

OPEN TEXT CORP
Form 10-Q
February 08, 2008
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

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

For the quarterly period ended December 31, 2007

OR

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

For the transition period from to

Commission file number: 0-27544

OPEN TEXT CORPORATION

(Exact name of registrant as specified in its charter)

CANADA
(State or other jurisdiction of

98-0154400
(IRS Employer

incorporation or organization)

Identification No.)

275 Frank Tompa Drive, Waterloo, Ontario, Canada N2L 0A1

(Address of principal executive offices)

Registrant's telephone number, including area code: (519) 888-7111

(former name former address and former fiscal year, if changed since last report)

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

At February 1, 2008 there were 50,897,629 outstanding Common Shares of the registrant.

Table of Contents

OPEN TEXT CORPORATION

TABLE OF CONTENTS

	Page No
PART I Financial Information:	
Item 1. Financial Statements	
<u>Unaudited Condensed Consolidated Balance Sheets as of December 31, 2007 and June 30, 2007</u>	3
<u>Unaudited Condensed Consolidated Statements of Income Three and Six Months Ended December 31, 2007 and 2006</u>	4
<u>Unaudited Condensed Consolidated Statements of Retained Earnings (Deficit) Three and Six Months Ended December 31, 2007 and 2006</u>	5
<u>Unaudited Condensed Consolidated Statements of Cash Flows Three and Six Months Ended December 31, 2007 and 2006</u>	6
<u>Unaudited Notes to Condensed Consolidated Financial Statements</u>	7
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	32
Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	45
Item 4. <u>Controls and Procedures</u>	45
PART II Other Information:	
Item 1A. <u>Risk Factors</u>	47
Item 4. <u>Submission of Matters to a Vote of Security Holders</u>	56
Item 5. <u>Other Information</u>	56
Item 6. <u>Exhibits</u>	57
<u>Signatures</u>	58
<u>Index to Exhibits</u>	59

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS**

(In thousands of U.S. Dollars, except share data)

	December 31, 2007 (Unaudited)	June 30, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 159,709	\$ 149,979
Accounts receivable trade, net of allowance for doubtful accounts of \$2,966 as of December 31, 2007 and \$2,089 as of June 30, 2007 (note 6)	120,588	128,781
Income taxes recoverable (note 11)	19,599	31,060
Prepaid expenses and other current assets	10,518	10,368
Deferred tax assets (note 11)	32,410	30,248
Total current assets	342,824	350,436
Capital assets (note 3)	42,879	43,614
Goodwill (note 4)	552,079	528,312
Acquired intangible assets (note 5)	313,118	343,324
Deferred tax assets (note 11)	29,201	42,078
Other assets	11,119	9,524
Long-term income taxes recoverable (note 11)	36,945	9,557
	\$ 1,328,165	\$ 1,326,845
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities (note 7)	\$ 101,403	\$ 100,211
Current portion of long-term debt (note 8)	3,488	4,048
Deferred revenues	134,399	143,097
Income taxes payable (note 11)	11,701	33,705
Deferred tax liabilities (note 11)	1,198	1,601
Total current liabilities	252,189	282,662
Long-term liabilities:		
Accrued liabilities (note 7)	22,338	22,516
Long-term debt (note 8)	306,458	366,765
Deferred revenues	3,313	3,840
Long-term income taxes payable (note 11)	41,893	
Deferred tax liabilities (note 11)	102,246	120,019
Total long-term liabilities	476,248	513,140
Minority interest	7,763	6,975
Shareholders' equity:		
Share capital (note 9)		
50,872,016 and 50,180,118 Common Shares issued and outstanding at December 31, 2007 and June 30, 2007, respectively; Authorized Common Shares: unlimited	435,422	426,188
Additional paid-in capital	37,795	35,311
Accumulated other comprehensive income	105,728	68,034
Retained earnings (deficit)	13,020	(5,465)

Edgar Filing: OPEN TEXT CORP - Form 10-Q

Total shareholders' equity	591,965	524,068
	\$ 1,328,165	\$ 1,326,845

Commitments and Contingencies (note 14)

See accompanying notes to unaudited condensed consolidated financial statements

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

(In thousands of U.S. dollars, except per share data)

	Three months ended December 31,		Six months ended December 31,	
	2007	2006	2007	2006
Revenues:				
License	\$ 55,158	\$ 51,425	\$ 99,418	\$ 80,250
Customer support	90,614	78,022	176,918	126,310
Service	36,762	33,814	70,165	57,856
Total revenues	182,534	163,261	346,501	264,416
Cost of revenues:				
License	4,649	3,322	8,203	6,122
Customer support	14,191	12,659	26,789	19,646
Service	30,192	29,108	57,696	49,408
Amortization of acquired technology-based intangible assets	10,308	10,396	20,460	15,242
Total cost of revenues	59,340	55,485	113,148	90,418
	123,194	107,776	233,353	173,998
Operating expenses:				
Research and development	25,924	22,595	49,656	36,813
Sales and marketing	42,523	43,824	80,633	68,696
General and administrative	16,955	15,474	33,965	26,693
Depreciation	3,752	3,907	6,736	6,899
Amortization of acquired customer-based intangible assets	7,514	7,369	14,929	9,751
Special charges (recoveries) (note 15)	(47)	4,843	(108)	4,375
Total operating expenses	96,621	98,012	185,811	153,227
Income from operations	26,573	9,764	47,542	20,771
Other income (expense)	(3,683)	329	(5,510)	702
Interest income (expense), net (note 8)	(7,567)	(7,512)	(15,439)	(7,120)
Income before income taxes	15,323	2,581	26,593	14,353
Provision for income taxes	4,511	173	7,854	4,507
Net income before minority interest	10,812	2,408	18,739	9,846
Minority interest	127	131	254	268
Net income for the period	\$ 10,685	\$ 2,277	\$ 18,485	\$ 9,578
Net income per share basic (note 10)	\$ 0.21	\$ 0.05	\$ 0.37	\$ 0.20
Net income per share diluted (note 10)	\$ 0.20	\$ 0.04	\$ 0.35	\$ 0.19
Weighted average number of Common Shares outstanding basic	50,736	49,152	50,511	49,063

Edgar Filing: OPEN TEXT CORP - Form 10-Q

Weighted average number of Common Shares outstanding				
diluted	52,689	50,739	52,224	50,497

See accompanying notes to unaudited condensed consolidated financial statements

Table of Contents

OPEN TEXT CORPORATION

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF RETAINED EARNINGS (DEFICIT)

(In thousands of U.S. Dollars)

	Three months ended December 31,		Six months ended December 31,	
	2007	2006	2007	2006
Retained Earnings (deficit), beginning of period	\$ 2,335	\$ (19,824)	\$ (5,465)	\$ (27,125)
Net income	10,685	2,277	18,485	9,578
Retained Earnings (deficit), end of period	\$ 13,020	\$ (17,547)	\$ 13,020	\$ (17,547)

See accompanying notes to unaudited condensed consolidated financial statements

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In thousands of U.S. Dollars)

	Three months ended December 31,		Six months ended December 31,	
	2007	2006	2007	2006
Cash flows from operating activities:				
Net income for the period	\$ 10,685	\$ 2,277	\$ 18,485	\$ 9,578
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	21,574	21,672	42,125	31,892
In-process research and development			500	
Share-based compensation expense	655	1,333	1,718	2,600
Employee long-term incentive plan	572		757	
Excess tax benefits from share-based compensation	(369)	(536)	(766)	(741)
Undistributed earnings related to minority interest	127	131	254	268
Amortization of debt issuance costs	421	257	711	257
Unrealized loss on financial instruments	1,444	212	2,851	212
Deferred taxes	(3,408)	(10,638)	(4,113)	(8,924)
Changes in operating assets and liabilities:				
Accounts receivable	(2,923)	25,191	7,579	23,497
Prepaid expenses and other current assets	302	277	(197)	894
Income taxes	8,070	(2,859)	8,554	(3,813)
Accounts payable and accrued liabilities	6,967	610	1,472	(4,913)
Deferred revenues	(5,110)	(10,475)	(8,883)	(13,437)
Other assets	336	3,976	510	3,695
Net cash provided by operating activities	39,343	31,428	71,557	41,065
Cash flows from investing activities:				
Acquisitions of capital assets	(2,170)	(1,106)	(3,386)	(3,891)
Additional purchase consideration for prior period acquisitions	(263)	(1,390)	(439)	(1,723)
Purchase of Hummingbird, net of cash acquired		(384,761)		(384,761)
Purchase of an asset group constituting a business			(2,209)	
Investments in marketable securities				(829)
Acquisition related costs	(3,813)	(17,752)	(11,842)	(20,200)
Net cash used in investing activities	(6,246)	(405,009)	(17,876)	(411,404)
Cash flows from financing activities:				
Excess tax benefits from share-based compensation	369	536	766	741
Proceeds from issuance of Common Shares	3,498	1,986	9,217	2,464
Repayment of long-term debt	(30,944)	(1,074)	(61,877)	(1,173)
Proceeds from long-term debt		390,000		390,000
Debt issuance costs		(7,412)	(349)	(7,433)
Net cash provided by (used in) financing activities	(27,077)	384,036	(52,243)	384,599
Foreign exchange gain on cash held in foreign currencies	3,383	2,722	8,292	2,787
Increase in cash and cash equivalents during the period	9,403	13,177	9,730	17,047

Edgar Filing: OPEN TEXT CORP - Form 10-Q

Cash and cash equivalents at beginning of period	150,306	111,224	149,979	107,354
Cash and cash equivalents at end of period	\$ 159,709	\$ 124,401	\$ 159,709	\$ 124,401

Supplementary cash flow disclosures (note 13)

See accompanying notes to unaudited condensed consolidated financial statements

Table of Contents

OPEN TEXT CORPORATION

UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

For the Three and Six Months Ended December 31, 2007

(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)

NOTE 1 BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements (Interim Financial Statements) include the accounts of Open Text Corporation and its wholly and partially owned subsidiaries, collectively referred to as Open Text or the Company . All inter-company balances and transactions have been eliminated.

These Interim Financial Statements are expressed in U.S. dollars and are prepared in accordance with United States generally accepted accounting principles (U.S. GAAP). These financial statements are based upon accounting policies and methods of their application are consistent with those used and described in the Company s annual consolidated financial statements for the year ended June 30, 2007. The Interim Financial Statements do not include all of the financial statement disclosures included in the annual consolidated financial statements prepared in accordance with U.S. GAAP and therefore should be read in conjunction with the consolidated financial statements and notes included in the Company s Annual Report on Form 10-K for the fiscal year ended June 30, 2007.

The information furnished reflects all adjustments necessary for a fair presentation of the results for the interim periods presented. The operating results for the three and six months ended December 31, 2007 are not necessarily indicative of the results expected for any succeeding quarter or the entire fiscal year ending June 30, 2008. Additionally, there have been no significant changes in new accounting pronouncements or in the Company s critical accounting policies that were disclosed in its Annual Report on Form 10-K for the fiscal year ended June 30, 2007 other than the impact of the Company s adoption of Financial Accounting Standards Board (FASB) Interpretation No. 48 Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109 (FIN 48), which affected the Company s Accounting for Income Taxes policy (see Note 11 Income Taxes).

Use of estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates, judgments and assumptions that affect the amounts reported in the Interim Financial Statements. These estimates, judgments and assumptions are evaluated on an ongoing basis. Management bases its estimates on historical experience and on various other assumptions that it believes are reasonable at that time, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from those estimates. In particular, significant estimates, judgments and assumptions include those related to: (i) revenue recognition, (ii) allowance for doubtful accounts, (iii) testing goodwill for impairment, (iv) the valuation of acquired intangible assets, (v) long-lived assets, (vi) the recognition of contingencies, (vii) facility and restructuring accruals, (viii) acquisition accruals and pre-acquisition contingencies, (ix) asset retirement obligations, (x) realization of investment tax credits, (xi) the valuation of stock options granted and liabilities related to share-based payments, (xii) the valuation of financial instruments and (xiii) accounting for income taxes.

Reclassifications

Certain prior period comparative figures have been adjusted to conform to current period presentation including the reclassifications related to a change in the method of allocating operating expenses within the Company.

As a result of such reclassifications, General and administrative expenses decreased by \$1.0 million with corresponding increases of \$256,000, \$438,000, \$39,000 and \$315,000 in Cost of revenues for Customer support, Cost of revenues for Service, Research and development expense and Sales and marketing expense, respectively, for the six months ended December 31, 2006 from previously reported amounts.

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Three and Six Months Ended December 31, 2007****(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)**

There was no change to income from operations, net income or net income per share in any of the periods presented as a result of these reclassifications.

Comprehensive income

Comprehensive income is comprised of net income and other comprehensive income, including the effect of foreign currency translation resulting from the consolidation of subsidiaries where the functional currency is a currency other than the U.S. Dollar. The Company's total comprehensive income was as follows:

	Three months ended December 31,		Six months ended December 31,	
	2007	2006	2007	2006
Other comprehensive income:				
Foreign currency translation adjustment	\$ 16,825	\$ 11,026	\$ 37,694	\$ 9,189
Unrealized gain on investments in marketable securities		226		432
Net income for the period	10,685	2,277	18,485	9,578
Comprehensive income for the period	\$ 27,510	\$ 13,529	\$ 56,179	\$ 19,199

NOTE 2 NEW ACCOUNTING PRONOUNCEMENTS

In September 2006, the FASB issued Statement of Financial Accounting Standard (SFAS) No. 157, *Fair Value Measurement*. SFAS 157, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157, does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. This statement is effective for the Company beginning July 1, 2008. The Company is currently assessing the potential impact that the adoption of SFAS 157 will have on its financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115* (SFAS 159). SFAS 159 permits an entity to choose to measure many financial instruments and certain other items at fair value. Most of the provisions in SFAS 159 are elective; however, the amendment to FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, applies to all entities with available-for-sale and trading securities. SFAS 159 is effective for the Company beginning July 1, 2008. The Company is currently assessing the potential impact that the adoption of SFAS 159 will have on its financial statements.

In June 2007, the FASB ratified Emerging Issues Task Force Issue (EITF) Issue No. 07-03 (EITF 07-03) *Accounting for Nonrefundable Advance Payments for Goods or Services for Use in Future Research and Development Activities*. EITF 07-03 requires that nonrefundable advance payments for goods or services that will be used for future research and development activities should be deferred and capitalized. Such amounts should be recognized as an expense as the related goods are delivered or the related services are performed. EITF 07-03 is effective for the Company beginning July 1, 2008. The Company is currently assessing the potential impact that the adoption of EITF 07-03 will have on its financial statements.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations* (SFAS 141R) which replaces SFAS No. 141. The statement retains the purchase method of accounting for acquisitions, but requires a number of changes, including changes in the way assets and

liabilities are recognized in the purchase

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Three and Six Months Ended December 31, 2007****(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)**

accounting. It also changes the recognition of assets acquired and liabilities assumed arising from contingencies, requires the capitalization of in-process research and development at fair value, and requires the expensing of acquisition-related costs as incurred. SFAS 141R is effective for the Company beginning July 1, 2009 and will apply prospectively to business combinations completed on or after that date.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB 51* (SFAS 160), which changes the accounting and reporting for minority interests. Minority interest will be recharacterized as noncontrolling interests and will be reported as a component of equity separate from the parent's equity, and purchases or sales of equity interest that do not result in a change in control will be accounted for as equity transactions. In addition, net income attributable to the noncontrolling interest will be included in consolidated net income on the face of the income statement and, upon a loss of control, the interest sold, as well as any interest retained, will be recorded at fair value with any gain or loss recognized in earnings. SFAS 160 is effective for the Company beginning July 1, 2009 and will apply prospectively, except for the presentation and disclosure requirements, which will apply retrospectively. The Company is currently assessing the impact that the adoption of SFAS 160 will have on its financial statements.

NOTE 3 CAPITAL ASSETS

	As of December 31, 2007		
	Cost	Accumulated Depreciation	Net
Furniture and fixtures	\$ 11,487	\$ 9,122	\$ 2,365
Office equipment	9,084	8,004	1,080
Computer hardware	77,712	69,584	8,128
Computer software	23,578	19,701	3,877
Leasehold improvements	13,315	9,396	3,919
Land and Buildings *	24,813	1,303	23,510
	\$ 159,989	\$ 117,110	\$ 42,879

	As of June 30, 2007		
	Cost	Accumulated Depreciation	Net
Furniture and fixtures	\$ 10,417	\$ 8,137	\$ 2,280
Office equipment	8,642	7,579	1,063
Computer hardware	72,997	64,252	8,745
Computer software	22,232	17,368	4,864
Leasehold improvements	13,135	8,962	4,173
Land and Buildings *	23,497	1,008	22,489
	\$ 150,920	\$ 107,306	\$ 43,614

*

Edgar Filing: OPEN TEXT CORP - Form 10-Q

Included in this balance is an asset held for sale with a fair value of approximately \$5.6 million as of December 31, 2007 (June 30, 2007 \$5.6 million). This asset is being held for sale as a result of a decision taken by the Company's management to sell a building acquired as part of the Hummingbird Ltd. (Hummingbird) acquisition. The Company expects to sell the building by way of a commercial sale and, at this point, is unable to predict the timing of its disposal. The building is being held for sale within the Company's North America reporting segment.

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Three and Six Months Ended December 31, 2007****(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)****NOTE 4 GOODWILL**

Goodwill is recorded when the consideration paid for an acquisition of a business exceeds the fair value of identifiable net tangible and intangible assets. The following table summarizes the changes in goodwill since June 30, 2006:

Balance, June 30, 2006	\$ 235,523
Acquisition of Momentum	3,340
Acquisition of Hummingbird	272,433
Adjustments relating to prior acquisitions	4,395
Adjustments on account of foreign exchange	12,621
Balance, June 30, 2007	528,312
Purchase of an asset group constituting a business	2,199
Adjustments relating to prior acquisitions	8,744
Adjustments relating to the adoption of FIN 48	(6,480)
Adjustments on account of foreign exchange	19,304
Balance, December 31, 2007	\$ 552,079

Adjustments relating to prior acquisitions relate primarily to the finalization during the three months ended September 30, 2007, of fair value estimates of Hummingbird assets and liabilities acquired, including adjustments reflecting plans formulated in accordance with Emerging Issues Task Force 95-3, Recognition of Liabilities in Connection With a Purchase Business Combination (EITF 95-3) that commenced on the date of consummation of the acquisition relating to employee termination and abandonment of excess facilities. Prior acquisition adjustments also relate, in the case of certain other prior acquisitions, to the evaluation of the tax attributes of acquisition-related operating loss carry forwards and deductions, including reductions in previously recognized valuation allowances, originally assessed at the various dates of acquisition.

For details relating to the reduction of goodwill upon the adoption of FIN 48 see Note 11 Income Taxes .

NOTE 5 ACQUIRED INTANGIBLE ASSETS

	Technology Assets	Customer Assets	Total
Net book value, June 30, 2006	\$ 55,174	\$ 47,152	\$ 102,326
Activity during fiscal 2007:			
Acquisition of Hummingbird	159,200	139,800	299,000
Amortization expense	(36,206)	(24,586)	(60,792)
Impairment of intangible assets	(697)		(697)
Foreign exchange impact	2,228	2,047	4,275
Other	(483)	(305)	(788)

Edgar Filing: OPEN TEXT CORP - Form 10-Q

Net book value, June 30, 2007	179,216	164,108	343,324
Activity during fiscal 2008:			
Amortization expense	(20,460)	(14,929)	(35,389)
Foreign exchange impact	2,311	2,720	5,031
Other	96	56	152
Net book value, December 31, 2007	\$ 161,163	\$ 151,955	\$ 313,118

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Three and Six Months Ended December 31, 2007****(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)**

The range of amortization periods for intangible assets is from 4-10 years.

The following table shows the estimated future amortization expense for the six months ended June 30, 2008 and for each of the next four years, assuming no further adjustments to acquired intangible assets:

	Fiscal years ending June 30,
2008	\$ 35,809
2009	65,651
2010	52,602
2011	49,980
2012	47,520
Total	\$ 251,562

NOTE 6 ALLOWANCE FOR DOUBTFUL ACCOUNTS

Balance of allowance for doubtful accounts (AfDA) as of June 30, 2007	2,089
Bad debt expense for the period	1,285
Write-off /adjustments	(408)
Balance of allowance for doubtful accounts as of December 31, 2007	\$ 2,966

Included in accounts receivable are unbilled receivables in the amount of \$3.4 million and \$3.4 million as of December 31, 2007 and June 30, 2007, respectively.

As part of the acquisition of Hummingbird the company assumed an AfDA of \$17.6 million. The acquired accounts receivable were recorded at fair value, net of this amount. The balance of this AfDA was \$6.9 million as of December 31, 2007 (June 30, 2007 \$5.5 million). This information is included herein for memorandum purposes only and has no impact on the net balance of accounts receivable included in these Interim Financial Statements.

NOTE 7 ACCOUNTS PAYABLE AND ACCRUED LIABILITIES**Current liabilities**

Accounts payable and accrued liabilities are comprised of the following:

Edgar Filing: OPEN TEXT CORP - Form 10-Q

	As of December 31, 2007	As of June 30, 2007
Accounts payable trade	\$ 5,637	\$ 8,140
Accrued salaries and commissions	28,814	29,437
Accrued liabilities	53,458	44,770
Amounts payable in respect of restructuring (note 15)	1,241	2,636
Amounts payable in respect of acquisitions and acquisition related accruals	12,253	15,228
	\$ 101,403	\$ 100,211

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Three and Six Months Ended December 31, 2007****(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)****Long-term accrued liabilities**

	As of December 31, 2007	As of June 30, 2007
Pension liabilities	\$ 322	\$ 322
Amounts payable in respect of restructuring (note 15)	836	1,382
Amounts payable in respect of acquisitions and acquisition related accruals	14,289	15,025
Other accrued liabilities	1,311	534
Asset retirement obligations	5,580	5,253
	\$ 22,338	\$ 22,516

Pension liabilities

The Company acquired a controlling interest in IXOS in March 2004. IXOS has pension commitments to certain employees. The actuarial cost method used in determining the net periodic pension cost, with respect to the IXOS employees, is the projected unit credit method. The liabilities and annual income or expense of the Company's pension plan are determined using methodologies that involve various actuarial assumptions, the most significant of which are the discount rate and the long-term rate of return on assets. The fair value of the plan assets as of December 31, 2007 is \$3.2 million (June 30, 2007 \$2.9 million). The fair value of the pension obligation as of December 31, 2007 is \$3.1 million, (June 30, 2007 \$2.9 million).

Asset retirement obligations

The Company is required to return certain of its leased facilities to their original state at the conclusion of the lease. The Company has accounted for such obligations in accordance with FASB SFAS No. 143, Accounting for Asset Retirement Obligations (SFAS 143). At December 31, 2007, the present value of this obligation was \$5.6 million, (June 30, 2007 \$5.3 million), with an undiscounted value of \$7.0 million, (June 30, 2007 \$7.5 million). These leases were primarily assumed in connection with the IXOS and Hummingbird acquisitions.

Excess facility obligations and accruals relating to acquisitions

The Company has accrued for the cost of excess facilities in connection with a number of its acquisitions, including its fiscal 2007 Hummingbird acquisition. These accruals include the Company's best estimate in respect of future sub-lease income and costs incurred to achieve sub-tenancy. These liabilities have been recorded using present value discounting techniques and will be discharged over the term of the respective leases. Any excess of the difference between the present value and actual cash paid for the excess facility will be charged to income and any deficits will be reversed to goodwill. The terms of the leases range from one year to 17 years.

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Three and Six Months Ended December 31, 2007****(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)**

The following table summarizes the activity with respect to the Company's acquisition accruals during the six months ended December 31, 2007.

	Balance June 30, 2007	Initial Accruals	Usage/ Foreign Exchange/ Other Adjustments	Subsequent Adjustments to Goodwill	Balance December 31, 2007
Hummingbird					
Employee termination costs	\$ 7,845	\$	\$ (6,620)	\$ (279)	\$ 946
Excess facilities	2,708		(689)	3,779	5,798
Transaction-related costs		975	(160)		815
	10,553	975	(7,469)	3,500	7,559
IXOS					
Employee termination costs					
Excess facilities	18,564		(467)	(221)	17,876
Transaction-related costs					
	18,564		(467)	(221)	17,876
Eloquent					
Employee termination costs					
Excess facilities					
Transaction-related costs	243				243
	243				243
Centrinity					
Employee termination costs					
Excess facilities	838		(19)		819
Transaction-related costs					
	838		(19)		819
Artesia					
Employee termination costs					
Excess facilities	55		(10)		45
Transaction-related costs					
	55		(10)		45
Totals					
Employee termination costs	7,845		(6,620)	(279)	946
Excess facilities	22,165		(1,185)	3,558	24,538
Transaction-related costs	243	975	(160)		1,058

Edgar Filing: OPEN TEXT CORP - Form 10-Q

\$ 30,253 \$ 975 \$ (7,965) \$ 3,279 \$ 26,542

The adjustments to goodwill relate to employee termination costs and excess facilities primarily to adjustments accounted for in accordance with EITF 95-3. The adjustments to goodwill relating to transaction costs are accounted for in accordance with SFAS No. 141, Business Combinations (SFAS 141).

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Three and Six Months Ended December 31, 2007****(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)****NOTE 8 LONG-TERM DEBT AND FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES****Long-term debt**

Long-term debt is comprised of the following:

	As of December 31, 2007	As of June 30, 2007
Long-term debt		
Term loan	\$ 295,502	\$ 357,151
Mortgage	14,444	13,662
	309,946	370,813
Less:		
Current portion of long-term debt		
Term loan	2,993	3,599
Mortgage	495	449
	3,488	4,048
Long-term portion of long-term debt	\$ 306,458	\$ 366,765

Term loan and Revolver

On October 2, 2006, the Company entered into a \$465.0 million credit agreement (the credit agreement) with a Canadian chartered bank (the bank) consisting of a \$390.0 million term loan facility (the term loan) and a \$75.0 million committed revolving long-term credit facility (the revolver). The term loan was used to finance a portion of the Hummingbird acquisition and the revolver will be used for general business purposes. The credit agreement is guaranteed by the Company and certain of its subsidiaries.

Term loan

The term loan has a seven year term and expires on October 2, 2013 and bears interest at a floating rate of LIBOR plus 2.25%. The term loan principal repayments are equal to 0.25% of the original principal amount, due each quarter with the remainder due at the end of the term, less ratable reductions for any prepayments made. To date the Company has made total prepayments of \$90.0 million of the principal including a prepayment of \$30.0 million in December 2007. These prepayments have reduced the quarterly principal payment to approximately \$748,000.

For the three and six months ended December 31, 2007, interest expense in the unaudited Condensed Consolidated Statements of Income includes \$6.1 million and \$13.2 million, respectively, (three and six months ended, December 31, 2006-\$7.5 million), on account of interest expense relating to the term loan.

Revolver

Edgar Filing: OPEN TEXT CORP - Form 10-Q

The revolver has a five year term and expires on October 2, 2011. Borrowings under this facility bear interest at rates specified in the credit agreement. The revolver is subject to a stand-by fee ranging between 0.30% and 0.50% per annum depending on the consolidated leverage ratio of the Company. There are no borrowings outstanding under the revolver as of December 31, 2007.

Table of Contents

OPEN TEXT CORPORATION

UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended December 31, 2007

(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)

For the three and six months ended December 31, 2007, interest expense in the unaudited Condensed Consolidated Statements of Income includes \$73,000, and \$145,000, respectively, (three and six months ended, December 31, 2006 \$84,000), on account of stand- by fees relating to the revolver.

Mortgage

The mortgage consists of a five year mortgage agreement entered into during December 2005 with the bank. The principal amount of the mortgage is CAD \$15.0 million. The mortgage: (i) has a fixed term of five years, (ii) matures on January 1, 2011, and (iii) is secured by a lien on the Company's headquarters in Waterloo, Ontario. Interest is to be paid monthly at a fixed rate of 5.25% per annum. Principal and interest are payable in monthly installments of CAD \$101,000 with a final lump sum principal payment of CAD \$12.6 million due on maturity.

As of December 31, 2007, the carrying value of the building was \$17.9 million. (June 30, 2007 \$16.9 million)

For the three and six months ended December 31, 2007, interest expense in the unaudited Condensed Consolidated Statements of Income includes \$188,000 and \$365,000, (three and six months ended December 31, 2006 \$170,000, and \$342,000 respectively), on account of interest expense relating to the mortgage.

Financial Instruments and Hedging Activities

In October 2006, Open Text entered into a three year interest-rate collar that had the economic effect of circumscribing the floating portion of the interest rate obligations associated with \$195.0 million of the term loan within an upper limit of 5.34% and a lower limit of 4.79%. This was pursuant to a requirement in the credit agreement that required the Company to maintain, from thirty days following the date on which the term loan was entered into through the third anniversary or such earlier date on which the term loan is paid, interest rate hedging arrangements with counterparties in respect of 50% of the term loan.

SFAS No. 133 Accounting for Derivative Instruments and Hedging Activities (SFAS 133) requires that changes in a derivative instrument's fair value be recognized in current earnings unless specific hedge accounting criteria are met and that an entity must formally document, designate and assess the effectiveness of transactions that qualify for hedge accounting.

SFAS 133 requires that written options must meet certain criteria in order for hedge accounting to apply. The Company determined that these criteria were not met and hedge accounting could not be applied for the three and six months ended December 31, 2007. The fair market value of the collar, which represents the cash the Company would receive or pay to settle the collar, was a payable of approximately \$2.5 million as of December 31, 2007 (June 30, 2007 receivable of approximately \$380,000), and has been included within Accounts payable and accrued liabilities (June 30, 2007 included within Prepaid expenses and other current assets) on the unaudited Condensed Consolidated Balance Sheets. The collar has a remaining term to maturity of 2.0 years.

For the three and six months ended December 31, 2007, interest expense in the unaudited Condensed Consolidated Statements of Income has been increased by \$1.4 million and \$2.8 million respectively, (three and six months ended December 31, 2006 \$ 212,000), representing the change in the fair value of the collar. Additionally, the Company records payments or receipts on the collar as adjustments to interest expense.

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Three and Six Months Ended December 31, 2007****(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)**

Interest expense in the unaudited Condensed Consolidated Statements of Income has been reduced by nil and \$10,000, on account of monies received under the collar for the three and six months ended December 31, 2007 respectively, (three and six months ended December 31, 2006 \$4,000).

The Company will continue to monitor changes in interest rates periodically and will assess whether hedge accounting could potentially be applied in future periods.

NOTE 9 SHARE CAPITAL AND SHARE BASED PAYMENTS***Share Capital***

The authorized share capital of the Company includes an unlimited number of Common Shares and an unlimited number of preference shares. No preference shares have been issued.

During the three and six months ended December 31, 2007 and 2006, the Company did not repurchase any of its Common Shares.

Share-Based Payments***Summary of Outstanding Stock Options***

As of December 31, 2007, options to purchase an aggregate of 3,920,039 Common Shares are outstanding under all of the Company's stock option plans. In addition, 1,421,570 Common Shares are available for issuance under the 1998 Stock Option Plan and the 2004 Stock Option Plan. The Company's stock options generally vest over four years and expire ten years from the date of the grant. The exercise price of the options the Company grants is set at an amount that is not less than the closing price of the Company's Common Shares on the trading day for the NASDAQ immediately preceding the applicable grant date.

A summary of option activity under the Company's stock option plans for the six months ended December 31, 2007 is as follows:

	Options	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (\$ 000s)
Outstanding at June 30, 2007	4,737,727	\$ 14.15		
Granted	25,000	24.87		
Exercised	(675,004)	13.16		
Forfeited or expired	(167,684)	16.20		
Outstanding at December 31, 2007	3,920,039	\$ 14.31	3.97	\$ 67,205
Exercisable at December 31, 2007	2,804,537	\$ 12.83	3.34	\$ 52,232

Edgar Filing: OPEN TEXT CORP - Form 10-Q

The Company estimates the fair value of stock options using the Black-Scholes option pricing model, consistent with the provisions of SFAS 123 (Revised 2004), Share-Based Payment (SFAS 123R) and SEC Staff Accounting Bulletin No. 107. The Black-Scholes option-pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable, while the options issued by the Company are subject to both vesting and restrictions on transfer. In addition, option-pricing models require input of subjective assumptions including the estimated life of the option and the expected volatility of the underlying stock over the estimated life of the option. The Company uses historical volatility as a basis for projecting the expected volatility of the underlying stock and estimates the expected life of its stock options based upon historical data.

Table of Contents

OPEN TEXT CORPORATION

UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended December 31, 2007

(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)

The Company believes that the valuation technique and the approach utilized to develop the underlying assumptions are appropriate in calculating the fair value of the Company's stock option grants. Estimates of fair value are not intended, however, to predict actual future events or the value ultimately realized by employees who receive equity awards.

For the three months ended December 31, 2007, there were no options granted by the Company. A forfeiture rate of 5%, based on historical rates, was used to determine the net amount of compensation expense recognized during this period.

For the six months ended December 31, 2007, the weighted-average fair value of options granted, as of the grant date, was \$11.12, using the following weighted average assumptions: expected volatility of 43%; risk-free interest rate of 5.0%; expected dividend yield of 0%; and expected life of 5.0 years. A forfeiture rate of 5%, based on historical rates, was used to determine the net amount of compensation expense recognized.

For the three months ended December 31, 2006, the weighted-average fair value of options granted, as of the grant date, was \$5.87, using the following weighted average assumptions: expected volatility of 46%; risk-free interest rate of 4.7%; expected dividend yield of 0%; and expected life of 4.8 years. A forfeiture rate of 5%, based on historical rates, was used to determine the net amount of compensation expense recognized for each of these periods.

For the six months ended December 31, 2006, the weighted-average fair value of options granted, as of the grant date, was \$6.66, using the following weighted average assumptions: expected volatility of 46%; risk-free interest rate of 4.6%; expected dividend yield of 0%; expected life of 4.7 years; and a forfeiture rate of 5%, based on historical rates, was used to determine the net amount of compensation expense recognized for each of these periods.

As of December 31, 2007, the total compensation cost related to the unvested stock awards not yet recognized was \$9.0 million, which will be recognized over a weighted average period of approximately 2 years.

As of December 31, 2006, the total compensation cost related to the unvested stock awards not yet recognized was \$11.6 million, which will be recognized over a weighted average period of approximately 2 years.

In each of the above periods, no cash was used by the Company to settle equity instruments granted under share-based compensation arrangements.

Share-based compensation cost included in the unaudited condensed consolidated statements of income for the three and six months ended December 31, 2007 was approximately \$655,000 and \$1.7 million respectively. Deferred tax assets of \$123,000 and \$261,000 were recorded, for the three and six months December 31, 2007 in relation to the tax effect of certain stock options that are eligible for a tax deduction when exercised. Share-based compensation cost included in the unaudited condensed consolidated statements of income for the three and six months ended December 31, 2006 was approximately \$1.3 million and \$2.6 million, respectively. Deferred tax assets of \$213,000 and \$384,000, respectively, were recorded, for the three and six months ended as of December 31, 2006 in relation to the tax effect of certain stock options that are eligible for a tax deduction when exercised. The Company has not capitalized any share-based compensation costs as part of the cost of an asset.

For the three and six months ended December 31, 2007, cash in the amount of \$3.4 million and \$8.9 million respectively, was received as the result of the exercise of options granted under share-based payment arrangements. The tax benefit realized by the Company, during the three and six months ended December 31, 2007 from the exercise of options eligible for a tax deduction was \$369,000, and \$766,000 respectively, which was recorded as additional paid-in capital.

Table of Contents

OPEN TEXT CORPORATION

UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended December 31, 2007

(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)

For the three and six months ended December 31, 2006, cash in the amount of \$1.8 million and \$ 2.1 million respectively, was received as the result of the exercise of options granted under share-based payment arrangements. The tax benefit realized by the Company, during the three and six months ended December 31, 2006 from the exercise of options eligible for a tax deduction was \$ 536,000 and \$741,000 respectively, which was recorded as additional paid-in capital.

Long Term Incentive Plan

On September 10, 2007 the Company's Board of Directors approved the implementation of a Long-Term Incentive Plan called the Open Text Corporation Long-Term Incentive Plan (LTIP). The LTIP took effect for the Company's Fiscal 2008, starting on July 1, 2007. The LTIP is a rolling three year program whereby the Company will make a series of annual grants, each of which covers a three year performance period, to certain of its employees, upon the employee meeting pre-determined performance targets. Awards may range from 100% to 150% of target, based on the employee's accomplishments over the three year period. The maximum amount that an employee may receive with regard to any single performance criterion is 1.5 times the target award for that criterion. The Company will pay LTIP awards in cash.

Three performance criteria will be used to measure performance over the relevant three year period:

Absolute share price if the Company's common shares appreciate to a predetermined price per share and that price is maintained for a minimum of 22 consecutive NASDAQ trading days, the absolute share price target will have been achieved;

Relative total shareholder return if, over a three year period, the Company's common shares appreciate at a rate which exceeds the rate of appreciation disclosed by the Standard & Poor's Mid Cap 400 Software and Services Index by a prearranged percentage, the relative total shareholder return target will have been achieved; and

Average adjusted earnings per share if the average of the adjusted earnings per share over the latter two years of a three year period reaches a preset amount, the average adjusted earnings per share target will have been met (adjusted earnings per share means net income plus certain non-operational charges that have no impact on the Company's operating decisions, as defined by the Company's Board of Directors from time to time, with the resulting sum divided by the total number of common shares outstanding).

The three performance criteria carry the following weightings:

Absolute share price = 37.5%;

Relative total shareholder return = 37.5%; and

Average adjusted earnings per share = 25%.

As part of the LTIP, the Company's Board of Directors approved certain target payments, under the LTIP, to certain employees during the three and six months ended December 31, 2007. Consistent with the provisions of SFAS 123R the Company has measured the fair value of the

Edgar Filing: OPEN TEXT CORP - Form 10-Q

liability under the LTIP as of December 31, 2007 and charged the expense relating to such liability to compensation cost in the amount of \$572,000 for the three months ended December 31, 2007 (Three months ended December 31, 2006 nil) and \$757,000 for the six months ended December 31, 2007 (Six months ended December 31, 2006 nil). The outstanding liability under

Table of Contents**OPEN TEXT CORPORATION****UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Three and Six Months Ended December 31, 2007****(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)**

the LTIP is re-measured based upon the change in the fair value of the liability. As of the end of every reporting period, a cumulative adjustment to compensation cost for the change in fair value is recognized. The cumulative compensation expense recognized upon completion of the LTIP will be equal to the payouts made.

Employee Share Purchase Plan (ESPP)

During the three months ended December 31, 2007, no Common Shares were issued under the ESPP. During the six months ended December 31, 2007, 16,894 Common Shares were issued under the ESPP for cash collected from employees, in prior periods, totaling \$350,000. In addition, cash in the amount of approximately \$151,000 and \$332,000, respectively, was received from employees for the three and six months ended December 31, 2007 that will be used to purchase Common Shares in future periods.

During the three months ended December 31, 2006, no Common Shares were issued under the ESPP. During the six months ended December 31, 2006, 22,209 Common Shares were issued under the ESPP for cash collected from employees, in prior periods, totaling \$305,000. In addition, cash in the amount of approximately \$160,000 and \$339,000, respectively, was received from employees for the three and six months ended December 31, 2006 that was used to purchase Common Shares in future periods.

NOTE 10 NET INCOME PER SHARE

Basic net income per share is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted net income per share is computed by dividing net income by the shares used in the calculation of basic net income per share plus the dilutive effect of common share equivalents, such as stock options, using the treasury stock method. Common share equivalents are excluded from the computation of diluted net income per share if their effect is anti-dilutive.

	Three months ended December 31,		Six months ended December 31,	
	2007	2006	2007	2006
Basic net income per share				
Net income	\$ 10,685	\$ 2,277	\$ 18,485	\$ 9,578
Basic net income per share	\$ 0.21	\$ 0.05	\$ 0.37	\$ 0.20
Diluted net income per share				
Net income	\$ 10,685	\$ 2,277	\$ 18,485	\$ 9,578
Diluted net income per share	\$ 0.20	\$ 0.04	\$ 0.35	\$ 0.19
Weighted average number of shares outstanding				
Basic	50,736	49,152	50,511	49,063
Effect of dilutive securities	1,953	1,587	1,713	1,434
Diluted	52,689	50,739	52,224	50,497

Excluded as anti-dilutive *	56	2,188	60	2,402
-----------------------------	----	-------	----	-------

* Certain options to purchase Common Shares are excluded from the calculation of diluted net income per share because the exercise price of the stock options was greater than or equal to the average price of the Common Shares, and therefore their inclusion would have been anti-dilutive.

Table of Contents

OPEN TEXT CORPORATION

UNAUDITED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended December 31, 2007

(Tabular dollar amounts in thousands of U.S. Dollars, except per share data)

NOTE 11 INCOME TAXES

The Company's effective tax rate represents the net effect of the mix of income earned in various tax jurisdictions that are subject to a wide range of income tax rates.

On July 1, 2007, the Company adopted FIN 48. FIN 48 contains a two-step approach to recognizing and measuring uncertain tax positions under SFAS No. 109, Accounting for Income Taxes. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates it is more likely than not, based solely on the technical merits, that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the appropriate amount of the benefit to recognize. The amount of benefit to recognize is measured as the maximum amount which is more likely than not to be realized. The tax position is derecognized when it is no longer more likely than not of being sustained. On subsequent recognition and measurement the maximum amount which is, more likely than not, capable to be recognized at each reporting date will represent the Company's best estimate, given the information available at the reporting date, although the outcome of the tax position is not absolute or final.

The Company did not recognize an increase in its net liability for unrecognized tax obligations, or record a change to the balance of retained earnings, as a result of the adoption FIN 48.

The total amount of unrecognized tax benefits as of December 31, 2007 was \$45.4 million of which \$10.4 million of unrecognized tax benefits would affect the Company's effective tax rate, if realized, and the remaining \$35.0 million would reduce goodwill recorded in connection with the Hummingbird acquisition. In addition, consistent with the provisions of FIN 4