the name of Toshiba. In addition, three individuals each employed by a different trading company involved in the transactions have been arrested for alleged involvement in a scheme to defraud the leasing companies. According to published news reports, the Toshiba employee and these other individuals are suspected of diverting some of the proceeds of the financings to a bank account controlled by one or more of them. Following these arrests, it was reported on October 23, 2007 that two former employees of PTC Japan were arrested on suspicion of demanding hush money from one of the participants in the fraudulent scheme. The press accounts indicate that the former PTC Japan employees who left employment with PTC Japan in 2003 and 2004, respectively were no longer working at PTC Japan at the time of the alleged demands. According to the press accounts, these individuals have not been charged with participating in the alleged underlying fraud.

To effect the restatement of revenue associated with the transactions placed by the Toshiba employee (the Revenue Adjustment ), we reduced previously recorded revenue by \$7.7 million in fiscal 2006, \$15.5 million in fiscal 2005, \$8.5 million in fiscal 2004, \$2.1 million in fiscal 2003 and \$7.1 million in prior years, and recorded related income tax effects. We did not make any adjustments to the costs incurred in connection with these transactions due to the uncertainty regarding our ultimate ability to retain the advances received for these transactions and our belief that all such costs are unrecoverable. Upon restatement, the revenue reversed from those prior periods was deferred and classified as Customer Advances in our consolidated balance sheets. That liability (which totaled \$39.5 million at both March 31, 2007 and September 30, 2006, respectively, after the effects of foreign currency movements) will remain recorded until the rights and obligations of the several companies connected with the Toshiba transactions are resolved. To the extent that matters are resolved in our favor, we will reduce Customer Advances and record revenue or other income at that time.

Our restatement of prior period financial statements also includes adjustments for other previously identified errors that we had corrected in the periods they became known to us rather than in the periods in which they originated because we believed that the amounts of such errors, individually and in the aggregate, were not material to our financial statements for the affected periods. In this restatement, we have now recorded those corrections in the periods in which each error originated. Such adjustments (the Other Adjustments ), which have been tax effected, primarily relate to (i) deferring or reversing revenue for certain customer orders in the Asia-Pacific region and (ii) reversing an income tax reserve that was unwarranted when established.

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The following tables present the effect of the restatement adjustments by financial statement line item for our consolidated balance sheets as of March 31, 2007 and September 30, 2006, our consolidated statements of operations for the three and six months ended April 1, 2006, our consolidated statement of cash flows for the six months ended April 1, 2006, and our consolidated statements of comprehensive income for the three and six months ended March 31, 2007 and April 1, 2006:

Consolidated Balance Sheet	As Reported	March 31, 2007		Restated
		Revenue Adjustment (in thousands)	Other Adjustments(1)	
<b>ASSETS</b>				
Current assets:				
Cash and cash equivalents	\$ 238,027	\$	\$	\$ 238,027
Accounts receivable	185,002			185,002
Prepaid expenses	24,779			24,779
Other current assets	65,907			65,907
Deferred tax assets	1,728			1,728
Total current assets	515,443			515,443
Property and equipment, net	52,284			52,284
Goodwill	262,936			262,936
Acquired intangible assets, net	79,256			79,256
Deferred tax assets	1,420	5,952		7,372
Other assets	68,844			68,844
Total assets	\$ 980,183	\$ 5,952	\$	\$ 986,135
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>				
Current liabilities:				
Accounts payable	\$ 17,965	\$	\$	\$ 17,965
Accrued expenses and other current liabilities	52,791			52,791
Accrued compensation and benefits	57,497			57,497
Accrued income taxes	10,259		(1,305)	8,954
Customer advances		39,510		39,510
Deferred revenue	240,475			240,475
Total current liabilities	378,987	39,510	(1,305)	417,192
Other liabilities	96,957			96,957
Deferred revenue	9,615			9,615
Stockholders' equity:				
Common stock	1,148			1,148
Additional paid-in capital	1,745,614			1,745,614
Accumulated deficit	(1,210,140)	(34,834)	1,305	(1,243,669)
Accumulated other comprehensive loss	(41,998)	1,276		(40,722)
Total stockholders' equity	494,624	(33,558)	1,305	462,371



Total liabilities and stockholders equity	\$ 980,183	\$ 5,952	\$	\$ 986,135
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(1) Consists of the effect of the correction we made in 2007 to reverse an income tax reserve that was unwarranted when established in 2004.

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<b>Consolidated Balance Sheet</b>	<b>As Reported</b>	<b>September 30, 2006</b>		<b>Restated</b>
		<b>Revenue Adjustment</b>	<b>Other Adjustments(1)</b>	
		<b>(in thousands)</b>		
<b>ASSETS</b>				
Current assets:				
Cash and cash equivalents	\$ 183,448	\$	\$	\$ 183,448
Accounts receivable	181,008			181,008
Prepaid expenses	20,495			20,495
Other current assets	51,824			51,824
Deferred tax assets	1,341			1,341
Total current assets	438,116			438,116
Property and equipment, net	51,603			51,603
Goodwill	249,252			249,252
Acquired intangible assets, net	77,870			77,870
Deferred tax assets	3,205	5,943		9,148
Other assets	75,398			75,398
Total assets	\$ 895,444	\$ 5,943	\$	\$ 901,387
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>				
Current liabilities:				
Accounts payable	\$ 17,109	\$	\$	\$ 17,109
Accrued expenses and other current liabilities	52,128			52,128
Accrued compensation and benefits	72,632			72,632
Accrued income taxes	7,066		(1,305)	5,761
Customer advances		39,475		39,475
Deferred revenue	197,769			197,769
Total current liabilities	346,704	39,475	(1,305)	384,874
Other liabilities	97,413			97,413
Deferred revenue	13,228			13,228
Stockholders' equity:				
Common stock	1,119			1,119
Additional paid-in capital	1,723,570			1,723,570
Accumulated deficit	(1,242,692)	(34,834)	1,305	(1,276,221)
Accumulated other comprehensive loss	(43,898)	1,302		(42,596)
Total stockholders' equity	438,099	(33,532)	1,305	405,872
Total liabilities and stockholders' equity	\$ 895,444	\$ 5,943	\$	\$ 901,387

(1) Consists of the effect of the

correction we  
made in 2007 to  
reverse an  
income tax  
reserve that was  
unwarranted  
when  
established in  
2004.

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<b>Consolidated Statement of Operations</b>	<b>Three months ended April 1, 2006(1)</b>			
		<b>Revenue</b>	<b>Other</b>	
	<b>As Reported</b>	<b>Adjustment</b>	<b>Adjustments</b>	<b>Restated</b>
	<b>(in thousands, except per share data)</b>			
Revenue:				
License	\$ 54,614	\$ (442)	\$	\$ 54,172
Service	145,580	(4,483)		141,097
Total revenue	200,194	(4,925)		195,269
Costs and expenses:				
Cost of license revenue	1,889			1,889
Cost of service revenue	63,641			63,641
Sales and marketing	64,260			64,260
Research and development	35,989			35,989
General and administrative	18,039			18,039
Amortization of acquired intangible assets	1,288			1,288
Total costs and expenses	185,106			185,106
Operating income (loss)	15,088	(4,925)		10,163
Other income (expense), net	804			804
Income (loss) before income taxes	15,892	(4,925)		10,967
Provision for (benefit from) income taxes	5,141	(732)		4,409
Net income (loss)	\$ 10,751	\$ (4,193)	\$	\$ 6,558
Earnings per share Basic	\$ 0.10			\$ 0.06
Earnings per share Diluted	\$ 0.09			\$ 0.06

<b>Consolidated Statement of Operations</b>	<b>Six months ended April 1, 2006(1)</b>			
		<b>Revenue</b>	<b>Other</b>	
	<b>As Reported</b>	<b>Adjustment</b>	<b>Adjustments(2)</b>	<b>Restated</b>
	<b>(in thousands, except per share data)</b>			
Revenue:				
License	\$ 113,141	\$ (442)	\$ 453	\$ 113,152
Service	279,571	(4,899)	297	274,969
Total revenue	392,712	(5,341)	750	388,121
Costs and expenses:				
Cost of license revenue	5,192			5,192
Cost of service revenue	122,363		279	122,642
Sales and marketing	127,905		279	128,184
Research and development	70,572			70,572

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General and administrative	37,668			37,668
Amortization of acquired intangible assets	2,646			2,646
Total costs and expenses	366,346		558	366,904
Operating income (loss)	26,366	(5,341)	192	21,217
Other income (expense), net	1,903			1,903
Income (loss) before income taxes	28,269	(5,341)	192	23,120
Provision for (benefit from) income taxes	10,002	(793)		9,209
Net income (loss)	\$ 18,267	\$ (4,548)	\$ 192	\$ 13,911
Earnings per share Basic	\$ 0.17			\$ 0.13
Earnings per share Diluted	\$ 0.16			\$ 0.12

(1) Our consolidated statements of operations for the three and six months ended March 31, 2007 were not affected by the restatement.

(2) Consists of the reversal of the corrections we made in 2006 of \$0.8 million for revenue erroneously recorded from 2002 to 2004 in the Asia-Pacific region as well as the reversal of related legal reserves recorded in 2004, net of the related income tax effects of these two items, which was \$0 because of our full valuation allowance against net

deferred tax  
assets.

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<b>Consolidated Statement of Cash Flows</b>	<b>As Reported</b>	<b>Six months ended April 1, 2006(1)</b>		<b>Restated</b>
		<b>Revenue Adjustment</b>	<b>Other Adjustments(2)</b>	
		<b>(in thousands)</b>		
Cash flows from operating activities:				
Net income (loss)	\$ 18,267	\$ (4,548)	\$ 192	\$ 13,911
Adjustments to reconcile net income (loss) to net cash provided by operating activities:				
Stock-based compensation	19,204			19,204
Depreciation and amortization	16,124			16,124
Other non-cash costs (credits), net	1,057	(793)		264
Changes in operating assets and liabilities, net of effects of acquisitions:				
Accounts receivable	5,721			5,721
Accounts payable and accrued expenses	(10,862)		558	(10,304)
Customer advances		5,341		5,341
Accrued compensation and benefits	(17,872)			(17,872)
Deferred revenue	21,311		(750)	20,561
Accrued income taxes, net of income tax receivable	(5,069)			(5,069)
Other current assets and prepaid expenses	(437)			(437)
Other noncurrent assets and liabilities	(7,970)			(7,970)
Net cash provided by operating activities	39,474			39,474
Cash flows from investing activities:				
Additions to property and equipment	(8,154)			(8,154)
Acquisitions of businesses, net of cash acquired	(10,675)			(10,675)
Net cash used by investing activities	(18,829)			(18,829)
Cash flows from financing activities:				
Proceeds from issuance of common stock	2,902			2,902
Payments of withholding taxes in connection with settlement of restricted stock units	(102)			(102)
Credit facility origination costs	(881)			(881)
Payments of capital lease obligations	(220)			(220)
Net cash provided by financing activities	1,699			1,699
Effect of exchange rate changes on cash and cash equivalents	(2,602)			(2,602)
Net increase in cash and cash equivalents	19,742			19,742
Cash and cash equivalents, beginning of period	204,423			204,423
Cash and cash equivalents, end of period	\$ 224,165	\$	\$	\$ 224,165

- (1) Our consolidated statement of cash flows for the six months ended March 31, 2007 was not affected by the restatement.



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<b>Consolidated Statement of Comprehensive Income</b>	<b>Three months ended March 31, 2007</b>			
		<b>Revenue</b>	<b>Other</b>	
	<b>As Reported</b>	<b>Adjustment</b>	<b>Adjustments</b>	<b>Restated</b>
Comprehensive income (loss):				
Net income	\$ 17,399	\$	\$	\$ 17,399
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustment, net of tax of \$0	772	(434)		338
Change in unrealized gain on investment securities, net of tax of \$0	(655)			(655)
Other comprehensive income (loss)	117	(434)		(317)
Comprehensive income	\$ 17,516	\$ (434)	\$	\$ 17,082

<b>Consolidated Statement of Comprehensive Income</b>	<b>Three months ended March 31, 2006</b>			
		<b>Revenue</b>	<b>Other</b>	
	<b>As Reported</b>	<b>Adjustment</b>	<b>Adjustments</b>	<b>Restated</b>
Comprehensive income (loss):				
Net income (loss)	\$ 10,751	\$ (4,193)	\$	\$ 6,558
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustment, net of tax of \$0	153	293		446
Change in unrealized gain on investment securities, net of tax of \$0	(560)			(560)
Other comprehensive income (loss)	(407)	293		(114)
Comprehensive income	\$ 10,344	\$ (3,900)	\$	\$ 6,444

<b>Consolidated Statement of Comprehensive Income</b>	<b>Six months ended March 31, 2007</b>			
		<b>Revenue</b>	<b>Other</b>	
	<b>As Reported</b>	<b>Adjustment</b>	<b>Adjustments</b>	<b>Restated</b>
Comprehensive income (loss):				
Net income	\$ 32,552	\$	\$	\$ 32,552
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustment, net of tax of \$0	2,580	(26)		2,554
Change in unrealized gain on investment securities, net of tax of \$0	(680)			(680)

Other comprehensive income (loss)	1,900	(26)		1,874
Comprehensive income	\$ 34,452	\$ (26)	\$	\$ 34,426

<b>Consolidated Statement of Comprehensive Income</b>	<b>Six months ended April 1, 2006</b>			
	<b>As Reported</b>	<b>Revenue Adjustment</b>	<b>Other Adjustments</b>	<b>Restated</b>
Comprehensive income (loss):				
Net income (loss)	\$ 18,267	\$ (4,548)	\$ 192	\$ 13,911
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustment, net of tax of \$0	(426)	1,277		851
Change in unrealized gain on investment securities, net of tax of \$0	(233)			(233)
Other comprehensive income (loss)	(659)	1,277		618
Comprehensive income	\$ 17,608	\$ (3,271)	\$ 192	\$ 14,529

**Table of Contents****3. Restructuring and Other Charges**

There were no restructuring and other charges recorded in the first six months of 2007 and 2006.

The following table summarizes restructuring accrual activity for the three and six months ended March 31, 2007:

	Three months ended March 31, 2007			Six months ended March 31, 2007		
	Employee Severance and Related Benefits	Facility Closures and Other Costs	Total	Employee Severance and Related Benefits	Facility Closures and Other Costs	Total
			(in thousands)			
Beginning balance	\$ 974	\$ 19,969	\$ 20,943	\$ 1,084	\$ 21,293	\$ 22,377
Cash disbursements	(679)	(1,527)	(2,206)	(821)	(2,926)	(3,747)
Foreign exchange impact	7	9	16	39	84	123
Balance, March 31, 2007	\$ 302	\$ 18,451	\$ 18,753	\$ 302	\$ 18,451	\$ 18,753

As of March 31, 2007, of the \$18.8 million remaining in accrued restructuring charges, \$7.4 million was included in current liabilities and \$11.4 million was included in other long-term liabilities, principally for facility costs to be paid out through 2014.

In determining the amount of the facilities accrual, we are required to estimate such factors as future vacancy rates, the time required to sublet properties and sublease rates. These estimates are reviewed quarterly based on known real estate market conditions and the credit-worthiness of subtenants, and may result in revisions to established facility reserves. We had accrued \$17.9 million as of March 31, 2007 related to excess facilities (compared to \$20.7 million at September 30, 2006), representing gross lease commitments with agreements expiring at various dates through 2014 of approximately \$41.6 million, net of committed and estimated sublease income of approximately \$23.3 million and a present value factor of \$0.4 million. We have entered into signed sublease arrangements for approximately \$20.9 million, with the remaining \$2.4 million based on future estimated sublease arrangements, including \$1.6 million for space currently available for sublease.

**4. Stock-based Compensation**

We adopted Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment* (SFAS 123(R)) on July 3, 2005, effective with the beginning of the fourth quarter of 2005. SFAS 123(R) requires us to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award using an option pricing model. That cost is recognized over the period during which an employee is required to provide service in exchange for the award.

Our equity incentive plans provide for grants of nonqualified and incentive stock options, common stock, restricted stock, restricted stock units and stock appreciation rights to employees, directors, officers and consultants. Until July 2005, we generally granted stock options. For those options, the option exercise price was typically the fair market value of our common stock at the date of grant and they generally vested over four years and expired ten years from the date of grant. Since our adoption of SFAS 123(R), we have awarded restricted stock and restricted stock units as the principal equity incentive awards, including performance-based awards that are earned based on achievement of performance criteria established by the Compensation Committee of our Board of Directors on or prior to the grant date. Each restricted stock unit represents the contingent right to receive one share of our common stock. Our equity incentive plans are described more fully in Note J to the Consolidated Financial Statements included in our Annual Report on Form 10-K for the fiscal year ended September 30, 2006.

In the second quarter of 2007, at our Annual Meeting our shareholders voted to amend our 2000 Equity Incentive Plan to increase the number of shares of common stock authorized for issuance under the plan by 5,000,000 shares.



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We made the following restricted stock and restricted stock unit grants in the first six months of 2007 and 2006:

Grant Period	Restricted Stock		Restricted Stock Units	
	Performance-based (Number of Shares)	Time-based (Number of Shares)	Performance-based (Number of Units)	Time-based (Number of Units)
Second quarter of 2007		442,590	3,181	380,355
First six months of 2007	495,768	442,590	60,561	728,182
Second quarter of 2006		88,000	14,046	490,140
First six months of 2006	515,617	434,800	335,867	1,292,277

*Restricted Stock*

*Performance-based awards.* In the first six months of 2007 and 2006, we granted to our executive officers performance-based shares that are earned based on achievement of certain company operating performance criteria specified by the Compensation Committee on or prior to the date of grant. With respect to the 2007 grants, if the specified performance criteria are achieved in full, the restrictions on approximately 251,235 shares will lapse on the later of November 9, 2007 or the date the Compensation Committee determines the extent to which the performance criteria have been achieved, and the restrictions on the remaining 244,533 shares will lapse in substantially equal amounts on November 9, 2008 and 2009, provided that the holder of the award remains employed by us at those dates. With respect to the 2006 grants, because the specified performance criteria were achieved in full, the restrictions on 284,417 of the shares lapsed on November 9, 2006 and the restrictions on the remaining shares will lapse in equal installments on November 9, 2007 and 2008, provided that the holder of the award remains employed by us at those dates.

*Time-based awards.* In the second quarter of 2007, we granted 366,800 and 75,790 shares to our executive officers and members of our Board of Directors, respectively. The restrictions on the executive shares will lapse in substantially equal installments on February 15, 2008, 2009 and 2010, provided that the holder of the award remains employed by us at those dates. The restrictions on the shares granted to our directors will lapse in substantially equal installments on March 7, 2008, 2009 and 2010, provided that the holder of the award remains a director at those dates. In the first quarter of 2006, we granted 346,800 shares to our executive officers. The restrictions on one-third of these shares lapsed on November 9, 2006 and those on the remaining shares will lapse in substantially equal installments on November 9, 2007 and 2008, provided that the holder of the award remains employed by us at those dates. In the second quarter of 2006, we issued 88,000 shares of restricted stock to our non-employee directors, the restrictions on one-third of the shares lapsed on February 15, 2007 and the restrictions on the remaining shares will lapse in substantially equal installments on each of February 15, 2008 and 2009.

*Restricted Stock Units*

*Performance-based awards.* In the first and second quarters of 2007, we granted 57,380 and 3,181 performance-based restricted stock units, respectively, to employees in connection with our employee management incentive plans for the 2007 fiscal year. These shares will vest on the later of November 9, 2007 or the date the Compensation Committee determines the extent to which the performance criteria have been achieved, provided that the holder of the award remains employed by us at that date. In the first six months of 2006, we granted 335,867 performance-based restricted stock units to employees in connection with our employee management incentive plans for the 2006 fiscal year which were earned in full on November 9, 2006 based on achievement of specified performance criteria established by the Compensation Committee.

*Time-based awards.* In the first and second quarters of 2007, we granted 347,827 and 380,355 restricted stock units, respectively, to employees. These restricted stock units will vest in three substantially equal installments on the anniversary of the date of grant, provided that the holder of the award remains employed by us at those dates. We expect to grant additional time-based restricted stock units to employees in the third quarter of 2007. In the first and second quarters of 2006, we granted 802,137 and 490,140 restricted stock units, respectively, to employees, which vest in three substantially equal installments on the anniversary of the date of grant, provided that the holder of the award remains employed by us at those dates.



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With respect to all types of equity awards, in the first six months of 2007, the restrictions on 664,463 restricted shares lapsed and 1,099,349 restricted stock units vested. The fair value of restricted shares and restricted stock units granted in the first six months of 2007 was based on the fair market value of our common stock on the date of grant. The weighted average fair value per share of restricted shares and restricted stock units granted in the first six months of 2007 was \$18.69.

The following table shows the classification of compensation expense recorded for our stock-based awards as reflected in our consolidated statements of operations:

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>March 31, 2007</b>	<b>April 1, 2006</b>	<b>March 31, 2007</b>	<b>April 1, 2006</b>
	<b>(in thousands)</b>			
Cost of license revenue	\$ 19	\$ 27	\$ 40	\$ 67
Cost of service revenue	1,768	1,914	3,678	3,861
Sales and marketing	2,326	2,379	3,891	4,694
Research and development	1,629	2,212	3,471	4,317
General and administrative	3,105	3,008	6,397	6,265
Total stock-based compensation expense	\$ 8,847	\$ 9,540	\$ 17,477	\$ 19,204

**5. Common Stock and Earnings Per Share (EPS)**

Basic EPS is calculated by dividing net income by the weighted average number of shares outstanding during the period. Unvested restricted shares, although legally issued and outstanding, are not considered outstanding for purposes of calculating basic earnings per share. Diluted EPS is calculated by dividing net income by the weighted average number of shares outstanding plus the dilutive effect, if any, of outstanding stock options, restricted shares and restricted stock units using the treasury stock method. The calculation of the dilutive effect of outstanding equity awards under the treasury stock method includes consideration of unrecognized compensation expense and any tax benefits as additional proceeds.

The following table presents the calculation for both basic and diluted EPS:

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>March 31, 2007</b>	<b>April 1, 2006</b>	<b>March 31, 2007</b>	<b>April 1, 2006</b>
	<b>Restated Note 2</b>		<b>Restated Note 2</b>	
	<b>(in thousands, except per share data)</b>			
Net income	\$ 17,399	\$ 6,558	\$ 32,552	\$ 13,911
Weighted average shares outstanding Basic	112,845	109,739	112,337	109,560
Dilutive effect of employee stock options, restricted shares and restricted stock units	4,641	3,664	5,047	3,425
Weighted average shares outstanding Diluted	117,486	113,403	117,384	112,985
Earnings per share-Basic	\$ 0.15	\$ 0.06	\$ 0.29	\$ 0.13
Earnings per share-Diluted	\$ 0.15	\$ 0.06	\$ 0.28	\$ 0.12

Stock options to purchase 3.5 million, 3.5 million, 4.1 million and 4.2 million shares for the second quarter and first six months of 2007 and the second quarter and first six months of 2006, respectively, were outstanding but were not included in the calculation of diluted earnings per share because the exercise prices per share, plus the per share tax benefits and unamortized compensation relating thereto, were greater than the average market price of our common stock for those periods. These shares were excluded from the computation of diluted EPS as the effect would have been anti-dilutive.



**Table of Contents****6. Acquisitions***ITEDO*

On October 18, 2006, we acquired ITEDO Software GmbH and ITEDO Software LLC (together, ITEDO), headquartered in Germany, for approximately \$16.7 million in cash. In addition, we agreed to pay up to \$0.5 million of additional cash consideration if specified product integration targets are achieved within three years of the acquisition date. ITEDO provided software solutions for creating and maintaining technical illustrations to customers in multiple discrete manufacturing vertical markets such as automotive, aerospace and defense, and industrial equipment. ITEDO had approximately 30 employees and generated revenue of approximately \$5 million for the twelve months ended July 31, 2006. Results of operations for ITEDO have been included in the accompanying consolidated statements of operations since October 19, 2006. Our results of operations prior to this acquisition if presented on a pro forma basis, as if the companies had been combined since the beginning of fiscal 2006, would not differ materially from our reported results.

This acquisition was accounted for as a business combination. The purchase price allocation resulted in goodwill of \$11.2 million; intangible assets of \$8.1 million (including purchased software of \$6.2 million, customer relationships of \$1.8 million, and other intangible assets of \$0.1 million, which are being amortized over estimated average useful lives of 4 to 10 years); other net liabilities of \$1.0 million; restructuring accruals of \$0.3 million related to our planned integration of ITEDO; deferred tax liabilities of \$2.5 million, equal to the tax effect of the amount of the acquired intangible assets other than goodwill not deductible for income tax purposes; and, as a result of recording those deferred tax liabilities, a \$1.2 million for a reduction in our valuation allowance recorded against our pre-acquisition deferred tax assets in the U.S. and a foreign jurisdiction. The goodwill and certain intangible assets are not deductible for tax purposes.

This transaction resulted in \$11.2 million of purchase price that exceeded the estimated fair values of tangible and intangible assets and liabilities, all of which was allocated to goodwill. We believe that the high amount of goodwill relative to identifiable intangible assets was the result of several factors including the potential to sell ITEDO products into our traditional manufacturing customer base, including leveraging our direct and indirect sales force and our established presence in geographies not previously served by ITEDO; and our intention to integrate our ITEDO, Arbortext, Windchill and Pro/ENGINEER solutions to enhance our technical publications capabilities.

*Mathsoft*

On April 28, 2006, we acquired Mathsoft Corporate Holdings, Inc., including its wholly owned subsidiary Mathsoft Engineering & Education, Inc. (together, Mathsoft). Mathsoft's primary product was Mathcad® software, which helps engineering organizations create, automate, document and reuse engineering calculations in the product development process, and in other mathematics-driven processes. Mathsoft had approximately 120 employees in offices primarily in the U.S. and Europe and generated revenue of approximately \$20 million for the twelve months ended March 31, 2006. Results of operations for Mathsoft have been included in the accompanying consolidated statement of operations since April 29, 2006. Our results of operations prior to this acquisition, if presented on a pro forma basis as if the companies had been combined since the beginning of fiscal 2006, would not differ materially from our reported results.

*DENC and Cadtrain*

In the first quarter of 2006, we acquired DENC AG and substantially all of the assets of Cadtrain, Inc. for an aggregate of \$9.9 million in cash. In addition, we agreed to pay up to an aggregate of \$2.0 million of additional cash consideration if specified targets, including revenue and customer retention results, were achieved within one year of the acquisition dates. As of September 30, 2006, the specified targets of the DENC contingent purchase price arrangement were met and related payments of \$0.5 million were recorded as additional goodwill. In the first quarter of 2007, the specified targets of the Cadtrain contingent purchase price arrangement were met and related payments of \$1.5 million were recorded as additional goodwill.

**7. Goodwill and Acquired Intangible Assets**

We have two reportable segments: (1) software products and (2) services. As of March 31, 2007 and September 30, 2006, goodwill and acquired intangible assets in the aggregate attributable to our software products reportable segment was \$314.9 million and \$300.9 million, respectively, and attributable to our services reportable segment



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was \$27.3 million and \$26.2 million, respectively. Goodwill and other intangible assets are tested for impairment at least annually, or on an interim basis if an event occurs or circumstances change that would, more likely than not, reduce the fair value of the reporting segment below its carrying value. We completed our annual impairment review as of July 1, 2006 and concluded that no impairment charge was required as of that date. Since that date, there have not been any events or changes in circumstances that indicate that the carrying values of goodwill or acquired intangible assets may not be recoverable.

Goodwill and acquired intangible assets consisted of the following:

	March 31, 2007			September 30, 2006		
	Gross Carrying Amount	Accumulated Amortization	Net Book Value (in thousands)	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Goodwill and intangible assets with indefinite lives (not amortized):						
Goodwill			\$ 262,936			\$ 249,252
Trademarks			4,252			4,200
			267,188			253,452
Intangible assets with finite lives (amortized):						
Purchased software	\$ 62,865	\$ 38,761	24,104	\$ 56,096	\$ 35,098	20,998
Capitalized software	22,877	22,722	155	22,877	22,252	625
Customer lists and relationships	66,757	18,344	48,413	64,634	15,195	49,439
Trademarks and tradenames	1,757	506	1,251	1,645	313	1,332
Other	1,946	865	1,081	1,910	634	1,276
	\$ 156,202	\$ 81,198	75,004	\$ 147,162	\$ 73,492	73,670
Total goodwill and acquired intangible assets			\$ 342,192			\$ 327,122

The changes in the carrying amounts of goodwill and intangible assets with indefinite lives at March 31, 2007 from September 30, 2006 are due to the impact of acquisitions (described in Note 6) and to foreign currency translation adjustments related to those asset balances that are recorded in non-U.S. currencies.

Changes in goodwill, presented by reportable segment, were as follows:

	Software Products Segment	Services Segment (in thousands)	Total
Balance, September 30, 2006	\$ 231,699	\$ 17,553	\$ 249,252
Acquisition of ITEDO	11,243		11,243

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Additional purchase price paid for Cadtrain acquisition		1,500	1,500
Foreign currency translation adjustments	849	92	941
Balance, March 31, 2007	\$ 243,791	\$ 19,145	\$ 262,936

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The aggregate amortization expense for intangible assets with finite lives was classified in our consolidated statements of operations as follows:

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>March 31, 2007</b>	<b>April 1, 2006</b>	<b>March 31, 2007</b>	<b>April 1, 2006</b>
	<b>(in thousands)</b>			
Amortization of acquired intangible assets	\$ 1,588	\$ 1,288	\$ 3,676	\$ 2,646
Cost of license revenue	1,926	1,195	3,637	2,391
Cost of service revenue	17	104	49	104
Total amortization expense	\$ 3,531	\$ 2,587	\$ 7,362	\$ 5,141

**8. Recent Accounting Pronouncements***Accounting for Uncertainty in Income Taxes*

In July 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure relative to uncertain tax positions. FIN 48 is effective for fiscal years beginning after December 15, 2006, with early adoption encouraged. We will adopt FIN 48 in fiscal 2008. We are currently evaluating whether or not the adoption of FIN 48 will have a material effect on our consolidated financial position, results of operations or cash flows.

*Fair Value Measurements*

In September 2006, the FASB issued Statement No. 157, *Fair Value Measurements* (SFAS 157). This Statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We do not believe the adoption of SFAS 157 in fiscal 2009 will have a material effect on our consolidated financial position, results of operations or cash flows.

*Fair Value Option for Financial Assets and Financial Liabilities*

In February 2007, the FASB issued Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* (SFAS 159). This Statement permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This Statement is expected to expand the use of fair value measurement, which is consistent with the FASB's long-term measurement objectives for accounting for financial instruments. The fair value option established by this Statement permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity must report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. This Statement is effective as of the beginning of fiscal 2009, with early adoption permitted. We do not believe the adoption of SFAS 159 will have a material effect on our consolidated financial position, results of operations or cash flows.

**Table of Contents****9. Segment Information**

We operate within a single industry segment – computer software and related services. Operating segments as defined by SFAS 131, *Disclosures about Segments of an Enterprise and Related Information*, are components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision-making group, in deciding how to allocate resources and in assessing performance. Our chief operating decision-making group is our executive officers. We have two operating and reportable segments: (1) Software Products, which includes license and maintenance revenue (including new releases and technical support); and (2) Services, which includes consulting, implementation, training and other support revenue. In our consolidated statements of operations, maintenance revenue is included in service revenue. We do not allocate certain sales, marketing or administrative expenses to our operating segments, as these activities are managed separately.

We report our revenue in two product categories:

Enterprise Solutions, which includes Windchill®, Pro/INTRALINK®, ProductView , Arbortext® Publishing Engine , Arbortext IsoView® and all other solutions that help companies collaborate and manage and publish information across an extended enterprise; and

Desktop Solutions, which includes Pro/ENGINEER®, Arbortext Editor , Arbortext IsoDraw®, Mathcad® and all other solutions that help companies create content and improve desktop productivity.

The revenue and operating income (loss) attributable to these operating segments are summarized as follows:

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>March</b>	<b>April 1,</b>	<b>March</b>	<b>April 1,</b>
	<b>31,</b>	<b>2006</b>	<b>31,</b>	<b>2006</b>
		<b>Restated</b>		<b>Restated</b>
		<b>Note 2</b>		<b>Note 2</b>
	<b>(in thousands)</b>			
Revenue:				
Software Products segment:				
License:				
Desktop solutions	\$ 48,698	\$ 34,626	\$ 92,028	\$ 70,723
Enterprise solutions	22,638	19,546	45,896	42,429
Total software products license revenue	71,336	54,172	137,924	113,152
Maintenance: (1)				
Desktop solutions	79,536	72,463	160,905	145,483
Enterprise solutions	19,230	16,036	38,445	32,366
Total software products maintenance revenue	98,766	88,499	199,350	177,849
Total software products revenue	170,102	142,671	337,274	291,001
Services segment:				
Desktop solutions	18,062	20,712	37,623	37,583
Enterprise solutions	39,932	31,886	74,866	59,537
Total service revenue	57,994	52,598	112,489	97,120
Total revenue:				

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Desktop solutions	146,296	127,801	290,556	253,789
Enterprise solutions	81,800	67,468	159,207	134,332
Total revenue	\$ 228,096	\$ 195,269	\$ 449,763	\$ 388,121
Operating income (loss): (2)				
Software Products segment	\$ 108,913	\$ 89,080	\$ 217,231	\$ 183,996
Services segment	4,617	3,382	5,766	3,073
Sales and marketing expenses	(71,560)	(64,260)	(141,121)	(128,184)
General and administrative expenses	(20,711)	(18,039)	(39,634)	(37,668)
Total operating income	\$ 21,259	\$ 10,163	\$ 42,242	\$ 21,217

(1) Maintenance revenue is included in Service Revenue in the consolidated statements of operations.

(2) The operating income (loss) reported for each operating segment does not represent the total operating results as it does not contain an allocation of sales, marketing, and general and administrative expenses incurred in support of the operating segments.

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Data for the geographic regions in which we operate is presented below:

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>March</b>	<b>April 1,</b>	<b>March</b>	<b>April 1,</b>
	<b>31,</b>	<b>2006</b>	<b>31,</b>	<b>2006</b>
	<b>2007</b>	<b>Restated</b>	<b>2007</b>	<b>Restated</b>
		<b>Note 2</b>		<b>Note 2</b>
	<b>(in thousands)</b>			
Revenue:				
North America (1)	\$ 89,409	\$ 78,065	\$ 175,890	\$ 153,920
Europe (2)	82,848	66,743	165,591	141,780
Asia-Pacific (3)	55,839	50,461	108,282	92,421
Total revenue	\$ 228,096	\$ 195,269	\$ 449,763	\$ 388,121

(1) Includes revenue in the United States totaling \$84.3 million and \$73.7 million for the three months ended March 31, 2007 and April 1, 2006, respectively, and \$166.8 million and \$146.3 million for the six months ended March 31, 2007 and April 1, 2006, respectively.

(2) Includes revenue in Germany totaling \$25.4 million and \$21.9 million for the three



months ended  
March 31, 2007  
and April 1,  
2006,  
respectively,  
and  
\$50.2 million  
and  
\$41.9 million  
for the six  
months ended  
March 31, 2007  
and April 1,  
2006,  
respectively.

- (3) Includes  
revenue in  
Japan totaling  
\$25.1 million  
and  
\$22.5 million  
for the three  
months ended  
March 31, 2007  
and April 1,  
2006,  
respectively,  
and  
\$49.6 million  
and  
\$41.8 million  
for the six  
months ended  
March 31, 2007  
and April 1,  
2006,  
respectively.

Total long-lived tangible assets by geographic region have not changed significantly since September 30, 2006.

#### **10. Income Taxes**

Our income tax provisions for the three and six months ended March 31, 2007 and April 1, 2006 consist primarily of taxes owed in relation to the income generated by our foreign subsidiaries as well as withholding taxes that we incurred in the U.S. in connection with certain foreign operations. The tax provisions of those periods include insignificant amounts in relation to the income that we generated in the U.S., due to our utilization of available net operating loss carryforwards that previously had been recorded in our balance sheet with a full valuation allowance. As of the end of the second quarter of 2007, a full valuation allowance was recorded against our net deferred tax assets in the U.S. and certain foreign jurisdictions. We concluded that as of March 31, 2007 it was still more likely than not that our net deferred tax assets in the U.S. and certain foreign jurisdictions would not be realized. While we have realized consolidated operating profits over the past three years and in the first six months of 2007, we have only recently begun to show consistent profitability in the U.S. and, as recently as the fourth quarter of 2005, our U.S. legal entities incurred a taxable loss, due principally to the tax expense associated with the grant and vesting of restricted

stock units and our employee stock option exchange.

Significant management judgment is required to determine when the realization of our deferred tax assets in the future is considered more likely than not. If and when we conclude that realization is more likely than not, we will record a reduction to our valuation allowance that will result in an increase to net income and adjustments to goodwill, accumulated other comprehensive loss, and additional paid-in capital in the period such determination is made.

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**11. Commitments and Contingencies**

*Revolving Credit Agreement*

On February 21, 2006, we entered into a multi-currency bank revolving credit facility with a syndicate of seven banks. The credit facility was established primarily for general corporate purposes, including acquisitions of businesses. The credit facility consists of a \$230 million revolving credit facility, which may be increased by up to an additional \$150 million if the existing or additional lenders are willing to make increased commitments. The credit facility expires on February 20, 2011, when all amounts will be due and payable in full. Any obligations under the credit facility are guaranteed by PTC's material domestic subsidiaries and are collateralized by a pledge of 65% of the capital stock of PTC's material first-tier non-U.S. subsidiaries. We have not borrowed any funds under the credit facility to date.

Interest rates under the credit facility would range from 0.75% to 1.50% above the Eurodollar rate for Eurodollar-based borrowings or would be at the defined base rate for base rate borrowings, in each case based upon our leverage ratio. In addition, we may borrow certain foreign currencies at the London interbank-offered interest rates for those currencies, with the same range above such rates based on our leverage ratio. A quarterly commitment fee based on the undrawn portion of the credit facility is required to be paid by us, ranging from 0.125% to 0.30% per year, depending upon our leverage ratio.

The credit facility limits our and our subsidiaries' ability to, among other things: incur additional indebtedness; incur liens or guarantee obligations; pay dividends and make other distributions; make investments and enter into joint ventures; dispose of assets; and engage in transactions with affiliates, except on an arms-length basis. Under the credit facility, we and our material domestic subsidiaries may not invest cash or property in, or loan cash to, our foreign subsidiaries in aggregate amounts exceeding \$25 million for any purpose and an additional \$50 million for acquisitions of businesses. In addition, under the credit facility, we and our subsidiaries must maintain specified leverage and fixed-charge ratios. Any failure to comply with the financial or operating covenants of the credit facility would not only prevent us from being able to borrow additional funds, but would also constitute a default, resulting in, among other things, the amounts outstanding, including all accrued interest and unpaid fees, becoming immediately due and payable. A change in control of PTC (as defined in the credit facility) also constitutes an event of default, permitting the lenders to accelerate the required payments of all amounts due and to terminate the credit facility. We were in compliance with all financial and operating covenants of the credit facility as of March 31, 2007.

*Legal Proceedings*

PTC is a party to an informal legal proceeding in which a large customer is disputing its payment obligations to its third party financing provider on a number of purchases, including purchases of PTC software and services during the period from 2003 to 2006. The customer is defending its non-payment on the grounds that the customer's employee who initiated the transactions was unauthorized to make the purchases or to enter into the financing arrangements.

PTC is not a party to the disputed contracts between the financing provider and the customer, and PTC has been paid for substantially all orders relating to this customer. The financing provider has indicated that, to the extent it does not receive payment from the customer, it may seek to recover from others, including PTC. PTC has fully performed its obligations relating to these orders and believes that neither the customer nor its financing provider has a valid basis for recourse against PTC. PTC would vigorously defend any effort to collect the disputed amounts from PTC.

Notwithstanding this matter, PTC continues to have a business relationship with the customer and, in the second quarter of 2007, PTC received additional orders from the customer, for which approximately \$2 million of revenue was recognized.

We also are subject to various legal proceedings and claims that arise in the ordinary course of business. We currently believe that resolving these other matters will not have a material adverse impact on our financial condition or results of operations.

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*Guarantees and Indemnification Obligations*

We enter into standard indemnification agreements in our ordinary course of business. Pursuant to these agreements, we indemnify, hold harmless, and agree to reimburse the indemnified party for losses suffered or incurred by the indemnified party, generally our business partners or customers, in connection with patent, copyright or other intellectual property infringement claims by any third party with respect to our products, as well as claims relating to property damage or personal injury resulting from the performance of services by us or our subcontractors. The maximum potential amount of future payments we could be required to make under these indemnification agreements is unlimited. Historically, our costs to defend lawsuits or settle claims relating to such indemnity agreements have been minimal and we accordingly believe the estimated fair value of these agreements is immaterial.

We warrant that our software products will perform in all material respects in accordance with our standard published specifications in effect at the time of delivery of the licensed products for a specified period of time (generally 90 to 180 days). Additionally, we generally warrant that our consulting services will be performed consistent with generally accepted industry standards. In most cases, liability for these warranties is capped. If necessary, we would provide for the estimated cost of product and service warranties based on specific warranty claims and claim history; however, we have never incurred significant cost under our product or services warranties. As a result, we believe the estimated fair value of these agreements is immaterial.

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

**Restatement of Previously Issued Financial Results**

As a result of an independent investigation led by the Audit Committee of our Board of Directors, the Audit Committee concluded on October 29, 2007 that we would need to restate our previously issued financial statements for the effect of certain transactions involving Toshiba Corporation of Japan ( Toshiba ), for which we recorded revenue of approximately \$41 million during fiscal 2001 through 2006. Based on its investigation, the Audit Committee concluded that the understanding of the arrangement was not fully reflected in the order paperwork for these transactions because there were additional circumstances known or knowable by one or more of our personnel in Japan. That condition required us to change our conclusion that the transactions met the revenue recognition criteria of Statement of Position 97-2, *Software Revenue Recognition*.

The results of the investigation indicate that during the period 2001 to 2006, an employee of Toshiba Corporation initiated purchases of both software and services from our subsidiary in Japan, PTC Japan K.K. ( PTC Japan ). Many of these purchases were completed through a third party trading company that procured the software and services on Toshiba's behalf. The transactions were supported by orders that were signed by employees of Toshiba and the third party trading company. PTC Japan delivered the items for which revenue was recorded and was paid for the orders in question. The Toshiba employee also allegedly entered into a series of financing agreements with third party leasing companies, including GE Capital Leasing Corporation of Japan ( GECL ), in the name of Toshiba to fund various purchases. As part of those transactions, the leasing companies allegedly entered into transactions with various third party trading companies to procure the purchased items on behalf of Toshiba. We

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were not a party to those financing agreements. Toshiba has disclaimed responsibility for repayment of these financed amounts and has alleged that the Toshiba employee who entered into the financing agreements was not authorized to do so and that Toshiba did not receive delivery of the items so financed.

Recently, the Toshiba employee involved in the transactions was arrested and charged with defrauding certain of the leasing companies. Among the allegations against him are that he forged contracts in the name of Toshiba. In addition, three individuals each employed by a different trading company involved in the transactions have been arrested for alleged involvement in a scheme to defraud the leasing companies. According to published news reports, the Toshiba employee and these other individuals are suspected of diverting some of the proceeds of the financings to a bank account controlled by one or more of them. Following these arrests, it was reported on October 23, 2007 that two former employees of PTC Japan were arrested on suspicion of demanding hush money from one of the participants in the fraudulent scheme. The press accounts indicate that the former PTC Japan employees who left employment with PTC Japan in 2003 and 2004, respectively were no longer working at PTC Japan at the time of the alleged demands. According to the press accounts, these individuals have not been charged with participating in the alleged underlying fraud.

To effect the restatement of revenue associated with the transactions placed by the Toshiba employee, we reduced previously recorded revenue by approximately \$8 million in fiscal 2006, \$15 million in fiscal 2005, \$9 million in fiscal 2004, \$2 million in fiscal 2003 and \$7 million in prior years, and recorded related income tax effects. We did not make any adjustments to the costs incurred in connection with these transactions due to the uncertainty regarding our ultimate ability to retain the advances received for these transactions and our belief that all such costs are unrecoverable. Upon restatement, the revenue reversed from those prior periods was deferred and classified as Customer Advances in our consolidated balance sheets. That liability (which totaled \$39.5 million at both March 31, 2007 and September 30, 2006, after the effects of foreign currency movements) will remain recorded until the rights and obligations of the several companies connected with the Toshiba transactions are resolved. To the extent that matters are resolved in our favor, we will reduce Customer Advances and record revenue or other income at that time. Our restatement of prior period financial statements also includes adjustments for other previously identified errors that we had corrected in the periods they became known to us rather than in the periods in which they originated because we believed that the amounts of such errors, individually and in the aggregate, were not material to our financial statements for the affected periods. In this restatement, we have now recorded those corrections in the periods in which each error originated. Such adjustments, which have been tax effected, primarily relate to (i) recording rent expense on a straight-line basis for one of our office facilities, (ii) recording stock-based compensation expense due to the timing of approvals for certain stock options we granted, (iii) deferring or reversing revenue for certain customer orders in the Asia-Pacific region, and (iv) reversing an income tax reserve that was unwarranted when established.

**Summary of the Restatement Effects**

A summary of the cumulative revenue and net income effects of the restatement on our consolidated financial statements is as follows:

	Year ended September 30,				Prior Years
	2006	2005	2004	2003	
		<b>(in thousands, except per share data)</b>			
Revenue, as previously reported	\$ 854,918	\$ 720,719	\$ 660,029	\$ 671,940	
Adjustments	(6,935)	(12,744)	(8,361)	(2,487)	\$ (10,506)
Revenue, as restated	\$ 847,983	\$ 707,975	\$ 651,668	\$ 669,453	
Net income (loss), as previously reported	\$ 60,866	\$ 83,592	\$ 34,813	\$ (98,280)	

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Adjustments	(4,062)	(10,405)	(3,228)	(2,907)	\$ (12,927)
Net income (loss), as restated	\$ 56,804	\$ 73,187	\$ 31,585	\$ (101,187)	
Earnings (loss) per share Diluted, as previously reported	\$ 0.54	\$ 0.75	\$ 0.32	\$ (0.93)	
Adjustments	(0.04)	(0.10)	(0.03)	(0.03)	
Earnings (loss) per share Diluted, as restated	\$ 0.50	\$ 0.65	\$ 0.29	\$ (0.96)	

The restatement had no effect on previously reported cash balances or on the amounts of net cash flows from operating, investing and financing activities. The adjustments made as a result of the restatement are more fully described in Note 2 to our consolidated financial statements included in Part I, Item 1 Unaudited Financial Statements of this Form 10-Q/A. Our assessment of the effectiveness of our disclosure controls and procedures is included in Part I, Item 4 Controls and Procedures of this Form 10-Q/A.

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**Disclosure Amended by this Form 10-Q/A**

All amounts referenced to March 31, 2007, September 30, 2006 and April 1, 2006 in the following discussion reflect the balances and amounts on a restated basis. Also, comparisons of the three and six months ended March 31, 2007 and April 1, 2006 to any other periods have been revised from those included in our Original Form 10-Q as necessary to reflect the restated information.

This Form 10-Q/A modifies only the disclosures described in the preceding paragraph to reflect the restatement and does not modify or update such disclosures in any other respect, or any other disclosures presented in the Original Form 10-Q. Further, this Form 10-Q/A does not reflect any other events occurring after May 10, 2007, the date we filed the Original Form 10-Q. We specifically note that we have not updated any forward-looking statements or our Risk Factors to reflect events occurring after the date we filed the Original Form 10-Q. Accordingly, this Form 10-Q/A should be read in conjunction with our filings made with the SEC since the filing date of the Original Form 10-Q, including our Current Reports on Form 8-K, our Annual Report on Form 10-K for the year ended September 30, 2007, and the amendments to our Quarterly Reports on Form 10-Q for the quarterly periods ended December 30, 2006 and June 30, 2007.

**Forward-Looking Statements**

Statements in this Quarterly Report on Form 10-Q about our anticipated financial results and growth, as well as about the development of our products and markets, are forward-looking statements that are subject to the inherent uncertainties in predicting future results and conditions. Risks and uncertainties that could cause actual results to differ materially from those projected include the following: our ability to increase revenues or successfully execute strategic and other business initiatives while containing costs; our ability to optimize our sales and services coverage and productivity through, among other means, effective use and management of our internal resources in combination with our resellers and other strategic partners and appropriate investment in our distribution channel; our ability to successfully integrate and achieve both revenue and earnings growth from newly acquired businesses; our ability to successfully differentiate our products and services from those of our competitors and to effectively pursue opportunities within the small and medium-size business market and with strategic larger accounts; our ability to successfully help our customers expand their product development technology infrastructure; as well as other risks and uncertainties referenced in Part II, Item 1A Risk Factors of this report.

**Our Business**

We develop, market and support product lifecycle management (PLM) and enterprise content management (ECM) software solutions and related services that help companies improve their processes for developing physical and information products.

Our software solutions include our Enterprise Solutions products a range of Internet-based collaboration, content and process management, and publishing technologies and our Desktop Solutions products a suite of mechanical computer-aided design, engineering calculation, and XML-based document authoring tools. Our software solutions help customers develop products faster, improve product quality, increase innovation and reduce product development cost.

The PLM market encompasses the mechanical computer-aided design, manufacturing and engineering (CAD, CAM and CAE) segment and the collaboration and product data management solutions segment, as well as many previously isolated markets that address various other phases of a product's lifecycle. These include but are not limited to component and supplier management, visualization and digital mockup, enterprise application integration, program and project management, after market service and portfolio management, requirements management, customer needs management, manufacturing planning, and technical and marketing publications.

The ECM market includes technologies for business process management, compliance management, document management, dynamic publishing, document archival and retrieval, knowledge management, records management and Web content management. Within the ECM market, PTC focuses on a subset of solutions that optimize the development of dynamic publications, such as those associated with technical manuals, service documents, and regulatory and compliance data sets, as well as government and financial document publishing and content management.





**Table of Contents****Executive Overview**

We delivered total revenue of \$228 million in the second quarter of 2007, reflecting revenue growth across our three major geographies and all major product categories. Revenue growth included both organic growth and revenue from acquisitions made since the second quarter of 2006, as we expanded our capability footprint and leveraged acquired solutions across our distribution model. PTC's total and organic revenue growth rates are higher than the growth rate of the overall PLM market as estimated by leading independent analyst firms. Additionally, our second quarter of 2007 operating margins and net income increased over those of the second quarter of 2006, reflecting increased direct and indirect sales productivity.

We believe our operating results reflect successful execution of our strategic initiatives over the past three years, as well as increased technology spending by our customers. Those initiatives focused on improving our product and service offerings, our distribution model, our strategic account relationships, our competitive position and our marketing programs. We believe our strategic initiatives have created three key competitive differentiators which we believe are causing customers to adopt our solutions: our broad product development system capabilities, our single platform architecture, and our unique process framework for addressing our customers' product development challenges. In particular, we believe our strategy to offer a product development system with fully integrated solutions on a common architecture provides us with a significant competitive advantage and is a major factor in our increased sales of Pro/ENGINEER® and Windchill®. We also believe that acquisitions by others of certain of our competitors have created and will continue to create competitive opportunities for us.

Looking forward to the second half of 2007, we expect to continue to grow revenue and increase our operating margins. We will continue to focus on customer satisfaction, product capability and quality, services profitability, and further productivity improvements from our direct and indirect distribution model. Additionally, while we have not yet concluded that realization of our U.S. deferred tax assets in the future is more likely than not, we will continue to review our operating results in the U.S. to determine if it becomes more likely than not that our U.S. deferred tax assets will be realized in the future. If this were to occur in the second half of 2007, we would release some or all of the valuation allowance. Any reduction in our valuation allowance in the future would result in an income tax benefit, higher stockholders' equity and a reduction to goodwill in the period such determination is made and could have a negative impact on our reported net income in future periods as we would expect to begin recording a higher provision for income taxes. Any reduction in our valuation allowance would not impact our cash flow. We discuss this further in Results of Operations - Costs and Expenses - Income Taxes on page 31.

**Results of Operations**

The following is a summary of our results of operations for the second quarters and first six months of 2007 and 2006, which includes the results of operations of companies we acquired beginning on their respective acquisition dates. A detailed discussion of these results follows the table below.

	Three months ended			Six months ended		
	March 31, 2007	April 1, 2006	Percent Change	March 31, 2007	April 1, 2006	Percent Change
	(Dollar amounts in millions)					
Total revenue	\$ 228.1	\$ 195.3	17%(1)	\$ 449.8	\$ 388.1	16%(1)
Total costs and expenses	206.8	185.1	12%	407.5	366.9	11%
Operating income	21.3	10.2		42.3	21.2	
Other income (expense), net	1.3	0.8		2.1	1.9	
Income before income taxes	22.6	11.0		44.4	23.1	
Provision for income taxes	5.2	4.4		11.8	9.2	
Net income	\$ 17.4	\$ 6.6		\$ 32.6	\$ 13.9	

- (1) On a consistent foreign currency basis, compared to the year-ago periods, total revenue for the second quarter and first six months of 2007 increased 14% and 13%, respectively.

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Revenue for the second quarter and first six months of 2007 reflects the following:

License revenue of \$71.3 million and \$137.9 million for the second quarter and first six months of 2007, respectively, a 32% and 22% increase in license revenue from the second quarter and first six months of 2006, respectively.

Service revenue of \$156.8 million and \$311.9 million for the second quarter and first six months of 2007, respectively, an 11% and 13% increase in service revenue from the second quarter and first six months of 2006, respectively.

Revenue by product category for the second quarter and first six months of 2007 reflects the following:

Enterprise Solutions revenue of \$81.8 million and \$159.2 million for the second quarter and first six months of 2007, respectively, a 21% and 19% increase from the second quarter and first six months of 2006, respectively.

Desktop Solutions revenue of \$146.3 million and \$290.6 million, respectively, a 14% increase from both the second quarter and first six months of 2006.

Total costs and expenses reflect increases in our operating cost structure from acquisitions and from measured increases to support our revenue growth.

The increase in net income in the second quarter and first six months of 2007 compared to 2006 reflects improved operating margin contributions from increased revenue year over year.

The following table shows certain consolidated financial data as a percentage of our total revenue for the second quarters and first six months of 2007 and 2006:

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>March</b>	<b>April 1,</b>	<b>March</b>	<b>April 1,</b>
	<b>31,</b>	<b>2006</b>	<b>31,</b>	<b>2006</b>
	<b>2007</b>		<b>2007</b>	
Revenue:				
License	31%	28%	31%	29%
Service	69	72	69	71
Total revenue	100	100	100	100
Costs and expenses:				
Cost of license revenue	2	1	2	1
Cost of service revenue	30	33	31	32
Sales and marketing	31	33	31	33
Research and development	18	18	17	18
General and administrative	9	9	9	10
Amortization of acquired intangible assets	1	1	1	1
Total costs and expenses	91	95	91	95
Operating income	9	5	9	5
Other income (expense), net	1		1	1
Income before income taxes	10	5	10	6
Provision for income taxes	2	2	3	2
Net income	8%	3%	7%	4%

**Revenue**

Our revenue consists of software license revenue and service revenue, which includes software maintenance revenue (consisting of providing our customers software updates and technical support) as well as consulting and training revenue (including implementation services).

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We report our revenue in two product categories:

**Enterprise Solutions**, which includes Windchill, Pro/INTRALINK, ProductView, Arbortext Publishing Engine, Arbortext IsoView and all other solutions that help companies collaborate and manage and publish information across an extended enterprise; and

**Desktop Solutions**, which includes Pro/ENGINEER, Arbortext Editor, Arbortext IsoDraw, Mathcad and all other solutions that help companies create content and improve desktop productivity.

The following table shows our software license revenue and our service revenue by product category for the periods stated.

	Three months ended			Six months ended		
	March 31, 2007	April 1, 2006	Percent Change	March 31, 2007	April 1, 2006	Percent Change
	(Dollar amounts in millions)					
License Revenue:						
Enterprise	\$ 22.6	\$ 19.6	16%	\$ 45.9	\$ 42.4	8%
Desktop	48.7	34.6	41%	92.0	70.7	30%
Total license revenue	71.3	54.2	32%	137.9	113.1	22%
Maintenance revenue:						
Enterprise	19.2	16.0	20%	38.4	32.4	19%
Desktop	79.5	72.5	10%	160.9	145.5	11%
Total maintenance revenue	98.7	88.5	12%	199.3	177.9	12%
Consulting and training service revenue:						
Enterprise	40.0	31.9	25%	74.9	59.5	26%
Desktop	18.1	20.7	(13)%	37.7	37.6	
Total consulting and training service revenue	58.1	52.6	10%	112.6	97.1	16%
Total service revenue	156.8	141.1	11%	311.9	275.0	13%
Total revenue	\$ 228.1	\$ 195.3	17%(1)	\$ 449.8	\$ 388.1	16%(1)
Total Enterprise Solutions revenue	\$ 81.8	\$ 67.5	21%	\$ 159.2	\$ 134.3	19%
Total Desktop Solutions revenue	\$ 146.3	\$ 127.8	14%	\$ 290.6	\$ 253.8	14%

(1) On a consistent foreign currency basis from the comparable year-ago period, in the second quarter and first six months of 2007 total

revenue  
increased 14%  
and 13%,  
respectively.

In the second quarter and first six months of 2007, we achieved year-over-year revenue growth in both Desktop Solutions and Enterprise Solutions. The revenue growth reflects both organic growth of our Desktop Solutions and Enterprise Solutions and revenue from the recently acquired Mathsoft and ITEDO businesses. Historically, Mathsoft generated revenue of approximately \$20 million for the twelve months ended March 31, 2006 and ITEDO generated revenue of approximately \$5 million for the twelve months ended July 31, 2006. The Mathsoft and ITEDO businesses have been included in our results of operations since their acquisition dates (Mathsoft on April 28, 2006 and ITEDO on October 18, 2006). Accordingly, results for the second quarter and first six months of 2006 do not include Mathsoft or ITEDO.

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Total revenue from our Enterprise Solutions software and related services was 36% and 35% of our total revenue in the second quarter of 2007 and 2006, respectively, and 35% of our total revenue in the first six months of both 2007 and 2006.

The increase in Enterprise Solutions revenue in the second quarter and first six months of 2007 compared to the second quarter and first six months of 2006 was due primarily to:

organic growth of our Windchill solutions, which reflects our success in helping customers and prospects understand the benefits of investing in PLM solutions, as well as our ability to help customers adopt our solutions incrementally, which lowers customer risk and

more wide-spread adoption of our solutions by both our existing and new customers, which we believe is a result of customer recognition of the benefits of our broad set of capabilities delivered on a single system architecture.

Total revenue from our Desktop Solutions software and related services was 64% and 65% of our total revenue in the second quarter of 2007 and 2006, respectively, and 65% of our total revenue in the first six months of both 2007 and 2006.

The increase in Desktop Solutions revenue in the second quarter and first six months of 2007 as compared to the second quarter and first six months of 2006 was due primarily to:

organic growth of our Pro/ENGINEER products and

revenue contribution from the recently acquired Mathsoft business.

We believe the increase in sales of our Pro/ENGINEER products reflects:

the success of the measures we took to better compete in the small and medium-size business segment of our market, which included offering Pro/ENGINEER packages with differing price points and functionality and developing a diverse, global network of reseller partners and

increasing adoption of our Pro/ENGINEER products by customers who see adopting our integrated product development system as an advantage over maintaining their current environments, typically consisting of multiple, disconnected CAD and data management applications.

***License Revenue***

***Total***

License revenue accounted for 31% of total revenue in each of the second quarter and first six months of 2007 and 28% and 29% of total revenue in the second quarter and first six months of 2006, respectively.

***Enterprise Solutions***

The increase in Enterprise Solutions license revenue in the second quarter of 2007 as compared to the second quarter of 2006 came primarily from sales of Windchill PDMLink® and visualization products. Revenue growth for the first six months of 2007 was lower than the growth rate for the second quarter of 2007. This was due primarily to the impact of revenue from a large customer transaction recorded in the first quarter of 2006.

***Desktop Solutions***

The increase in Desktop Solutions license revenue in the second quarter and first six months of 2007 compared to the second quarter and first six months of 2006 was due primarily to organic growth, primarily from sales of Pro/ENGINEER, as well as revenue contribution from Mathsoft products. For the first six months of 2007, Pro/ENGINEER revenue grew across our high and low-end packages, as well as upgrades and modules.

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***Maintenance Revenue***

*Total*

Maintenance revenue represented 43% and 45% of total revenue in the second quarter of 2007 and 2006, respectively and 44% and 46% of total revenue in the first six months of 2007 and 2006, respectively. Growth in our maintenance revenue was due to recent acceleration in our license revenue growth and reflects continued success in improving customer satisfaction with our solutions, product enhancements and technical support.

*Enterprise Solutions*

Increases in our Enterprise Solutions maintenance revenue were due primarily to an increase in the number of new users of our Enterprise Solutions as new customers have been added and as existing customers have expanded their implementations to additional users.

*Desktop Solutions*

The increase in our Desktop Solutions maintenance revenue was due to higher renewal rates, the recent growth of license revenue, and revenue contributions from our acquired products.

***Consulting and Training Service Revenue***

*Total*

Consulting and training service revenue, which has a lower gross profit margin than license and maintenance revenues, accounted for 25% and 27% of total revenue in the second quarter of 2007 and 2006, respectively, and 25% of total revenue in the first six months of both 2007 and 2006, respectively. Consulting and training service revenue reflects an increase in consulting service revenue for the second quarter and first six months of 2007, partially offset by a decrease in training service revenue for the same periods, as compared to 2006 year-ago periods.

*Enterprise Solutions*

Increases in our Enterprise Solutions consulting and training service revenue were due to increased customer demand for process and implementation consulting services as a result of increased adoption of our software solutions. Also, during the first six months of 2007, our Enterprise Solutions consulting and training revenue included a large customer engagement which contributed to the growth in the 2007 periods as compared to the 2006 periods.

*Desktop Solutions*

Desktop Solutions consulting and training service revenue reflects a decrease in training service revenue for the second quarter and first six months of 2007, partially offset by an increase in consulting service revenue for the same periods, as compared to the second quarter and first six months of 2006. The decrease in Desktop Solutions training service revenue was partially attributable to a large customer training order completed in the second quarter of 2006. Desktop Solutions consulting service revenue did not grow at the same rate as Desktop license revenue in part because license revenue included revenue from acquired products and the reseller channel for which we provide less consulting and training services than Pro/ENGINEER licenses sold through our direct channel.



**Table of Contents****Revenue by Geography**

The following table shows our revenue by geography for the periods stated.

	Three months ended			Six months ended		
	March 31, 2007	April 1, 2006	Percent Change (Dollar amounts in millions)	March 31, 2007	April 1, 2006	Percent Change
Revenue by geography:						
North America	\$89.4	\$78.1	15%	\$175.9	\$153.9	14%
Europe	\$82.8	\$66.7	24%(1)	\$165.6	\$141.8	17%(2)
Asia-Pacific	\$55.9	\$50.5	11%(1)	\$108.3	\$ 92.4	17%(2)

(1) On a consistent foreign currency basis from the comparable year-ago period, in the second quarter of 2007 revenue in Europe increased 13% and revenue in Asia-Pacific increased 12%.

(2) On a consistent foreign currency basis from the comparable year-ago period, in the first six months of 2007 revenue in Europe increased 8% and revenue in Asia-Pacific increased 18%.

We derived 61% of our total revenue from sales to customers outside North America in the second quarter and first six months of 2007 and 60% in the second quarter and first six months of 2006.

*North America.* Total revenue growth in North America was primarily due to organic growth and contributions from the recently acquired Mathsoft business, whose revenues were concentrated in that region. North American revenue performance reflects positive results from our strategic account program and from our indirect channel.

*Europe.* The increase in European revenue in the second quarter and first six months of 2007 compared to the second quarter and first six months of 2006 reflects strong performance in both Enterprise and Desktop Solutions and contributions from the Mathsoft and ITEDO acquisitions, and was favorably impacted by foreign currency exchange rates. European revenue for the second quarter and first six months of 2007 includes a large customer Enterprise

Solutions consulting and training engagement, while revenue for the first six months of 2006 included a large license transaction from a single customer completed in the first quarter.

*Asia-Pacific.* Revenue performance in Asia-Pacific for the second quarter of 2007 compared to the second quarter of 2006 reflected a 10% increase in revenue in the Pacific Rim and an 12% increase in revenue in Japan. Revenue for the first six months of 2007 compared to the first six months of 2006 reflected a 16% increase in the Pacific Rim and a 19% increase in Japan. We believe that the growth in the Pacific-Rim reflects better execution after strategic and organizational changes we made in that region in 2006 and a growing market opportunity particularly, strong demand for our PLM solutions in China. Revenue performance in Japan in the first six months of 2007 reflected strong first quarter revenue relative to recent quarters and included revenue from a relatively large customer transaction completed in the first quarter. We continue to focus on improving results in Japan and we expect that revenue will grow modestly there for fiscal 2007.

***Revenue from Individual Customers***

We enter into customer contracts that may result in revenue being recognized over multiple reporting periods. Accordingly, revenue recognized in a current quarter may be attributable to contracts entered into during the current period or in prior periods. License and/or consulting and training service revenue of \$1 million or more recognized from individual customers in the second quarter and first six months of 2007 was \$35.6 million and \$63.8 million, respectively, and in the second quarter and first six months of 2006 was \$22.3 million and \$49.4 million, respectively. The second quarter of 2007 results include 16 customers with license and service revenue over \$1 million each, compared to 11 such customers in the second quarter of 2006, reflective of continued success in our strategic account program. While our customers may not continue to spend at these levels in future periods, we believe the strong performance in 2006 and the first half of 2007 is the result of a shift in customer priorities toward PLM solutions relative to other IT spending initiatives, our improved ability to provide broader solutions to our customers, and improvements in our competitive position due to our system architecture and product development process knowledge.

**Table of Contents****Channel Revenue**

Total sales from our reseller channel, which are primarily for our Desktop Solutions, grew 24% and 22% to \$48.9 million and \$96.2 million in the second quarter and first six months of 2007, respectively, from \$39.4 million and \$78.7 million in the second quarter and first six months of 2006, respectively. Sales from our reseller channel comprised 21% of total revenue for both the second quarter and first six months of 2007 compared to 20% of total revenue for both the second quarter and first six months of 2006. We achieved revenue growth in our reseller channel across all major geographies, which we attribute to our efforts to expand our reseller channel, to the success of Pro/ENGINEER Wildfire among small and medium-size businesses, and to sales of recently acquired products.

**Costs and Expenses**

Over the past several years, we have made significant investments to transform our business from providing a single line of technical software with a largely direct distribution model, supplemented by a small number of channel partners, to providing integrated product development system solutions with an expanded channel and partner-involved distribution model. As part of this effort, we broadened our product development system through a series of eight acquisitions completed and substantially integrated since the third quarter of 2004.

The following table shows our costs and expenses by expense category for the periods stated.

	Three months ended			Six months ended		
	March 31, 2007	April 1, 2006	Percent Change	March 31, 2007	April 1, 2006	Percent Change
<b>(Dollar amounts in millions)</b>						
<b>Costs and expenses:</b>						
Cost of license revenue	\$ 4.2	\$ 1.9	123%	\$ 7.8	\$ 5.2	50%
Cost of service revenue	68.6	63.6	8%	137.2	122.6	12%
Sales and marketing	71.5	64.3	11%	141.1	128.2	10%
Research and development	40.2	36.0	12%	78.1	70.6	11%
General and administrative	20.7	18.0	15%	39.6	37.7	5%
Amortization of acquired intangible assets	1.6	1.3	23%	3.7	2.6	39%
Total costs and expenses	\$ 206.8	\$ 185.1	12%(1)	\$ 407.5	\$ 366.9	11%(1)

(1) On a consistent foreign currency basis from the prior period, total costs and expenses increased 9% in both the second quarter and first six months of 2007 compared to the second quarter and first six months of 2006.

Headcount increased to 4,523 at March 31, 2007 from 4,309 at September 30, 2006 and 4,052 at April 1, 2006. Our increases in costs and expenses in the second quarter and first six months of 2007 were primarily due to the following: increases in services delivery capacity to address customer demand for consulting services; and

the Mathsoft and ITEDO acquisitions completed in the third quarter of 2006 and the first quarter of 2007, respectively, which added operating costs and increased headcount.

While we intend to continue to invest in our strategic initiatives to support planned revenue growth and to fund revenue-generating initiatives, we remain focused on achieving our operating margin goals.

*Cost of License Revenue*

Our cost of license revenue consists of fixed and variable costs associated with reproducing and distributing software and documentation as well as royalties paid to third parties for technology embedded in or licensed with our software products. Cost of license revenue as a percentage of license revenue was 6% and 3% for the second quarter of 2007 and 2006, respectively, and 6% and 5% for the first six months of 2007 and 2006, respectively. The increase in cost of license revenue in the second quarter and first six months of 2007 compared to the second quarter and first six months of 2006 was due primarily to higher amortization of purchased software attributable to recent

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acquisitions, which was \$1.1 million and \$1.6 million higher, respectively. Additionally, royalty expense was \$1.1 million and \$0.7 million higher in the second quarter and first six months of 2007, respectively, compared to the year-ago periods. Cost of license revenue as a percent of license revenue can vary depending on product mix sold and the effect of fixed and variable royalties and the level of amortization of acquired software intangible assets.

*Cost of Service Revenue*

Our cost of service revenue includes costs associated with training, customer support and consulting personnel, such as salaries and related costs; third-party subcontractor fees; costs associated with the release of maintenance updates (including related royalty costs); and facility costs. Cost of service revenue as a percentage of service revenue was 44% for both the second quarter and first six months of 2007 and 45% for both the second quarter and first six months of 2006. Service margins can vary based on the product mix sold in the period. Service-related headcount increased to 1,340 at March 31, 2007 from 1,291 at September 30, 2006 and 1,193 at April 1, 2006. Total salaries, commissions, benefits and travel costs were \$2.4 million and \$8.5 million higher in the second quarter and first six months of 2007, respectively, compared to the second quarter and first six months of 2006 due to planned increases in our services delivery capacity. The cost of third-party consulting services was \$1.7 million and \$3.6 million higher in the second quarter and first six months of 2007, respectively, compared to the second quarter and first six months of 2006, due to the use of such services in support of increases in consulting and training service revenue.

*Sales and Marketing*

Our sales and marketing expenses primarily include salaries and benefits, sales commissions, advertising and marketing programs, travel and facility costs. Sales and marketing expenses as a percentage of total revenue were 31% for both the second quarter and first six months of 2007 and 33% for both the second quarter and first six months of 2006. Sales and marketing headcount increased to 1,192 at March 31, 2007 from 1,145 at September 30, 2006 and 1,115 at April 1, 2006. As a result of increases in headcount, primarily due to acquisitions, and higher commissions due to revenue growth, our salaries and benefit costs, sales commissions and travel expenses were higher by an aggregate of \$6.0 million and \$10.8 million in the second quarter and first six months of 2007 compared to the second quarter and first six months of 2006, respectively.

*Research and Development*

Our research and development expenses consist principally of salaries and benefits, costs of computer equipment and facility expenses. Major research and development activities include developing new releases of our software that work together in a more integrated fashion and that include functionality enhancements. Research and development expenses as a percentage of total revenue were 18% in both the second quarter of 2007 and 2006 and 17% and 18% in the first six months of 2007 and 2006, respectively. Research and development headcount increased to 1,535 at March 31, 2007 from 1,437 at September 30, 2006 and 1,335 at April 1, 2006. As a result of these increases in headcount, total salaries, benefits and travel costs were higher in the second quarter and first six months of 2007 compared to the second quarter and first six months of 2006 by an aggregate of \$3.8 million and \$7.3 million, respectively.

*General and Administrative*

Our general and administrative expenses include the costs of our corporate, finance, information technology, human resources, legal and administrative functions as well as bad debt expense. General and administrative expenses as a percentage of total revenue were 9% in both the second quarter of 2007 and 2006 and 9% and 10% in the first six months of 2007 and 2006, respectively. General and administrative headcount was 438 at March 31, 2007, up from 420 at September 30, 2006 and 392 at April 1, 2006. Total salaries, benefits and travel costs were higher in the second quarter and first six months of 2007 compared to the second quarter and first six months of 2006 by an aggregate of \$1.4 million and \$2.9 million, respectively. General and administrative expenses also include costs associated with outside professional services, including accounting and legal fees. The second quarter of 2007 included higher costs for outside professional services incurred in connection with our corporate development initiatives. The first quarter of 2006 included higher costs for outside professional services incurred in connection with our investigation in the Asia-Pacific region described in our 2005 Annual Report on Form 10-K.

**Table of Contents***Amortization of Acquired Intangible Assets*

These costs represent the amortization of acquired intangible assets. The increase in expense in the second quarter and first six months of 2007 compared to the second quarter and first six months of 2006 was due to amortization of intangible assets resulting from the Mathsoft and ITEDO acquisitions completed in the third quarter of 2006 and the first quarter of 2007, respectively.

Our acquisition of Mathsoft in the third quarter of 2006 resulted in an increase in acquired intangible assets of \$25.6 million and goodwill of \$42.0 million. Acquired intangible assets consisted of \$13.9 million of customer relationship intangibles, \$10.3 million of purchased software, and \$1.4 million of trademarks and distributor networks, each of which are being amortized over estimated useful lives of 7 to 10 years, 5 years and 5 years, respectively.

Our acquisition of ITEDO in the first quarter of 2007 resulted in an increase in acquired intangible assets of \$8.1 million and goodwill of \$11.2 million. Acquired intangible assets consisted of purchased software of \$6.2 million, customer relationships of \$1.8 million, and other intangible assets of \$0.1 million, which are being amortized over estimated useful lives of 5 years, 10 years, and 4 years, respectively.

*Other Income (Expense), net*

Other income (expense), net includes interest income, interest expense, costs of hedging contracts, certain realized and unrealized foreign currency transaction gains or losses, charges incurred in connection with obtaining corporate and customer contract financing, and exchange gains or losses resulting from the required period-end currency remeasurement of the financial statements of our subsidiaries that use the U.S. dollar as their functional currency. A large portion of our revenue and expenses are transacted in foreign currencies. To reduce our exposure to fluctuations in foreign exchange rates, we engage in hedging transactions involving the use of foreign currency forward contracts, primarily in the Euro and Asian currencies. Other income (expense), net was \$1.3 million and \$0.8 million for the second quarter of 2007 and 2006, respectively, and \$2.1 million and \$1.9 million for the first six months of 2007 and 2006, respectively. The increase in other income (expense), net in the second quarter and first six months of 2007 is due primarily to higher interest income, partially offset by higher foreign exchange losses and other expense of \$0.7 million recorded in the second quarter of 2007 related to the settlement of a disputed obligation related to a previously divested business unit.

*Income Taxes*

In the second quarter of 2007, our effective tax rate was 23% on pre-tax income of \$22.6 million compared to 40% in the second quarter of 2006 on pre-tax income of \$11.0 million. In the first six months of 2007, our effective tax rate was 27% on pre-tax income of \$44.4 million compared to 40% in the first six months of 2006 on pre-tax income of \$23.1 million. In the second quarter and first six months of 2007, our effective tax rate was lower than the statutory federal income tax rate of 35% due primarily to our use of net operating loss carryforwards (NOLs) to offset our U.S. taxable income (which reduced the valuation allowance we had previously recorded against those NOLs) and to taxes owed in foreign jurisdictions at rates lower than the U.S. statutory tax rate, partially offset by the impact of losses in foreign jurisdictions that could not be benefited, as well as withholding taxes that we incurred in the U.S. in connection with certain foreign operations. In the second quarter and first six months of 2006, our effective tax rate was higher than the statutory federal income tax rate of 35% due primarily to losses in foreign jurisdictions that could not be benefited, as well as withholding taxes that we incurred in the U.S. in connection with certain foreign operations, offset by our use of NOLs to offset our U.S. taxable income (which reduced the valuation allowance we had previously recorded against those NOLs) and to taxes owed in foreign jurisdictions at rates lower than the U.S. statutory tax rate.

In 2002, we recorded a full valuation allowance to completely reserve against our deferred tax assets (which consist primarily of operating loss carryforwards) due to the uncertainty of their realization. Significant management judgment is required to determine when the realization of our deferred tax assets in the future is considered more likely than not. While we have realized consolidated operating profits over the past three years and in the first six months of 2007, we have only recently begun to show consistent profitability in the U.S., and as recently as the fourth quarter of 2005, our U.S. legal entities incurred a taxable loss, due principally to the tax expense associated

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with the grant and vesting of restricted stock units and our employee stock option exchange. Accordingly, we have not yet concluded that realization of our deferred tax assets in the future is more likely than not in the U.S. and certain foreign jurisdictions. As of March 31, 2007, a full valuation allowance was still recorded against remaining deferred tax assets in these jurisdictions. For the remainder of 2007, we will continue to review our operating results to determine if it becomes more likely than not that our deferred tax assets will be realized in the U.S. and certain foreign jurisdictions in the future, at which time we would release some or all of the valuation allowance. Any reduction in our valuation allowance in the future would result in an income tax benefit, higher stockholders' equity and a reduction to goodwill in the period such determination is made and could have a negative impact on our reported net income in future periods as we would expect to begin recording a higher provision for income taxes. Any reduction in our valuation allowance would not impact our cash flow.

Our future effective tax rate may be materially impacted by the amount of income taxes associated with our foreign earnings, which are taxed at rates different from the U.S. federal statutory rate, as well as the timing and extent of the realization of deferred tax assets and changes in the tax law. Further, our tax rate may fluctuate within a fiscal year, including from quarter to quarter, due to items arising from discrete events, including settlements of tax audits and assessments; the resolution or identification of tax position uncertainties; and acquisitions of other companies.

**Liquidity and Capital Resources**

	<b>March 31, 2007</b>	<b>April 1, 2006</b>
	<b>(in thousands)</b>	
Cash and cash equivalents	\$ 238,027	\$ 224,165
Amounts below are for the six months ended:		
Cash provided by operating activities	\$ 76,123	\$ 39,474
Cash used by investing activities	(30,032)	(18,829)
Cash provided by financing activities	4,353	1,699
Cash provided by operating activities included the following:		
Cash disbursements for restructuring and other charges	(3,747)	(5,782)
Cash used by investing activities included the following:		
Cash paid to acquire businesses, net of cash acquired	(17,639)	(10,675)

**Cash and cash equivalents**

We invest our cash with highly rated financial institutions and in diversified domestic and international money market mutual funds. The portfolio is invested in short-term instruments to ensure cash is available to meet requirements as needed. At March 31, 2007, cash and cash equivalents totaled \$238.0 million, up from \$183.4 million at September 30, 2006. The increase in cash and cash equivalents in the first six months of 2007 is due primarily to \$76.1 million of cash provided by operations, partially offset by \$17.6 million paid for acquisitions, primarily ITEDO, and \$12.4 million for additions to property and equipment.

**Cash provided by operating activities**

Cash provided by operating activities was \$76.1 million in the first six months of 2007 compared to cash provided by operating activities of \$39.5 million in the first six months of 2006. This change was due primarily to higher net income and improved customer collections in the first six months of 2007 compared to the first six months of 2006. In addition, cash provided by operating activities in the first six months of 2006 was net of a cash contribution to our U.S. defined benefit pension plan of \$4.2 million.

Days sales outstanding (DSO) was 74 days as of the end of the second quarter of 2007 compared to 69 days as of the end of the second quarter of 2006 and 67 days at September 30, 2006. DSO in the second quarter of 2007 improved from 80 days as of the end of the first quarter of 2007. DSO at the end of the first and second quarters of 2007 compared to year-ago periods were affected by the amount of extended payment term deals we offered to customers during 2006 and the first half of 2007. We offer these terms to some customers with established payment and credit

histories.



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We provided extended payment terms on transactions accounting for approximately \$51 million of revenue in 2006 and \$14 million and \$12 million in the first six months of 2007 and 2006, respectively. Other assets in the accompanying consolidated balance sheets include non-current receivables from customers related to extended payment term contracts totaling \$25.6 million and \$31.1 million at March 31, 2007 and September 30, 2006, respectively.

***Cash used by investing activities***

Cash used by investing activities was \$30.0 million in the first six months of 2007 compared to \$18.8 million in the first six months of 2006. The increase in cash used by investing activities in the first six months of 2007 was primarily due to disbursements for acquisitions of \$17.6 million in the first six months of 2007, including \$16.7 million for the ITEDO acquisition, compared to \$10.7 million in the first six months of 2006. In addition, cash used for additions to property and equipment increased to \$12.4 million in the first six months of 2007 compared to \$8.2 million in the first six months of 2006, primarily as a result of increased headcount. Our expenditures for property and equipment consist primarily of computer equipment, software, office equipment and facility improvements.

***Cash provided by financing activities***

Cash provided by financing activities was \$4.4 million and \$1.7 million in the first six months of 2007 and 2006, respectively. The increase in 2007 compared to 2006 is primarily due to higher proceeds from the issuance of common stock upon the exercise of stock options, which were \$10.9 million in the first six months of 2007 compared to \$2.9 million in the first six months of 2006. During the first six months of 2007, we used \$6.5 million to pay employee withholding taxes related to restricted stock units that vested during the period in lieu of issuing shares to employees with respect to those awards.

***Credit Facility***

On February 21, 2006, we entered into a multi-currency bank revolving credit facility. The credit facility consists of a \$230 million revolving credit facility, which may be increased by up to an additional \$150 million if the existing or additional lenders are willing to make such increased commitments. The credit facility expires on February 20, 2011, when all amounts will be due and payable in full. We expect to use the credit facility for general corporate purposes, including acquisitions of businesses. We have not borrowed any funds under the credit facility to date.

The credit facility limits our and our subsidiaries' ability to take certain actions and requires that we and our subsidiaries maintain specified leverage and fixed-charge ratios. These limitations are described in Note 11 to our Consolidated Financial Statements. We were in compliance with all financial and operating covenants of the credit facility as of March 31, 2007.

***Share Repurchase Authorization***

In September 1998, our Board of Directors authorized the repurchase of up to 8.0 million shares of our common stock and in July 2000 increased the shares authorized for repurchase to 16.0 million. Since 1998, we have repurchased, at a cost of \$366.8 million, a total of 12.5 million shares of the 16.0 million shares authorized. Although we have not repurchased any shares since 2003, we periodically consider repurchasing shares. If we were to repurchase shares, it would reduce our cash balances.

***Expectations for Fiscal 2007***

We believe that existing cash and cash equivalents together with cash we expect to generate from operations will be sufficient to meet our working capital and capital expenditure requirements through at least the next twelve months. During the remainder of 2007, we expect to make cash disbursements estimated at \$4 million for restructuring charges incurred in 2006 and prior periods, capital expenditures of approximately \$10 million, and a contribution of approximately \$7 million to a non-US pension plan.

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We have evaluated, and expect to continue to evaluate, possible strategic transactions on an ongoing basis and at any given time may be engaged in discussions or negotiations with respect to possible strategic transactions. Our cash position could be reduced and we may incur debt obligations to the extent we complete any significant transactions.

### **Critical Accounting Policies and Estimates**

Our critical accounting policies and estimates are set forth under the heading *Critical Accounting Policies and Estimates* in Part II, Item 7 *Management's Discussion and Analysis of Financial Condition and Results of Operations* of our 2006 Annual Report on Form 10-K. There have been no changes to these policies and no significant changes to these estimates since September 30, 2006.

### **New Accounting Pronouncements**

#### *Accounting for Uncertainty in Income Taxes*

In July 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure relative to uncertain tax positions. FIN 48 is effective for fiscal years beginning after December 15, 2006, with early adoption encouraged. We will adopt FIN 48 in fiscal 2008. We are currently evaluating whether or not the adoption of FIN 48 will have a material effect on our consolidated financial position, results of operations or cash flows.

#### *Fair Value Measurements*

In September 2006, the FASB issued Statement No. 157, *Fair Value Measurements* (SFAS 157). This Statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We do not believe the adoption of SFAS 157 in fiscal 2009 will have a material effect on our consolidated financial position, results of operations or cash flows.

#### *Fair Value Option for Financial Assets and Financial Liabilities*

In February 2007, the FASB issued Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* (SFAS 159). This Statement permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This Statement is expected to expand the use of fair value measurement, which is consistent with the FASB's long-term measurement objectives for accounting for financial instruments. The fair value option established by this Statement permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity must report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. This Statement is effective as of the beginning of fiscal 2009, with early adoption permitted. We do not believe the adoption of SFAS 159 will have a material effect on our consolidated financial position, results of operations or cash flows.

## **ITEM 4. CONTROLS AND PROCEDURES**

### ***Evaluation of Effectiveness of Disclosure Controls and Procedures***

Our management maintains disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the *Exchange Act*) that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Exchange Act is processed, recorded, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer (our principal executive officer and principal financial officer, respectively), as appropriate, to allow for timely decisions

regarding required disclosure.

We, under the supervision and with the participation of our management, including our principal executive and principal financial officers, evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of March 31, 2007 in connection with the filing of the Original Form 10-Q. Based on that evaluation, we concluded at that time that our disclosure controls and procedures were effective.

Subsequent to the evaluation made in connection with the filing of the Original Form 10-Q, and in connection with the restatement of our prior period financial statements described in Part I, Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations of this Form 10-Q/A and the filing of this Form 10-Q/A, we, under the supervision and with the participation of our management, including our principal executive and principal financial officers, re-evaluated the effectiveness of the design and operation of our disclosure controls and procedures and concluded that, because the material weakness in our internal control over financial reporting described below existed at that time, our disclosure controls and procedures were not effective as of March 31, 2007.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis.

Subsequent to the filing of the Original Form 10-Q, we identified a material weakness in our internal control over financial reporting in that we did not maintain effective controls over the accounting for income taxes, including the determination and reporting of accrued income taxes, deferred taxes and the related income tax provision.

Specifically, we did not have adequate personnel to enable us to properly consider and apply generally accepted accounting principles for taxes, review and monitor the accuracy and completeness of the components of the income tax provision calculations and the related deferred taxes and accrued income taxes, ensure that the rationale for certain tax positions was appropriate, and ensure that effective oversight of the work performed by our outside tax advisors was exercised. This material weakness resulted in the restatement of our unaudited interim consolidated financial statements as of and for the period ended March 31, 2007. In addition, until remediated, this material weakness could result in a misstatement in the tax-related accounts described above that would result in a material misstatement to our interim or annual consolidated financial statements and disclosures that would not be prevented or detected.

Notwithstanding the existence of this material weakness, we have concluded that the consolidated financial statements in this Form 10-Q/A fairly present, in all material respects, our financial position, results of operations and cash flows for the periods presented.

#### ***Remediation Initiatives***

Our management is in the process of actively addressing and remediating the material weakness in internal control over financial reporting described above. During 2008, we will undertake the following actions to remediate the material weakness identified:

Hire additional personnel and retain professional advisors trained and experienced in income tax accounting;

Re-evaluate the design of income tax accounting processes and controls and implement new and improved processes and controls, if warranted; and

Increase the level of review and discussion of significant tax matters and supporting documentation with senior finance management.

As part of our 2008 assessment of internal control over financial reporting, our management will conduct sufficient testing and evaluation of the controls to be implemented as part of this remediation plan to ascertain that they operate effectively.

#### ***Changes in Internal Control over Financial Reporting***

There was no change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the third fiscal quarter ended March 31, 2007 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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**PART II OTHER INFORMATION**

**ITEM 6. EXHIBITS**

- 10 Compensatory Arrangements with Directors (filed as Exhibit 10 to our Quarterly Report on Form 10-Q for the period ended March 31, 2007 (File No. 0-18059) and incorporated herein by reference).
- 31.1 Certification of the Chief Executive Officer Pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a).
- 31.2 Certification of the Chief Financial Officer Pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a).
- 32\* Certification of Periodic Financial Report Pursuant to 18 U.S.C. Section 1350.

\* Indicates that the exhibit is being furnished with this report and is not filed as a part of it.

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**SIGNATURE**

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

Parametric Technology Corporation

By: /s/ Cornelius F. Moses, III  
**Cornelius F. Moses, III**  
**Executive Vice President and**  
**Chief Financial Officer**  
**(Principal Financial Officer)**

Date: December 11, 2007

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