ANSYS INC
Form 10-Q
May 05, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2006

OR

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

Commission File Number: 0-20853

ANSYS, Inc.

(exact name of registrant as specified in its charter)

Delaware	**04-3219960**
(State or other jurisdiction of incorporation or organization)	**(IRS Employer Identification No.)**
275 Technology Drive, Canonsburg, PA	**15317**
(Address of principal executive offices)	**(Zip Code)**

724-746-3304

(Registrant s telephone number, including area code)

Indicate by a 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 x No ¨

Indicate by a check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Exchange Act Rule 12b-2). (Check one):

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by a check mark whether the Registrant is a shell company (as defined in Exchange Act Rule 12b-2). Yes ¨ No x

The number of shares of the Registrant s Common Stock, par value $.01 per share, outstanding as of May 3, 2006 was 38,273,775 shares.

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PART I UNAUDITED FINANCIAL INFORMATION

Item 1. Financial Statements:

ANSYS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share information)

(Unaudited)

	March 31, 2006	December 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 197,159	$ 176,166
Short-term investments	6,071	18,066
Accounts receivable, less allowance for doubtful accounts of $2,214 and $2,231, respectively	22,491	19,134
Other receivables and current assets	28,014	25,065
Deferred income taxes	4,179	4,055
Total current assets	257,914	242,486
Property and equipment, net	6,265	6,362
Capitalized software costs, net	528	642
Goodwill	44,582	43,277
Other intangibles, net	9,440	10,122
Other long-term assets	3,864	467
Deferred income taxes	2,950	2,153
Total assets	$ 325,543	$ 305,509
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 1,385	$ 1,330
Accrued bonuses	4,368	9,631
Other accrued expenses and liabilities	16,845	19,677
Deferred revenue	57,724	49,894
Total current liabilities	80,322	80,532
Long-term liabilities	1,375	
Commitments and contingencies		
Stockholders equity:		
Preferred stock, $.01 par value; 2,000,000 shares authorized; zero issued or outstanding		
Common stock, $.01 par value; 50,000,000 shares authorized; 33,169,516 shares issued and outstanding	332	332
Additional paid-in capital	62,913	59,543
Retained earnings	192,084	179,171
Treasury stock, at cost: 923,512 and 1,121,726 shares, respectively	(16,028)	(18,340)
Accumulated other comprehensive income	4,546	4,271

Total stockholders equity	243,846	224,977
Total liabilities and stockholders equity	$ 325,543	$ 305,509

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

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ANSYS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(in thousands, except per share data)

(Unaudited)

	Three Months Ended	
	March 31, 2006	March 31, 2005
Revenue:		
Software licenses	$ 26,752	$ 20,475
Maintenance and service	19,259	17,149
Total revenue	46,011	37,624
Cost of sales:		
Software licenses	1,490	1,253
Amortization of software and acquired technology	908	907
Maintenance and service	4,470	3,858
Total cost of sales	6,868	6,018
Gross profit	39,143	31,606
Operating expenses:		
Selling and marketing	7,159	6,428
Research and development	9,357	7,313
Amortization	128	326
General and administrative	4,680	4,118
Total operating expenses	21,324	18,185
Operating income	17,819	13,421
Other income	1,698	613
Income before income tax provision	19,517	14,034
Income tax provision	6,604	4,351
Net income	$ 12,913	$ 9,683
Earnings per share - basic:		
Basic earnings per share	$ 0.40	$ 0.31
Weighted average shares - basic	32,122	31,492
Earnings per share - diluted:		
Diluted earnings per share	$ 0.38	$ 0.29
Weighted average shares - diluted	34,165	33,766

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

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ANSYS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

	Three Months Ended	
	March 31, 2006	March 31, 2005
Cash flows from operating activities:		
Net income	$ 12,913	$ 9,683
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,872	2,021
Deferred income tax benefit	(819)	(395)
Provision for bad debts	59	125
Stock-based compensation expense	1,224	
Changes in operating assets and liabilities:		
Accounts receivable	(3,276)	1,415
Other receivables and current assets	(2,743)	(1,077)
Accounts payable, accrued expenses and liabilities	(4,198)	(3,377)
Deferred revenue	7,596	6,925
Net cash provided by operating activities	12,628	15,320
Cash flows from investing activities:		
Capital expenditures	(790)	(1,461)
Acquisition payments, net of cash acquired	(6,925)	(4,157)
Purchases of short-term investments	(6,000)	(24,866)
Maturities of short-term investments	18,000	200
Net cash provided by (used in) investing activities	4,285	(30,284)
Cash flows from financing activities:		
Proceeds from issuance of common stock under Employee Stock Purchase Plan	490	338
Proceeds from exercise of stock options	1,698	1,387
Loan commitment fees	(250)	
Excess tax benefits from stock options	1,964	
Net cash provided by financing activities	3,902	1,725
Effect of exchange rate fluctuations on cash and cash equivalents	178	(402)
Net increase/(decrease) in cash and cash equivalents	20,993	(13,641)
Cash and cash equivalents, beginning of period	176,166	83,547
Cash and cash equivalents, end of period	$ 197,159	$ 69,906
Supplemental disclosures of cash flow information:		
Cash paid during the period for income taxes	$ 7,308	$ 3,384

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

ANSYS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2006

(Unaudited)

1. Organization

ANSYS, Inc. (the Company or ANSYS) develops and globally markets engineering simulation software and technologies widely used by engineers and designers across a broad spectrum of industries, including aerospace, automotive, manufacturing, electronics, biomedical and defense.

The Company operates as one segment, as defined by Statement of Financial Accounting Standards No. 131, *Disclosures about Segments of an Enterprise and Related Information*. Given the integrated approach to the multi-discipline problem-solving needs of the Company s customers, a single sale of software may contain components from multiple product areas and include combined technologies. There is no means by which the Company can provide accurate historical or current reporting among its various product-line segmentations. Disclosure of such information is impracticable.

2. Summary of Significant Accounting Policies

The accompanying unaudited condensed consolidated financial statements have been prepared by ANSYS, Inc. in accordance with accounting principles generally accepted in the United States of America for interim financial information for commercial and industrial companies and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, the accompanying statements do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. The accompanying condensed consolidated financial statements should be read in conjunction with the Company s consolidated financial statements (and notes thereto) included in the Company s Annual Report on Form 10-K for the year ended December 31, 2005. The condensed consolidated December 31, 2005 balance sheet presented is derived from the audited December 31, 2005 balance sheet included in the most recent Form 10-K. In the opinion of management, all adjustments considered necessary for a fair presentation of the financial statements have been included, and all adjustments are of a normal and recurring nature. Operating results for the three months ended March 31, 2006 are not necessarily indicative of the results that may be expected for any future period.

Concentrations of Credit Risk: The Company has a concentration of credit risk with respect to trade receivables due to the limited number of distributors through which the Company sells its products. The Company performs periodic credit evaluations of its customers financial condition and generally does not require collateral.

In addition to the concentration of credit risk with respect to trade receivables, the Company s cash and cash equivalents are also exposed to concentration of credit risk. The Company maintains its cash accounts primarily in U.S. banks, which are insured by the F.D.I.C. up to $100,000 per bank. The Company had cash balances on deposit with a U.S. bank at March 31, 2006 that exceeded the balance insured by the F.D.I.C. in the amount of approximately $40.5 million. A significant portion of the Company s remaining U.S. cash balance is also uninsured. As a result of the Company s operations in international locations, it also has significant, uninsured cash balances denominated in foreign currencies and held outside of the U.S.

Stock-Based Compensation: In December 2004, the FASB issued a revised version of FASB Statement No. 123, *Accounting for Stock-Based Compensation* (Statement No. 123(R)). The statement requires a public entity 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. The cost will be recognized over the period during which an employee is required to provide service in exchange for the award, typically the vesting period. Statement No. 123(R) also requires the benefits of tax deductions in excess of recognized compensation expense to be reported as a financing cash flow, rather than as an operating cash flow as prescribed under the prior accounting rules. This requirement reduces net operating cash flows and increases net financing cash flows in periods after adoption. Total cash flow remains unchanged from what would have been reported under prior accounting rules. The Company adopted Statement No. 123(R), using a modified prospective application, in compliance with the revised implementation date on January 1, 2006. Under the modified prospective application, prior periods are not revised for comparative purposes. The valuation provisions of Statement No. 123(R) apply to new awards and to awards that were outstanding at the effective date and subsequently modified or cancelled.

On November 10, 2005, the FASB issued FASB Staff Position No. FAS 123(R)-3, *Transition Election Related to Accounting for Tax Effects of Share-Based Payment Awards.* The Company has elected to adopt the alternative transition method provided in this FASB Staff Position for calculating the tax effects of share-based compensation pursuant to Statement No. 123(R). The alternative transition method includes a simplified method to establish the beginning balance of the additional paid-in capital pool (APIC pool) related to the tax effects of employee share-based compensation, which is available to absorb tax deficiencies recognized subsequent to the adoption of Statement No. 123(R).

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Share-Based Compensation Information under Statement No. 123(R).

The Company issues both nonqualified and incentive stock options; however, incentive stock options comprise a significant portion of outstanding stock options. The tax benefits associated with incentive stock options are unpredictable, as they are predicated upon an award recipient triggering an event that disqualifies the award and which then results in a tax deduction to the Company. Statement No. 123(R) requires that these tax benefits be recorded at the time of the triggering event. The triggering events for each option holder are not easily projected. In order to estimate the tax benefits related to incentive stock options, the Company makes many assumptions and estimates, including the number of incentive stock options that will be exercised during the period by U.S. employees, the number of incentive stock options that will be disqualified during the period and the fair market value of the Company s stock price on the exercise dates. Each of these items is subject to significant uncertainty. Additionally, a significant portion of the tax benefits related to disqualified incentive stock options are accounted for as increases to equity (additional paid-in capital) rather than as reductions in income tax expense, especially in the periods most closely following the adoption date of Statement 123(R). Although all such benefits continue to be realized through the Company s tax filings, this accounting treatment has the effect of increasing tax expense and reducing net income. For example, the Company realized a tax benefit of $1.9 million during the first quarter of 2006 related to disqualified incentive stock options; however, only $25,000 of such amount was recorded as a reduction in income tax expense. Although there are significant limitations in estimating the impact of Statement 123(R), including those discussed above, the Company currently estimates that the adoption of Statement 123(R) will decrease 2006 net income by $4.5 $5.0 million in 2006, or approximately $0.13 - $0.15 per diluted share, including $982,000, or $0.03 per diluted share, recorded in the quarter ended March 31, 2006. This estimate does not include the impact of additional stock options that may be issued to Fluent employees in connection with the acquisition of Fluent Inc. that is discussed in Note 6 below.

The weighted-average fair value of options granted during the three months ended March 31, 2006 was $20.15 per share. The fair value of each option grant is estimated on the date of grant using the Black-Scholes options pricing model, which was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. The Company s options have characteristics significantly different from those of traded options, and changes in input assumptions can materially affect the fair value estimates. The fair values of options granted were estimated using the Black-Scholes pricing model with a risk-free interest rate of 4.73%. The interest rates used were determined by using the five-year Treasury Note yield at the date of grant. The following assumptions were also used to determine the fair value of each option grant: dividend yields of 0%; expected volatility of 48%, and expected term of 5.0 years. The volatility was determined based on the historic volatility of the Company s stock during the preceding five years.

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As share-based compensation expense recognized in the Condensed Consolidated Statement of Income for the first quarter of fiscal 2006 is based on awards ultimately expected to vest, it should be reduced for estimated forfeitures. Statement 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Pre-vesting forfeitures were estimated to be approximately 0.8% in the first quarter of fiscal 2006 based on historical experience. The effect of pre-vesting forfeitures on the Company s recorded expense has historically been negligible due to the relatively low turnover of holders of stock options. In the Company s pro forma information required under Statement No. 123(R) for the periods prior to fiscal 2006, the Company also accounted for forfeitures as they occurred.

Total estimated share-based compensation expense, related to the Company s share-based awards, recognized for the three months ended March 31, 2006 was comprised as follows:

(in thousands, except per share data)

	Three Months Ended March 31, 2006
Cost of sales:	
Software licenses	$ 10
Maintenance and service	42
Operating Expenses:	
Selling and marketing	415
Research and development	298
General and administrative	459
Share-based compensation expense before taxes	1,224
Related income tax benefits	(240)
Share-based compensation expense, net of taxes	$ 984

The Company recorded $550 in share-based compensation expense during the three months ended March 31, 2006 related to share-based awards granted during the first quarter of 2006. In addition, for the three months ended March 31, 2006, the adoption of Statement No. 123(R) resulted in a reclassification to reduce net cash provided by operating activities with an offsetting increase in net cash provided by financing activities of $2.0 million related to the incremental tax benefits from stock options exercised in the period.

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Pro Forma Information under SFAS No. 123 for Periods Prior to January 1, 2006

Prior to the adoption of Statement No. 123(R), the Company had elected to account for stock-based compensation arrangements through the intrinsic value method under the provisions of Accounting Principles Board Opinion No. 25, *Accounting for Stock-Based Compensation*. Under the intrinsic value method, compensation expense is measured as the excess, if any, of the market value of the underlying common stock over the amount the employee is required to pay on the date both the number of shares and the price to be paid are known. No compensation expense had been recognized in the consolidated statements of income as option grants generally are made with exercise prices equal to the fair value of the underlying common stock on the award date, which is typically the date of compensation measurement. Had compensation cost been determined based on the fair value at the date of grant, in accordance with the provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*, the Company s net income and basic and diluted earnings per share for the three months ended March 31, 2005 would have been reduced to the pro forma amounts indicated below:

(in thousands, except per share data)	**Three Months Ended March 31, 2005**	
Net income, as reported	$	9,683
Add: Stock-based employee compensation expense included in net income, net of related tax effects		
Deduct: Stock-based employee compensation expense determined under the fair value-based method for all awards, net of related tax effects		(865)
Pro forma net income	$	8,818
Earnings per share:		
Basic as reported	$	0.31
Basic pro forma	$	0.28
Diluted as reported	$	0.29
Diluted pro forma	$	0.26

The weighted-average fair value of options granted during the three months ended March 31, 2005 was $16.03 per share. The fair values of options granted were estimated using the Black-Scholes pricing model with a weighted average risk-free interest rate of 3.66%. The interest rates used were determined by using the five-year Treasury Note yield at the date of grant. The following assumptions were also used to determine the fair value of each option grant: dividend yields of 0%; expected volatility of 50%, and expected term of 5.1 years.

Reclassifications: Certain reclassifications have been made to the 2005 condensed consolidated balance sheet and to the Goodwill and Intangible Assets footnote to conform to the 2006 presentation.

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3. Accumulated Other Comprehensive Income

As of March 31, 2006 and December 31, 2005, accumulated other comprehensive income, as reflected on the Condensed Consolidated Balance Sheets, was comprised of foreign currency translation adjustments.

Comprehensive income for the three-month periods ended March 31, 2006 and 2005 was as follows:

(in thousands)	Three Months Ended	
	March 31, 2006	**March 31, 2005**
Comprehensive income	$ 13,188	$ 8,910

4. Other Current Assets

The Company reports accounts receivable related to the portion of annual lease licenses and software maintenance that has not yet been recognized as revenue as a component of other current assets. These amounts totaled $22.6 million and $21.0 million as of March 31, 2006 and December 31, 2005, respectively.

5. Earnings Per Share

Basic earnings per share (EPS) amounts are computed by dividing earnings by the average number of common shares outstanding during the period. Diluted EPS amounts assume the issuance of common stock for all potentially dilutive equivalents outstanding. The details of basic and diluted earnings per share are as follows:

(in thousands, except per share data)	Three Months Ended	
	March 31, 2006	**March 31, 2005**
Net income	$ 12,913	$ 9,683
Weighted average shares outstanding basic	32,122	31,492
Basic earnings per share	$ 0.40	$ 0.31
Effect of dilutive securities:		
Shares issuable upon exercise of dilutive outstanding stock options	2,043	2,274
Weighted average shares outstanding diluted	34,165	33,766
Diluted earnings per share	$ 0.38	$ 0.29
Anti-dilutive shares/options	5	252

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6. Acquisitions

On January 5, 2005, the Company acquired Century Dynamics, Inc. (hereafter CDI), for an initial purchase price of approximately $5.1 million in cash. In addition, the agreement provided for a future cash payment contingent upon the attainment of certain 2005 performance criteria. This payment was $4.5 million and was accounted for as an addition to both goodwill and other accrued expenses and liabilities in 2005. It was paid to the previous owners of CDI in the first quarter of 2006. The operating results of CDI have been included in ANSYS, Inc. s consolidated financial statements since the date of acquisition.

Had the acquisition occurred on January 1, 2005, the 2005 results would not be materially different from those presented in these consolidated financial statements. Accordingly, the Company has not presented pro forma information on revenue, net income or earnings per share.

In October 2005, the Company acquired substantially all of the assets and certain liabilities of Harvard Thermal, Inc. (hereafter HTI), a leader in thermal analysis software tools, for an up-front purchase price of approximately $1.3 million in cash and stock. In addition, the acquisition agreement provides for future payments of up to $400,000, contingent upon the attainment of certain performance criteria, of which $100,000 was recorded as an addition to goodwill during the first quarter of 2006 and paid primarily through the issuance of treasury stock. The operating results for HTI have been included with the Company s operating results from the date of acquisition.

Had the acquisition of HTI occurred on January 1, 2005, the 2005 results would not be materially different from those presented in these financial statements. Accordingly, the Company has not presented pro forma information on revenue, net income or earnings per share.

On May 1, 2006, the Company completed its acquisition of Fluent Inc. (hereafter Fluent), a global provider of CFD-based computer-aided engineering software and services. Under the terms of the merger agreement, the Company issued 5,999,948 shares of its common stock, valued at approximately $274 million based on the average closing market price on the two days preceding and the two days following the announcement of the acquisition, and paid approximately $299 million in net cash to acquire Fluent. The total purchase price of approximately $573 million includes approximately $12 million in transaction fees. The Company used a combination of existing cash and approximately $200 million from committed bank financing to fund the transaction. The interest rate on the indebtedness associated with the transaction is based on the Company s consolidated leverage ratio and generally ranges from LIBOR + (0.50% - 1.25%) or, at the Company s election, Prime Rate + (0.00% - 0.25%.) The debt is scheduled to be repaid over a period of five years and includes covenants related to the consolidated leverage ratio and the consolidated fixed charge coverage ratio, as well as certain restrictions on additional investments and indebtedness. The acquisition of Fluent is expected to enhance the breadth, functionality, usability and interoperability of the ANSYS portfolio of simulation solutions. This will increase operational efficiency and lower design and engineering costs for customers, and accelerate development and delivery of new and innovative products to the marketplace. Transaction-related costs of $3.9 million were incurred as of March 31, 2006 and have been recorded as other long-term assets within the condensed consolidated balance sheet.

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The acquisition of Fluent will be included in the Company s operations as of May 1, 2006. Accordingly, the condensed consolidated statements of income included in this Form 10-Q do not include any operating results related to Fluent. Because of the timing of the acquisition with respect to the filing of this Form 10-Q, the Company has not yet completed the valuation of the assets and liabilities of Fluent. As such, information concerning the amounts assigned to each major asset and liability, including amounts assigned to intangible assets and goodwill, is not yet available.

7. Goodwill and Intangible Assets

During the first quarter of 2006, the Company completed the annual impairment test for goodwill and intangible assets with indefinite lives, and determined these assets had not been impaired as of January 1, 2006. The Company tested the goodwill and identified intangible assets attributable to each of its reporting units utilizing estimated cash flow methodologies and market comparable information. No events occurred or circumstances changed during the three months ended March 31, 2006 that required an interim goodwill impairment test.

Identifiable intangible assets with finite lives continue to be amortized on a straight-line basis over their estimated useful lives and are reviewed for impairment whenever events or circumstances indicate that the carrying amounts may not be recoverable.

As of March 31, 2006 and December 31, 2005, the Company s intangible assets have estimated useful lives and are classified as follows:

(in thousands)	**March 31, 2006**		**December 31, 2005**	
	Gross Carrying Amount	**Accumulated Amortization**	**Gross Carrying Amount**	**Accumulated Amortization**
Amortized intangible assets:				
Core technology and trademarks (3 10 years)	$ 18,632	$ (11,264)	$ 18,544	$ (10,393)
Non-compete agreements (4 5 years)	3,082	(2,576)	2,892	(2,531)
Customer lists (3 5 years)	2,408	(2,408)	2,399	(2,344)
Total	$ 24,122	$ (16,248)	$ 23,835	$ (15,268)
Unamortized intangible assets:				
Trademarks	$ 1,566		$ 1,555	

Amortization expense for the amortized intangible assets reflected above for the three months ended March 31, 2006 and March 31, 2005 was approximately $900,000 and $1.1 million, respectively.

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Amortization expense for the amortized intangible assets reflected above is expected to be approximately $3.5 million, $3.4 million, $860,000, $360,000 and $270,000 for the years ending December 31, 2006, 2007, 2008, 2009 and 2010, respectively.

The changes in goodwill during the three-month period ended March 31, 2006 are as follows:

(in thousands)	
Balance January 1, 2006	$ 43,277
Acquisition payments	1,125
Currency translation & other	180
Balance March 31, 2006	$ 44,582

8. Geographic Information

Revenue by geographic area for the three months ended March 31, 2006 and 2005 is as follows:

(in thousands)	**Three Months Ended**	
	March 31, 2006	**March 31, 2005**
United States	$ 17,805	$ 11,935
Canada	1,249	1,071
United Kingdom	3,062	2,811
Germany	6,684	5,845
Japan	5,338	5,468
Other European	7,525	6,951
Other International	4,348	3,543
Total revenue	$ 46,011	$ 37,624

Long-lived assets (excluding deferred tax assets) by geographic area are as follows:

(in thousands)	**March 31, 2006**	**December 31, 2005**
United States	$ 41,669	$ 37,470
Canada	5,805	6,041
United Kingdom	7,273	7,521
Germany	3,536	3,473
Japan	854	862
Other European	5,271	5,225
Other International	271	278
Total long-lived assets	$ 64,679	$ 60,870

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9. Stock Repurchase Program

In October 2001, the Company announced that its Board of Directors had amended its existing stock repurchase program to acquire up to an additional one million shares, or four million shares in total under the program that was initially announced in February 2000. Under this program, no shares were repurchased in the three-month period ended March 31, 2006 or 2005. As of March 31, 2006, 2.0 million shares remain authorized for repurchase under the program.

10. Stock Option and Grant Plans

The Company has two stock option and grant plans the 1994 Stock Option and Grant Plan (1994 Stock Plan) and the Second Amended and Restated 1996 Stock Option and Grant Plan (1996 Stock Plan). The 1994 and 1996 Stock Plans, as amended, authorize the grant of up to 1,736,220 and 10,700,000 shares, respectively, of the Company s common stock in the form of: (i) incentive stock options (ISOs), (ii) nonqualified stock options or (iii) the issuance or sale of common stock with or without vesting or other restrictions. Additionally, the 1996 Stock Plan permits the grant of common stock upon the attainment of specified performance goals and the grant of the right to receive cash dividends with the holders of the common stock as if the recipient held a specified number of shares of the common stock. No further grants may be made under the 1994 Stock Plan.

The 1994 and 1996 Stock Plans provide that: (i) the exercise price of an ISO must be no less than the fair value of the stock at the date of grant and (ii) the exercise price of an ISO held by an optionee who possesses more than 10% of the total combined voting power of all classes of stock must be no less than 110% of the fair market value of the stock at the time of grant. The Board of Directors has the authority to set expiration dates no later than ten years from the date of grant (or five years for an optionee who meets the 10% criteria), payment terms and other provisions for each grant. Shares associated with unexercised options or reacquired shares of common stock become available for options or issuances under the 1996 Stock Plan. The Compensation Committee of the Board of Directors may, at its sole discretion, accelerate or extend the date or dates on which all or any particular award or awards granted under the 1994 and 1996 Stock Plans may vest or be exercised. In the event of a merger, liquidation or sale of substantially all of the assets of the Company, the Board of Directors has the discretion to accelerate the vesting of the options granted under the 1994 and 1996 Stock Plans, except that options granted to Independent Directors and certain key executives vest automatically. Under certain scenarios, other optionees may also automatically vest upon the occurrence of such an event. In addition, the 1994 and 1996 Stock Plans and the grants issued thereunder terminate upon the effectiveness of any such transaction or event, unless a provision is made in connection with such transaction for the assumption of grants theretofore made. Under the 1996 Stock Plan, at the discretion of the Compensation Committee, any option may include a reload feature. Such feature allows an optionee exercising an option to receive, in addition to the number of shares of common stock due on the exercise, an additional option with an exercise price equal to the fair market value of the common stock on the date such additional option is granted.

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In addition, the 1996 Stock Plan provided for the automatic grant of non-qualified options to Independent Directors. Under such provisions, each Independent Director received an annual grant to purchase 12,000 shares of common stock. These options vested in annual installments over four years, commencing with the date of grant, and expired ten years after the grant, subject to earlier termination if the optionee ceased to serve as a director. Recently, the Board of Directors modified the director compensation arrangements such that the Chairman of the Board of Directors and the non-affiliate Independent Directors will receive, at their option, (i) an annual grant of 3,600 deferred stock units, which are rights to receive shares of common stock upon termination of service as a director, or (ii) options to purchase 12,000 shares of common stock. The stock options have a vesting period of four years and the deferred stock units have a vesting period of one year. The exercisability of unvested stock options will be accelerated upon the occurrence of a merger, liquidation or sale of substantially all of the assets of the Company.

The Company currently issues shares related to exercised stock options from its existing pool of treasury shares and currently has no specific policy to repurchase treasury shares as stock options are exercised.

Information regarding stock option transactions for the three months ended March 31, 2006 is summarized below:

(options in thousands)	Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (in thousands)
Outstanding, beginning of year	3,622	$ 14.05		
Granted	5	$ 49.57		
Exercised	(180)	$ 9.41		
Forfeited	(1)	$ 24.05		
Outstanding, March 31, 2006	3,446	$ 14.35	6.00	$ 137,153
Exercisable, March 31, 2006	2,335	$ 8.94	4.92	$ 105,559

The Company s determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by the Company s stock price as well as assumptions regarding a number of highly complex and subjective variables. The total estimated grant date fair value of stock options that vested during the three months ended March 31, 2006 was $1.2 million. At March 31, 2006, total unrecognized estimated compensation cost related to non-vested stock options granted prior to that date was $12.6 million, which is expected to be recognized over a weighted average period of 2.6 years. The total intrinsic value of stock options exercised during the three months ended March 31, 2006 was $6.9 million. The Company recorded cash received from the exercise of stock options of $1.7 million and related tax benefits of $2.2 million during the three months ended March 31, 2006.

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Information regarding stock options outstanding as of March 31, 2006 is summarized below:

(options in thousands)	Options Outstanding			Options Exercisable	
		Weighted Average Remaining Contractual Life	Weighted Average Exercise Price		Weighted Average Exercise Price
Range of Exercise Prices	**Options**	**(years)**	**Price**	**Options**	**Price**
$3.00 - $4.94	436	2.43	$ 4.14	436	$ 4.14
$5.00 - $9.89	1,490	5.03	$ 7.49	1,383	$ 7.30
$11.13 - $21.72	778	7.04	$ 15.19	417	$ 13.92
$31.09 - $49.57	742	8.94	$ 33.24	99	$ 32.17

11. Employee Stock Purchase Plan

The Company s 1996 Employee Stock Purchase Plan (the Purchase Plan) was adopted by the Board of Directors on April 19, 1996 and was subsequently approved by the Company s stockholders. The stockholders approved an amendment to the Purchase Plan on May 6, 2004 to increase the number of shares available for offerings to 800,000 shares. The Purchase Plan is administered by the Compensation Committee. Offerings under the Purchase Plan commence on each February 1 and August 1, and have a duration of six months. An employee who owns or is deemed to own shares of stock representing in excess of 5% of the combined voting power of all classes of stock of the Company may not participate in the Purchase Plan.

During each offering, an eligible employee may purchase shares under the Purchase Plan by authorizing payroll deductions of up to 10% of his cash compensation during the offering period. The maximum number of shares that may be purchased by any participating employee during any offering period is limited to 1,920 shares (as adjusted by the Compensation Committee from time to time). Unless the employee has previously withdrawn from the offering, his accumulated payroll deductions will be used to purchase common stock on the last business day of the period at a price equal to 85% of the fair market value of the common stock on the first or last day of the offering period, whichever is lower. Under applicable tax rules, an employee may purchase no more than $25,000 worth of common stock in any calendar year. At March 31, 2006, 423,139 shares of common stock had been issued under the Purchase Plan of which 407,371 were issued as of December 31, 2005. The total estimated fair value of purchase rights outstanding under the Purchase Plan that vested during the three months ended March 31, 2006 was $72,000.

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12. Contingencies and Commitments

From time to time, the Company is involved in various investigations, claims and legal proceedings that arise in the ordinary course of business activities. Management believes, after consulting with legal counsel, that the ultimate liabilities, if any, resulting from such matters will not materially affect the Company s financial position, liquidity or results of operations.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of

ANSYS, Inc.

Canonsburg, Pennsylvania

We have reviewed the accompanying condensed consolidated balance sheet of ANSYS, Inc. and subsidiaries (the Company) as of March 31, 2006, and the related condensed consolidated statements of income and cash flows for the three-month periods ended March 31, 2006 and 2005. These interim financial statements are the responsibility of the Company s management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of ANSYS, Inc. and subsidiaries as of December 31, 2005, and the related consolidated statements of income, stockholders equity, and cash flows for the year then ended (not presented herein); and in our report dated March 1, 2006, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2005 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Deloitte & Touche LLP

Pittsburgh, Pennsylvania

April 27, 2006

(May 1, 2006 as to Note 6)

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

Overview:

ANSYS, Inc. s (the Company) quarterly results for the three-month period ended March 31, 2006 reflect revenue growth of 22.3% and diluted earnings per share growth of 31.0%. These results were impacted by various factors, including higher revenues from the Company s software products and services, an improvement in operating margins and higher interest income, partially offset by the adverse impact of foreign currency fluctuations and the prospective adoption of SFAS No. 123(R), *Accounting for Stock-Based Compensation* .

ANSYS, Inc. develops and globally markets engineering simulation software and technologies widely used by engineers and designers across a broad spectrum of industries, including aerospace, automotive, manufacturing, electronics, biomedical and defense. Headquartered at Southpointe in Canonsburg, Pennsylvania, the Company and its subsidiaries employ approximately 600 people and focus on the development of open and flexible solutions that enable users to analyze designs directly on the desktop, providing a common platform for fast, efficient and cost-conscious product development, from design concept to final-stage testing and validation. The Company distributes its ANSYS®, ANSYS® Workbench , CFX®, DesignSpace®, ICEM CFD and AUTODYN® products through a global network of channel partners, in addition to its own direct sales offices in strategic, global locations. It is the Company s intention to continue to maintain this mixed sales and distribution model.

The Company licenses its technology to businesses, educational institutions and governmental agencies. The growth in the Company s revenue is affected by the strength of the global economies, general business conditions, customer budgetary constraints and the competitive position of the Company s products. The Company believes that the features, functionality and integrated multiphysics capabilities of its software products are as strong as they have ever been. However, the software business is generally characterized by long sales cycles. These long sales cycles increase the difficulty of predicting sales for any particular quarter. As a result, the Company believes that its overall performance is best measured by fiscal year results rather than by quarterly results.

The following discussion should be read in conjunction with the accompanying unaudited condensed consolidated financial statements and notes thereto for the three-month periods ended March 31, 2006 and 2005, and with the Company s audited financial statements and notes thereto for the year ended December 31, 2005 filed on Form 10-K with the Securities and Exchange Commission.

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This Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including, but not limited to, the following statements, as well as statements that contain such words as anticipates, intends, believes, plans and other similar expressions:

the Company s intentions related to investments in global sales and marketing, and research and development

increased exposure to volatility of foreign exchange rates

exposure to changes in domestic and foreign tax laws in future periods

plans related to future capital spending

the Company s intentions regarding its mixed sales and distribution model

the sufficiency of existing cash and cash equivalent balances to meet future working capital and capital expenditure requirements

the Company s estimates regarding the effect that Statement No. 123(R) will have on the net income of the Company for fiscal year 2006

management s assessment of the ultimate liabilities arising from various investigations, claims and legal proceedings

Forward-looking statements should not be unduly relied upon because they involve known and unknown risks, uncertainties and other factors, some of which are beyond the Company s control. The Company s actual results could differ materially from those set forth in forward-looking statements. Certain factors that might cause such a difference include risks and uncertainties detailed in the Management s Discussion and Analysis of Financial Condition and Results of Operations section in the 2005 Annual Report to Stockholders and any such changes to these factors have been included within Part II, Item 1A of this Form 10-Q.

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Results of Operations

Three Months Ended March 31, 2006 Compared to Three Months Ended March 31, 2005

Revenue:

(in thousands, except percentages)	Three Months Ended March 31,		Change	
	2006	**2005**	**Amount**	**%**
Revenue:				
Software licenses	**$ 26,752**	$ 20,475	$ 6,277	30.7
Maintenance and service	**19,259**	17,149	2,110	12.3
Total revenue	**46,011**	37,624	8,387	22.3

The increase in revenue is primarily due to the following reasons:

- newly generated software license revenue of $6.3 million, including $3.3 million related to an order with a long-standing major customer

- increase of $2.1 million in product maintenance revenue, primarily associated with annual maintenance subscriptions sold in connection with new perpetual license sales in recent quarters

- engineering consulting revenue has remained consistent in the current period compared to the same period in the prior year

With respect to revenue, on average, for the first quarter of 2006, the U.S. Dollar was approximately 6.8% stronger, when measured against the Company s primary foreign currencies, than for the first quarter of 2005. The U.S. Dollar strengthened against the British Pound, the Japanese Yen, the Indian Rupee and the Euro, while it weakened against the Canadian Dollar. The overall strengthening resulted in decreased revenue and operating income during the 2006 first quarter, as compared with the corresponding 2005 first quarter, of approximately $1.1 million and $600,000, respectively.

International and domestic revenues, as a percentage of total revenue, were 61.3% and 38.7%, respectively, in the quarter ended March 31, 2006 and 68.3% and 31.7%, respectively, in the quarter ended March 31, 2005.

A substantial portion of the Company s maintenance revenue is derived from annual maintenance contracts. These contracts are generally renewed on an annual basis and have a high rate of customer renewal. In addition to the recurring revenue base associated with these contracts, a majority of customers purchasing new perpetual licenses also purchase related annual maintenance contracts. As a result of the significant recurring revenue base, the Company s maintenance revenue growth rate in any period does not necessarily correlate to the growth rate of new maintenance contracts sold during that period. To the extent the rate of customer renewal for maintenance contracts remains at current levels, incremental maintenance contracts sold with new perpetual licenses will result in maintenance revenue growth.

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Cost of Sales and Gross Profit:

(in thousands, except percentages)	Three Months Ended March 31, 2006		2005		Change	
	Amount	% of Revenue	Amount	% of Revenue	Amount	%
Cost of sales:						
Software licenses	**$ 1,490**	**3.2**	$ 1,253	3.3	$ 237	18.9
Amortization of software and acquired technology	**908**	**2.0**	907	2.4	1	0.1
Maintenance and service	**4,470**	**9.7**	3,858	10.3	612	15.9
Total cost of sales	**6,868**	**14.9**	6,018	16.0	850	14.1
Gross profit	**39,143**	**85.1**	31,606	84.0	7,537	23.8

The change in cost of sales is due to the following primary reasons:

increase in salaries and headcount related costs, including incentive compensation, of $670,000

increase in third party software royalties of $200,000

The improvement in the gross profit was a result of the increase in revenue offset by a smaller increase in related cost of sales.

Operating Expenses:

(in thousands, except percentages)	Three Months Ended March 31, 2006		2005		Change	
	Amount	% of Revenue	Amount	% of Revenue	Amount	%
Operating expenses:						
Selling and marketing	**$ 7,159**	**15.5**	$ 6,428	17.1	$ 731	11.4
Research and development	**9,357**	**20.3**	7,313	19.4	2,044	28.0
Amortization	**128**	**0.3**	326	0.9	(198)	(60.7)
General and administrative	**4,680**	**10.2**	4,118	10.9	562	13.6
Total operating expenses	**21,324**	**46.3**	18,185	48.3	3,139	17.3

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Selling and Marketing Expenses: Selling and marketing expenses increased $400,000 as a result of stock-based compensation expense recorded associated with the adoption of Statement No. 123(R) during the first quarter of 2006. In addition, there were increases in salary and headcount related costs, including incentive compensation, of $300,000.

The Company anticipates that it will continue to make investments throughout the remainder of 2006 in its global sales and marketing organization to enhance major account sales activities and to support its worldwide sales distribution and marketing strategies.

Research and Development: Research and development expenses increased due to the following primary reasons: incentive compensation costs increased $900,000, salary and headcount related expenses increased $700,000 and stock-based compensation expense of $300,000 associated with the adoption of Statement No. 123(R) was recorded during the first quarter of 2006. The Company has traditionally invested significant resources in research and development activities and intends to continue to make significant investments in this area.

Amortization: Amortization decreased by $200,000 as a result of certain customer lists and non-compete agreements that became fully amortized.

General and Administrative: General and administrative expenses increased due to $460,000 in stock-based compensation costs recorded related to the adoption of Statement No. 123 (R) during the first quarter of 2006. In addition, salaries and incentive compensation increased by a net $90,000 as compared to the prior-year quarter.

Other Income: Other income increased from $613,000 during the quarter ended March 31, 2005 to $1.7 million for the quarter ended March 31, 2006. This net increase was the result of the following three factors:

Investment Income - Interest and dividend income was $1.5 million for the quarter ended March 31, 2006, compared to $725,000 for the quarter ended March 31, 2005. This increase of $775,000 is a result of an increased level of funds invested, as well as higher interest rates in 2006 as compared with 2005.

Foreign Currency Transaction - During the quarter ended March 31, 2006, the Company had a net foreign exchange gain of $70,000 as compared with a loss of $120,000 for the quarter ended March 31, 2005. Because the Company has significant operations in non-U.S. locations, the Company, for the foreseeable future, will have financial and operational exposure to volatility of foreign exchange rates. The Company is most impacted by movements among and between the Canadian Dollar, British Pound, Euro, Indian Rupee, Japanese Yen and the U.S. Dollar.

Other Income from other non-operating transactions increased $100,000 during the first qu