CITRIX SYSTEMS INC
Form 10-Q/A
March 07, 2005
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q/A

AMENDMENT NO. 1

(Mark One)

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

For the quarterly period ended June 30, 2004

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 0-27084

CITRIX SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**75-2275152**
(State or other jurisdiction of incorporation or organization)	**(IRS Employer Identification No.)**
851 West Cypress Creek Road Fort Lauderdale, Florida	**33309**
(Address of principal executive offices)	**(Zip Code)**

Registrant s Telephone Number, Including Area Code:

(954) 267-3000

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 x No ¨

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes x No ¨

As of August 2, 2004 there were 169,143,510 shares of the registrant s Common Stock, $.001 par value per share, outstanding.

Table of Contents

EXPLANATORY NOTE

Citrix Systems, Inc. (the Company) is filing this Amendment No. 1 to its Form 10-Q for the quarter ended June 30, 2004 (the 2004 Second Quarter 10-Q), which was originally filed on August 6, 2004, to restate its condensed consolidated balance sheets for the period ended June 30, 2004 and December 31, 2003, its condensed consolidated statements of cash flows for the six months ended June 30, 2004 and 2003 and the related disclosures.

This Amendment No. 1 is being filed to address comments from the staff (the Staff) of the Securities and Exchange Commission (the SEC) in connection with the Staff s normal periodic review of the Company s filings. As a result of the review, the Company is restating the accompanying June 30, 2004 and December 31, 2003 condensed consolidated balance sheets to correct an error in the classification of the portion of the Company s cash equivalents and investments that are pledged as collateral under the Company s synthetic lease arrangement, credit default contracts, and interest rate swaps to classify such assets separately as restricted cash equivalents and investments. In its filings with the SEC, the Company has disclosed in narrative form the specific amounts pledged under its synthetic lease arrangement, credit default contracts and interest rate swaps from the inception of each arrangement and is now separately classifying the aggregate amounts pledged as long-term restricted cash equivalents and investments in its condensed consolidated balance sheets. Please refer to Note 1 to the accompanying condensed consolidated financial statements for additional information.

The Company has also made certain balance sheet, income statement and cash flow reclassifications. The Company reclassified investments in auction rate securities that were previously classified as cash equivalents in the accompanying June 30, 2004 and December 31, 2003 condensed consolidated balance sheets to short-term investments. The condensed consolidated statements of cash flows for the six months ended June 30, 2004 and 2003 were adjusted to reflect the impact of the reclassification. The Company also reclassified the amortization of core and product technology previously classified as an operating expense to a component of cost of revenues in the accompanying condensed consolidated income statements. The condensed consolidated statements of income for the three months and six months ended June 30, 2004 and 2003 were adjusted to reflect the impact of this change in classification. Additionally, the Company reclassified certain items in its condensed consolidated statement of cash flows to separately present investing cash flows for available-for-sale investments and held-to-maturity investments and to separately present investing cash flows from sales of investments and maturities of investments. Please refer to Note 1 to the accompanying condensed consolidated financial statements for additional information on the reclassifications.

This Amendment No. 1 does not result in a change in the Company s previously reported revenues, net income, earnings per share, cash flow from operations, total assets, or total cash and investments shown in its condensed consolidated financial statements. Further, except as discussed above, the Company has not modified or updated disclosures presented in the 2004 Second Quarter 10-Q in this Form 10-Q/A, except as required to reflect the effects of the items discussed above. For the convenience of the reader, this Form 10-Q/A, sets forth the complete text of the originally filed 2004 Second Quarter 10-Q rather than just the amended portions thereof. Accordingly, this Form 10-Q/A does not reflect events occurring after the filing of the 2004 Second Quarter 10-Q or modify or update those disclosures affected by subsequent events. Information not affected by these restatements and reclassifications are unchanged and reflects the disclosures made at the time of the original filing of the 2004 Second Quarter 10-Q on August 6, 2004. Events occurring after the filing of the 2004 Second Quarter 10-Q or other disclosures necessary to reflect subsequent events have been or will be addressed in the Company s original Quarterly Reports on Form 10-Q for the quarterly period ending September 30, 2004 or amended Quarterly Report on Form 10-Q/A for such quarterly period which is being filed concurrently with the filing of this Form 10-Q/A and any reports filed with the SEC subsequent to the date of this filing.

This Form 10-Q/A should be read in conjunction with the Company s filings made with the SEC subsequent to the filing of the 2004 Second Quarter 10-Q, including any amendments to those filings. The following items have been amended as a result of the restatements and reclassifications described above:

Table of Contents

CITRIX SYSTEMS, INC.

Form 10-Q/A

For the Quarterly Period Ended June 30, 2004

CONTENTS

Table of Contents

PART I: FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Citrix Systems, Inc.

Condensed Consolidated Balance Sheets

(Unaudited)

	June 30, 2004	December 31, 2003
	(As restated)	(As restated)
	(In thousands, except par value)	
Assets		
Current assets:		
Cash and cash equivalents	**$ 106,684**	$ 182,969
Short-term investments	**85,417**	385,431
Accounts receivable, net of allowances of $6,862 and $6,365 at June 30, 2004 and December 31, 2003, respectively	**86,479**	87,464
Prepaid expenses and other current assets	**31,254**	58,167
Current portion of deferred tax assets	**52,238**	51,540
Total current assets	**362,072**	765,571
Restricted cash and cash equivalents	**143,152**	146,460
Long-term investments	**186,603**	183,411
Property and equipment, net	**68,932**	65,837
Goodwill, net	**313,584**	152,364
Other intangible assets, net	**74,998**	21,300
Long-term portion of deferred tax assets	**112**	3,168
Other assets	**8,650**	6,828
	$ 1,158,103	$ 1,344,939
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable and accrued expenses	**$ 107,682**	$ 114,456
Current portion of deferred revenues	**184,002**	152,938
Convertible subordinated debentures		351,423
Total current liabilities	**291,684**	618,817
Long-term portion of deferred revenues	**9,777**	12,137
Other liabilities	**9,447**	7,187
Commitments and contingencies		
Stockholders equity:		

Preferred stock at $.01 par value: 5,000 shares authorized, none issued and outstanding		
Common stock at $.001 par value: 1,000,000 shares authorized; 209,805 and 202,622 issued at June 30, 2004 and December 31, 2003, respectively	**210**	203
Additional paid-in capital	**828,706**	700,111
Retained earnings	**687,541**	646,740
Accumulated other comprehensive income	**624**	7,810
	1,517,081	1,354,864
Less common stock in treasury, at cost (39,209 and 38,150 shares at June 30, 2004 and December 31, 2003, respectively)	**(669,886)**	(648,066)
Total stockholders equity	**847,195**	706,798
	$ 1,158,103	$ 1,344,939

See accompanying notes

4

Table of Contents

Citrix Systems, Inc.

Condensed Consolidated Statements of Income

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	**2003**	**2004**	**2003**
	(In thousands, except per share information)			
Revenues:				
Software licenses	**$ 87,716**	$ 92,200	**$ 175,142**	$ 189,074
Software license updates	**66,981**	39,560	**125,878**	74,800
Services	**23,605**	11,289	**38,592**	22,666
Total net revenues	**178,302**	143,049	**339,612**	286,540
Cost of revenues:				
Cost of software license revenues	**756**	3,486	**2,169**	6,779
Cost of services revenues	**4,169**	1,550	**6,992**	2,988
Amortization of core and product technology	**3,598**	2,637	**6,632**	5,511
Total cost of revenues	**8,523**	7,673	**15,793**	15,278
Gross margin	**169,779**	135,376	**323,819**	271,262
Operating expenses:				
Research and development	**22,173**	16,244	**41,211**	31,369
Sales, marketing and support	**80,804**	60,550	**154,932**	122,261
General and administrative	**27,837**	23,022	**52,588**	44,044
Amortization of other intangible assets	**1,873**	62	**2,599**	162
In-process research and development			**18,700**	
Total operating expenses	**132,687**	99,878	**270,030**	197,836
Income from operations	**37,092**	35,498	**53,789**	73,426
Interest income	**2,567**	4,512	**8,252**	10,175
Interest expense	**(8)**	(4,523)	**(4,352)**	(9,072)
Write-off of deferred debt issuance costs			**(7,219)**	
Other income, net	**190**	1,629	**1,175**	1,975
Income before income taxes	**39,841**	37,116	**51,645**	76,504
Income taxes	**8,366**	7,772	**10,845**	16,831
Net income	**$ 31,475**	$ 29,344	**$ 40,800**	$ 59,673
Earnings share:				
Basic	**$ 0.18**	$ 0.18	**$ 0.24**	$ 0.36

Diluted	**$ 0.18**	$ 0.17	**$ 0.23**	$ 0.35
Weighted average shares outstanding:				
Basic	**170,327**	165,409	**168,392**	166,349
Diluted	**176,273**	171,925	**174,428**	171,158

See accompanying notes

Table of Contents

Citrix Systems, Inc.

Condensed Consolidated Statements of Cash Flows

(Unaudited)

	Six Months Ended June 30, 2004 (As restated)	Six Months Ended June 30, 2003 (As restated)
	(In thousands)	
OPERATING ACTIVITIES		
Net income	**$ 40,800**	$ 59,673
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization	**9,231**	5,673
Depreciation and amortization of property and equipment	**10,142**	12,900
Write-off of deferred debt issuance costs	**7,219**	
Realized gain on investments	**(574)**	(1,209)
In-process research and development	**18,700**	
Provision for doubtful accounts	**995**	1,254
Provision for product returns	**2,425**	482
Provision for inventory reserves	**312**	507
Tax benefit related to the exercise of non-statutory stock options and disqualifying dispositions of incentive stock options	**12,103**	8,999
Accretion of original issue discount and amortization of financing cost	**4,318**	9,065
Other non-cash items	**265**	(135)
Total adjustments to reconcile net income to net cash provided by operating activities	**65,136**	37,536
Changes in operating assets and liabilities, net of the effects of acquisition:		
Accounts receivable	**420**	(16,511)
Prepaid expenses and other current assets	**11,195**	4,752
Other assets	**(394)**	2,300
Deferred tax assets	**(369)**	(270)
Accounts payable and accrued expenses	**(16,304)**	(2,327)
Deferred revenues	**23,704**	24,160
Other liabilities	**(1,333)**	4,499
Total changes in operating assets and liabilities Acquisitions	**16,919**	16,603
Net cash provided by operating activities	**122,855**	113,812
INVESTING ACTIVITIES		
Purchases of investments	**(96,285)**	(189,784)
Proceeds from sales of available-for-sale investments	**153,090**	44,014
Proceeds from maturities of available-for-sale investments	**43,090**	84,713
Proceeds from maturities of held-to-maturities investments	**195,350**	
Purchases of property and equipment	**(11,736)**	(3,886)
Cash paid for licensing agreements	**(12,942)**	(372)
Cash paid for acquisition, net of cash acquired	**(90,750)**	

Net cash provided by (used in) investing activities	**179,817**	(65,315)
FINANCING ACTIVITIES		
Proceeds from issuance of common stock	**19,876**	25,201
Cash paid under stock repurchase programs	**(43,174)**	(70,633)
Cash paid to redeem convertible subordinated debentures	**(355,659)**	
Proceeds from sale of put warrants		655
Other		(11)
Net cash used in financing activities	**(378,957)**	(44,788)
Change in cash and cash equivalents	**(76,285)**	3,709
Cash and cash equivalents at beginning of period	**182,969**	82,350
Cash and cash equivalents at end of period	**$ 106,684**	$ 86,059
Supplemental non-cash investing activity		
Decrease in restricted cash equivalents and investments	**$ (3,308)**	$ (23,182)

See accompanying notes

Table of Contents

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

1. BASIS OF PRESENTATION

The Company recently reviewed its financial statement presentation and disclosure in response to comments received from the staff of the Securities and Exchange Commission (the SEC) in a normal periodic review of the Company s filings. As a result, the Company is restating the accompanying June 30, 2004 and December 31, 2003 condensed consolidated balance sheets to correct an error in the classification of the portion of the Company s cash equivalents and investments pledged as collateral under the Company s synthetic lease arrangement, credit default contracts and interest rate swaps to classify such assets separately as restricted cash equivalents and investments. In its filings with the SEC, the Company has disclosed in narrative form the specific amounts pledged under its synthetic lease arrangement, credit default contracts and interest rate swaps and is now separately classifying the aggregate amounts pledged as long-term restricted cash equivalents and investments in its condensed consolidated balance sheets. The condensed consolidated statements of cash flows for the six months ended June 30, 2004 and 2003 were restated to reflect the impact of the change.

In addition, certain reclassifications of items in the prior periods financial statements have been made to conform to the current period s presentation. The Company reclassified investments in auction rate securities previously classified as cash equivalents to short-term investments. Also in accordance with Statement of Financial Accounting Standards (SFAS) No. 95, *Statement of Cash Flows,* the Company reclassified certain items in its condensed consolidated statements of cash flows to separately present investing cash flows for available-for-sale investments and held-to-maturity investments and to separately present investing cash flows from sales of investments and maturities of investments. The accompanying condensed consolidated balance sheets and statements of cash flows for all periods presented were adjusted to reflect the reclassification of these items.

The Company also reclassified the amortization of core and product technology previously classified as an operating expense to a component of cost of revenues in the accompanying condensed consolidated statements of income.

The changes to the Company s presentation described above do not change the Company s total cash and investments and have no impact on operating cash flows, total assets, net revenues or net income. All such changes have been consistently applied to all periods presented and a comparison of the amounts previously reported to the adjusted amounts presented in this Quarterly Report on Form 10-Q/A (in thousands):

	June 30, 2004		December 31, 2003	
	As Reported	As Adjusted	As Reported	As Adjusted
Condensed Consolidated Balance Sheet Information				
Cash and cash equivalents	$ 183,958	$ 106,684	$ 359,343	$ 182,969

Short-term investments	56,407	85,417	252,971	385,431
Total current assets	410,336	362,072	809,485	765,571
Restricted cash equivalents and investments		143,152		146,460
Long-term investments	281,491	186,603	285,957	183,411

	For the Six Months Ended June 30,			
	2004		2003	
	As Reported	As Adjusted	As Reported	As Adjusted
Condensed Consolidated Statements of Cash Flow Information				
Net income	$ 40,800	$ 40,800	$ 59,673	$ 59,673
Net cash provided by operating activities	122,855	122,855	113,812	113,812
Cash flows from investing activities:				
Purchases of investments	(65,506)	(96,285)	(83,822)	(189,784)
Proceeds from sales and maturities of investments	261,651		124,578	
Proceeds from sales of available-for-sale investments		153,090		44,014
Proceeds from maturities of available-for-sale investments		43,090		84,713
Proceeds from maturity of held-to-maturity investments		195,350		
Net cash provided by (used in) investing activities	80,717	179,817	36,498	(65,315)
Net cash used in financing activities	(378,957)	(378,957)	(44,788)	(44,788)
Change in cash and cash equivalents	(175,385)	(76,285)	105,522	3,709
Cash and cash equivalents at beginning of year	359,343	182,969	142,700	82,350
Cash and cash equivalents at end of year	183,958	106,684	248,222	86,059

Table of Contents

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

	For the Three Months Ended June 30,			
	2004		2003	
	As Reported	As Adjusted	As Reported	As Adjusted
Condensed Consolidated Income Statement Information				
Net revenues	$ 178,302	$ 178,302	$ 143,049	$ 143,049
Total cost of revenues	4,925	8,523	5,036	7,673
Gross margin	173,377	169,779	138,013	135,376
Total operating expenses	136,285	132,687	102,515	99,878
Net income	31,475	31,475	29,344	29,344

	For the Six Months Ended June 30,			
	2004		2003	
	As Reported	As Adjusted	As Reported	As Adjusted
Condensed Consolidated Income Statement Information				
Net revenues	$ 339,612	$ 339,612	$ 286,540	$ 286,540
Total cost of revenues	9,161	15,793	9,767	15,278
Gross margin	330,451	323,819	276,773	271,262
Total operating expenses	276,662	270,030	203,347	197,836
Net income	40,800	40,800	59,673	59,673

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. All adjustments, which, in the opinion of management, are considered necessary for a fair presentation of the results of operations for the periods shown, are of a normal recurring nature and have been reflected in the unaudited condensed consolidated financial statements. The results of operations for the periods presented are not necessarily indicative of the results expected for the full year or for any future period. The information included in these unaudited condensed consolidated financial statements should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations contained in this report and the consolidated financial statements and accompanying notes included in the Citrix Systems, Inc. (the Company) to Form 10-K for the year ended December 31, 2003, as amended.

2. Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. While the Company believes that such estimates are fair when considered in conjunction with the condensed consolidated financial position and results of operations taken as a whole, the actual amount of such estimates, when known, will vary from these estimates.

Restricted Cash Equivalents and Investments

Restricted cash equivalents and investments at June 30, 2004 and December 31, 2003 include approximately $62.8 million in investment securities and cash equivalents that were pledged as collateral for specified obligations under the Company s synthetic lease arrangement. In addition, at June 30, 2004 and December 31, 2003 approximately $80.3 million and $83.6 million, respectively, in investment securities were pledged as collateral for certain of the Company s

8

Table of Contents

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

credit default contracts and interest rate swaps. The Company maintains the ability to manage the composition of the restricted investments within certain limits and to withdraw and use excess investment earnings from the restricted collateral for operating purposes. For further information, see Notes 8 and 13.

Revenue Recognition

The Company markets and licenses software products primarily through value-added resellers, channel distributors, system integrators and independent software vendors. The Company also separately sells software license updates and services, which include product training, technical support and consulting services, as well as Web-based desktop access services. The Company s software licenses are generally perpetual, and are delivered by means of packaged products and electronically.

The Company s packaged products are typically purchased by medium and small-sized businesses with a minimal number of locations. In these cases, the software license is delivered with the packaged product. Electronic license arrangements are used with more complex multiserver environments typically found in larger business enterprises that deploy the Company s products on a department or enterprise-wide basis, which could require differences in product features and functionality at various customer locations. Once the Company receives a software license agreement and purchase order, the enterprise customer licenses are electronically delivered to the customer with software activation keys that enable the feature configuration ordered by the end-user. Software may be delivered indirectly by a channel distributor, via download from the Company s website or directly to the end-user by the Company.

Revenue is recognized when it is earned. The Company s revenue recognition policies are in compliance with Statement of Position (SOP) 97-2 (as amended by SOP 98-4 and SOP 98-9) and related interpretations, *Software Revenue Recognition.* In addition, the Company s Online Division recognizes revenue in accordance with Emerging Issues Task Force (EITF) No. 00-3, *Application of AICPA Statement of Position 97-2 to Arrangements That Include the Right to Use Software Stored on Another Entity s Hardware.* The Company recognizes revenue when all of the following criteria are met: persuasive evidence of the arrangement exists; delivery has occurred and the Company has no remaining obligations; the fee is fixed or determinable; and collectibility is probable. The Company defines these four criteria as follows:

Persuasive evidence of the arrangement exists. The Company recognizes revenue on packaged product upon shipment to distributors and resellers. For packaged product sales, it is the Company s customary practice to require a purchase order from distributors and resellers who have previously negotiated a master packaged product distribution or resale agreement. For enterprise customer license arrangements involving software licenses and software license updates, the Company typically requires a purchase order from the distributor or reseller and an executed software license agreement from the end-user. For Web-based desktop access services, the Company requires the customer or reseller to electronically accept the terms of the on-line service agreement or execute a contract and also submit a purchase order. The Company requires a purchase order and agreement for technical support, product training and consulting services.

Delivery has occurred and the Company has no remaining obligations. The Company s standard delivery method is free-on-board shipping point. Consequently, it considers delivery of packaged product to have occurred when the products are shipped to distributors pursuant to an agreement and purchase order. The Company considers delivery of licenses under electronic licensing agreements to have occurred when the related products are shipped and the end-user has been electronically provided with the licenses that include the activation keys that allow the end-user to take immediate possession of the software. For product training and consulting services, the Company fulfills its obligation when the services are performed. For software license updates, technical support and Web-based desktop access services, the Company assumes that the obligations are satisfied ratably over the respective terms of the agreements, which are typically 12 to 24 months.

The fee is fixed or determinable. In the normal course of business, the Company does not provide customers the right to a refund of any portion of their license fees or extended payment terms. The Company sells software license updates, and services, which includes technical support, product training and consulting services, separately and it determines vendor specific objective evidence (VSOE) of fair value by the price charged for each product when sold separately or applicable renewal rates.

Collectibility is probable. The Company determines collectibility on a customer-by-customer basis and generally does not require collateral. The Company typically sells to distributors or resellers for whom there are histories of successful collection. New customers are subject to a credit review process that evaluates the customers financial position and ultimately their ability to pay. Customers are subject to an ongoing credit

Table of Contents

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

review process. If the Company determines from the outset of an arrangement that collectibility is not probable, revenue recognition is deferred until customer payment is received and the other parameters of revenue recognition described above have been achieved. Management s judgment is required in assessing the probability of collection, which is generally based on evaluation of customer specific information, historical experience and economic market conditions.

Net revenues include the following categories: Software Licenses, Software License Updates and Services. Software Licenses primarily represents fees related to the licensing of the MetaFrame products, additional user licenses and management products (such as MetaFrame Presentation Server and MetaFrame Access Suite). These revenues are reflected net of sales allowances and provisions for stock balancing return rights. Software License Updates consists of fees related to the Subscription Advantage program (the Company s terminology for post contract support) that are recognized ratably over the term of the contract, which is typically 12-24 months. Subscription Advantage is an annual renewable program that provides subscribers with automatic delivery of software upgrades, enhancements and maintenance releases when and if they become available during the term of subscription. Services consist primarily of technical support services and Web-based desktop access services revenue recognized ratably over the contract term, revenue from product training and certification, and consulting services revenue related to implementation of the Company s software products, which is recognized as the services are provided.

The Company sells most of its software products bundled with an initial subscription for software license updates that provides the end-user with free enhancements and upgrades to the licensed product on a when and if available basis. Customers may also elect to purchase technical support, product training or consulting services. The Company allocates revenue to software license updates and any other undelivered elements of the arrangement based on VSOE of fair value of each element and such amounts are deferred until the applicable delivery criteria and other revenue recognition criteria described above have been met. The balance of the revenue, net of any discounts inherent in the arrangement, is allocated to the delivered software product using the residual method and recognized at the outset of the arrangement as the software licenses are delivered. If management cannot objectively determine the fair value of each undelivered element based on VSOE, revenue recognition is deferred until all elements are delivered, all services have been performed, or until fair value can be objectively determined.

In the normal course of business, the Company does not permit product returns, but it does provide most of its distributors and value added resellers with stock balancing and price protection rights. Stock balancing rights permit distributors to return products to the Company by the forty-fifth day of the fiscal quarter, subject to ordering an equal dollar amount of the Company s other products prior to the last day of the same fiscal quarter. Price protection rights require that the Company grant retroactive price adjustments for inventories of products held by distributors or resellers if it lowers prices for such products. The Company establishes provisions for estimated returns for stock balancing and price protection rights, as well as other sales allowances, concurrently with the recognition of revenue. The provisions are established based upon consideration of a variety of factors, including, among other things, recent and historical return rates for specific products and distributors, estimated distributor inventory levels by product, the impact of any new product releases and projected economic conditions. Actual product returns for stock balancing and price protection provisions incurred are, however, dependent upon future events, including the amount of stock balancing activity by distributors and the level of distributor inventories at the time of any price adjustments. The Company continually monitors the factors that influence the pricing of its products and distributor inventory levels and makes adjustments to these provisions when it believes actual returns and other allowances could differ from established reserves. The Company s ability to recognize revenue upon shipment to distributors is predicated on its ability to reliably estimate future stock balancing returns. If actual experience or changes in market condition impairs the Company s ability to estimate returns, it would be required to defer the recognition of revenue until the delivery of the product to the end-user. Allowances for estimated product returns amounted to approximately $2.0 million at June 30, 2004 and $3.0 million at December 31, 2003. The Company has not reduced and has no current plans to reduce its prices for inventory currently held by distributors or resellers.

Accordingly, there were no reserves required for price protection at June 30, 2004 or December 31, 2003. The Company records estimated reductions to revenue for customer programs and incentive offerings including volume-based incentives. If market conditions were to decline, the Company could take actions to increase its customer incentive offerings, which could result in an incremental reduction to revenue at the time the incentive is offered.

Accounting for Stock-Based Compensation

The Company s stock-based compensation program is a broad based, long-term retention program that is intended to attract and reward talented employees and align stockholder and employee interest. At June 30, 2004, the Company had four stock-based employee compensation plans. The number and frequency of stock option grants are based on competitive practices, operating results of the Company, the number of options available for grant under the Company s shareholder approved plans, and other factors. All employees are eligible to participate in the stock option program.

Table of Contents

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

SFAS No. 123, *Accounting for Stock-Based Compensation*, as amended by SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure,* defines a fair value method of accounting for issuance of stock options and other equity instruments. Under the fair value method, compensation cost is measured at the grant date based on the fair value of the award and is recognized over the service period, which is usually the vesting period. Pursuant to SFAS No. 123, companies are not required to adopt the fair value method of accounting for employee stock-based transactions. Companies are permitted to account for such transactions by applying the intrinsic value method of accounting under Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, but are required to disclose in a note to the consolidated financial statements pro forma net income and per share amounts as if a company had applied the methods prescribed by SFAS No. 123.

The Company applies APB Opinion No. 25 and related interpretations in accounting for its plans, stock options granted to employees and non-employee directors and has complied with the disclosure requirements of SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*. Except for non-employee directors, the Company has not granted any options to non-employees. The Company has elected to follow APB Opinion No. 25 because the alternative fair value accounting provided for under SFAS No. 123 requires use of option valuation models, including the Black-Scholes model, that were developed for use with traded options that have no vesting restrictions and are fully transferable, as opposed to employee stock options, which are typically non-transferable and last up to ten years. Currently, management believes there is not one agreed upon option valuation method that is comparable among all reporting companies. Specifically, the Black-Scholes model requires the input of highly subjective assumptions, including assumptions related to the expected stock price volatility over the expected life of the option. Because the Company s stock-based awards to employees have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the fair value estimate, in management s opinion, the existing pricing models do not necessarily provide a reliable single measure of the fair value of its stock-based awards to employees. Because the Black-Scholes model is based on statistical expectations, the calculation can result in substantial earnings volatility that may not agree, as to timing or amount, with the actual gain or loss accrued or realized by the option holder.

Had compensation cost for the Company s four stock-based compensation plans been determined based on the fair value on the grant dates for grants under those plans consistent with SFAS No. 123, the Company s cash flows would have remained unchanged, however net income and earnings per share would have been reduced to the pro forma amounts indicated below (in thousands, except per share information):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	**2003**	**2004**	**2003**
Net income:				
As reported	**$ 31,475**	$ 29,344	**$ 40,800**	$ 59,673
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	**(11,743)**	(23,328)	**(27,002)**	(47,413)

Pro forma	**$ 19,732**	$ 6,016	**$ 13,798**	$ 12,260
Basic earnings per share:				
As reported	**$ 0.18**	$ 0.18	**$ 0.24**	$ 0.36
Pro forma	**$ 0.12**	$ 0.04	**$ 0.08**	$ 0.07
Diluted earnings per share:				
As reported	**$ 0.18**	$ 0.17	**$ 0.23**	$ 0.35
Pro forma	**$ 0.11**	$ 0.03	**$ 0.08**	$ 0.07

For purposes of the pro forma calculations, the fair value of each option is estimated on the date of the grant using the Black-Scholes option-pricing model, assuming no expected dividends and the following assumptions:

	Stock options granted during the					
	Three Months ended June 30,		Six Months ended June 30,			
	2004	2003	2004		2003	
Expected volatility factor	**0.49**	0.61	**0.42**	**0.49**	0.61	0.68
Approximate risk free interest rate	**3.5%**	2.5%	**3.0%**	**3.5%**	2.5%	-3.0 %
Expected lives (in years)	**4.76**	4.73	**4.75**	**4.76**	4.70	4.73

Table of Contents

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

3. Earnings Per Share

Basic earnings per share is calculated by dividing income available to shareholders by the weighted-average number of common shares outstanding during each period. Diluted earnings per share is computed using the weighted average number of common and dilutive common share equivalents outstanding during the period. Dilutive common share equivalents consist of shares issuable upon the exercise of stock options (calculated using the treasury stock method). Certain shares under the Company s stock-based compensation programs, and common stock potentially issuable upon conversion of the Company s convertible subordinated debentures were excluded from the computation of diluted earnings per share due to their anti-dilutive effect for the respective periods.

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except per share information):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	**2003**	**2004**	**2003**
Numerator:				
Net income	**$ 31,475**	$ 29,344	**$ 40,800**	$ 59,673
Denominator:				
Denominator for basic earnings per share weighted-average shares	**170,327**	165,409	**168,392**	166,349
Effect of employee stock options: Employee stock options	**5,946**	6,516	**6,036**	4,809
Denominator for diluted earnings per share weighted-average shares	**176,273**	171,925	**174,428**	171,158
Basic earnings per share	**$ 0.18**	$ 0.18	**$ 0.24**	$ 0.36
Diluted earnings per share	**$ 0.18**	$ 0.17	**$ 0.23**	$ 0.35
Anti-dilutive weighted shares	**32,689**	45,083	**31,564**	46,819

The decrease in anti-dilutive weighted shares for the three and six months ended June 30, 2004 compared to the three and six months ended June 30, 2003 is due to the redemption of the Company s convertible subordinated debentures during March 2004.

4. Acquisition

On February 27, 2004, the Company acquired all of the issued and outstanding capital stock of Expertcity.com, Inc. (Expertcity), a market leader in Web-based desktop access, as well as a leader in Web-based training and customer assistance products.

The consideration for this transaction was approximately $230.6 million, comprised of approximately $112.6 million in cash and approximately 5.6 million shares of the Company s common stock valued at approximately $118.0 million. In addition to the purchase price, there were direct transaction costs associated with the merger of approximately $4.4 million. The merger agreement provides for additional purchase price consideration of up to approximately 0.6 million shares of Citrix common stock to be issued to the Expertcity stockholders in the event certain revenue and other financial milestones are achieved by the Expertcity business in 2004. The fair value of the shares issued as additional purchase price consideration, if any, will be based on the market value of the Company s common stock at the date that the shares are earned. Additional purchase price consideration, if any, is expected to be recorded as goodwill.

Table of Contents

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

The results of operations of Expertcity are included in the Company s results of operations beginning after February 27, 2004 and is the Company s new segment, the Citrix Online Division. The following unaudited pro forma information combines the consolidated results of operations of the Company and Expertcity as if the acquisition had occurred at the beginning of fiscal year 2003 (in thousands, except per share data):

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2004	**2003**	**2004**	**2003**
	(unaudited)			
Revenues	**$ 178,302**	$ 151,372	**$ 347,302**	$ 302,095
Income from operations	**37,092**	31,793	**45,539**	65,689
Net income	**31,475**	26,706	**34,071**	54,163
Per share basic	**0.18**	0.16	**0.20**	0.32
Per share diluted	**0.18**	0.15	**0.19**	0.31

Under the purchase method of accounting, the purchase price was allocated to Expertcity s net tangible and intangible assets based on their estimated fair values as of the date of the completion of the acquisition. Independent valuation specialists conducted a valuation in order to assist the Company in determining the fair values of a significant portion of Expertcity s net assets. The work performed by the independent valuation specialists was considered in management s allocation of the purchase price summarized below (in thousands):

	Purchase Price Allocation	Asset Life
Current assets	$ 26,085	
Property and equipment	1,998	Various
In-process research and development	18,700	
Intangible assets	50,800	3-7 years
Goodwill	161,221	Indefinite
Assets acquired	258,804	
Current liabilities	14,019	
Deferred tax liability	9,796	
Total liabilities assumed	23,815	
Net assets acquired, including direct transaction costs	$ 234,989	

Current assets and liabilities acquired from Expertcity consisted mainly of cash and investments, accounts receivable, deferred revenues and other current liabilities.

The fair values used in determining the purchase price allocation for certain intangible assets were based on estimated discounted future cash flows, royalty rates and historical data, among other information. Purchased in-process research and development (IPR&D) of approximately $18.7 million was expensed immediately upon closing of the merger in accordance with Financial Accounting Standards Board Interpretation No. 4, *Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method* due to the fact that it pertains to technology that was not currently technologically feasible, meaning it had not reached the working model stage, did not contain all of the major functions planned for the product, was not ready for initial customer testing and had no alternative future use. The fair value assigned to in-process research and development was determined using the income approach, which includes estimating the revenue and expenses associated with a project s sales cycle and by estimating the amount of after-tax cash flows attributable to the projects. The future cash flows were discounted to present value utilizing an appropriate risk-adjusted rate of return, which ranged from 17% to 20%. The rate of return included a factor that takes into account the uncertainty surrounding the successful development of the IPR&D.

5. Goodwill and Other Intangible Assets

Goodwill. As a result of the Expertcity acquisition during the six months ended June 30, 2004, the Company recorded approximately $161.2 million of goodwill reflected in its new segment, the Citrix Online Division.

Intangible Assets. Intangible assets are recorded at cost, less accumulated amortization. Amortization is computed over the estimated useful lives of the respective assets, generally one to seven years. Intangible assets consist of the following (in thousands):

	June 30, 2004		December 31, 2003	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets:				
Core and product technologies	**$ 119,286**	**$ 69,724**	$ 82,486	$ 63,092
Other	**35,576**	**10,140**	9,447	7,541
	$ 154,862	**$ 79,864**	$ 91,933	$ 70,633

13

Table of Contents

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

Amortization expense for the three and six months ended June 30, 2004 was $5.5 million and $9.2 million, respectively, and $2.7 million and $5.7 million for the three and six months ended June 30, 2003, respectively. Estimated future amortization expense is as follows (in thousands):

Year ending December 31,	
2004	$ 19,745
2005	20,867
2006	15,720
2007	10,126
2008	7,754
Thereafter	7,459

6. Convertible Subordinated Debentures

In March 1999, the Company sold $850 million principal amount at maturity of its zero coupon convertible subordinated debentures (the Debentures) due March 22, 2019, in a private placement. On March 22, 2004, the Company redeemed all of the outstanding Debentures for a redemption price of approximately $355.7 million. The Company used the proceeds from its held-to-maturity investments that matured on March 22, 2004 and cash on hand to fund the aggregate redemption price. At the date of redemption, the Company incurred a charge for the associated deferred debt issuance costs of approximately $7.2 million.

7. Segment Information

The Company operates in a single market consisting of the design, development, marketing, sales and support of access infrastructure software and services for enterprise applications, as well as Web-based desktop access. The Company s revenues are derived from MetaFrame Access Suite sales and related services in the Americas, Europe, the Middle East and Africa (EMEA) and Asia-Pacific regions and from Web-based desktop access services sold by its Citrix Online Division. These three geographic regions and the Citrix Online Division constitute the Company s four reportable segments.

The Company does not engage in intercompany revenue transfers between segments. The Company s management evaluates performance based primarily on revenues in the geographic locations in which the Company operates and separately evaluates revenues from the Citrix Online Division. Segment profit for each segment includes certain sales, marketing, research and development, general and administrative expenses directly attributable to the segment and excludes certain expenses that are managed outside the reportable segments. Costs excluded from segment profit primarily consist of research and development costs associated with the MetaFrame Access Suite products, amortization of core and product technology, amortization of other intangible assets, interest, corporate expenses and income taxes, as well as, non-recurring charges for in-process research and development. Corporate expenses are comprised primarily of corporate marketing costs, operations and certain general and administrative expenses, which are separately managed. Accounting policies of the segments are the same as the Company s consolidated accounting policies.

Net revenues and segment profit, classified by the Company s four reportable segments are as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Net revenues:				
Americas [1]	**$ 84,249**	$ 76,159	**$ 159,139**	$ 143,835
EMEA [2]	**66,867**	55,219	**136,378**	117,064
Asia-Pacific	**16,731**	11,671	**30,844**	25,641
Citrix Online Division	**10,455**		**13,251**	
Consolidated	**$ 178,302**	$ 143,049	**$ 339,612**	$ 286,540
Segment profit (loss):				
Americas [1]	**$ 52,659**	$ 41,889	**$ 94,702**	$ 74,901
EMEA [2]	**38,656**	32,330	**80,683**	71,152
Asia-Pacific	**5,017**	3,347	**9,134**	10,863
Citrix Online Division	**(2,046)**		**(4,654)**	
Unallocated expenses [3]:				
Amortization of intangible assets	**(5,471)**	(2,699)	**(9,231)**	(5,673)
Research and development	**(20,542)**	(16,244)	**(38,997)**	(31,369)
In-process research and development			**(18,700)**	
Net interest and other income (expense)	**2,749**	1,618	**(2,144)**	3,078
Other corporate expenses	**(31,181)**	(23,125)	**(59,148)**	(46,448)
Consolidated income before income taxes	**$ 39,841**	$ 37,116	**$ 51,645**	$ 76,504

(1) The Americas segment is comprised of the United States, Canada and Latin America.
(2) Defined as Europe, the Middle East and Africa
(3) Represents expenses presented to management on a consolidated basis only and not allocated to the operating segments.

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

Identifiable assets classified by the Company s four reportable segments are shown below (in thousands):

	June 30, 2004	December 31, 2003
Identifiable assets:		
Americas	**$ 474,096**	$ 975,054
EMEA	**425,065**	328,689
Asia-Pacific	**41,209**	41,196
Citrix Online Division	**217,733**	
Total identifiable assets	**$ 1,158,103**	$ 1,344,939

8. Derivative Financial Instruments

Cash Flow Hedges. At June 30, 2004 and December 31, 2003, the Company had in place foreign currency forward sale contracts with a notional amount of $41.9 million and $37.2 million, respectively, and foreign currency forward purchase contracts with a notional amount of $145.9 million and $160.9 million, respectively. The fair values of these contracts at June 30, 2004 and December 31, 2003 were assets of $4.0 million and $12.8 million, respectively, and liabilities of $3.0 million and $4.9 million, respectively. A substantial portion of the Company s anticipated overseas expense will be transacted in local currencies. To protect against fluctuations in operating expenses and the volatility of future cash flows caused by changes in currency exchange rates, the Company has established a program that uses forward foreign exchange contracts to reduce its exposure to these potential changes. The terms of these instruments, and the hedging transactions to which they relate, generally do not exceed 12 months. Currencies hedged are Euros, British pounds sterling, Australian dollars, Swiss francs and Japanese yen. There was no material ineffectiveness of the Company s foreign currency forward contracts for the three and six months ended June 30, 2004 and 2003.

Fair Value Hedges. The Company uses interest rate swap instruments to hedge against the changes in fair value of certain of its available-for-sale securities due to changes in interest rates. The instruments have an aggregate notional amount of $182.4 million related to specific available-for-sale securities and expire on various dates through September 2008. Each of the instruments swap the fixed rate interest on the underlying investments for a variable rate based on the London Interbank Offered Rate, or LIBOR, plus a specified margin. Changes in the fair value of the interest rate swap instruments are recorded in earnings along with related designated changes in the value of the underlying investments. The fair value of the instruments were assets of approximately $1.4 million and liabilities of $1.5 million at June 30, 2004 and liabilities of $4.2 million at December 31, 2003. There was no material ineffectiveness of the Company s interest rate swaps for the three and six months ended June 30, 2004 or 2003.

Derivatives Not Designated as Hedges. The Company utilizes credit derivatives for investment purposes that either do not qualify or are not designated for hedge accounting treatment under SFAS No. 133 *Accounting for*

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

Derivative Instruments and Hedging Activities and its related interpretations. Accordingly, changes in the fair value of these contracts are recorded in other income, net, if any. Under the terms of these contracts, the Company assumes the default risk, above a certain threshold, of a portfolio of specified high credit quality referenced issuers in exchange for a fixed yield that is recorded in interest income. In the event of default by underlying referenced issuers above specified amounts, the Company will pay the counterparty an amount equivalent to its loss, not to exceed the notional value of the contract. The primary risk associated with these contracts is the default risk of the underlying issuers. The risk levels of these instruments are equivalent to AAA and Super AAA , single securities. The purpose of the credit derivatives is to provide additional yield on certain of the Company s underlying available-for-sale investments.

The Company is a party to three credit default contracts that have an aggregate notional amount of $75.0 million that expire on various dates through March 2008. The fixed yield earned on these contracts was not material at June 30, 2004 or December 31, 2003, and is included in interest income in the accompanying condensed consolidated statements of income. For the three and six months ended June 30, 2004, there was no change in fair value of these credit default contracts.

The Company has restricted approximately $80.3 million of investment securities as collateral for its credit default contracts and certain of its interest rate swaps, which are included in restricted cash equivalents and investments in the accompanying condensed consolidated balance sheet. The Company maintains the ability to manage the composition of the pledged investments within certain limits and to withdraw and use excess and investment earnings from restricted collateral are available for operating purposes. As of June 30, 2004, the Company had $5.4 million of derivative assets and $4.5 million of derivative liabilities, representing the fair values of the Company s outstanding derivative instruments, which are recorded in other current assets, other assets, accrued expenses and other liabilities in the accompanying condensed consolidated balance sheets. The change in derivatives recognized in other comprehensive income presented in the table below (in thousands) includes unrealized gains (losses) that arose from changes in market value of derivatives that were held during the period, and gains (losses) that were previously unrealized, but have been recognized in current period net income due to termination or maturities of derivative contracts. This reclassification has no effect on total comprehensive income or stockholders equity.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	**2003**	**2004**	**2003**
Unrealized gains (losses) on derivative instruments	**$ (2,171)**	$ 2,715	**$ (1,548)**	$ 3,958
Reclassification of realized gains	**(2,038)**	(1,423)	**(5,042)**	(2,416)
(Decrease) increase in net unrealized derivative gains recognized in other comprehensive income (loss) due to derivative instruments	**$ (4,209)**	$ 1,292	**$ (6,590)**	$ 1,542

9. Comprehensive Income

The components of comprehensive income, net of tax, are as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Net income	**$ 31,475**	$ 29,344	**$ 40,800**	$ 59,673
Other comprehensive income:				
Change in unrealized gain (loss) on available-for-sale securities	**(514)**	51	**(596)**	510
Change in unrealized gain (loss) on derivative instruments	**(4,209)**	1,292	**(6,590)**	1,542
Comprehensive income	**$ 26,752**	$ 30,687	**$ 33,614**	$ 61,725

The components of accumulated other comprehensive income, net of tax, are as follows (in thousands):

	June 30, 2004	December 31, 2003
Unrealized gain on available-for-sale securities	**$ 30**	$ 626
Unrealized gain on derivative instruments	**594**	7,184
Accumulated other comprehensive income	$ 624	$ 7,810

Table of Contents

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

10. Income Taxes

The Company maintains certain operational and administrative processes in overseas subsidiaries and its foreign earnings are taxed at lower foreign tax rates. The Company does not expect to remit earnings from its foreign subsidiaries. The Company s effective tax rate decreased to 21% for the six months ended June 30, 2004 compared to 22% for the same period in the prior year, primarily due to the effects of the redemption of the Company s convertible subordinated debentures and the impact of amortization of intangibles from the Expertcity acquisition.

11. Stock Repurchase Programs

The Company s board of directors has authorized an ongoing stock repurchase program with a total repurchase authority granted to the Company of $800 million, the objective of which is to manage actual and anticipated dilution. At June 30, 2004, approximately $120.7 million was available to repurchase common stock pursuant to the stock repurchase program. All shares repurchased are recorded as treasury stock.

The Company is authorized to make open market purchases of its common stock using general corporate funds. Additionally, from time to time, the Company has entered into structured stock repurchase arrangements with large financial institutions using general corporate funds as part of its stock repurchase program in order to lower the average cost to acquire shares. These programs include terms that require the Company to make up front payments to a counter-party financial institution and result in the receipt of stock during the period of the agreement or the receipt of either stock or cash at the maturity of the agreement. Delivery of stock under certain programs may be dependent on market conditions.

The Company expended $43.2 and $70.0 million during the first six months of 2004 and 2003, respectively, under stock repurchase transactions, net of all premiums received. During the six months ended June 30, 2004, the Company took delivery of a total of 1,059,813 shares of outstanding common stock with an average per share price of $20.59; and during the six months ended June 30, 2003, the Company took delivery of a total of 6,245,186 shares of outstanding common stock with an average per share price of $13.85. Some of these shares were received pursuant to prepaid programs that were initiated in prior periods. Since the inception of the stock repurchase programs, the average cost of shares acquired was $16.40 per share compared to an average close price during open trading windows of $19.62 per share.

12. Legal Proceedings

The Company is a defendant in various matters of litigation generally arising out of the normal course of business. Although it is difficult to predict the ultimate outcome of these cases, management believes, after discussions with counsel, that any ultimate liability would not materially affect the Company s financial position, result of operations or cash flows.

13. Commitments

The Company is party to a synthetic lease arrangement totaling approximately $61.0 million for its corporate headquarters office space in Fort Lauderdale, Florida. The synthetic lease represents a form of off-balance sheet financing under which an unrelated third party lessor funded 100% of the costs of acquiring the property and leases the asset to the Company. The synthetic lease qualifies as an operating lease for accounting purposes and as a financing lease for tax purposes. The Company does not include the property or the lease debt as an asset or a liability on its condensed consolidated balance sheet. Consequently, payments made pursuant to the lease are recorded as operating expenses in the Company s condensed consolidated statements of income. The Company entered into the synthetic lease in order to lease its headquarters properties under more favorable terms than under its previous lease arrangements.

The lease payments vary based on LIBOR plus a margin. If the Company chooses not to purchase the property at the end of the lease term, it has guaranteed a residual value to the lessor of approximately $51.9 million and possession of the buildings will be returned to the lessor. If the fair value of the building were to decline below $51.9 million, the Company would be responsible for the difference under its residual value guarantee, which could have a material adverse effect on the Company s results of operations and financial condition.

The synthetic lease includes certain financial covenants including a requirement for the Company to maintain a pledged balance of approximately $62.8 million in cash and/or investment securities as collateral, which is classified as restricted cash equivalents and investments in the accompanying condensed consolidated balance sheets. The Company maintains the ability to manage the composition of the restricted investments within certain limits and to withdraw and use excess investment earnings from the restricted collateral for operating purposes. Additionally, the Company must maintain a minimum cash and investment balance of $100.0 million, excluding the Company s collateralized investments and equity investments, as of the end of each fiscal quarter. As of June 30, 2004,

Table of Contents

Citrix Systems, Inc.

Notes to Condensed Consolidated Financial Statements (As restated)

(Unaudited)

June 30, 2004

the Company had approximately $278.3 million in cash and investments in excess of those required levels. The synthetic lease includes non-financial covenants including the maintenance of the properties and adequate insurance, prompt delivery of financial statements to the lender of the lessee and prompt payment of taxes associated with the properties. As of June 30, 2004, the Company was in compliance with all material provisions of the arrangement.

Table of Contents

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

Overview

We develop, market, license and support access infrastructure software and services that enable effective and efficient enterprise-wide deployment, management and access of applications and information, including those designed for Microsoft Windows operating systems, for UNIX operating systems, such as Sun Solaris, HP-UX or IBM-AIX, and for Web-based information systems, as well as Web-based desktop access. Our MetaFrame products permit organizations to provide access to Windows based, Web-based, and UNIX applications regardless of a user s location, network connection or type of client hardware platforms. We market and license our products primarily through multiple channels such as value-added resellers, channel distributors, system integrators and independent software vendors. We also promote our products through relationships with a wide variety of industry participants.

Acquisition

On February 27, 2004, we acquired all of the issued and outstanding capital stock of Expertcity.com, Inc., or Expertcity, a market leader in Web-based desktop access, as well as a leader in Web-based training and customer assistance products. The results of operations of Expertcity are included in our results of operations beginning after February 27, 2004 and are included in our segment, the Citrix Online Division.

The consideration for this transaction was $230.6 million, comprised of $112.6 million in cash and approximately 5.6 million shares of our common stock valued at $118.0 million. In addition to the purchase price, there were direct transaction costs associated with the merger of approximately $4.4 million. The merger agreement provides for additional purchase price consideration of up to approximately 0.6 million shares of our common stock to be issued to the Expertcity stockholders in the event certain revenue and other financial milestones are achieved by the Expertcity business in 2004. The fair value of the shares issued as additional purchase price consideration, if any, will be based on the market value of our common stock at the date that the shares are earned. Additional purchase price consideration, if any, is expected to be recorded as goodwill.

Under the purchase method of accounting, the total purchase price was allocated to Expertcity s net tangible and intangible assets based on their estimated fair values as of the date of the completion of the acquisition. Independent valuation specialists conducted a valuation in order to assist us in determining the fair values of a significant portion of Expertcity s net assets. We considered the work performed by the independent valuation specialists in our allocation of the purchase price summarized below (in thousands):

	Purchase Price Allocation	Asset Life
Current assets	$ 26,085	
Property and equipment	1,998	Various
In-process research and development	18,700	
Intangible assets	50,800	3-7 years
Goodwill	161,221	Indefinite

Assets acquired		258,804
Current liabilities		14,019
Deferred tax liability		9,796
Total liabilities assumed		23,815
Net assets acquired, including direct transaction costs	$	234,989

Current assets and liabilities acquired from Expertcity consisted mainly of cash and investments, accounts receivable, deferred revenues and other current liabilities.

Intangible assets are comprised primarily of core and product technology, trade names, covenants not to compete and customer relationships. The valuation of core and product technology was based on the estimated discounted future cash flows associated with Expertcity s existing products. The valuation of the trade names was determined based on assigning a royalty rate to the revenue stream that was expected from the services using the trade name. The pre-tax royalty rate was applied to the product revenue and discounted to a present value. The value of customer relationships was determined based on estimated future discounted cash flows of the relationships in place after considering historical attrition rates.

Table of Contents

We expensed purchased in process research and development of approximately $18.7 million immediately upon closing the merger. For more information regarding the in-process research and development acquired from Expertcity, see Management s Discussion and Analysis of Financial Condition and Results of Operations Results of Operations and note 4 to our condensed consolidated financial statements.

Revenue Recognition

The accounting related to revenue recognition in the software industry is complex and affected by interpretations of the rules and an understanding of industry practices, both of which are subject to change. As a result, revenue recognition accounting rules require us to make significant judgments. In addition, our judgment is required in assessing the probability of collection, which is generally based on evaluation of customer-specific information, historical collection experience and economic market conditions. If market conditions decline, or if the financial condition of distributors or customers deteriorates, we may be unable to determine that collectibility is probable, and we could be required to defer the recognition of revenue until we receive customer payment.

We sell most of our software products bundled with an initial subscription for software license updates that provide the end-user with free enhancements and upgrades to the licensed product on a when and if available basis. Customers may also elect to purchase technical support, product training or consulting services. We allocate revenue to software license updates and any other undelivered elements of the arrangement based on vendor specific objective evidence, or VSOE, of fair value of each element and such amounts are deferred until the applicable delivery criteria and other revenue recognition criteria described in note 2 to our condensed consolidated financial statements have been met. The balance of the revenue, net of any discounts inherent in the arrangement, is allocated to the delivered software product using the residual method and recognized at the outset of the arrangement as the software licenses are delivered. If we cannot objectively determine the fair value of each undelivered element based on VSOE, we defer revenue recognition until all elements are delivered, all services have been performed, or until fair value can be objectively determined. We must apply judgment in determining all elements of the arrangement and in determining the VSOE of fair value for each element, considering the price charged for each product or applicable renewal rates for software license updates.

In the normal course of business, we do not permit product returns, but we do provide most of our distributors and value added resellers with stock balancing and price protection rights. Stock balancing rights permit distributors to return products to us by the forty-fifth day of the fiscal quarter, subject to ordering an equal dollar amount of our other products prior to the last day of the same fiscal quarter. Price protection rights require that we grant retroactive price adjustments for inventories of our products held by distributors or resellers if we lower our prices for such products. We establish provisions for estimated returns for stock balancing and price protection rights, as well as other sales allowances, concurrently with the recognition of revenue. The provisions are established based upon consideration of a variety of factors, including, among other things, recent and historical return rates for specific products and distributors, estimated distributor inventory levels by product, the impact of any new product releases and projected economic conditions. Actual product returns for stock balancing and price protection provisions incurred are, however, dependent upon future events, including the amount of stock balancing activity by our distributors and the level of distributor inventories at the time of any price adjustments. We continually monitor the factors that influence the pricing of our products and distributor inventory levels and make adjustments to these provisions when we believe actual returns and other allowances could differ from established reserves. Our ability to recognize revenue upon shipment to our distributors is predicated on our ability to reliably estimate future stock balancing returns. If actual experience or changes in market condition impairs our ability to estimate returns, we would be required to defer the recognition of revenue until the delivery of the product to the end-user. Allowances for estimated product returns amounted to approximately $2.0 million at June 31, 2004 and $3.0 million at December 31, 2003. We have not reduced and have no current plans to reduce our prices for inventory currently held by distributors or resellers. Accordingly, there were no reserves required for price protection at June 30, 2004 or December 31, 2003. We record estimated reductions to revenue for customer programs and incentive offerings including volume-based incentives. If market conditions were to decline, we could take actions to increase our customer incentive offerings, which could result in an incremental reduction to our revenue at the time the incentive is offered.

Stock-Based Compensation Disclosures

Our stock-based compensation program is a broad based, long-term retention program that is intended to attract and reward talented employees and align stockholder and employee interest. The number and frequency of stock option grants are based on competitive practices, our operating results, the number of options available for grant under our approved shareholder plans and other factors. All employees are eligible to participate in the stock-based compensation program.

Table of Contents

Statement of Financial Accounting Standards, or SFAS, No. 123, *Accounting for Stock-Based Compensation*, as amended by SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure,* defines a fair value method of accounting for issuance of stock options and other equity instruments. Under the fair value method, compensation cost is measured at the grant date based on the fair value of the award and is recognized over the service period, which is usually the vesting period. Pursuant to SFAS No. 123, companies are not required to adopt the fair value method of accounting for employee stock-based transactions. Companies are permitted to account for such transactions under Accounting Principles Board, or APB, Opinion No. 25, *Accounting for Stock Issued to Employees*, but are required to disclose in a note to the consolidated financial statements pro forma net income and per share amounts as if a company had applied the methods prescribed by SFAS No. 123.

As of June 30, 2004, we had four stock-based compensation plans. We grant stock options for a fixed number of shares to employees and non-employee directors with an exercise price equal to or above the fair value of the shares at the date of grant. As discussed above and in note 2 to our condensed consolidated financial statements, we apply the intrinsic value method under APB Opinion No. 25 and related interpretations in accounting for its plans. Accordingly, no compensation cost has been recognized for our fixed stock plans and our stock purchase plan. However, the impact on our condensed consolidated financial statements from the use of options is reflected in the calculation of earnings per share in the form of dilution (see note 3 to our condensed consolidated financial statements).

The following table (in thousands, except option price) provides information as of June 30, 2004 about the securities authorized for issuance to our employees and non-employee directors under our fixed stock-based compensation plans, consisting of our Amended and Restated 1995 Stock Plan, the Second Amended and Restated 1995 Employee Stock Purchase Plan, the 1995 Non-Employee Director Option Plan and the Second Amended and Restated 2000 Director and Officer Stock Option and Incentive Plan:

Plan	(A) Number of securities to be issued upon exercise of outstanding options, warrants and rights	(B) Weighted-average exercise price of outstanding options, warrants and rights	(C) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (A))
Equity compensation plans approved by security holders	38,887	$ 24.57	43,932
Equity compensation plans not approved by security holders			
Total	38,887	24.57	43,932

The following table provides information about stock options granted for the six months ended June 30, 2004 and for the year ended December 31, 2003 for employees, non-employee directors and for certain executive officers. The stock option data for listed officers relates to our Named Executive Officers. The Named Executive Officers for the six months ended June 30, 2004 and the year ended December 31, 2003 consist of our chief executive officer and the four other most highly compensated executive officers who earned a total salary and bonus in excess of $100,000 in 2003, as reported in our Proxy Statement dated April 2, 2004 and who are current employees:

	Six Months Ended	Year Ended

	June 30, 2004	December 31, 2003
Net grants to all employees, non-employee directors and executive officers as a percent of outstanding shares (1) (2)	1.26 %	1.03 %
Grants to Named Executive Officers as a percent of outstanding shares (2)	0.06 %	0.24 %
Grants to Named Executive Officers as a percent of total options granted	3.36 %	6.89 %
Cumulative options held by Named Executive Officers as a percent of total options outstanding (3)	9.50 %	10.08 %

(1) Net grants represent total options granted during the period net of options forfeited during the period.
(2) Calculation is based on outstanding shares of common stock as of the beginning of the respective period.
(3) Calculation is based on total options outstanding as of the end of the respective period.

Table of Contents

The following table presents our option activity from December 31, 2002 through June 30, 2004 (in thousands, except weighted-average exercise price). Some amounts may not add due to rounding.

	Options Available for Grant	Options Outstanding: Number of Shares	Options Outstanding: Weighted Average Exercise Price
Balance at December 31, 2002	30,001	41,221	$ 24.51
Granted at market value	(5,575)	5,575	16.19
Granted above market value	(349)	349	12.00
Exercised		(4,723)	11.64
Forfeited/cancelled	4,199	(4,199)	28.14
Reduction in plan shares [(1)]	(500)	N/A	N/A
Additional shares reserved	9,249	N/A	N/A
Balance at December 31, 2003	37,025	38,222	24.56
Granted at market value	(3,198)	3,198	21.13
Exercised		(1,474)	11.95
Forfeited/cancelled	1,059	(1,059)	26.12
Additional shares reserved	9,046	N/A	N/A
Balance at June 30, 2004	43,932	38,887	24.57

(1) The number of shares reserved for issuance under our Amended and Restated 2000 Director and Officer Stock Option and Incentive Plan was reduced by 500,000 shares pursuant to an amendment to such option plan authorized by our Board of Directors on May 15, 2003.

A summary of our in-the-money and out-of-the-money option information as of June 30, 2004 is as follows (in thousands, except weighted average exercise price):

	Exercisable		Unexercisable		Total	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
In-the-money	10,865	$ 13.89	7,626	$ 12.56	18,491	$ 13.34
Out-of-the-money [(1)]	15,453	53.72	4,943	52.44	20,396	34.75
Total options outstanding	26,318	37.28	12,569	28.24	38,887	24.57

(1) Out-of-the-money options are those options with an exercise price equal to or above the closing price of $20.36 per share for our common stock at June 30, 2004.

The following table provides information with regard to our stock option grants during the six months ended June 30, 2004 to the Named Executive Officers:

	Individual Grants [1]		
	Number of Securities Underlying Options Grant (#)	Exercise Price ($/share)	Expiration Date
Mark Templeton	37,500	$ 22.47	April 12, 2009
John Burris	25,000	$ 22.47	April 12, 2009
David Henshall	17,500	$ 22.47	April 12, 2009
Robert Kruger	15,000	$ 22.47	April 12, 2009
Stefan Sjostrom	12,500	$ 22.47	April 12, 2009

(1) These options vest over four years at a rate of 25% of the shares underlying the option one year from the date of the grant and at a rate of 2.08% monthly thereafter.

The following table presents certain information regarding option exercises and outstanding options held by Named Executive Officers as of and for the six months ended June 30, 2004:

	Shares Acquired on Exercise (#)	Value Realized ($)[1]	Number of Securities Underlying Unexercised Options at June 30, 2004 Exercisable/Unexercisable	Values of Unexercised In-the-Money Options at June 30, 2004 ($) Exercisable/Unexercisable [2]
Mark Templeton			1,957,500 /207,500	$4,268,052 / $1,024,823
John Burris			437,716 / 123,034	$676,720 / $668,053
Robert Kruger	6,500	$ 95,060	256,045 / 157,047	$325,459 / $648,791
David Henshall			58,333 / 159,167	$349,998 / $850,002
Stefan Sjostrom			216,381 / 123,369	$405,494 / $517,017

(1) Amounts disclosed in this column were calculated based on the difference between the fair market value of our common stock on the date of exercise and the exercise price of the options in accordance with regulations promulgated under the Securities and Exchange Act of 1934, as amended (the Exchange Act), and do not reflect amounts actually received by the named officers.

(2) Value is based on the difference between the option exercise price and the fair market value at June 30, 2004 ($20.36 per share), multiplied by the number of shares underlying the option.

Table of Contents

For further information regarding our stock-based compensations plans, see note 2 to our condensed consolidated financial statements.

Critical Accounting Policies and Estimates

Our discussion and analysis of financial condition and results of operations are based upon our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent liabilities. We base these estimates on our historical experience and on various other assumptions that we believe to be reasonable under the circumstances, and these estimates form the basis for our judgments concerning the carrying values of assets and liabilities that are not readily apparent from other sources. We periodically evaluate these estimates and judgments based on available information and experience. Actual results could differ from our estimates under different assumptions and conditions. If actual results significantly differ from our estimates, our financial condition and results of operations could be materially impacted. Please refer to Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies and Estimates included in our Annual Report on Form 10-K for the year ended December 31, 2003, as amended, for further information regarding our critical accounting policies and estimates.

The notes to our consolidated financial statements and Management s Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended December 31, 2003, as amended, the unaudited interim condensed consolidated financial statements and the related notes to the unaudited interim condensed consolidated financial statements included in Item 1 of this Quarterly Report on Form 10-Q/A and the factors and events described elsewhere in Management s Discussion and Analysis of Financial Condition and Results of Operations, including in Certain Factors Which May Affect Future Results, contain additional information related to our accounting policies and should be read in conjunction with the following discussion and analysis relating to the individual financial statement captions and our overall financial performance, operations and financial position.

Results of Operations

The following table sets forth our condensed consolidated statements of income data and presentation of that data as a percentage of change from period-to-period (in thousands).

	Three Months Ended June 30,	Six	Increase/(decrease) for the