OPNET TECHNOLOGIES INC
Form 10-K
June 04, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended March 31, 2010

OR

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

Commission file number: 000-30931

OPNET TECHNOLOGIES, INC.

(Exact name of registrant as specified in its charter)

DELAWARE	**52-1483235**
(State or other jurisdiction of	**(I.R.S. Employer**
Incorporation or organization)	**Identification No.)**

7255 Woodmont Avenue, Bethesda, Maryland 20814-7900

(Address of principal executive offices) (Zip Code)

Registrant s telephone number, including area code: (240) 497-3000

Securities registered pursuant to Section 12(b) of the Act: Common Stock, $0.001 par value

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES ¨ NO x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES ¨ NO x

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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

Large accelerated filer ¨	Accelerated filer x	Non-accelerated filer ¨	Smaller reporting company ¨

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES ¨ NO ¨

The aggregate market value of the voting stock held by non-affiliates of the registrant, computed using the closing sale price of the registrant s Common Stock on September 30, 2009, as reported on the NASDAQ Global Select Market, was approximately $115,925,897. Shares of Common Stock held by each officer and director and by each person who owns 5% or more of the outstanding Common Stock have been excluded because such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily conclusive for other purposes.

The number of shares of the registrant s Common Stock outstanding on June 1, 2010 was 21,099,864.

DOCUMENTS INCORPORATED BY REFERENCE

Certain portions of the registrant s definitive Proxy Statement for the 2010 Annual Meeting of Stockholders are incorporated by reference into Part III of this Form 10-K.

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OPNET TECHNOLOGIES, INC.

ANNUAL REPORT ON FORM 10-K FOR THE FISCAL YEAR ENDED MARCH 31, 2010

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PART I

Forward Looking Information

This Annual Report contains forward-looking statements that involve substantial risks and uncertainties. You can identify these statements by forward-looking words such as anticipate, believe, could, estimate, expect, intend, may, plan, potential, should, and would should read statements that contain these words carefully because they discuss our future expectations, contain projections of our future results of operations or of our financial position, or state other forward-looking information. We believe that it is important to communicate our future expectations to our investors. However, there may be events in the future that we are not able to predict accurately or control. The factors listed in this Annual Report on Form 10-K under Risk Factors, as well as any cautionary language in this Annual Report on Form 10-K, provide examples of risks, uncertainties, and events that may cause our actual results to differ materially from the expectations we describe in our forward-looking statements. You should also carefully review the risks outlined in other documents that we file from time to time with the Securities and Exchange Commission, including our Quarterly Reports on Form 10-Q that we will file in fiscal 2011.

The forward-looking statements provided in this Annual Report on Form 10-K represent our expectations as of June 4, 2010. We anticipate that subsequent events and developments may cause our expectations to change. However, while we may elect to update this forward-looking information at some point in the future, we specifically disclaim any obligation to do so. This forward-looking information should not be relied upon as representing our expectations as of any date subsequent to June 4, 2010.

Fiscal Year Convention

The years ended March 31, 2010, 2009, and 2008, are referred to as fiscal 2010, fiscal 2009, and fiscal 2008, respectively, in this Annual Report on Form 10-K.

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ITEM 1. BUSINESS

In this Annual Report on Form 10-K, or Annual Report, the Company we, us, and our refer to OPNET Technologies, Inc. and its wholly- owned and wholly-controlled subsidiaries unless the context otherwise indicates.

OPNET Technologies, Inc. is a provider of software products and related services for managing applications and networks. Our software products address application performance management, network planning, engineering and operations, and network research and development. Our customers include corporate enterprises, government and defense agencies, network service providers, and network equipment manufacturers. Our software products and related services are designed to help our customers make better use of resources, reduce operational problems, and improve competitiveness.

OPNET differentiates itself from traditional providers of application and network management products by focusing on analytics and producing actionable results. Traditional application and network management products focus on data collection and monitoring. These systems typically report on historical trends and the status of networks and systems. They are limited by their lack of understanding of the underlying technologies that support applications, and the relationships among these technologies. While they provide useful information, they do not automate the next important step, which is analyzing collected data to transform it into actionable information. OPNET s analysis capabilities drive the rapid resolution of performance problems, and also proactively prevent problems from occurring. These problems include, for example, poorly designed applications, network configuration errors, network congestion, poor interaction between the network and applications, inefficient use of the network by applications, application bugs, and database inefficiencies. We believe that OPNET s analytics and real-time performance monitoring can significantly improve the performance and availability of mission-critical applications and networks.

Embedded in OPNET software is expert knowledge about how application components, network devices, network protocols, and servers operate and interact. This intelligence enables users in application development, data center management, and network operations, engineering, planning, and security functions to be more effective in optimizing performance and availability of their applications and infrastructure. We believe our software products appeal to a broad customer base, including corporate enterprises, government and defense agencies, network service providers, and network equipment manufacturers, empowering them to make better use of resources, rapidly troubleshoot operational problems, and improve competitiveness.

We market focused software products for each of our target markets. We sell our products to both Fortune 1000 and mid-size companies. Some examples of our customers include:

- corporate enterprises, such as Autodesk, BNP Paribas, Cardinal Health, Embraer, GEICO Insurance, GlaxoSmithKline, GoDaddy.Com, The Hershey Company, IBM Global Services, Lowe s, Medtronic, Moody s, Universal Music Group, Saudi Aramco, and VeriSign;

- government agencies, such as the Federal Bureau of Investigations, the Federal Communications Commission, the Internal Revenue Service, the United States Department of Defense, the United States Department of Homeland Security, and the United States Government Accountability Office;

- service providers, such as Asia Pacific Telecom Group, British Telecom, France Telecom, Cox Communications, NTT, Telus, and WilTel; and

- network equipment manufacturers, such as Cisco Systems, Ericsson, Research in Motion, and Samsung.

Industry Background

Growth and Increased Complexity of Networks and Dependence on Applications

Organizations rely on enterprise software applications and networks to successfully execute their strategies. The increasing use of applications, such as enterprise resource planning, business intelligence, corporate

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intranets, e-mail, web meetings, virtualization, portals, web services, voice over IP, wireless, and streaming multimedia has resulted in significant growth in underlying network and application infrastructures. In addition, the proliferation and widespread adoption of the Internet and web services architectures have expanded the role of networks beyond organizational boundaries.

Enterprises and service providers must now manage the convergence of voice, data, and video traffic over traditional, wireless, and optical architectures by integrating numerous existing and emerging technologies. The complexity is exacerbated by the current corporate regulatory environment, which requires improved management processes and documentation. As a result of these factors, businesses and government entities are forced to confront significant challenges related to the cost, risk, and performance of information technology, or IT.

IT infrastructures are sophisticated, dynamic systems that evolve on a daily basis. Applications are typically distributed across many clients, servers, and network segments. New and enhanced business applications are regularly being deployed and re-deployed. The geographic distribution of users relative to IT services shifts due to the consolidation of organizations and resources. Traffic levels exhibit steady growth, necessitating constant evaluation of and improvements to the underlying network infrastructure in order to maintain business and application performance. However, due to the dependencies among network, server, and application configurations, it is very difficult for IT professionals to identify the true root cause of performance problems when they occur. The data required to diagnose problems is often difficult to obtain, and processes for analyzing this data are often manual and time consuming, requiring significant experience and expertise. When an end-user experiences performance problems with an important business application, the challenge facing a typical IT manager is to determine: whether there is enough bandwidth available; whether the database server has enough capacity; whether network routing protocols are tuned properly; whether protocols on the client and server are likewise tuned properly; and whether the application was designed and implemented efficiently with end-user performance in mind.

Without a clear understanding of the source of problems and the specific changes required to solve them, IT managers resort to uninformed decision-making that often results in wasteful spending on unnecessary and ineffective server and network upgrades. IT professionals need software products that enable them to focus their time and resources in the right places when problems occur in distributed enterprise applications, and to maximize the use of existing infrastructure. Further, since modifications to infrastructure have the potential to cause service level degradation or even network failures, there is a growing need to plan and implement network changes in a controlled manner, taking into account the potential consequences of each action.

Market Opportunity for OPNET Software Products

Organizations need application and network management software products that possess the analytics required to overcome the limitations of traditional tools for rapidly detecting and resolving complex problems and proactively preventing problems from occurring. OPNET software products are focused on these areas. Our software products have embedded knowledge and operational understanding of applications, networks, and systems for quickly troubleshooting problems and automatically predicting the impact of changes. We believe business executives and IT professionals require software products like ours to:

- ensure fast response times for mission critical applications, including customer-facing web-based applications;
- reduce down time of mission critical applications;
- reduce operating and capital costs;
- increase business productivity; and
- manage risk, enabling faster deployment of critical, IT-dependent strategic business initiatives.

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We believe the value proposition from OPNET software products apply to a broad range of potential customers including:

- large and medium-sized enterprises that rely on IT to conduct business;
- government/defense agencies;
- service providers, including telecommunications carriers, internet service providers, or ISPs, and managed service providers, or MSPs; and
- network equipment manufacturers.

Enterprises require analytics for more effectively identifying the root causes of application performance problems, ensuring the successful deployment of new applications, auditing device configurations for security and policy compliance, validating changes, and performing critical operational and strategic planning functions.

Government and defense agencies have needs similar to those of enterprises, service providers, and network equipment manufacturers. These agencies also sometimes require specialized services to support large projects that incorporate OPNET s technology. United States government customers, including the Department of Defense, utilize our software and professional services to take advantage of our extensive expertise and intellectual property in applications, networking, and protocols. For the Department of Defense, our software products and related services are used for both application and network performance management, as well as for analyzing and developing communications technologies for network-centric transformational programs. Our ability to model and simulate end-to-end application and network performance is valuable in determining the impact of tactical or strategic changes to networks, planning for contingencies, and evaluating the impact of new network technologies and protocols. In addition, our software products are scalable and address large, complex military systems and networks, such as mobile networks, with a variety of operationally proven, advanced predictive performance techniques.

Service providers require analytics for optimizing their investments in network infrastructure, more effectively troubleshooting network issues, ensuring network configuration integrity and security, planning for services based on new technologies including wireless and optical, and making better use of network resources to increase competitiveness.

Network equipment manufacturers require advanced modeling and simulation software products for accelerating network research and development, reducing time-to-market for new technologies, developing custom network design and analysis software, and for reducing sales cycles for sophisticated technology products.

OPNET Software Products

Our software products use a variety of advanced technologies to support the analysis of application, network, and server performance under a wide range of current and future operating conditions. Many OPNET software products share a significant amount of core software based on an open architecture. Our software architecture enables us to create new software more efficiently, to foster interoperability of our software products, and to provide interfaces to a wide range of external data sources including third party management tools and network topology, traffic, and configuration information. We also deliver extensive cross-product integration, to enable our users to realize added value when products are deployed together.

The following sections summarize the OPNET software product portfolio by target market:

Primary Target Market: Enterprise IT (Corporate and Government/Defense)

- *ACE Analyst*, first introduced in May 2000 as ACE, enables application performance management through advanced analytics. ACE Analyst is used to troubleshoot performance problems in production applications and to enable successful application deployment during quality assurance.

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ACE Live was introduced in November 2007 following OPNET s acquisition of specified assets from Network Physics. ACE Live performs real-time end user experience monitoring, leveraging on-board analytics to quickly determine the root source of application performance problems. ACE Live is a hardware appliance, and can also be deployed as a software solution on an existing PC or server for accelerating application traffic over a wide area network.

IT Guru Network Planner was first introduced in August 1998 as IT Guru. It provides predictive network capacity planning and design optimization, as well as validation of network configuration changes.

IT Guru Systems Planner was introduced in December 2006 as an option for IT Guru. It provides capacity planning for servers, including planning for migration from physical-to-virtual server environments.

nCompass for Enterprises was first introduced in September 2003 as NETCOP. It provides enterprises with centralized, real-time visibility of network topology, traffic, and status in a single, integrated view. nCompass for Enterprises provides a unified view to quickly recognize the impact of network events, and assisted troubleshooting to rapidly resolve problems.

IT Sentinel was first introduced in August 2004. IT Sentinel provides automatic and continuous network configuration integrity and security auditing, and proactive change validation.

OPNET Panorama was first introduced in December 2004 following OPNET s acquisition of Altaworks Corporation. Panorama provides real-time system analytics for application performance management. Like ACE Analyst, it is used throughout the application life cycle to ensure the successful deployment of applications, and rapidly troubleshoot performance problems in production applications. With Panorama focusing on advanced application analysis from the server perspective, and ACE Analyst s network perspective, we believe that we are well positioned to address the complex issues that our clients may face as they migrate to web services architectures.

VNE Server was first introduced in June 2002. VNE Server, or Virtual Network Environment Server automatically maintains a detailed, near real-time data model of the production IT network. VNE Server includes a suite of adapters that obtain topology, traffic, and other information from network devices as well as a broad range of third party data sources. VNE Server automates the data collection process for other OPNET products, including IT Guru Network Planner and SP Guru Network Planner. VNE Server capabilities are included in IT Sentinel and SP Sentinel.

Primary Target Market: Network Service Providers (both Commercial and Government/Defense)

SP Guru Network Planner was first introduced in June 2001. SP Guru Network Planner is built on the IT Guru Network Planner product, and contains analytics that are valuable to service providers for planning, network design optimization, and validation of configuration changes. SP Guru Network Planner includes modeling and analysis technologies for IP, MPLS, and ATM networks, and when combined with SP Guru Transport Planner, provides a single environment for network-level and optical transport-level analysis.

SP Guru Transport Planner, formerly WDM Guru*,* was first introduced in December 2001. SP Guru Transport Planner is an optical network-planning product for designing resilient, cost-efficient optical networks. SP Guru Transport Planner is also sold to network equipment manufacturers.

nCompass for Service Providers was first introduced in September 2003 as NETCOP. nCompass for Service Providers provides centralized, real-time visibility of network topology, traffic, and status in a single, integrated view. nCompass for Service Providers provides a unified view to quickly recognize the impact of network events, and assisted troubleshooting to rapidly resolve problems.

SP Sentinel was first introduced in August 2004. SP Sentinel provides automated and continuous network configuration integrity and security auditing for service providers, and proactive change validation.

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ACE Live is used by service providers who deliver managed network and data center services to enterprises to ensure application performance.

Primary Target Market: Network R&D Organizations (Defense and Equipment Manufacturers)

OPNET Modeler was OPNET s first product, introduced in 1987. OPNET Modeler is a network modeling and simulation product. It enables users to evaluate how networking equipment, communications technologies, systems, and protocols will perform under simulated network conditions.

Modeler Wireless Suite is based on OPNET Modeler, and incorporates additional functionality germane to wireless network R&D organizations.

Modeler Wireless Suite for Defense is based on OPNET Modeler, and incorporates additional functionality that supports unique network R&D undertaken by the defense community.

OPNET Modules

We develop and sell a variety of software modules that provide additional functions to our application and network management software products.

OPNET Model Libraries

The model libraries are used by OPNET software to simulate and analyze major networking technologies and communication protocols. These libraries provide the building blocks used to generate models of networks. A network model consists of software objects that correspond to the devices, computers, and links that constitute the actual network of interest. The behavior of these objects is controlled by models of devices, computers, applications, communication protocols, and links. *IT Guru Network Planner, IT Guru Systems Planner, IT Netcop, IT Sentinel, SP Guru Network Planner, SP Netcop, SP Sentinel,* and *OPNET Modeler* include extensive libraries of popular and emerging networking technologies and communication protocols, such as TCP/IP, hypertext transfer protocol, or HTTP, open shortest path first routing, or OSPF, asynchronous transfer mode, or ATM, frame relay, IP-QoS, 802.11, or Wi-Fi, and 802.16, or WiMAX. Some of our model libraries are included in our base products and others are available for an additional fee as modules.

Our product agreements provide our customers with perpetual and term licenses for use by a specified number of concurrent users or for use by an unlimited number of concurrent users.

Customers

For fiscal 2010, 2009, and 2008 we generated 22.5%, 21.1%, and 20.2%, respectively, of our total revenue from customers located outside the United States. No single customer accounted for 10% or more of revenue for fiscal 2010, 2009 or 2008. Note 15 to our consolidated financial statements presents information regarding revenue generated in the United States and internationally.

We derive a substantial portion of our revenue from sales directly or indirectly to United States government agencies. For fiscal 2010, 2009 and 2008, revenue from transactions with United States government agencies was approximately 39.9%, 35.3%, and 40.7%, respectively, of our total revenue. Government sales are subject to a variety of risks, including appropriation of funds by the United States Congress, termination for convenience, contract renegotiations/extensions and a decline in government spending.

Sales and Marketing

We sell our software products and related services through our direct sales force, our international subsidiaries, third-party distributors, and a number of original equipment manufacturers, or OEMs, and value- added resellers, or VARs. To date, OEMs and VARs have not accounted for more than 10% of our revenue. In

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North America, our direct sales force accounts for the majority of our sales. As of March 31, 2010, our sales and marketing teams consisted of 189 employees, including 98 quota-carrying and inside salespersons located in our headquarters in Bethesda, Maryland and our domestic offices in Cary, North Carolina; Dallas, Texas; Nashua, New Hampshire; and Santa Clara, California; our overseas subsidiaries in Paris, France; Slough, United Kingdom; Mainz, Germany; Ghent, Belgium; and Singapore; and our branch office in Beijing, China.

Our international sales activities are also supported by 69 VARs that offer our products in Australia, Austria, Brazil, Finland, France, Germany, Greece, India, Indonesia, Israel, Japan, Netherlands, New Zealand, Norway, Poland, Romania, Russia, South Africa, South Korea, Spain, Sweden, Switzerland, Turkey and the United Kingdom. Our marketing division works internally with our engineering and sales teams to develop customer value propositions and product messages, and externally with various third parties to develop brand awareness and leads for sales. Our external marketing activities are aimed at existing customers, new customer prospects, the media, and industry analysts. These include:

- participation in industry tradeshows;
- technology seminars and user group meetings;
- advertisements in trade journals and online;
- direct mailings;
- product collateral development and maintaining OPNET s website;
- free software for academic use at universities;
- specialized product sales support;
- specialized sales support with OPNET resellers;
- briefings with industry analysts; and
- a variety of public relations activities.

For twelve of the past thirteen years, we have sponsored OPNETWORK, an international technology conference convened in Washington, D.C. that focuses on application and network management for professionals in all areas of networking and information technology. OPNETWORK 2008, which was held in August 2008, included approximately 775 hours of classes, labs, and panels led by OPNET employees and outside experts. Not including OPNET employees, more than 1,672 IT and engineering professionals, representing 30 countries, participated in the conference. We did not hold the event in 2009 due to travel restrictions imposed on many of our users in response to the economic climate. We intend to hold OPNETWORK again in August 2010.

Service and Support

Our service and support offerings include:

consulting services;

product updates, technical support and services, which includes product updates, training for customers with current maintenance agreements, and technical support by telephone, e-mail or fax, all except technical support provided on a when-and-if-available basis under our maintenance agreement; and

training for customers without current maintenance agreements, which includes courses that enable our customers to more effectively use our products.

We offer consulting services to assist our clients, facilitate the adoption of our software products, and to provide installation services for our product offerings. Installation services are performed by our consulting staff, which consists of software development engineers, quality assurance engineers, technical documentation specialists, and project managers. Some customers also choose to engage our consulting services for

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troubleshooting application performance problems, network planning, network design, communication protocol design and customization services. As of March 31, 2010, our consulting staff consisted of 98 employees.

Our customers may purchase product updates, technical support and services, all of which except technical support are provided on a when-and-if available basis under our maintenance agreement. Payments for product updates, technical support and services whether on initial order or on renewal, are generally made in advance and are nonrefundable.

Product updates consist of the right to unspecified software updates on a when-and-if-available basis and customers typically purchase this right in connection with the initial product purchase. Product updates, technical support and services may be renewed upon expiration of each contract term purchased, which is generally one year. Customers can purchase product updates separately from technical support and services. Customers purchasing technical support are still required to purchase periodic unspecified product updates.

We provide customer support from our support center at our headquarters in Bethesda, Maryland, as well as from support staff in France, the United Kingdom and Singapore. We have designed and implemented a comprehensive information system to ensure that customer inquiries are addressed promptly, tracked until fully resolved, and recorded for future reference. Reports on the overall responsiveness of the technical support infrastructure, and the status of pending customer inquiries, are provided regularly to our technical support staff, technical support management, and executive management.

We have a core team of 13 technical support staff supplemented by a number of product developers and consultants who perform technical support on a rotational basis. We believe this staffing approach maximizes the access customers have to the best available product expertise, while providing product developers with direct customer feedback, which in turn helps us improve our software products.

We regularly offer training courses to our customers to assist them in maximizing the benefit they receive from using our products. Our training classes cover a broad range of topics. Training classes are offered at our headquarters in Bethesda, Maryland, our facilities in Santa Clara, California; Cary, North Carolina; Paris, France; and Slough, United Kingdom; and at our customers locations under separate contracts. As of March 31, 2010, our full-time training staff consisted of 5 employees.

Research and Development

We believe that our ability to enhance our current software products and create new software products in response to the needs of our customer base is an important factor for our future success. Accordingly, we intend to continue to commit significant resources to product research and development. We expect to accomplish a large part of our software product improvements and new software product development through internal development efforts. New capabilities may also be integrated into our product lines through the acquisition of technologies or businesses, or the licensing of externally developed technologies.

Our total research and development expense for fiscal 2010, 2009, and 2008 were approximately $32.0 million, $30.8 million, and $27.5 million, respectively. Our research and development efforts to date have been conducted at our offices in Bethesda, Maryland; Cary, North Carolina; Nashua, New Hampshire; Santa Clara, California: and Ghent, Belgium. All related costs have been expensed as incurred. As of March 31, 2010, our research and development staff consisted of 205 engineers and technical professionals.

Our research and development efforts are directed at increasing our revenue by expanding the scope of our software products and service offerings to address additional customer requirements. Our existing customers provide a meaningful source of information regarding customer requirements, which we use in order to guide our future research and development activities. In addition, we invest in third-party research and analysis of trends in our industry and our product markets in an effort to proactively reflect these trends in our future software products.

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Competition

The market for our software products and related services is evolving rapidly and is highly competitive. We believe that this market is likely to become more competitive as the demand for intelligent application and network management software products continues to increase. Although we believe that none of our competitors offer software products that are identical to ours, we are subject to current and potential competition from:

- software and hardware vendors with application and network performance management offerings, such as Computer Associates, Hewlett-Packard, Compuware Corporation, IBM Tivoli, NetScout Systems, and Quest Software;
- consultants who offer advisory services related to application and network performance management; and
- customers who develop their own application and network management capabilities, either internally or through outsourcing.

Also, it is possible that other vendors as well as some of our customers or distributors may develop and market competitive products in the future. Many of our current and potential competitors are larger and have substantially greater financial and technical resources than we do. We believe the principal competitive factors affecting the market for our software products and related services are the following:

- scope, quality, and cost-effectiveness of application and network management software products;
- industry knowledge and expertise embedded in the software;
- the interoperability of software products with existing network management software products;
- product performance, accuracy, technical features, ease of use, and price;
- customer service and support;
- consultants who offer advisory services related to application and network performance management; and
- customers who develop their own application and network management capabilities, either internally or through outsourcing.

Intellectual Property

We rely on a combination of copyright, trademark, patent, and trade secret laws, confidentiality agreements, and contractual provisions to protect our intellectual property. However, we believe that these laws and agreements afford us only limited protection. Despite our efforts to protect and oversee our intellectual property rights, there may be unauthorized parties who encroach upon our proprietary rights. In addition, the laws of some foreign countries do not provide as much protection of our proprietary rights as do the laws of the United States.

We currently hold registered trademarks in the United States for all of our primary marks, including OPNET, OPNETWORK, IT Guru, IT Sentinel, Netbiz, NetMapper, OPNET Modeler, SP Guru, SP Sentinel, VNE Server, WDM Guru, OPNET LoadScaler, OPNET TestCreator, OPNET Panorama, and OPNET nCompass. We have pending applications in the United States for the trademark registrations of Ace Live Insights, Know Your Network, Service Insight and NetOne. We also hold additional registered and unregistered trademarks in the United States and have additional pending applications. We intend to maintain our trademark portfolio commensurate with the continued use of these marks, especially our house mark OPNET. We have applied for and obtained numerous registrations for our marks in foreign countries. For the term OPNET, we hold registrations in the following countries: Benelux, France, Germany, Japan, the Peoples Republic of China, Taiwan, Spain and the United Kingdom and have additional applications pending in Italy and Spain. Other trademarks or service marks appearing in this Annual Report on Form 10-K are the property of their respective holders.

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In addition, we have 32 patents granted by the United States Patent and Trademark Office. Our patents will expire between 2018 and 2028. We also have 69 pending United States patent applications that, if granted, would expire approximately 20 years from their respective filing dates. Four of these are provisional patent applications for which we expect to pursue non-provisional applications within the next year. With regard to foreign patent protection, we have one patent granted by the European Patent Office and five pending European patent applications. Additionally, we plan on pursuing three more European patent applications within the next year. We believe that, because of the rapid pace of change in our industry, intellectual property protection for our products and the knowledge, abilities, and experience of our employees will be significant factors for our future success.

Executive Officers and Directors of the Registrant

Our executive officers and directors, and their ages as of June 4, 2010, are as follows:

Name	Age	Position
Marc A. Cohen	46	Chairman of the Board and Chief Executive Officer
Alain J. Cohen	43	President, Chief Technology Officer and Director
Mel F. Wesley	38	Vice President and Chief Financial Officer

Set forth below is information regarding the professional experience for each of our executive officers and directors. These executive officers and directors were elected to serve until their successors have been elected. Marc A. Cohen and Alain J. Cohen are brothers. There is no other family relationship between any of our other executive officers or between any of these officers and any of our directors.

Marc A. Cohen, one of our founders, has served as our Chairman of the Board since our inception in 1986 and as our Chief Executive Officer since 1994. From 1986 to 1992, Mr. Cohen was also a consultant with Booz Allen Hamilton Inc., or Booz Allen, an international management and consulting company. Mr. Cohen received a bachelor s degree in engineering science from Harvard University and a master s degree in electrical engineering from Stanford University. Mr. Cohen also serves as a Trustee and as a member of the Board of Directors of the Dana-Farber Cancer Institute in Boston, Massachusetts.

Alain J. Cohen, one of our founders, has served as our President and Chief Technology Officer and as a member of our Board of Directors since our inception in 1986. Mr. Cohen received a bachelor s degree in electrical engineering from the Massachusetts Institute of Technology, or M.I.T.

Mel F. Wesley has served as our Vice President and Chief Financial Officer since July 2005. Mr. Wesley served as our Acting Chief Financial Officer from December 2004 to July 2005 and our Corporate Controller from June to December 2004. From August 2003 to June 2004, Mr. Wesley served as Corporate Controller for SteelCloud, Inc., a publicly traded corporation that provides design, development and manufacturing of network appliances and infrastructure server products. From October 2000 to August 2003, Mr. Wesley served as an Assistant Controller for Learning Tree International, Inc., a publicly traded corporation that provides training to information technology professionals and managers.

Employees

As of March 31, 2010, we had 579 full-time employees, 528 of whom were located in the United States. The 579 full-time employees included 189 in sales and marketing, 124 in professional services and support, 205 in engineering, research and development, and 61 in general and administrative functions. Our employees are not represented by a collective bargaining agreement and we consider our relations with our employees to be good.

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Corporate Information

We are a Delaware corporation that was incorporated in November 1988, our principal executive office is located at 7255 Woodmont Avenue, Bethesda, Maryland 20814-7900 and our telephone number is (240) 497-3000. Our website address is www.opnet.com. The information on our website is not incorporated by reference into this Annual Report on Form 10-K and should not be considered to be a part of this Annual Report on Form 10-K. Our website address is included in this Annual Report on Form 10-K as an inactive textual reference only.

Availability of SEC Reports

Our website address is www.opnet.com. We make available free of charge on our website our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, and amendments to these reports, as soon as reasonably practicable after we electronically file such material with, or furnish such material to, the Securities and Exchange Commission, or SEC.

We file our reports with the SEC electronically via the SEC s Electronic Data Gathering, Analysis and Retrieval system, or EDGAR. The SEC maintains a website that contains reports, proxy and information statements, and other information regarding companies that file electronically with the SEC via EDGAR. The address of this website is www.sec.gov.

Any reports, statements or other information that we file with the SEC may be read or copied at the SEC s Public Reference Room at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Copies of these documents can be requested upon payment of a duplicating fee, by writing to the SEC. Please call the SEC at 1 (800) SEC-0300 for further information on the operation of the Public Reference Room. Upon request, we make available free of charge, electronic or paper copies of any reports, statements or other information that we file with the SEC.

Code of Business Conduct and Ethics

On May 4, 2004 we adopted a code of business conduct and ethics for all directors, officers, and employees pursuant to Section 406 of the Sarbanes-Oxley Act of 2002. The Code of Business Conduct and Ethics is available on our website at www.opnet.com. Suspected violations of this Code may be reported on a confidential or anonymous basis by facsimile or by e-mail to our General Counsel and to the Chairman of the Audit Committee of the Board of Directors. We intend to disclose any amendment to, and any waiver from, any provision of this Code that applies to any director, the Chief Executive Officer, Chief Financial Officer, or any other executive officer and that relates to any element of this Code enumerated in Item 406(b) of Regulation S-K, on Form 8-K.

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ITEM 1A. RISK FACTORS

The following important factors, among others, could cause actual results to differ materially from those indicated by forward-looking statements made in this Annual Report and presented elsewhere by management from time to time. You should consider carefully the following information before making an investment in our securities.

General instability in the economy, including concerns regarding the after-effects of the global recession, or unfavorable economic conditions in a particular region, business or industry sector, may cause our customers to postpone or forego technology investments and could have other impacts, any of which could hurt our business, financial results and cash flow.

Our products are designed to enhance our customers ability to manage their applications and networks. However, general instability in the economy, including concerns regarding the after-effects of the global recession, or a general slowdown in the global economy, or in a particular region, or business or industry sector, such as the financial services sector, or tightening of credit markets, could cause our customers to

- have difficulty accessing credit sources;
- delay contractual payments; or
- postpone or forego decisions to purchase our products and services, or maintain them at originally purchased levels.

The global economy appears to be recovering from a severe recession, which hurt our product and services revenue in fiscal 2010 and fiscal 2009. Despite what appears to be a trend toward recovery, we cannot provide any assurance that instability in the global economy will end or not become more severe. The longer this global economic instability persists, the greater the probability that these factors could hurt our business, financial results and cash flow.

Our operating results may fluctuate significantly as a result of factors outside of our control, including current economic conditions which could cause the market price of our stock to decline.

Our operating results have fluctuated in the past, and are likely to fluctuate significantly in the future. Our financial results may as a consequence fall short of the expectations of public market analysts or investors, which could cause the price of our common stock to decline. Our revenue and operating results may vary significantly from quarter to quarter due to a number of factors, many of which are beyond our control. Factors that could affect our operating results include:

- general economic conditions, which can affect our customers purchasing decisions, the length of our sales cycle, and our customers ability to pay us on time, if at all;
- the timing of large orders;
- changes in the proportion of software arrangements requiring contract accounting;
- changes in the mix of our sales, including the mix between higher margin software products and lower margin services and maintenance, and the proportion of our product sales requiring us to make royalty payments;
- the timing and amount of our marketing, sales, and product development expenses;

the cost and time required to develop new software products;

the introduction, timing, and market acceptance of new products introduced by us or our competitors;

changes in network technology or in applications, which could require us to modify our products or develop new products;

changes in our pricing policies or those of our competitors; and

the timing and size of potential acquisitions by us.

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We expect to make significant expenditures in all areas of our business, particularly sales and marketing operations, in order to promote future growth. Because the expenses associated with these activities are relatively fixed in the short term, we may be unable to adjust spending quickly enough to offset any unexpected shortfall in revenue growth or any decrease in revenue levels. In addition, our revenue in any quarter depends substantially on orders we receive and ship in that quarter. We typically receive a significant portion of orders in any quarter during the last month of the quarter, and we cannot predict whether those orders will be placed and shipped in that period. If we have lower revenue than we expect, we may not be able to respond quickly enough to reduce our operating expenses. Therefore, any significant shortfall in revenue or delay of customer orders could have an immediate adverse impact on our operating results in that quarter.

For all of these reasons, quarterly comparisons of our financial results are not necessarily meaningful, and you should not rely on them as an indication of our future performance.

If we do not successfully expand our sales force, we may be unable to increase our sales.

We sell our products primarily through our direct sales force, and we must expand the size of our direct sales force to increase revenue. If we are unable to hire or retain qualified sales personnel, if newly hired personnel fail to develop the necessary skills to be productive, or if they reach productivity more slowly than anticipated, our ability to increase our revenue and grow our business could be compromised. Our sales people require a long period of time to become productive, typically three to nine months. The time required to reach productivity, as well as the challenge of attracting, training, and retaining qualified candidates, may make it difficult to meet our direct sales force growth targets. Further, we may not generate sufficient sales to offset the increased expense resulting from growing our direct sales force, or we may be unable to manage a larger direct sales force.

The market for intelligent network management software is new and evolving, and if this market does not develop as anticipated, our revenue could decline.

We derive all of our revenue from the sale of products and services that are designed to allow our customers to manage the performance of applications and networks. Accordingly, if the market for intelligent application and network management software does not continue to grow, we could face declining revenue, which could ultimately lead to our becoming unprofitable. The market for intelligent application and network management software products is evolving. Therefore, we cannot accurately assess the size of the market and may be unable to identify an effective distribution strategy, the competitive environment that will develop, and the appropriate features and prices for products to address the market. If we are to be successful, our current and potential customers must recognize the value of intelligent network management software products, decide to invest in the management of their networks, and, in particular, adopt and continue to use our software products.

Our customers are primarily in four target groups and our operating results may be adversely affected by changes in one or more of these groups.

Our software products and related services are designed to meet the needs of enterprises, United States government agencies, service providers, and network equipment manufacturers, and we market our software products and related services to those four customer groups. Consequently, our financial results depend, in significant part, upon the economic conditions of enterprises, United States government agencies, service providers, and network equipment manufacturers. An economic downturn or adverse change in the regulatory environment or business prospects for one or more of these customer groups may decrease our revenue or lower our growth rate.

A decline in information technology spending may result in a decrease in our revenue or lower our growth rate.

A decline in the demand for information technology among our current and prospective customers may result in decreased revenue or a lower growth rate for us because our sales depend, in part, on our customers

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budgets for new or additional information technology systems and services. A continued economic downturn may cause our customers to reduce or eliminate information technology spending and force us to lower prices of our software products and related services, which would substantially reduce the number of software products we sell and the average sales price for these products. Accordingly, we cannot be certain that we will be able to increase or maintain our revenue.

Our sales to United States government agencies subject us to special risks that could adversely affect our business.

We derive a substantial portion of our revenue from sales directly or indirectly to United States government agencies. Transactions with United States government agencies accounted for approximately 39.9%, 35.3%, and 40.7% of our total revenue for fiscal 2010, 2009, and 2008, respectively. Government sales entail a variety of risks including:

Government contracts are subject to the approval of appropriations by the United States Congress to fund the expenditures by the agencies under these contracts. Congress often appropriates funds for government agencies on a yearly basis, even though their contracts may call for performance over a number of years.

A significant decline in government expenditures generally, or a shift in budget priorities away from agencies or programs that we support, could cause a material decline in our government business. In particular, a decline in government spending on information technology or related services could hurt our government business.

Our products and services are included on a General Services Administration, or GSA schedule. We believe that the GSA schedule facilitates our sales to United States government agencies. The loss of the GSA schedule covering our products and services could adversely affect our results of operations.

We must comply with complex federal procurement laws and regulations in connection with government contracts, which may impose added costs on our business.

Some of our government business requires that we maintain facility security clearances, and requires some of our employees to maintain individual security clearances. If we were to lose these clearances, our government business might decline.

The federal government audits and reviews the performance of federal contractors on contracts, pricing practices, cost structure, and compliance with applicable laws, regulations, and standards. An audit of our work could result in a finding that we overcharged the government, which could result in an adjustment to our previously reported operating results. If a government audit uncovers improper or illegal activities, we may be subject to civil and criminal penalties and administrative sanctions, including termination of contracts, forfeiture of profits, suspension of payments, fines, and suspension or debarment from doing business with United States federal government agencies.

Many of our government contracts are firm fixed-price contracts. To the extent that the assumptions we have used in pricing these contracts prove inaccurate, we could incur and accrue losses on contracts, which would adversely affect our operating results.

A portion of our sales to the United States government are made indirectly as a subcontractor to another government contractor, referred to as the prime contractor, who has the direct relationship with the government. We also team with prime contractors to bid on competitive government opportunities for which we hope to serve as a subcontractor. If prime contractors lose existing business on which we serve as a subcontractor, or fail to win the competitive bids on which we team with them, our government business would be hurt.

We could face expense and delay if any of our competitors, or competitors of the prime contractors to which we serve as a subcontractor, protest or challenge contract awards made to us or our prime contractors pursuant to competitive bidding.

Federal government contracts contain provisions and are subject to laws and regulations that provide government clients with rights and remedies not typically found in commercial contracts. These rights and remedies allow government clients, among other things, to terminate existing contracts, with short notice, for convenience without cause; reduce or modify contracts or subcontracts; and claim rights in products, systems, and technology produced by us.

If our newest products, particularly those targeted primarily for enterprises and United States government agencies, do not gain widespread market acceptance, our revenue might not increase and could even decline.

We expect to derive a substantial portion of our revenue in the future from sales to enterprises and United States government agencies of our Application Performance Management and Network Operations product offerings. Our business depends on customer acceptance of these products and our revenue may not increase, or may even decline, if our target customers do not adopt and expand their use of our products.

We may not be able to grow our business if service providers do not buy our products.

An element of our strategy is to continue selling to service providers our network planning and design and our network operations product offerings. Accordingly, if our products fail to perform favorably in the service provider environment, or fail to gain wider adoption by service providers, our business and future operating results could suffer.

Our lengthy and variable sales cycle makes it difficult to predict operating results.

It is difficult for us to forecast the timing and recognition of revenue from sales of our products because prospective customers often take significant time evaluating our products before purchasing them. The period between initial customer contact and a purchase by a customer may vary from three months to more than a year. During the sales process, the customer may decide not to purchase or may reduce proposed orders of our products for various reasons, including changes in budgets and purchasing priorities. Our prospective customers routinely require education regarding the use and benefit of our products. This may also lead to delays in receiving customers orders.

Our ability to increase our sales may be impaired if we do not expand and manage our indirect distribution channels.

To increase our sales, we must, among other things, further expand and manage our indirect distribution channels, which consist primarily of international distributors and original equipment manufacturers and resellers. If we are unable to expand and manage our relationships with our distributors, our distributors are unable or unwilling to market and sell our products effectively, or we lose existing distributor relationships, we might not be able to increase our revenue. Our international distributors and original equipment manufacturers and resellers have no obligation to market or purchase our products. In addition, they could partner with our competitors, bundle or resell competitors products, or internally develop products that compete with our products.

We may not be able to successfully manage our expanding operations, which could impair our ability to operate profitably.

We may be unable to operate our business profitably if we fail to manage our growth. Our growth has sometimes strained, and may in the future continue to strain, our managerial, administrative, operational, and financial resources and controls. We plan to continue to expand our operations and increase the number of our full-time employees. Our ability to manage growth may depend in part on our ability to continue to enhance our operating, financial, and management information systems. Our personnel, systems, and controls may not be adequate to support our growth. In addition, our revenue may not continue to grow at a sufficient rate to absorb the costs associated with a larger overall employee base.

If we are unable to introduce new and enhanced products on a timely basis that respond effectively to changing technology, our revenue may decline.

Our market is characterized by rapid technological change, changes in customer requirements, frequent new product and service introductions and enhancements, and evolving industry standards. If we fail to develop and introduce new and enhanced products on a timely basis that respond to these changes, our products could become obsolete, demand for our products could decline and our revenue could fall. Advances in network management technology, software engineering, and simulation technology, or the emergence of new industry standards, could lead to new competitive products that have better performance, more features, or lower prices than our products and could render our products unmarketable.

Our future revenue is substantially dependent upon our existing customers continuing to license additional products, renew maintenance agreements, and purchase additional services.

Our existing customers have traditionally generated additional revenue from consulting services, renewed maintenance agreements, and the purchase of additional software products, which represent the majority of our annual revenue. The maintenance agreements are generally renewable at the option of the customers and there are no mandatory payment obligations or obligations to license additional software. In addition, customers may decide not to purchase additional products or services. If our existing customers fail to renew their maintenance agreements or purchase additional products or services, our revenue could decrease.

Increases in professional services revenue as a percentage of total revenue could decrease overall margin.

We realize significantly lower margin on professional service revenue than we do on other types of revenue. As a result, if professional services revenue increases as a proportion of total revenue, our gross margin will be lower. Although professional services revenue has been declining as a percentage of revenue, accounting for 21.2%, 23.3% and 27.4% of our total revenue for fiscal 2010, 2009, and 2008, respectively, this trend may not continue.

If we fail to retain our key personnel and attract and retain additional qualified personnel, we might not be able to maintain our current level of revenue.

Our future success and our ability to maintain our current level of revenue depend upon the continued service of our executive officers and other key sales and research and development personnel. The loss of any of our key employees, in particular Marc A. Cohen, our Chairman of the Board and Chief Executive Officer, who is also our principal sales executive, and Alain J. Cohen, our President and Chief Technology Officer, could also adversely affect our ability to pursue our growth strategy. We do not have employment agreements or any other agreements that obligate any of our officers or key employees to remain with us.

We must also continue to hire highly qualified individuals, particularly software engineers and sales and marketing personnel. Our failure to attract and retain technical personnel for our product development, consulting services, and technical support teams may limit our ability to develop new products or product enhancements. Competition for these individuals is intense, and we may not be able to attract and retain additional highly qualified personnel in the future. In addition, limitations imposed by federal immigration laws and the availability of visas could impair our ability to recruit and employ skilled technical professionals from other countries to work in the United States.

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Our international operations subject our business to additional risks, which could cause our sales or profitability to decline.

In fiscal 2010, 22.5% of our revenue, or $28.4 million, was generated from customers outside the United States. In fiscal 2009, 21.2% of our revenue, or $26.0 million, was generated from customers outside the United States. In fiscal 2008, 20.2% of our revenue, or $20.5 million, was generated from customers outside the United States. We plan to increase our international sales activities, but these plans are subject to a number of risks that could cause our sales to decline or could otherwise cause a decline in profitability. These risks include:

- difficulty in attracting distributors that will market and support our software products effectively;
- greater difficulty in accounts receivable collection and longer collection periods;
- the need to comply with varying employment policies and regulations that could make it more difficult and expensive to manage our employees if we need to establish more direct sales or support staff outside the United States;
- potentially adverse tax consequences;
- the effects of currency fluctuations; and
- political and economic instability.

We expect to face increased competition, which could cause us to lose sales, resulting in lower profitability.

Increasing competition in our market could cause us to lose sales and become unprofitable. We believe that the market for intelligent application and network management software is likely to become more competitive as it evolves and the demand for intelligent application and network management software products continues to increase. At least one of our current competitors and many of our potential competitors are larger and have substantially greater financial and technical resources than we do. In addition, it is possible that other vendors as well as some of our customers or distributors may develop and market software products that compete with our software products in the future.

If our products contain errors and we are unable to correct those errors, our reputation could be harmed and our customers could demand refunds from us or assert claims for damages against us.

Our software products could contain significant errors or bugs that may result in:

- the loss of or delay in market acceptance and sales of our products;
- the delay in introduction of new products or updates to existing products;
- diversion of our resources;
- injury to our reputation; and

increased support costs.

Bugs may be discovered at any point in a product s life cycle. We expect that errors in our products may be found in the future, particularly in new product offerings and new releases of our current products.

Because our customers use our products to manage networks that are critical to their business operations, any failure of our products could expose us to product liability claims. In addition, errors in our products could cause our customers networks and systems to fail or compromise their data, which could also result in liability to us. Product liability claims brought against us could divert the attention of management and key personnel, could be expensive to defend, and may result in adverse settlements and judgments.

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Our software products rely on our intellectual property, and any failure to protect our intellectual property could enable our competitors to market products with similar features that may reduce our revenue and could allow the use of our products by users who have not paid the required license fee.

If we are unable to protect our intellectual property, our competitors could use our intellectual property to market products similar to our products, which could reduce our revenue. In addition, we may be unable to prevent the use of our products by persons who have not paid the required license fee, which could reduce our revenue. Our success and ability to compete depend substantially upon the internally-developed technology that is incorporated in our products. Policing unauthorized use of our products is difficult, and we may not be able to prevent misappropriation of our technology, particularly in foreign countries where the laws may not protect our proprietary rights as fully as those in the United States. Others may circumvent the patents, copyrights, and trade secrets we own. In the ordinary course of business, we enter into a combination of confidentiality, non-competition, and non-disclosure agreements with our employees.

These measures afford only limited protection and may be inadequate, especially because our employees are highly sought after and may leave our employ with significant knowledge of our proprietary information. In addition, any confidentiality, non-competition and non-disclosure agreements we enter into may be found to be unenforceable, or our copy protection mechanisms embedded in our software products could fail or could be circumvented.

Our products employ technology that may infringe on the proprietary rights of others, and, as a result, we could become liable for significant damages.

We expect that our software products may be increasingly subject to third-party infringement claims as the number of competitors in our industry segment grows and the functionalities of products in different industry segments overlap.

Regardless of whether these claims have any merit, they could:

- be time-consuming to defend;
- result in costly litigation;
- divert our management s attention and resources;
- cause us to delay or cease product shipments; or
- require us to enter into royalty or licensing agreements.

These royalty or licensing agreements may not be available on terms acceptable to us, or at all. A successful claim of product infringement against us or our failure or inability to license the infringed or similar technology could adversely affect our business because we would not be able to sell the affected product without redeveloping it or incurring significant additional expense.

As with other software vendors, we may be required to delay revenue recognition into future periods, which could adversely affect our operating results.

We have in the past had to, and in the future may have to, defer recognition for product fees due to several factors, including whether:

- product arrangements include undelivered elements for which we do not have vendor specific evidence of fair value;

we must deliver services for significant customization, enhancements and modifications of our products;

the transaction involves material acceptance criteria or there are other identified product-related issues;

- the transaction involves contingent payment terms or fees; or

- we are required to accept extended payment terms.

Because of the factors listed above and other specific requirements under accounting principles generally accepted in the United States of America for software revenue recognition, we must have very precise terms in our product arrangements in order to recognize revenue when we initially deliver products or perform services. Negotiation of mutually acceptable terms and conditions can extend the sales cycle, and sometimes we do not obtain terms and conditions that permit revenue recognition at the time of delivery.

If we undertake acquisitions, they may be expensive and disruptive to our business and could cause the market price of our common stock to decline.

We completed our acquisition of specified assets of Network Physics in October 2007. We may continue to acquire or make investments in companies, products or technologies if opportunities arise. Any acquisition could be expensive, disrupt our ongoing business, distract our management and employees, and adversely affect our financial results and the market price of our common stock. We may not be able to identify suitable acquisition or investment candidates, and if we do identify suitable candidates, we may not be able to make these acquisitions or investments on commercially acceptable terms or at all. If we make an acquisition, we could have difficulty integrating the acquired technology, employees, or operations. In addition, the key personnel of the acquired company may decide not to work for us.

We also expect that we would incur substantial expenses if we acquire other businesses or technologies. We might use cash on hand, incur debt, or issue equity securities to pay for any future acquisitions. If we issue additional equity securities, our stockholders could experience dilution and the market price of our stock may decline.

Our products are subject to changing computing environments, including operating system software and hardware platforms, which could render our products obsolete.

The evolution of existing computing environments and the introduction of new popular computing environments may require us to redesign our products or develop new products. Computing environments, including operating system software and hardware platforms, are complex and change rapidly. Our products are designed to operate in currently popular computing environments. Due to the long development and testing periods required to adapt our products to new or modified computing environments, our research and development efforts could be distracted and we could experience significant delays in product releases or shipments, which could result in lost revenue and significant additional expense.

The impairment of a significant amount of goodwill on our balance sheet could result in a decrease in earnings and, as a result, our stock price could decline.

In the course of our operating history, we have acquired assets and businesses. Some of our acquisitions have resulted in the recording of a significant amount of goodwill on our financial statements. We had approximately $14.6 million of goodwill recorded on our balance sheet as of March 31, 2010. The goodwill reflects the fact that the fair value of the net tangible assets acquired in past acquisitions was less than the purchase price. We may not realize the full value of the goodwill. We evaluate goodwill for impairment on an annual basis or more frequently if events and circumstances suggest that the asset may be impaired. If goodwill is determined to be impaired, we will write off the unrecoverable portion as a charge to our earnings. If we acquire new assets and businesses in the future, we may record additional goodwill. The possible write-off of the associated goodwill could negatively impact our future earnings and, as a result, the market price of our common stock could decline.

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The price of our common stock may decrease due to market volatility.

The market price of our common stock has been volatile and has fluctuated since the initial public offering of our common stock on August 1, 2000. The market price of our common stock may continue to fluctuate in response to a number of factors, some of which are beyond our control. Trading activity of our stock has historically been relatively thin, in part as a result of officers and directors and institutional stockholders holding a significant percentage of our stock. In addition, the market price of securities of technology companies have been volatile and have experienced fluctuations that often have been unrelated or disproportionate to the operating performance of these companies. Also, broad market fluctuations could adversely impact the market price of our common stock, which in turn could cause impairment of goodwill that could materially and adversely impact our financial condition and results of operations.

It is not uncommon when the market price of a stock has been volatile for holders of that stock to institute securities class action litigation against the company that issues that stock. If any of our stockholders brought such a lawsuit against us, even if the lawsuit is without merit, we could incur substantial costs defending the lawsuit beyond any insurance coverage which we may have for such risks. Such a lawsuit could also divert the time and attention of our management.

The Board may decide that future dividends will be in amounts that are different than the amounts we have historically paid or may decide to suspend or discontinue the payment of cash dividends altogether.

The declaration of cash dividends in the future is subject to final determination each quarter by the Board based on a number of factors, including our financial performance and available cash resources, our cash requirements and alternative uses of cash that the Board may conclude would represent an opportunity to generate a greater return on investment for us.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 2. PROPERTIES

Our corporate office and principal facilities are located in Bethesda, Maryland and consist of approximately 82,000 square feet of office space held under two leases. The lease for 60,000 square feet expires on January 31, 2011, exclusive of renewal options, and the lease for 22,000 square feet expires on January 31, 2016, exclusive of renewal options. We also lease office space in the following locations: Cary, North Carolina; Dallas, Texas; Santa Clara, California; Nashua, New Hampshire; Ghent, Belgium; Paris, France; Slough, United Kingdom; Singapore; Beijing China; and Mainz, Germany.

ITEM 3. LEGAL PROCEEDINGS

We are involved in various claims and legal proceedings arising from our normal operations. We do not regard any of those matters to be material.

ITEM 4. REMOVED AND RESERVED

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PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market for Common Stock

Our common stock began trading on the NASDAQ Global Select Market on August 2, 2000, under the symbol OPNT. The following table sets forth, on a per share basis, for the indicated periods, the intra-day high and low sale prices of our common stock as reported by the NASDAQ Global Select Market.

Quarter ended	High	Low
June 30, 2008	$ 10.50	$ 7.84
September 30, 2008	14.39	8.02
December 31, 2008	12.80	8.48
March 31, 2009	10.81	7.37
June 30, 2009	10.75	6.92
September 30, 2009	11.56	8.24
December 31, 2009	12.70	10.01
March 31, 2010	16.20	11.70

Number of Stockholders of Record

As of June 1, 2010, we had approximately 106 holders of record of common stock. Because many of these shares are held by brokers and other institutions on behalf of stockholders, we are unable to estimate the total number of stockholders represented by these holders of record.

Securities Authorized for Issuance Under Equity Compensation Plans

The following table provides information regarding our current equity compensation plans as of March 31, 2010.

Equity Compensation Plan Information

Plan Category	Number of securities to be issued upon exercise of outstanding options (a)	Weighted-average exercise price of outstanding options	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	2,494,082	$ 10.86	2,943,409(1)(2)
Equity compensation plans not approved by security holders			
Total	2,494,082	$ 10.86	2,943,409

(1) In addition to being available for future issuance upon exercise of options that may be granted after March 31, 2010, all of the remaining 2,131,488 shares under our Amended and Restated 2010 Stock Incentive Plan, or the 2010 Plan, may instead be issued in the form of restricted stock, stock appreciation rights or other stock-based awards.

(2) Includes 811,921 shares issuable under our 2000 Employee Stock Purchase Plan, including shares issuable in connection with the current offering period which ends on July 31, 2010. Also includes 2,131,488 shares issuable under the 2010 Plan. Under the 2010 Plan, beginning with the 2011 calendar year, the number of shares available for issuance automatically increases on the first trading day of each calendar

year by an

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amount equal to the lesser of (i) 3% of the shares of common stock outstanding on the last trading day of the preceding calendar year, or (ii) an amount determined by the Board of Directors, or the Board, in either case not to exceed an annual increase of 1,000,000 shares. See Note 2, Stock-Based Compensation, in the accompanying notes to our consolidated financial statements for more information.

Dividends

We did not declare or pay any dividends in fiscal 2008 or 2009. The following table summarizes our quarterly cash dividend payments for fiscal 2010:

Declaration Date	Stockholder Record Date	Payment Date	Amount per Share
May 13, 2009	June 15, 2009	June 29, 2009	$0.09
July 30, 2009	September 15, 2009	September 29, 2009	$0.09
October 28, 2009	December 15, 2009	December 30, 2009	$0.09
January 27, 2010	March 15, 2010	March 30, 2010	$0.09

The declaration of cash dividends in the future is subject to final determination each quarter by the Board based on a number of factors, including our financial performance and available cash resources, our cash requirements and alternative uses of cash that the Board may conclude would represent an opportunity to generate a greater return on investment for us. The Board may decide that future dividends will be in amounts that are different than the amount described above or may decide to suspend or discontinue the payment of cash dividends altogether.

Stock Repurchase Plan

Issuer Repurchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Number of Shares That May Yet Be Purchased Under the Plans or Programs
January 1 31, 2010				787,704
February 1 28, 2010	62,851	$ 14.09	62,851	724,853
March 1 31, 2010	22,814	$ 14.98	22,814	702,039
Total	85,665	$ 14.33	85,665	702,039

(1) On January 31, 2005, we announced a stock repurchase program pursuant to which we are authorized to purchase up to 1,000,000 shares of common stock from time to time on the open market or in privately negotiated transactions. This program does not have a specified termination date. On February 4, 2008, we announced that our Board approved an increase of an additional 1,000,000 shares under our stock repurchase program. Any repurchased shares will be available for use in connection with our stock plans or other corporate purchases. As of March 31, 2010, we had repurchased 1,297,961 shares of common stock under this program.

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ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The following selected consolidated financial data should be read in conjunction with our consolidated financial statements and the related notes and Management s Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this Annual Report. The statement of operations data for the years ended March 31, 2010, 2009, and 2008, and the balance sheet data as of March 31, 2010 and 2009, are derived from our audited consolidated financial statements included in this Annual Report. The balance sheet data as of March 31, 2008, 2007 and 2006 and the statement of operations data for the years ended March 31, 2007 and 2006 are derived from our consolidated financial statements that are not included in this Annual Report. Historical results are not necessarily indicative of results that may be expected for any future period.

	Year Ended March 31,				
	2010	2009	2008	2007	2006
	(in thousands, except per share data)				
Statement of Operations Data:					
Revenue:					
Product	$ 52,252	$ 51,211	$ 38,838	$ 43,186	$ 31,976
Product updates, technical support and services	47,264	43,067	34,787	28,062	24,226
Professional services	26,831	28,601	27,721	23,882	19,913
Total revenue	126,347	122,879	101,346	95,130	76,115
Cost of revenue:					
Product	5,983	3,536	1,035	638	657
Product updates, technical support and services	4,859	4,665	4,514	3,264	2,637
Professional services	19,328	20,911	19,154	15,904	13,705
Amortization of acquired technology	1,835	2,172	1,486	723	832
Total cost of revenue	32,005	31,284	26,189	20,529	17,831
Gross profit	94,342	91,595	75,157	74,601	58,284
Operating expenses:					
Research and development	32,043	30,791	27,471	21,688	18,643
Sales and marketing	43,181	42,533	39,357	34,133	26,300
General and administrative	11,011	11,857	11,747	10,994	13,375
Total operating expenses	86,235	85,181	78,575	66,815	58,318
Income (loss) from operations	8,107	6,414	(3,418)	7,786	(34)
Interest and other (expense) income, net	(70)	1,246	3,579	3,834	2,680
Income before provision (benefit) for income taxes	8,037	7,660	161	11,620	2,646
Provision (benefit) for income taxes	2,214	2,928	(372)	3,655	509
Net income	$ 5,823	$ 4,732	$ 533	$ 7,965	$ 2,137
Basic net income per common share	$ 0.28	$ 0.23	$ 0.03	$ 0.39	$ 0.10
Diluted net income per common share	$ 0.28	$ 0.23	$ 0.03	$ 0.37	$ 0.11
Basic weighted average shares outstanding	20,529	20,296	20,342	20,357	20,200
Diluted weighted average shares outstanding	20,790	20,533	20,596	21,189	20,506
Balance Sheet Data (end of period):					
Cash, cash equivalents and marketable securities	$ 104,681	$ 91,989	$ 85,829	$ 91,381	$ 85,861

Total assets	$ 178,352	$ 166,064	$ 153,538	$ 147,658	$ 127,347
Long-term debt	$	$	$	$	$ 103
Dividends declared per common share	$ 0.36	$	$	$	$
Total stockholders equity	$ 118,676	$ 116,505	$ 110,645	$ 112,871	$ 99,398

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ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis in conjunction with our consolidated financial statements and the related notes included elsewhere in this Annual Report on Form 10-K. This discussion and analysis contains forward-looking statements that involve risks, uncertainties, and assumptions. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including, but not limited to, those set forth under Item 1A. Risk Factors and elsewhere in this Annual Report on Form 10-K.

Overview

OPNET Technologies, Inc. is a provider of software products and related services for managing applications and networks. Our software products and related services address: application performance management, network operations, capacity management, and network research and development. Our customers include corporate enterprises, government and defense agencies, network service providers, and network equipment manufacturers. Our software products and related services are designed to help our customers make better use of resources, reduce operational problems and improve competitiveness.

We operate in one reportable industry segment, the development and sale of computer software programs and related services. Our operations are principally in the United States, and we have subsidiaries in Belgium, France, Germany, the United Kingdom and Singapore. We primarily depend upon our direct sales force to generate revenue in the United States. Sales outside the United States are made through our international sales team as well as third-party distributors and value-added resellers, who generally are responsible for providing technical support and service to customers within their territory.

Our revenue is derived from three primary sources: (1) product, (2) product updates, technical support and services, and (3) professional services, which include consulting and training services for customers without current maintenance agreements. Product revenue represents all fees earned from granting customers licenses to use our software and fees associated with hardware necessary to run our software, and excludes revenue derived from product updates, which are included in product updates, technical support, and services revenue. Our software master license agreement provides our customers with the right to use our software either perpetually, which we refer to as perpetual licenses, or during a defined term, generally for one to four years, which we refer to as term licenses. For the years ended March 31, 2010, 2009, and 2008, perpetual licenses represented approximately 92%, 93%, and 97% of product revenue, respectively. Substantially all of our product arrangements include both product licenses and product updates, technical support, and services. Product updates, technical support, and services revenue represent fees associated with the sale of unspecified product updates, technical support and when-and-if available training under our maintenance agreements. We offer professional services, under both time-and-material and fixed-price agreements, primarily to facilitate the adoption of our software products.

We consider our consulting services to be an integral part of our business model as they are centered on our software product offerings. Because our consulting services facilitate the adoption of our software product offerings, we believe that they ultimately generate additional sales of product licenses.

The key strategies of our business plan include increasing sales to existing customers, increasing deal size by selling modules and introducing new software products, improving our sales and marketing execution, establishing alliances to extend our market reach, increasing our international presence and increasing profitability. We have focused our sales, marketing, and other efforts on corporate enterprise and United States government opportunities, and to a much lesser extent, service provider and network equipment manufacturer opportunities. Our focus and strategies are designed to increase revenue and profitability. Because of the uncertainty surrounding the amount and timing of revenue growth, we expect to need to closely control the increases in our total expenses as we implement these strategies.

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In March 2008, we launched an initiative to extend our market reach by establishing sales alliances with third parties called the Synergy program. The Synergy program is designed to increase the penetration of our software products into mid-sized organizations. The Synergy program s focus is on selling our application performance management software products, including ACE Live that provides end-user experience monitoring and real-time application performance analytics, as we believe these software products are particularly well-suited for channel distribution.

Summary of Our Fiscal 2010 Financial Performance

During fiscal 2010, as compared to fiscal 2009, we generated an increase in total revenue, which allowed us to grow income from operations and net income. The increase in total revenue was primarily the result of growth in sales of our application performance management products to United States government and corporate enterprise customers. We believe the increase in sales of our application performance management products is the result of competitive advantages offered by our products, together with loosening customer budgets and more normal purchasing patterns as compared to fiscal 2009.

During fiscal 2010, as compared to fiscal 2009, we also generated an increase in deferred revenue and cash flows from operations. The increase in deferred revenue was largely the result of growth in the renewal of customer maintenance contracts. The increase in cash flows from operations was largely the result of growth in sales of our products and maintenance contracts together with strong collections activity during fiscal 2010.

The following table summarizes information on some of our key financial and operating metrics.

	Fiscal 2010	Fiscal 2009	Amount Change	Percentage Change
	(dollars in thousands, except per share data)			
Financial Data:				
Total revenue	$ 126,347	$ 122,879	$ 3,468	2.8%
Total cost of revenue	$ 32,005	$ 31,284	$ 721	2.3%
Gross profit	$ 94,342	$ 91,595	$ 2,747	3.0%
Gross profit as a percentage of total revenue (gross margin)	74.7	%74.5%		
Total operating expenses	$ 86,235	$ 85,181	$ 1,054	1.2%
Income from operations	$ 8,107	$ 6,414	$ 1,693	26.4%
Income from operations as a percentage of total revenue (operating margin)	6.4	%5.2%		
Net income	$ 5,823	$ 4,732	$ 1,091	23.1%
Diluted net income per common share	$ 0.28	$ 0.23	$ 0.05	21.7%
Other Operations Data:				
Total employees (period end)	579	593	(14)	(2.4)%
Total average employees	580	585	(5)	(0.9)%
Total consultants (period end)	98	118	(20)	(16.9)%
Total period end quota-carrying sales persons (excluding directors and inside sales representatives)	72	70	2	2.9%
Financial Condition and Liquidity Data:				
Cash, cash equivalents, and marketable securities (period end)	$ 104,681	$ 91,989	$ 12,692	13.8%
Cash flows from operating activities	$ 21,777	$ 12,104	$ 9,673	80.0%
Total deferred revenue (period end)	$ 43,371	$ 33,133	$ 10,238	30.9%

We achieved growth in product revenue and product updates, technical support and services revenue, offset by a decrease in professional services revenue during fiscal 2010, as compared to fiscal 2009. Product revenue increased by $1.0 million, and product updates, technical support and services revenue increased by $4.2 million, which was offset in part by a decrease in professional services revenue of $1.8 million. The increase in product revenue was the result of growth in sales to United States government and corporate enterprise customers, which was partially offset by a decline in sales to service providers and network equipment manufacturers. The increase in revenue from product updates, technical support and services revenue reflects growth in the overall customer installed base. Increases in the overall customer installed base increase the demand for annual renewals of maintenance contracts. The sequential decrease in revenue from professional services was largely the result of a decrease in billable hours worked on projects for corporate enterprise customers and service providers. We believe the decrease in billable hours worked was related to the increase in the proportion of sales of our application performance management products as compared to our other products, as our application performance management products generally require less consulting services to implement. Total revenue generated from sales to United States government customers increased by $7.0 million during fiscal 2010 as compared to fiscal 2009. The percentage of total revenue from United States government customers increased to 39.9% in fiscal 2010 from 35.3% in fiscal 2009. The increase in the percentage of revenue from United States government customers was due to an increase in sales of our application performance management products.

Our international revenue increased 9.3% to $28.4 million, or 22.5% of total revenue, for fiscal 2010. We expect revenue from sales outside the United States to continue to account for a significant portion of our total revenue in the future. The increase in international revenue was primarily the result of growth in sales of our application performance management products to corporate enterprise customers. International revenue in fiscal 2010 also benefited from a more experienced direct sales force and our increased focus on sales to corporate enterprises. Sales to corporate enterprises accounted for the largest portion of our international revenue during fiscal 2010. We believe that continued growth and profitability will require further expansion of our sales, marketing and customer service functions in international markets.

During fiscal 2010, gross profit increased 3.0% to $94.3 million. Our gross margin increased slightly to 74.7% for fiscal 2010 from 74.5% in fiscal 2009. The increase in our gross profit and gross margin was primarily due to an increase in product updates, technical support and services revenue of $4.2 million in fiscal 2010 and, to a lesser extent, an increase in product revenue of $1.0 million. The increases in revenue were partially offset by an increase in the cost of product revenue of $2.4 million which primarily resulted from growth in the demand for our hardware-based ACE Live solutions.

During fiscal 2010, operating income increased to $8.1 million from $6.4 million during fiscal 2009. The increase in operating income was largely the result of an increase in revenue from product updates, technical support and services revenue and product revenue, partially offset by an increase in operating expenses.

Trends that May Affect Our Business and Future Results

While we anticipate a challenging economic environment in the near term, we believe the competitive advantages offered by our products have positioned us well to grow market share and drive profitability as economic conditions improve. The demand for our software products and related services by corporate enterprise and United States government customers has been much stronger than the demand from service providers and network equipment manufacturers, which is consistent with our expectations. We believe that lower business activity with service providers and network equipment manufacturers is primarily due to the weakened economy in which these businesses operate, which we expect to continue, at least in the near term. Consequently, our revenue growth and profitability depend, in significant part, upon our ability to sell in a weakened economic environment and the economic health of corporate enterprises and United States government agencies.

We anticipate the following trends and patterns over the next several quarters:

Total Revenue. We believe the current economic environment is showing signs of improvement, but our ability to generate increased revenue domestically and internationally will depend upon continued and sustained improvement in economic conditions. We expect future growth opportunities in product revenue and product updates, technical support and services revenue to come from sales to corporate enterprise customers and the

United States government, as we believe our products offer competitive advantages in these markets. We expect product revenue and product updates, technical support and services revenue from sales to service providers and network equipment manufacturers to fluctuate from quarter to quarter with the potential for periods of declining revenue. Our ability to increase professional services revenue will depend upon our ability to maintain several large consulting contracts with the United States government and to attract and retain additional qualified consultants, including those with security clearances. We believe that continued increases in the proportion of sales of our application performance management products, as compared to our other products, will cause the percentage of our total revenue attributable to professional services revenue to decline, and might also cause an absolute decline in professional services revenue, since our application performance management products generally require less consulting time to implement. As a result of these factors, we believe that we may experience fluctuations in quarterly revenue.

Gross Profit Margin. Our overall gross profit margin will continue to be affected by the percentage of total revenue generated from product revenue and product updates, technical support and services revenue, as revenue from these sources have substantially higher gross margins than the gross margin on revenue from professional services. Our overall gross profit margin will also be affected by the profitability of individual consulting engagements. Amortization of technology associated with the purchase and/or acquisition of technology we may make in future periods may also affect our gross profit margin.

Research and Development Expenses. We believe that continued investment in research and development will be required to maintain our competitive position and broaden our software product lines, as well as enhance the features and functionality of our current software products, especially our application performance management products. We believe that more investment in research and development will be required in order to maintain our competitive position and grow sales of our application performance management products as compared to our other products, as we believe there is more competition in the markets served by these products as compared to the markets for our other products. We made personnel investments in research and development during fiscal 2010, and we plan to continue making modest investments in additional personnel during the next several quarters. We expect that the absolute dollar amount of these expenses will continue to grow but generally decrease modestly as a percentage of total revenue in future periods. Our ability to decrease these expenses as a percentage of revenue will depend upon increases in our revenue, among other factors.

Sales and Marketing Expenses. We depend upon our direct sales model to generate revenue and believe that increasing the size of our quota-carrying sales team is essential for long-term growth. During fiscal 2010, we focused on improving the productivity of our sales force, and only made modest investments in additional direct sales personnel. We plan to continue this approach during the next several quarters. We anticipate increases in marketing expenditures during fiscal 2011 as compared to fiscal 2010 as a result of our plans to reinstate OPNETWORK. We did not hold OPNETWORK during fiscal 2010 due to travel restrictions many companies had in place as a result of economic conditions. We also plan to increase expenditures in areas we believe will enhance the visibility of our products in the marketplace, especially our application performance management products. While we expect that the absolute dollar amount of sales and marketing expenses will increase in fiscal 2011 as compared to fiscal 2010, our ability to lower these expenses as a percentage of revenue will depend upon increases in our revenue.

General and Administrative Expenses. We expect the dollar amount of general and administrative expenses to increase as we continue to expand our operations but generally decrease as a percentage of total revenue in future periods. Our ability to decrease these expenses as a percentage of revenue will depend upon increases in our revenue, among other factors.

Operating Margin. Since a significant portion of our product arrangements close in the latter part of each quarter, we may not be able to adjust our cost structure in the short-term to respond to lower than expected revenue, which would adversely impact our operating margin and earnings. Our operating margin increased to 6.4% during fiscal 2010 from 5.2% during fiscal 2009. We remain committed to increasing profitability and generating long-term growth. As the economy improves, we plan to strategically increase research and

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development and marketing expenditures in order to maintain our products competitive advantages and increase market share. While we intend to strategically increase expenditures in certain areas, we intend to closely monitor and control overall operating expenses in order to maximize our operating margin.

Critical Accounting Policies and Use of Estimates

The accompanying discussion and analysis of our financial condition and results of operations are based upon our audited consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America, or GAAP. The preparation of these financial statements requires that we make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, 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 could differ from the estimates made by management with respect to these and other items that require management s estimates.

We have identified the accounting policies that are critical to understanding our historical and future performance, as these policies affect the reported amounts of revenue and the more significant areas involving management s judgments and estimates. These critical accounting policies relate to revenue recognition and deferred revenue, stock based compensation, allowance for doubtful accounts, valuation of long-lived assets, including intangible assets and impairment review of goodwill, software development costs, and income taxes. These policies, and our procedures related to these policies, are described in detail below. In addition, please refer to Note 1 to our consolidated financial statements included elsewhere in this Annual Report on Form 10-K for further discussion of our accounting policies.

Revenue Recognition. We derive revenue from three primary sources: (1) products, (2) product updates, technical support and services, which include product updates, certain training provided and offered on a when-and-if available basis to customers, and technical support, and (3) professional services, which include consulting and custom training services for customers without a current maintenance agreement. We recognize revenue based on the provisions of Accounting Standards Codification 605-985 Revenue Recognition Software, or ASC 605-985.

Product Revenue

Product revenue represents all fees earned from granting customers perpetual and term licenses to use our software as well as the hardware that we use to deliver our ACE Live software products. It excludes revenue derived from product updates, which are included in product updates, technical support and services revenue. For the years ended March 31, 2010, 2009, and 2008, perpetual licenses represented approximately 92%, 93%, and 97% of product revenue, respectively. Product revenue is recognized when the following four criteria are met: (i) persuasive evidence of an arrangement exists, (ii) delivery of the product has occurred, (iii) the product fee is fixed or determinable, and (iv) collectibility is probable. We analyze each of these four criteria as follows:

> ***Persuasive evidence of an arrangement exists.*** For license arrangements with end-users, it is our customary practice to have a written software license agreement, which is signed by both the end user and us, and a purchase order or equivalent. A written contract can be executed based on the customer-specific format or on the standard shrink wrap software master license agreement. For those end users who have previously negotiated a software license agreement with us, the initial software license agreement is used as evidence of a written contract. Sales to distributors, resellers, and value-added resellers, which we collectively refer to as resellers, are primarily made outside of North America and are evidenced by a master reseller agreement governing the relationship, which is signed by both the reseller and us, together with a purchase order on a transaction-by-transaction basis. To further evidence an arrangement, our master reseller agreement requires that the reseller provide us copies of the end user s executed software master license agreements.

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Delivery has occurred. Physical delivery of our software products to end users or resellers, which are collectively referred to as customers, is generally considered to have occurred upon the transfer of media containing our software products to a common carrier, usually FOB shipping point based on standard agreement terms. Software licenses may also be delivered electronically to end users. Electronic delivery is deemed to occur after end users have been provided with access codes that allow them to take immediate possession of the software. If a software arrangement includes undelivered software products or services that are essential to the functionality of delivered software products, delivery is not considered to have occurred until these software products or services are delivered.

The fee is fixed or determinable. It is our policy to not provide customers the right to any adjustments or refund of any portion of their license fees paid, acceptance provisions, cancellation privileges, or rights of return. Our normal payment terms for our software products and services currently range from net 30 days to net 90 days and primarily vary based on the country in which an agreement is executed. Payments that extend beyond our normal payment terms from the contract date but that are due within six months are generally deemed to be fixed or determinable based on our successful collection history on such arrangements, and thereby satisfy the required criteria for revenue recognition**.** Arrangements with payment terms extending beyond six months are considered not to be fixed or determinable, and revenue from such arrangements is recognized as payments become due and payable.

Collectibility is probable. Collectibility is assessed on a customer-by-customer basis. We typically sell to customers for whom there is a history of successful collection. New customers are subject to a credit review process that evaluates the customer s ability to pay**.** If we determine from the outset of an arrangement that collectibility is not probable, revenue is recognized as cash is collected.

In instances when any of the four criteria are not met, we defer recognition of product revenue until the criteria are met. When the sale of the software product requires us to make significant enhancements, customization or modifications to the software that are essential to its functionality, product revenue and consulting fees are recognized using contract accounting under ASC 605-35, Revenue Recognition Construction-Type and Production. We estimate the percentage-of-completion, under ASC 605-35, based on our estimate of total hours to complete the project as a percentage of total hours incurred and the estimated hours to complete.

The process of estimation inherent in the application of the percentage-of-completion method of accounting for revenue is subject to judgments and uncertainties and may affect the amounts of product revenue and professional services revenue under certain contracts and related expenses reported in our consolidated financial statements. A number of internal and external factors can affect our estimates to complete client engagements, including skill level and experience of project managers, staff assigned to engagements and continuity and attrition level of professional services staff. Changes in the estimated stage of completion of a particular project could create variability in our revenue and results of operations if it is required to increase or decrease previously recognized revenue related to a particular project or if it expects to incur a loss on the project.

All fees billed to clients for shipping and handling are classified as product revenue. All costs associated with shipping and handling are classified as cost of product revenue.

Product Updates, Technical Support and Services Revenue

Product updates, technical support and services revenue represents fees associated with the sale of product updates, training, and technical support, all except technical support provided on a when-and-if-available basis under our maintenance agreement. Payments for product updates, technical support and services on initial order or on renewal are generally made in advance and are nonrefundable. Product updates consist of the right to unspecified software updates on a when-and-if-available basis and are typically entered into in connection with the initial product purchase. Product updates, technical support and services may be renewed upon expiration of the term. Customers can purchase product updates separately from technical support and services. Revenue from product updates, technical support and services is deferred and recognized as revenue on a straight-line basis over the term of the maintenance agreement.

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We allocate revenue under multiple-element arrangements, which typically include product, consulting services, training and maintenance agreements sold together, to each element in the arrangement primarily using the residual method based upon the fair value of the undelivered elements, which is specific to our vendor-specific objective evidence of fair value, or VSOE. This means that we defer revenue from the arrangement fee equivalent to the fair value of the undelivered elements. We apply discounts, if any, to the delivered elements, usually product, under the residual method. For periodic unspecified product updates and technical support agreements, VSOE is based upon either the renewal rate specified in each contract or the price charged when sold separately. For consulting services and training for customers without a current maintenance agreement, VSOE is based upon the rates charged for these services when sold separately.

If we are unable to establish VSOE for an undelivered post contract support, or PCS, element, for example, in a two-year term license where the license term and PCS are coterminous and no PCS renewal period exists, all revenue is recognized ratably over the contract period. For income statement classification purposes, our allocation methodology is based on VSOE of fair value for our professional services which is determined by the price charged when sold separately, and the contractually stated renewal rates for our PCS, generally 18% to 21% of the license fee paid on perpetual licenses. We use the residual method to allocate any remaining arrangement fee to product revenue.

Professional Services Revenue

Professional services revenue consists of fees from consulting services and training for customers without a current maintenance agreement and is recognized as the services are performed. When we enter into consulting service arrangements that include significant modifications to the software that are essential to the customer s use and the arrangement is bundled with software, we recognize revenue under the entire arrangement under the percentage-of-completion method. For income statement classification purposes, we have developed a revenue allocation methodology for these arrangements that is consistent with the residual method used, and described under ASC 605-985, when services are not essential to the functionality of the software. In these circumstances, we allocate revenue to the various elements of the arrangement based on our VSOE of fair value and the residual amount is allocated to product revenue.

We sell product, product updates, technical support and services agreements to distributors at predetermined prices. Sales to distributors are not contingent upon resale of the software to the end user. In most cases, we provide product updates, technical support and services agreements directly to distributors and the distributors provide support to the end customer. We record revenue from sales to distributors at the amounts charged to the distributor and in the same manner as product, product updates, technical support and services sales sold through our direct sales force. We classify amounts received in advance of revenue recognition as deferred revenue.

Sales taxes and other taxes collected from customers and remitted to governmental authorities are presented on a net basis and, as such, are excluded from revenues.

Income Taxes. We account for income taxes in accordance with ASC 740, Income Taxes. The income tax provision includes income taxes currently payable plus the net change during the year in deferred tax assets or liabilities. Under ASC 740, deferred tax assets and liabilities reflect the differences between the carrying value under GAAP and the tax basis of assets and liabilities using enacted statutory tax rates in effect for the period in which the differences are expected to reverse. Judgments and estimates are required in the calculation of the deferred tax assets, valuation allowance, research and development tax credits, and foreign tax credits.

ASC 740 prescribes a recognition threshold of more-likely-than-not, and a measurement attribute for all tax positions taken or expected to be taken on a tax return, in order for these positions to be recognized in the financial statements. We continually review tax laws, regulations and guidance in order to properly record any uncertain tax positions. At March 31, 2010, the gross unrecognized benefit related to uncertain tax benefits was $786,000, $761,000 of which would favorably affect the effective income tax rate in future periods. The total amount of gross unrecognized tax benefits related to uncertain tax positions as of April 1, 2009 was $804,000. Of this total, $775,000 represents the amount of unrecognized tax benefits, net of federal benefit on state issues that, if recognized, would favorably affect the effective income tax rate in any future periods. A reconciliation of the beginning and ending amount of unrecognized tax benefits for fiscal 2010, 2009, and 2008 follows:

	2010	2009	2008
		(in thousands)	
Beginning balance	$ 804	$ 838	$ 810
Gross decreases tax positions in prior period	45		(80)
Gross increases current period tax positions	150	139	79
Settlements	(19)		
Lapse of statute of limitations	(197)	(159)	
Foreign currency translation adjustment	3	(14)	29
Ending balance	$ 786	$ 804	$ 838

The following table summarizes the tax years that are either currently under audit or remain open under the statute of limitations and are subject to examination by the tax authorities in the most significant jurisdictions that we operate:

Australia	FY06	FY09
Belgium	FY07	FY09
France	FY06	FY09
Germany	FY05	FY09
Singapore	FY08	FY09
United Kingdom	FY08	FY09
United States	FY07	FY09
Maryland	FY06	FY09

We are currently under an income tax audit in Germany for fiscal years 2005 through 2007 and in the United States for fiscal year 2007.

Our continuing practice is to recognize interest, if any, related to income tax matters in interest expense in our consolidated statements of operations and penalties as part of general and administrative expense in our consolidated statements of operations. During fiscal 2010, we recognized $6,000 in potential interest expense associated with uncertain tax positions and reversed $13,000 associated with potential claims now barred by the statute of limitations. During fiscal 2009, we recognized $4,000 in potential interest expense associated with uncertain tax positions and reversed $17,000 associated with potential claims now barred by the statute of limitations. The total accrued interest and accrued penalties related to uncertain tax positions at March 31, 2010 was $7,000 and $26,000, respectively.

We believe it is reasonably possible that significant changes in the liability for uncertain tax positions will occur in the next twelve months as a result of final decisions related to the voluntary payments of our state and local income taxes and lapse of statute of limitations. In the aggregate, we believe the liability for uncertain tax positions could decrease by $340,000 in the next twelve months.

Stock-Based Compensation. ASC 718 Compensation Stock Compensation requires an entity to recognize an expense within its income statement for all share-based payment arrangements, which include employee stock option plans, restricted stock grants, and employee stock purchase plans. We have elected to use straight-line amortization of stock-based compensation expense for the entire award over the service period since the awards have only service conditions and graded vesting. Our stock options and nonvested stock do not contain performance conditions. There have been no modifications to awards in 2010 or 2009.

Our stock option grants are accounted for as equity awards. The expense is based on the grant-date fair value of the options granted, which we recognize over the requisite service period.

To estimate the grant-date fair value of our stock options, we use the Black-Scholes option-pricing model. The Black-Scholes model estimates the per share fair value of an option on its date of grant based on the following: the option s exercise price; the price of the underlying stock on the date of grant; the estimated dividend yield; a risk-free interest rate; the estimated option term; and the expected volatility. For the risk-free interest rate, we use a U.S. Treasury bond due in a number of years equal to the option s expected term. To estimate expected volatility, we analyze the historic volatility of our common stock. We granted 275,000 stock options during fiscal 2010. As of March 31, 2010, nonvested stock-based deferred compensation associated with the stock options totaled $916,000, which we expect to recognize over a weighted average period of 2 years.

We recognize compensation cost for stock option grants on a straight-line basis over the requisite service period for the entire award from the date of grant through the period of the last separately vesting portion of the grant. We recognize compensation cost within the income statement in the same expense line as the cash compensation paid to the respective employees. ASC 718 also requires us to estimate forfeitures in calculating the expense related to stock-based compensation. We have concluded that our historical forfeiture rate is the best measure to estimate future forfeitures of granted stock options. We will recognize the impact on compensation cost due to changes in the expected forfeiture rate of 10% in the period that they become known. We do not apply a forfeiture rate to the options granted to certain key executives or directors. We have concluded that historically certain key executives and directors will perform the requisite service to vest in the award.

We account for our restricted stock grants as equity awards. The expense is based on the price of our common stock, and is recognized on a straight-line basis over the requisite service period. The restricted stock agreements do not contain any post-vesting restrictions. We have concluded that our historical forfeiture rate is the best measure to estimate future forfeitures of granted stock options. As of March 31, 2010, nonvested stock-based deferred compensation associated with restricted stock totaled $1.2 million, which we expect to recognize over a weighted average period of 1 year.

Our 2000 Employee Stock Purchase Plan, or ESPP, provides all eligible employees to collectively purchase up to a total of 3,070,000 shares of our common stock. On September 14, 2009, our stockholders voted to increase the number of shares authorized for issuance under the ESPP from 820,000 shares to 3,070,000 shares, effective February 1, 2010. An employee may authorize a payroll deduction up to a maximum of 10% of his or her compensation during the plan period. The purchase price for each share purchased is the lesser of 85% of the closing price of the common stock on the first or last day of the plan period. The plan period for the ESPP ends on the last day of January and July of each year. To estimate the fair value of shares issued under our ESPP, we use the Black-Scholes option-pricing model. The Black-Scholes model estimates the per share fair value of an ESPP share at the beginning of the plan period based on the following: the price of the underlying stock on the first day of the plan period; the estimated dividend yield; a risk-free interest rate; the term of the plan period, which is six months; and the expected volatility. For the risk-free interest rate, we use a U.S. Treasury Bond due in six months. To determine expected volatility, we analyze the historical volatility of our stock over the 6 months prior to the first day of the plan period. We calculate the expense based on the difference between the fair market value of the shares purchased at the close of each plan period and the discounted price paid by the employee, and we recognize that expense on a straight-line basis over the plan period. As of March 31, 2010, nonvested stock-based deferred compensation associated with the ESPP totaled $139,000 and we expect to recognize over a weighted average period of 4 months.

Cash, Cash Equivalents, and Marketable Securities. We measure our cash and cash equivalents using the fair value measurement principles of ASC 820 Fair Value Measurements and Disclosures, or ASC 820, which requires that fair value be based on the assumptions that market participants would use when pricing an asset or liability. ASC 820 requires disclosures regarding the manner in which fair value is determined for assets and

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liabilities and establishes a three-tiered value hierarchy into which these assets and liabilities must be grouped, based upon significant levels of inputs as follows:

Level 1 Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 Observable inputs, other than Level 1 prices, such as quoted prices in active markets for similar assets and liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable inputs.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

The lowest level of significant input determines the placement of the entire fair value measurement in the hierarchy. We view corporate notes as Level 2 assets, and money market funds as Level 1 assets. We did not hold any marketable securities at March 31, 2010.

The following table summarizes the composition of our marketable securities at March 31, 2009:

	March 31, 2009 (in thousands)				Classification on Balance Sheet	
	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Market Value	Short-Term Investments	Long-Term Investments
Corporate notes	$ 999	$	$	$ 999	$ 999	$
Total marketable securities	$ 999	$	$	$ 999	$ 999	$

The following table details the fair value measurements within the three levels of fair value hierarchy of our financial assets, consisting of cash, cash equivalents, and marketable securities, at March 31, 2010 and 2009:

	Total Fair Value At March 31, 2010	Fair Value Measurement at March 31, 2010 Using		
		Level 1	Level 2	Level 3
		(in thousands)		
Cash	$ 21,545	$ 21,545	$	$
Money market funds	83,136	83,136		
Total	$ 104,681	$ 104,681	$	$

	Total Fair Value At March 31, 2009	Fair Value Measurement at March 31, 2009 Using		
		Level 1	Level 2	Level 3
		(in thousands)		
Cash	$ 11,759	$ 11,759	$	$

Money market funds	79,231	79,231		
Corporate note	999		999	
Total	$ 91,989	$ 90,990	$ 999	$

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At March 31, 2010, we grouped money market funds using a Level 1 valuation because market prices in active markets for identical assets were readily available. The per-share net asset value of our money market funds has remained at a constant amount of $1.00 per share. Also, as of March 31, 2010, there were no withdrawal limits on redemptions for any of the money market funds that we hold. All money market funds were classified as cash and cash equivalents at March 31, 2010 and 2009. We did not group any financial assets using Level 2 or Level 3 valuations at March 31, 2010.

Allowance for Doubtful Accounts. We maintain an allowance for doubtful accounts receivable for estimated losses resulting from the inability of our customers to make required payments and for the limited circumstances when the customer disputes the amounts due us. Our methodology for determining this allowance requires significant estimates. In estimating the allowance, we consider the age of the receivable, the creditworthiness of the customer, the economic conditions of the customer s industry and general economic conditions. While we believe that the estimates we use are reasonable, should any of these factors change, our estimates may also change, which could affect the amount of our future allowance for doubtful accounts as well as future operating income. Specifically, if the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments to us, additional allowances could be required. As of March 31, 2010 and 2009, accounts receivable totaled $32.8 million and $29.6 million, net of an allowance for doubtful accounts of $336,000 and $713,000, respectively.

Valuation of Intangible Assets and Goodwill. We account for our goodwill and intangible assets in accordance with ASC 805, Business Combinations and ASC 350, Intangibles Goodwill and Other. Our intangible assets consist of acquired technology related to our acquisitions of a software product for modeling voice communications in December 2003, Altaworks in October 2004, purchased technology we purchased from RadView Software, Ltd. in December 2005, SQMworks, Inc. in April 2006 and Network Physics, Inc. in October 2007. Our intangible assets also consist of customer relationships and acquired workforce assets we purchased from Network Physics, Inc. related to the purchase of specified assets of Network Physics in October 2007. The acquired and purchased technologies are stated at the lower of unamortized cost or net realizable value and are amortized on a straight-line basis over their expected useful lives of three to five years. We amortize our customer relationship and workforce intangible assets we purchased from Network Physics, Inc. on an accelerated depreciation basis over their expected useful lives of four and one half years and five years, respectively.

We use the projected discounted cash flow method in valuing our acquired technology and purchased customer relationships using certain assumptions including revenue growth, cost levels, present value discount rate, and working capital requirements. We use the lower of the amount of cash paid or the present value of projected discounted cash flows to value purchased technology. We valued the workforce asset associated with the purchase of specified assets of Network Physics, Inc. on a replacement cost basis. While we believe the assumptions used to value our acquired technology related to acquisitions are reasonable, actual results will likely differ from those assumptions. Future cash flows are subject to change for a variety of internal and external factors. We will periodically review the value of acquired technology and purchased intangible assets for reasonableness in accordance with ASC 360, Property, Plant and Equipment. If changes in our assumptions at the time of future periodic reviews indicate that the carrying value of our acquired technology and purchased intangible assets exceeds their fair value and we determine that carrying amounts can not be recovered, it would result in impairment losses. As of March 31, 2010 and 2009, intangible assets totaled $5.1 million and $6.2 million, net of accumulated amortization of $9.7 million and $7.7 million, respectively. We have not recorded any impairment losses to date.

We record goodwill when the consideration paid for acquisitions exceeds the fair value of net tangible and intangible assets acquired. Goodwill is not amortized. We perform an annual review in the fourth quarter to identify any facts or circumstances that indicate the carrying value of goodwill is impaired. The review is based on various analyses including cash flow and profitability projections and the market capitalization of our common stock. Impairment, if any, is based on the excess of the carrying amount of goodwill over its fair value.

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We performed our annual impairment test of goodwill as of March 31, 2010 and 2009 and concluded that the fair value substantially exceeded the carrying value; therefore, we did not record any impairment. As of March 31, 2010 and 2009, goodwill was $14.6 million. No impairment losses have been recorded to date.

Accounting for Software Development Costs. We expense costs incurred in the research and development of new software products as incurred until technological feasibility is established. Development costs are capitalized beginning when a product s technological feasibility has been established and ending when the product is available for general release to our customers. Technological feasibility is reached when the product reaches the working model stage. To date, products and enhancements have generally reached technological feasibility and have been released for sale at substantially the same time and all research and development costs have been expensed. Consequently, we did not capitalize any research and development costs in fiscal 2010, 2009 or 2008.

Results of Operations

The following table sets forth items from our consolidated statements of operations expressed as a percentage of total revenue for the periods indicated:

	Fiscal 2010	Fiscal 2009	Fiscal 2008
Revenue:			
Product	41.4%	41.7%	38.3%
Product updates, technical support and services	37.4	35.0	34.3
Professional services	21.2	23.3	27.4
Total revenue	100.0	100.0	100.0
Cost of revenue:			
Product	4.7	2.9	1.0
Product updates, technical support, and services	3.8	3.8	4.4
Professional services	15.3	17.0	18.9
Amortization of acquired technology	1.5	1.8	1.5
Total cost of revenue	25.3	25.5	25.8
Gross profit	74.7	74.5	74.2
Operating expenses:			
Research and development	25.4	25.1	27.1
Sales and marketing	34.2	34.6	38.9
General and administrative	8.7	9.6	11.6
Total operating expenses	68.3	69.3	77.6
Income (loss) from operations	6.4	5.2	(3.4)
Interest and other income, net	0.0	1.0	3.5
Income before provision (benefit) for income taxes	6.4	6.2	0.1
Provision (benefit) for income taxes	1.8	2.3	(0.4)
Net income	4.6%	3.9%	0.5%

Revenue

Product Revenue. Product revenue was $52.3 million, $51.2 million, and $38.8 million, in fiscal 2010, 2009, and 2008, respectively, representing an increase of 2.0% in fiscal 2010 from fiscal 2009 and an increase of 31.9% in fiscal 2009 from fiscal 2008. For fiscal 2010, the increase in product revenue was primarily due to an increase in sales to United States government customers and corporate enterprise customers, partially offset by a decrease in sales to service providers and network equipment manufacturers. For fiscal 2009, the increase in product revenue was primarily due to an increase in sales to corporate enterprise customers and service providers. The increase in fiscal 2010 and 2009 was primarily due to an increase in revenue from sales of our application performance management products.

Product Updates, Technical Support and Services Revenue. Product updates, technical support and services revenue was $47.3 million, $43.1 million, and $34.8 million, in fiscal 2010, 2009, and 2008, respectively, representing increases of 9.7% in fiscal 2010 from fiscal 2009 and 23.8% in fiscal 2009 from fiscal 2008. Product updates, technical support and services revenue growth rates are affected by the overall product revenue growth rates, as well as the renewal rate of annual maintenance contracts by existing customers. The increase in product updates, technical support and services revenue in fiscal 2010 and fiscal 2009 primarily reflected increases in the overall customer installed base as compared to the prior fiscal year. Increases in the overall customer installed base increase the demand for annual renewals of maintenance contracts.

The dollar amount of our deferred revenue under our maintenance contracts at the end of each year is a key factor in determining the near-term growth of our product updates, technical support and services revenue. The balance of deferred revenue under our maintenance contracts generally increases when we sell product licenses and when we sell renewals of annual maintenance contracts. The amount of deferred revenue under our maintenance contracts was $35.5 million, $29.0 million, and $24.0 million at March 31, 2010, 2009, and 2008, respectively. The amount of deferred revenue under our maintenance contracts will generally be recognized as product updates, technical support and services revenue over the life of each individually purchased maintenance contract, which is typically a twelve-month period.

Professional Services Revenue. The components of professional services revenue for fiscal 2010, 2009, and 2008 were as follows:

	Fiscal 2010	Fiscal 2009	Fiscal 2008
		(in thousands)	
Consulting services	$ 26,399	$ 27,949	$ 27,099
Training and other revenue	432	652	622
Professional services	$ 26,831	$ 28,601	$ 27,721

Professional services revenue was $26.8 million, $28.6 million, and $27.7 million in fiscal 2010, 2009, and 2008, respectively, representing a decrease of 6.2% in fiscal 2010 from fiscal 2009 and an increase of 3.2% in fiscal 2009 from fiscal 2008. Consulting services revenue accounted for 98.4%, 97.7%, and 97.8%, of professional services revenue for fiscal 2010, 2009, and 2008, respectively. For fiscal 2010, the decrease in professional services revenue was primarily due to a decrease in billable hours worked on projects related to corporate enterprise customers and service providers. We believe the decrease in billable hours worked in fiscal 2010 was related to the increase in the proportion of sales of our application performance management products as compared to our other products, as our application performance management products generally require less consulting services to implement. For fiscal 2009, the increase in professional services revenue was primarily due to an increase in billable hours worked on projects related to service providers and, to a lesser extent, corporate enterprise customers. The percentage of total consulting revenue from United States government customers for fiscal 2010, fiscal 2009, and fiscal 2008 was 70.4%, 65.8%, and 68.8%, respectively, representing an increase of 1.1% in fiscal 2010 from fiscal 2009, and a decrease of 1.4% in fiscal 2009 from fiscal 2008.

Training and other revenue was $432,000, $652,000, and $622,000 in fiscal 2010, 2009 and 2008, respectively. The decrease in training and other revenue in fiscal 2010 as compared to fiscal 2009 was the result of a decrease in custom trainings. The increase in training revenue in fiscal 2009 as compared to fiscal 2008 was due to increased sales of our training services to service providers, which was offset by a decrease in sales to corporate enterprise customers.

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International Revenue. Our international revenue increased 9.3% to $28.4 million, or 22.5% of total revenue, in fiscal 2010 from $26.0 million, or 21.1% of total revenue, for fiscal 2009. Our international revenue increased 2.2% during fiscal 2008 from $20.5 million, or 20.2% of total revenue, for fiscal 2008. The increase in international revenue in fiscal 2010 was primarily the result of an increase in sales to international corporate enterprise customers, which was partially offset by a decrease in sales to international network equipment manufacturers. The increase in international revenue in fiscal 2009 was primarily the result of an increase in sales to international government customers and service providers, which was partially offset by a decrease in sales to international corporate enterprise customers. Our international revenue is primarily generated in Europe and Asia. Our goal is to increase sales to international corporate enterprise customers. International revenue from corporate enterprises comprised the largest portion of international revenue for fiscal 2010. During each of fiscal 2010, 2009, and 2008, we expanded our operations outside the United States through the hiring of additional direct sales persons in our foreign subsidiaries.

Cost of Revenue

The following table sets forth, for each component of revenue, the cost of the revenue as a percentage of the related revenue for the periods indicated:

	Fiscal 2010	**Fiscal 2009**	**Fiscal 2008**
Cost of product	11.5%	6.9%	2.7%
Cost of product updates, technical support, and services	10.3	10.8	13.0
Cost of professional services	72.0	73.1	69.1

Cost of product revenue consists primarily of the cost of hardware platforms associated with the delivery of some software products, royalties and, to a lesser extent, media, manuals, and distribution costs. Cost of product updates, technical support and services revenue consists of personnel-related costs necessary to provide technical support and training to customers with active maintenance contracts on a when-and-if-available basis, royalties, media, and distribution costs. Cost of professional services revenue consists primarily of personnel-related costs necessary to provide consulting and training to customers without active maintenance contracts. Gross margins on product revenue and product updates, technical support and services revenue are substantially higher than gross margin on professional services revenue, due to the low cost of delivering product revenue and providing technical support and maintenance compared with the relatively high personnel costs associated with providing consulting services and customer training.

Cost of Product Revenue. Cost of product revenue was $6.0 million, $3.5 million, and $1.0 million in fiscal 2010, 2009, and 2008, respectively. The 69.2% increase in costs from fiscal 2009 to fiscal 2010 was primarily the result of a $2.5 million increase in costs related to hardware platforms used to deliver our ACE Live software products. The 241.6% increase in costs and the decrease in gross margin for fiscal 2009 as compared to fiscal 2008 was primarily the result of a $2.1 million increase in the cost of hardware platforms associated with delivery of our ACE live software products. We began selling ACE Live software products, which are typically delivered on hardware platforms, in the third fiscal quarter of fiscal 2008. Total hardware platform costs related to the delivery of our ACE Live software products for fiscal 2010, fiscal 2009, and fiscal 2008 were $4.9 million, $2.4 million, and $383,000 respectively. Gross margin on product revenue was 88.6%, 93.1%, and 97.3%, for fiscal 2010, 2009, and 2008, respectively.

Cost of Product Updates, Technical Support and Services Revenue. Cost of product updates, technical support and services revenue was $4.9 million, $4.7 million, and $4.5 million in fiscal 2010, 2009, and 2008, respectively. Gross margin on product updates, technical support and services revenue was 89.7%, 89.2%, and 87.0%, for fiscal 2010, 2009, and 2008, respectively. The 4.2% increase in cost of product updates, technical support and services revenue for fiscal 2010 as compared to fiscal 2009 was primarily the result of a $93,000 increase in personnel costs necessary to provide technical support and a $35,000 increase in the cost of supplies necessary to support our products. The 3.3% increase in cost of product updates, technical support and services revenue for fiscal 2009 as compared to fiscal 2008 was primarily the result of an $82,000 increase in personnel costs necessary to provide technical support and a $42,000 increase in royalty payments required for some of our product update sales. The increase in gross margin on product updates, technical support and services revenue for fiscal year 2010 as compared to 2009 was primarily the result of a 9.7% increase in product license updates, technical support and services revenue. The increase in gross margin on product updates, technical support and services revenue for fiscal year 2009 as compared to 2008 was primarily the result of a 23.8% increase in product updates, technical support and services revenue. Stock-based compensation expense included in cost of product updates, technical support and services was $17,000, $20,000, and $21,000 for fiscal 2010, 2009, and 2008, respectively.

Cost of Professional Services Revenue. Cost of professional services revenue was $19.3 million, $20.9 million, and $19.2 million in fiscal 2010, 2009, and 2008, respectively. Gross margin on professional services revenue increased to 28.0% for fiscal 2010 from 26.9% in fiscal 2009. Gross margin on professional services revenue decreased to 26.9% for fiscal 2009 from 30.9% for fiscal 2008. The 7.6% decrease in cost of professional services revenue in fiscal 2010 from fiscal 2009 was largely due to a $1.3 million decrease in direct labor expense attributable to a decrease in the number of consulting personnel in response to weaker demand for our consulting services. We believe the weaker demand for our consulting services during fiscal 2010, as compared to fiscal 2009, was due to the increase in the proportion of sales of our application performance management products to sales of our other products, as our application performance management products generally require less time to implement. The 9.2% increase in cost of professional services in fiscal 2009 from fiscal 2008 was largely due to a $1.8 million increase in direct labor expense attributable to the use of more external contractors. The increase in gross margin on professional services in fiscal 2010 from fiscal 2009 was primarily due to the increase in profitability related to certain consulting engagements. The decrease in gross margin on professional services in fiscal 2009 from fiscal 2008 was primarily due to the increase in direct labor costs. We expect the cost of professional services revenue as a percentage of professional services revenue to vary based primarily on the profitability of individual consulting engagements. Stock-based compensation expense included in cost of professional services was $83,000, $113,000, and $148,000 for fiscal 2010, 2009, and 2008, respectively.

Operating Expenses

Research and Development. Research and development expenses were $32.0 million, $30.8 million, and $27.5 million in fiscal 2010, 2009, and 2008, respectively, representing increases of 4.1% in fiscal 2010 from fiscal 2009 and 12.1% in fiscal 2009 from fiscal 2008. The increase in fiscal 2010 from fiscal 2009 was primarily due to a $1.6 million increase in compensation expense as a result of increased staffing levels required for developing new products as well as sustaining and upgrading existing products, which was partially offset by a $305,000 decrease in contractor costs. The increase in fiscal 2009 from fiscal 2008 was primarily due to a $3.1 million increase in compensation expense as a result of increased staffing levels. We do not capitalize research and development costs since we release our products to the market at the same time that technological feasibility is reached. Stock-based compensation expense included in research and development was $676,000, $591,000, and $568,000 for fiscal 2010, 2009, and 2008, respectively.

Sales and Marketing. Sales and marketing expenses were $43.2 million, $42.5 million, and $39.4 million in fiscal 2010, 2009, and 2008, respectively. The 1.5% increase in fiscal 2010 from fiscal 2009 was due to a $2.2 million increase in compensation and commission expense as a result of increased staffing levels and higher bookings, travel costs of $337,000 and depreciation expense of $239,000, which were partially offset by a reduction in conference and marketing expenditures of $2.2 million. The 8.1% increase in fiscal 2009 from fiscal 2008 was due to a $3.5 million increase in compensation and commission expense as a result of increased staffing levels and increased sales, which was partially offset by a $265,000 reduction in travel expenses and a $217,000 reduction in marketing costs. Stock-based compensation expense included in sales and marketing was $343,000, $376,000, and $374,000 for fiscal 2010, 2009, and 2008, respectively.

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General and Administrative. General and administrative expenses were $11.0 million, $11.9 million, and $11.7 million, in fiscal 2010, 2009, and 2008, respectively. The 7.1% decrease in fiscal 2010 from fiscal 2009 was largely due to a decrease in compensation expense and bad debt expense. The 0.9% increase in fiscal 2009 from fiscal 2008 was largely due to an increase in bad debt expense and compensation expense partially offset by a decrease in professional services costs. Stock-based compensation expense included in general and administrative was $440,000, $433,000, and $428,000 for fiscal 2010, 2009, and 2008, respectively.

Interest and Other (Expense) Income, net. Interest and other (expense) income, net were negative $70 thousand, $1.2 million, and $3.6 million in fiscal 2010, 2009, and 2008, respectively. The 105.6% decrease in fiscal 2010 from fiscal 2009 was primarily the result of a decrease in the interest rates earned on our investment holdings. The 65.2% decrease in fiscal 2009 from fiscal 2008 was primarily the result of a change in our portfolio holdings to predominantly United States government-backed money market funds from a mix of United States government-backed money market funds and investment grade marketable securities and, to a lesser extent, a decrease in the interest rates earned on our investment holdings.

Provision for Income Taxes. Our effective tax rates were 27.5%, 38.2%, and negative 231% for fiscal 2010, 2009, and 2008, respectively. For fiscal 2010, the effective tax rate differed from the statutory tax rate principally due to state income taxes, differential in the United States and foreign tax rates, research and development credits and the domestic production activities deduction. The decrease in our effective tax rate in fiscal 2010 from fiscal 2009 was primarily due to an increase in tax credits and a decrease in foreign tax expense. The increase in our effective tax rate in fiscal 2009 from fiscal 2008 was primarily due to an increase in our book income which diluted the impact of permanent differences as compared to the same periods in the prior fiscal year. The effective tax rate differs from the statutory tax rate and varies from period to period due principally to the amount of income before taxes from various tax jurisdictions, tax-exempt interest income, foreign tax expense, and the amount of tax credits available to us in each period from incremental research expenditures. Future provisions for taxes will depend, among other things, on the mix and amount of worldwide income, the tax rates in effect for various tax jurisdictions and the amount of research and development tax credits, foreign tax credits and other items for which we are eligible.

Liquidity and Capital Resources

As of March 31, 2010 and 2009, we had cash, cash equivalents, short-term and long-term marketable securities totaling $104.7 million and $92.0 million, respectively. Due to our available cash balances and our anticipated cash flows, we do not believe that the current credit crisis will have a material impact on our operational cash requirements.

Cash provided by operating activities was $21.8 million, $12.1 million, and $12.9 million for fiscal 2010, 2009, and 2008, respectively. Cash provided by operating activities is primarily derived from net income, as adjusted for non-cash items such as depreciation and amortization expense, tax benefits from the exercise of employee stock options, and changes in operating assets and liabilities. The increase in cash provided by operating activities in fiscal 2010 from fiscal 2009 was primarily attributable to increases in deferred revenue and net income in fiscal 2010, as compared to fiscal 2009, which were slightly offset by a decrease in accrued liabilities. The decrease in cash provided by operating activities in fiscal 2009 from fiscal 2008 was primarily attributable to an increase in accounts receivable and a decrease in the growth of deferred revenue during fiscal 2009, as compared to fiscal 2008, which was partially offset by an increase in cash resulting from an increase in net income and accrued liabilities.

Net cash used in investing activities was $2.6 million in fiscal 2010. Net cash provided by investing activities was $8.3 million and $27.3 million in fiscal 2009 and fiscal 2008, respectively. Investing activities include the purchase, sale or maturity of marketable securities, acquisition of property and equipment, and net expenditures for business combinations and technology acquisitions. For fiscal 2010, we used funds of $3.1 million to purchase property and equipment, and funds of $433,000 to acquire technology. We received proceeds of $1.0 million from the maturity of investments. For fiscal 2009, we used funds of $999,000 to purchase short-term marketable securities, and funds of $5.5 million to purchase property and equipment. We received proceeds

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of $14.8 million from the sale or maturity of short-term and long-term marketable securities for fiscal 2009. For fiscal 2008, we used funds of $10.0 million to purchase specified assets from Network Physics, funds of $114.8 million to purchase short-term and long-term marketable securities, and funds of $4.6 million to purchase property and equipment. We received proceeds of $156.6 million from the sale or maturity of short-term marketable securities for fiscal 2008.

Cash used in financing activities was $5.7 million in fiscal 2010. Cash provided by financing activities was $861,000 in fiscal 2009. Cash used in financing activities was $3.6 million for fiscal 2008. We used $7.5 million during fiscal 2010 to pay a quarterly cash dividend of $0.09 per share to stockholders of record on June 15, 2009, September 15, 2009, December 15, 2009, and March 15, 2010. We used cash of $2.3 million, $955,000, and $5.0 million to acquire 186,550, 75,724, and 521,849 shares of our common stock pursuant to our stock repurchase program during fiscal 2010, fiscal 2009, and fiscal 2008, respectively. During fiscal 2010, fiscal 2009, and fiscal 2008, 26,352, 15,724 and 6,474 shares, respectively, were withheld from employees to satisfy the minimum statutory tax withholding obligations with respect to the income recognized by these employees upon the vesting of their restricted stock shares during the period. Cash provided by financing activities generally reflects the proceeds received from the exercise of stock options and the sale of common stock under our employee stock purchase plan. During fiscal 2010, 2009, and 2008, we received proceeds of approximately $2.7 million, 644,000, and $365,000, respectively, and issued 277,110, 92,648, and 59,975 shares of common stock, pursuant to employee and director exercises of stock options. During fiscal 2010, 2009, and 2008, we received proceeds of approximately $1.3 million, $1.1 million and $989,000, respectively, and issued 170,271, 150,712, and 120,295 shares of common stock, respectively, pursuant to the issuance of common stock under our employee stock purchase plan. Excess tax benefits from the exercise of stock options are presented as a cash flow from financing activities. For fiscal 2010, 2009, and 2008, excess tax benefits from the exercise of stock options were $51,000, $49,000, and $29,000, respectively.

We have commitments under contractual arrangements to make future payments for goods and services. These contractual arrangements secure the rights to various assets and services to be used in the future in the normal course of business. For example, we are contractually committed to make minimum lease payments for the use of property under operating lease agreements. In accordance with current accounting rules, the future rights and related obligations pertaining to such contractual arrangements are not reported as assets or liabilities on our consolidated balance sheets. Our liability for unrecognized tax benefits under ASC 740 is reported on our consolidated balance sheets. We expect to fund these contractual arrangements with our cash, cash equivalents and marketable securities as well as cash generated from operations in the normal course of business.

The following table summarizes our contractual operating lease arrangements and our liability for unrecognized tax benefits at March 31, 2010, and the timing and effect that such commitments are expected to have on our liquidity and cash flow in future periods.

Contractual Obligations and Unrecognized Tax Benefits		**Payments Due by Period**			
(in thousands)	**Total**	**Fiscal 2011**	**Fiscal 2012 Fiscal 2013**	**Fiscal 2014 Fiscal 2015**	**After Fiscal 2015**
Facilities Operating Lease Obligations	$ 19,921	$ 4,913	$ 4,095	$ 3,425	$ 7,488
Other Operating Lease Obligations	103	79	24		
Unrecognized Tax Benefits	786	340	130	316	
Total	$ 20,810	$ 5,332	$ 4,249	$ 3,741	$ 7,488

See Notes 9 and 10 to our consolidated financial statements for additional information related to our operating leases. As of March 31, 2010, we had no capital lease obligations.

Effective June 10, 2002, we entered into a credit facility with a commercial bank. The credit facility permitted the use of funds for general corporate purposes and the issuance of letters of credit up to a maximum of

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$10.0 million in the aggregate. As of March 31, 2010, the lender under our credit facility had issued letters of credit in favor of the beneficiaries under a number of our operating leases in the aggregate amount of $1.1 million. Upon a default, as defined in the respective office lease agreement, the applicable landlord has the right to draw upon its letter of credit in whole or in part. Interest under this facility, including interest on any amounts drawn under the letters of credit, is payable monthly at an annual rate of 1.25%. The credit facility is collateralized by our accounts receivable. Effective March 31, 2009, in light of our strong cash position, we elected to eliminate any borrowing capacity under the credit facility in excess of our existing outstanding letters of credit.

We expect working capital needs to increase in the foreseeable future in order for us to execute our business plan and growth strategies. We anticipate that operating activities, as well as expected capital expenditures incurred in the normal course of business, will constitute a material use of our cash resources. In addition, we may utilize cash resources to fund acquisitions or investments in complementary businesses, technologies or products as well as repurchase our common stock in accordance with our stock repurchase program authorized by our Board in January 2005, and the payment of dividends to our stockholders.

We believe that our current cash and cash equivalents, marketable securities, and cash generated from operations will be sufficient to meet our anticipated cash requirements for working capital, capital expenditures, and dividends at least through fiscal 2011.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements with unconsolidated entities or related parties and, accordingly, there are no off-balance sheet risks to our liquidity and capital resources from unconsolidated entities.

Recently Issued Accounting Pronouncements

In June 2009, the Financial Accounting Standards Board, or FASB, approved the FASB Accounting Standards Codification (Accounting Standards Update, or ASU, 2009-01), or the Codification, as the single source of authoritative non-government GAAP. All existing accounting standard documents, such as FASB, American Institute of Certified Public Accountants, Emerging Issues Task Force and other related literature, excluding guidance from the Securities and Exchange Commission, or SEC, have been superseded by the Codification. All other non-grandfathered, non-SEC accounting literature not included in the Codification has become non-authoritative. The Codification did not change GAAP, but instead introduces a new structure that combines all authoritative standards into a comprehensive, topically organized online database. We adopted the Codification on July 1, 2009, which impacts our financial statements as all future references to authoritative accounting literature have been referenced in accordance with the Codification. There have been no changes to the content of our financial statements or disclosures as a result of implementing the Codification.

In June 2008, the FASB issued FASB Staff Position No. EITF 03-6-1, Determining Whether Instruments Granted in Share-Based Payment Transactions are Participating Securities (as codified in ASC 260 Earnings per Share), or FSP No. EITF 03-6-1. FSP No. EITF 03-6-1 states that unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings per share, or EPS, pursuant to the two-class method. FSP EITF 03-6-1 is effective for fiscal years beginning after December 15, 2008. We applied the provisions of FSP EITF 03-6-1 in fiscal 2010. Our participating securities include nonvested restricted stock. FSP EITF 03-6-1 was applied retrospectively and therefore prior period information was adjusted.

In October 2009, the FASB issued Accounting Standards Update 2009-13 Multiple Deliverable Revenue Arrangements, or ASU 2009-13 which amends EITF Issue No. 08-1, Revenue Arrangements With Multiple Deliverables (as codified in ASC 605 Revenue Recognition) and EITF Issue No. 09-3, Applicability of

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AICPA Statement 97-2 to Certain Arrangements That Include Software Elements (as codified in ASC 985 Software). ASU 2009-13 amends the current guidance on arrangements with multiple elements to (1) eliminate the separation criterion that requires entities to establish objective and reliable evidence of fair value for undelivered elements, (2) establish a selling price hierarchy to help entities allocate arrangement consideration to the separate units of account, (3) require the relative selling price allocation method for all arrangements (i.e., eliminate the residual method), and (4) significantly expand required disclosures. ASU 2009-13 also amends the scoping guidance for software arrangements to exclude tangible products that contain software elements and nonsoftware elements that function together to interdependently deliver the product s essential functionality. ASU 2009-13 will be effective for the first annual reporting period beginning on or after June 15, 2010. ASU 2009-13 will be effective for us beginning April 1, 2011. Early adoption is permitted. We have not adopted ASU 2009-13, nor have we determined the impact that the adoption will have on our results of operations or financial condition.

In May 2009, the FASB issued Statement of Financial Accounting Standards, or SFAS, No. 165, Subsequent Events (as codified in ASC 855 Subsequent Events), or SFAS No. 165, to be effective for interim or annual financial periods ending after June 15, 2009. ASC 855 establishes the accounting for, and disclosure of, events that occur after the balance sheet date but before financial statements are issued or are available to be issued. See Note 19 to the consolidated financial statements for the related disclosures. Our adoption of ASC 855 did not have a material impact on our results of operations, financial position or cash flows.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

(dollars in thousands)

We consider all highly liquid investments purchased with a maturity of three months or less to be cash equivalents, and those with maturities greater than three months are considered to be marketable securities. Cash equivalents and short-term marketable securities consist primarily of investment grade securities with high credit ratings of relatively short duration that trade in highly liquid markets. Accordingly, we have no quantitative information concerning the market risks and believe that the risk is minimal. We currently do not hedge interest rate exposure, but do not believe that an increase in interest rates would have a material effect on the value of our cash equivalents or marketable securities.

At March 31, 2010, we had $104.7 million in cash and cash equivalents and did not have any short-term marketable securities. As of March 31, 2009, we had $91.0 million in cash and cash equivalents and $999,000 in short-term marketable securities. Based on our cash, cash equivalents, and marketable securities as of March 31, 2010, a one percentage point increase or decrease in interest rates would increase or decrease our annual interest income and cash flows by approximately $1.0 million.

At March 31, 2010, $83.1 million of our $104.7 million in cash and cash equivalents was held in money market funds. The money market funds are predominately backed by United States government securities. The per-share net asset value of our money market funds has remained at a constant amount of $1.00 per share. Also, as of March 31, 2010 there were no withdrawal limits on redemptions for any of the money market funds that we hold.

Our consolidated financial statements are denominated in United States dollars and, accordingly, changes in the exchange rate between foreign currencies and the United States dollar will affect the translation of our subsidiaries financial results into United States dollars for purposes of reporting our consolidated financial results. The accumulated currency translation adjustment, recorded as a separate component of stockholder s equity, was a loss of $999,000 and a loss of $1.2 million at March 31, 2010 and 2009, respectively. A majority of our revenue transactions outside the United States are denominated in local currencies and the majority of operating expenses associated with our foreign subsidiaries are denominated in local currencies; therefore, our results of operations and financial condition are subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the British pound and the European Union euro. We currently do not

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hedge foreign exchange rate risk. Approximately 22.5%, 21.1%, and 20.2% of our total revenue for fiscal 2010, fiscal 2009, and fiscal 2008, respectively, was generated from outside of the United States. Due to the limited nature of our foreign operations, we do not believe that a 10% change in exchange rates would have a material effect on our business, financial condition, or results of operations. Based on our revenue and operating expenses denominated in foreign currencies during fiscal 2010, fiscal 2009, and fiscal 2008, a 10% increase or decrease in exchange rates would increase or decrease our consolidated net income by approximately $56,000, $107,000, and $43,000, respectively.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Our financial statements together with the related notes and the report of Deloitte & Touche LLP, our independent registered public accounting firm, are set forth in the Index to Financial Statements at Item 15 of this Form 10-K.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURES

None.

ITEM 9A. CONTROLS AND PROCEDURES

Our management, with the participation of the Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the disclosure controls and procedures as of March 31, 2010. The disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of March 31, 2010, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

Managements report on our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) and the independent registered public accounting firm s related audit report on internal control over financial reporting are included in this Item 9A of this Form 10-K.

No change in our internal control over financial reporting occurred during the fiscal quarter ended March 31, 2010 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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MANAGEMENT S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of OPNET Technologies, Inc. and its subsidiaries (the Company) is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) or 15d-15(f) promulgated under the Securities Exchange Act of 1934 as a process designed by, or under the supervision of, the company s principal executive and principal financial officers and effected by the Company s Board of Directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

(i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company;

(ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorization of management and directors of the Company; and

(iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our management assessed the effectiveness of our internal control over financial reporting as of March 31, 2010. In making this assessment, our management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework. Based on our assessment and those criteria, management concluded that the Company s internal control over financial reporting was effective as of March 31, 2010.

OPNET Technologies, Inc.

June 4, 2010

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Audit Committee and Stockholders of OPNET Technologies, Inc.

Bethesda, Maryland

We have audited the internal control over financial reporting of OPNET Technologies, Inc. and its subsidiaries (the Company) as of March 31, 2010, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying *Management s Report on Internal Control Over Financial Reporting*. Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed by, or under the supervision of, the company s principal executive and principal financial officers, or persons performing similar functions, and effected by the company s board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of March 31, 2010, based on the criteria established in *Internal Control Integrated Framework issued* by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended March 31, 2010 of the Company and our report dated June 4, 2010 expressed an unqualified opinion on those consolidated financial statements.

/s/ DELOITTE & TOUCHE LLP

McLean, Virginia

June 4, 2010

ITEM 9B. OTHER INFORMATION

Not applicable.

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PART III

Certain information required by Part III is omitted from this Annual Report as we intend to file our definitive Proxy Statement for the 2010 Annual Meeting of Stockholders (the Proxy Statement) pursuant to Regulation 14A of the Securities Exchange Act of 1934, as amended, not later than 120 days after the end of the fiscal year covered by this Annual Report, and certain information included in the Proxy Statement is incorporated herein by reference.

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information in the section entitled Executive Officers and Directors of the Registrant in Part I hereof is incorporated herein by reference. The information in the sections entitled Election of Directors, Section 16(a) Beneficial Ownership Reporting Compliance and Code of Business Conduct and Ethics in the Proxy Statement is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

The information in the sections entitled Summary Compensation Table, Compensation of Directors , Compensation Committee Interlocks and Insider Participation and Compensation Discussion and Analysis in the Proxy Statement is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information in the section entitled Equity Compensation Plan Information in Part I hereof is incorporated by reference. The information in the section entitled Security Ownership of Certain Beneficial Owners and Management in the Proxy Statement is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information in the section entitled Certain Transactions in the Proxy Statement is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information in the section entitled Independent Registered Public Accounting Firm Fees and Other Matters in the Proxy Statement is incorporated herein by reference.

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PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) The following documents are filed as part of this Form 10-K:

1. Financial Statements. The following financial statements of OPNET Technologies, Inc. are filed as part of this Form 10-K on the pages indicated:

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

(b) Exhibits. The exhibits listed in the exhibits index immediately preceding such exhibits are filed as part of this Annual Report on Form 10-K.

(c) Financial Statement Schedules. Financial statement schedules are omitted as the required information is inapplicable or the information is presented in the financial statements or related notes in this Annual Report on Form 10-K.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on the 4th day of June, 2010.

OPNET TECHNOLOGIES, INC.

By: /s/ MARC A. COHEN
Marc A. Cohen

Chairman of the Board and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the 4th day of June, 2010.

Signature	Title
/s/ MARC A. COHEN **Marc A. Cohen**	Chairman of the Board of Directors and Chief Executive Officer (Principal Executive Officer)
Alain J. Cohen	President, Chief Technology Officer and Director
/s/ MEL F. WESLEY **Mel F. Wesley**	Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)
/s/ STEVEN G. FINN **Steven G. Finn, PhD**	Director
/s/ RONALD W. KAISER **Ronald W. Kaiser**	Director
/s/ WILLIAM F. STASIOR **William F. Stasior**	Director

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Audit Committee and Stockholders of OPNET Technologies, Inc.

Bethesda, Maryland

We have audited the accompanying consolidated balance sheets of OPNET Technologies, Inc. and its subsidiaries (the Company) as of March 31, 2010 and 2009, and the related consolidated statements of operations, changes in stockholders equity, and cash flows for each of the three years in the period ended March 31, 2010. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of OPNET Technologies, Inc. and its subsidiaries as of March 31, 2010 and 2009, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 2010, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company s internal control over financial reporting as of March 31, 2010, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated June 4, 2010 expressed an unqualified opinion on the effectiveness of the Company s internal control over financial reporting.

/s/ DELOITTE & TOUCHE LLP

McLean, Virginia

June 4, 2010

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OPNET TECHNOLOGIES, INC.

CONSOLIDATED BALANCE SHEETS

(in thousands, except per share data)

	March 31, 2010	March 31, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 104,681	$ 90,990
Marketable securities		999
Accounts receivable, net of $336 and $713 in allowance for doubtful accounts at March 31, 2010 and 2009, respectively	28,015	24,086
Unbilled accounts receivable	4,765	5,476
Inventory	872	722
Prepaid expenses and other current assets	2,816	4,043
Total current assets	141,149	126,316
Property and equipment, net	13,245	13,984
Intangible assets, net	5,109	6,193
Goodwill	14,639	14,639
Deferred income taxes and other assets	4,210	4,932
Total assets	$ 178,352	$ 166,064
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 1,405	$ 485
Accrued liabilities	10,932	11,561
Deferred and accrued income taxes	498	849
Deferred rent	432	364
Deferred revenue	38,425	30,223
Total current liabilities	51,692	43,482
Accrued liabilities	145	69
Deferred rent	2,138	2,571
Deferred revenue	4,946	2,910
Other income tax	755	527
Total liabilities	59,676	49,559
Commitments and contingencies (Note 9)		
Stockholders equity:		
Common stock par value $0.001; 100,000,000 shares authorized; 28,386,958 and 27,903,470 shares issued at March 31, 2010 and 2009, respectively; 20,955,452 and 20,658,514 shares outstanding at March 31, 2010 and 2009, respectively	28	28
Additional paid-in capital	99,229	93,292
Retained earnings	37,920	39,570
Accumulated other comprehensive loss	(999)	(1,171)
Treasury stock 7,431,506 and 7,244,956 shares at March 31, 2010 and 2009, respectively, at cost	(17,502)	(15,214)

Total stockholders equity	118,676	116,505
Total liabilities and stockholders equity	$ 178,352	$ 166,064

See accompanying notes to consolidated financial statements.

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OPNET TECHNOLOGIES, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

	Year Ended March 31, 2010	2009	2008
Revenue:			
Product	$ 52,252	$ 51,211	$ 38,838
Product updates, technical support and services	47,264	43,067	34,787
Professional services	26,831	28,601	27,721
Total revenue	126,347	122,879	101,346
Cost of revenue:			
Product	5,983	3,536	1,035
Product updates, technical support and services	4,859	4,665	4,514
Professional services	19,328	20,911	19,154
Amortization of acquired technology	1,835	2,172	1,486
Total cost of revenue	32,005	31,284	26,189
Gross profit	94,342	91,595	75,157
Operating expenses:			
Research and development	32,043	30,791	27,471
Sales and marketing	43,181	42,533	39,357
General and administrative	11,011	11,857	11,747
Total operating expenses	86,235	85,181	78,575
Income (loss) from operations	8,107	6,414	(3,418)
Interest and other (expense) income, net	(70)	1,246	3,579
Income before provision (benefit) for income taxes	8,037	7,660	161
Provision (benefit) for income taxes	2,214	2,928	(372)
Net income	$ 5,823	$ 4,732	$ 533
Basic net income per common share	$ 0.28	$ 0.23	$ 0.03
Diluted net income per common share	$ 0.28	$ 0.23	$ 0.03
Basic weighted average common shares outstanding	20,529	20,296	20,342
Diluted weighted average common shares outstanding	20,790	20,533	20,596

See accompanying notes to consolidated financial statements.

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OPNET TECHNOLOGIES, INC.

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

(in thousands)

	Common Stock				Treasury Stock				
	Shares Issued	Shares Outstanding	Amount	Additional Paid in Capital	Shares	Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders Equity
Balance, April 1, 2007	27,289	20,641	$ 27	$ 86,881	6,647	$ (9,246)	$ 34,815	$ 394	$ 112,871
Net income							533		533
Foreign currency translation								147	147
Unrealized loss on marketable securities, net of tax								(381)	(381)
Total comprehensive income									299
Adoption of ASC 740 cumulative effect							(510)		(510)
Exercise of options	60	60		365					365
Employee stock purchase plan	121	121	1	988					989
Tax benefit from exercise of stock options				105					105
Restricted stock issuance, net of forfeitures	107	107							
Purchase of treasury shares		(522)			522	(5,013)			(5,013)
Deferred compensation									
Stock based compensation expense				1,539					1,539
Balance, March 31, 2008	27,577	20,407	28	89,878	7,169	(14,259)	34,838	160	110,645
Net income							4,732		4,732
Foreign currency translation								(1,712)	(1,712)
Reversal of unrealized loss on marketable securities, net of tax								381	381
Total comprehensive income									3,401
Exercise of options	93	93		644					644
Employee stock purchase plan	151	151		1,123					1,123
Tax benefit from exercise of stock options				114					114
Restricted stock issuance, net of forfeitures	83	83							
Purchase of treasury shares		(76)			76	(955)			(955)
Stock based compensation expense				1,533					1,533
Balance, March 31, 2009	27,904	20,658	28	93,292	7,245	(15,214)	39,570	(1,171)	116,505
Net income							5,823		5,823
Foreign currency translation								172	172
Total comprehensive income									5,995
Exercise of options	277	277		2,720					2,720
Employee stock purchase plan	170	170		1,307					1,307
Tax benefit from exercise of stock options				351					351
Restricted stock issuance, net of forfeitures	36	36							
Purchase of treasury shares		(186)			186	(2,288)			(2,288)
Stock based compensation expense				1,559					1,559
Dividends declared ($0.36 per share)							(7,473)		(7,473)
Balance, March 31, 2010	28,387	20,955	$ 28	$ 99,229	7,431	$ (17,502)	$ 37,920	$ (999)	$ 118,676

See accompanying notes to consolidated financial statements.

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OPNET TECHNOLOGIES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Year Ended March 31, 2010	2009	2008
Cash flows from operating activities:			
Net income	$ 5,823	$ 4,732	$ 533
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	5,340	5,528	4,018
Loss on disposition of fixed assets	45	74	11
Provision for losses on accounts receivable	297	646	96
Deferred income taxes	(328)	(431)	(882)
Non-cash stock-based compensation expense	1,559	1,533	1,539
Non-cash accretion of market discount on marketable securities	(1)		
Excess tax benefit from exercise of stock options	(51)	(49)	(29)
Changes in assets and liabilities:			
Accounts receivable	(3,518)	(3,926)	(942)
Inventory	197	569	(116)
Prepaid expenses and other current assets	(364)	(70)	1,315
Other assets	(40)	(434)	(49)
Accounts payable	874	(10)	213
Accrued liabilities	158	1,682	466
Accrued income taxes	1,913	(130)	(382)
Deferred revenue	10,238	2,638	7,187
Deferred rent	(365)	(248)	(78)
Net cash provided by operating activities	21,777	12,104	12,900
Cash flows from investing activities:			
Acquisition of specified assets from Network Physics			(10,005)
Acquired technology	(433)		
Purchase of property and equipment	(3,148)	(5,466)	(4,557)
Purchase of investments		(999)	(114,799)
Proceeds from sale/maturity of investments	1,000	14,800	156,615
Net cash (used in) provided by investing activities	(2,581)	8,335	27,254
Cash flows from financing activities:			
Acquisition of treasury stock	(2,288)	(955)	(5,013)
Excess tax benefit from exercise of stock options	51	49	29
Proceeds from exercise of stock options	2,720	644	365
Issuance of common stock under employee stock purchase plan	1,307	1,123	989
Payment of dividend to stockholders	(7,473)		
Net cash (used in) provided by financing activities	(5,683)	861	(3,630)
Effect of exchange rate changes on cash and cash equivalents	178	(1,720)	120
Net increase in cash and cash equivalents	13,691	19,580	36,644
Cash and cash equivalents, beginning of year	90,990	71,410	34,766

Cash and cash equivalents, end of year	$ 104,681	$ 90,990	$ 71,410

See accompanying notes to consolidated financial statements

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OPNET TECHNOLOGIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010, 2009, and 2008

1. Organization and Significant Accounting Policies

Organization. OPNET Technologies, Inc. and its subsidiaries, (hereafter, the Company or OPNET), provides software products and related services for managing networks and applications. The Company s software products address application performance management, network operations, capacity management and network research and development. The Company sells products to corporate enterprises, government and defense agencies, network service providers, and network equipment manufacturers. The Company markets software products and related services in North America primarily through a direct sales force and, to a lesser extent, several resellers and original equipment manufacturers. Internationally, the Company conducts research and development through a wholly-controlled subsidiary in Ghent, Belgium and markets software products and related services through wholly-owned subsidiaries in Paris, France; Mainz, Germany; Slough, United Kingdom; and Singapore; a sales office in Beijing, China; third-party distributors; and value-added resellers. The Company is headquartered in Bethesda, Maryland and has domestic offices in Cary, North Carolina; Dallas, Texas; Santa Clara, California; and Nashua, New Hampshire.

Principles of Consolidation. The consolidated financial statements include the results of OPNET Technologies, Inc., its wholly-owned subsidiaries: OPNET Technologies SAS; OPNET Technologies Limited; OPNET Analysis, Inc.; OPNET Technologies, GmbH; and OPNET Technologies Asia, Pte. Ltd., and its wholly-controlled subsidiary OPNET Technologies, BVBA. All intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates. The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America, or GAAP, requires management to make estimates, judgments and assumptions. These estimates, judgments, and assumptions affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results may differ from these estimates. Significant items subject to such estimates, judgments, and assumptions include revenue recognition, the carrying amount and useful lives of long-lived assets, valuation allowances for accounts receivable and deferred tax assets, research and development tax credits, determination of uncertain tax position benefits under ASC 740 Income Taxes, or ASC 740, software development costs, valuation of acquired intangible assets, valuation of stock based compensation, and loss contingencies, such as litigation, claims and assessments.

Cash and Cash Equivalents. Cash and cash equivalents consist of deposits in banks and all highly liquid investments with maturities of three months or less when purchased.

Marketable Securities. The Company has determined that its investments in marketable securities are to be classified as available-for-sale. Available-for-sale securities are carried at fair value, with the unrealized gains and losses reported in stockholders equity in the accompanying consolidated balance sheets under the caption Accumulated other comprehensive income. The amortized cost of debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization is included in the Interest income line item on the accompanying consolidated statements of operations. Realized gains and losses on available-for-sale securities are included in the Interest and other income, net line item on the consolidated statements of operations. The cost of securities sold is based on the specific identification method. Interest and dividends on securities classified as available-for-sale are included in the Interest and other income, net line item on the consolidated statements of operations. As of March 31, 2010 the Company did not have any marketable securities.

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OPNET TECHNOLOGIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

March 31, 2010, 2009, and 2008

Supplemental Cash Flow Information.

	Year ended March 31,		
	2010	2009	2008
		(in thousands)	
Cash paid during the fiscal year for:			
Income taxes	$ 527	$ 3,239	$ 768
Non-cash financing and investing activities:			
Unrealized gain (loss) on marketable securities	$	$ 381	$ (381)
Restricted stock issued	$ 622	$ 860	$ 1,022
Accrued liability for the purchase of property and equipment	$ 11	$ 72	$ 218
Tenant improvement allowance received from landlord	$	$ 1,095	$ 880

Advertising Expense. Advertising costs are expensed when incurred. Advertising expense for fiscal 2010, 2009, and 2008 was $497,000, $389,000, and $525,000, respectively.

Concentration of Credit Risk. Financial instruments that potentially subject the Company to a concentration of credit risk consist principally of cash, cash equivalents, marketable securities and accounts receivable. The Company generally does not require collateral on accounts receivable, as the majority of its customers are large, well-established companies or government entities.

The Company maintains its cash balances at several financial institutions. The Federal Deposit Insurance Corporation insures the bank accounts up to $250,000. Although balances exceed that amount, the Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk related to cash.

Fair Value of Financial Instruments. The fair value of the Company s cash and cash equivalents, marketable securities, accounts receivable, accounts payable, and accrued expenses approximates their respective carrying amounts.

The Company measures its cash and cash equivalents using the fair value measurement principles of ASC 820 Fair Value Measurements and Disclosures, or ASC 820, which requires that fair value be based on the assumptions that market participants would use when pricing an asset or liability.

ASC 820 requires disclosures regarding the manner in which fair value is determined for assets and liabilities and establishes a three-tiered fair value hierarchy into which these assets and liabilities must be grouped, based upon significant levels of inputs as follows:

Level 1 Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 Observable inputs, other than Level 1 prices, such as quoted prices in active markets for similar assets and liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable inputs.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

The lowest level of significant input determines the placement of the entire fair value measurement in the hierarchy.

OPNET TECHNOLOGIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

March 31, 2010, 2009, and 2008

Software Development Costs. Development costs incurred in the research and development of new software products and enhancements to existing software products are expensed as incurred until technological feasibility has been established. The Company considers technological feasibility to be established when all planning, designing, coding, and testing has been completed according to design specifications. After technological feasibility has been established, any additional costs are capitalized in accordance with ASC 985 Software, or ASC 985. Through March 31, 2010, software development has been substantially completed concurrently with the establishment of technological feasibility and, accordingly, no costs have been capitalized to date.

Property and Equipment. Property and equipment are stated at cost. Depreciation on property and equipment is computed using the straight-line method over the estimated useful lives of the assets, of five to seven years. Leasehold improvements are depreciated over the shorter of the estimated useful life of the assets, the non-cancelable term of the related lease, or the non-cancelable lease term plus all periods for which executive management believes that the failure to renew the lease imposes a penalty in an amount such that the renewal appears, at the inception of the lease, to be reasonably assured. Repairs and maintenance are expensed as incurred.

Intangible Assets. The Company accounts for its goodwill and intangible assets in accordance with ASC 805 Business Combinations, or ASC 805, and ASC 350 Intangibles Goodwill and Other, or ASC 350. The acquired and purchased technology are stated at the lower of unamortized cost or net realizable value and are amortized on a straight-line basis over their expected useful lives of three to five years. The Company s customer relationship and workforce intangible assets are amortized on an accelerated basis over their expected useful lives of four and one-half years and five years, respectively. The Company uses the projected discounted cash flow method in valuing its acquired technology and purchased customer relationships using certain assumptions including revenue growth, cost levels, present value discount rate, and working capital requirements. The Company uses the lower of the amount of cash paid or the present value of projected discounted cash flows to value purchased technology. The workforce asset was valued on a replacement cost basis. While the Company believes the assumptions used to value its acquired technology related to acquisitions are reasonable, actual results will likely differ from those assumptions. Future cash flows are subject to change for a variety of internal and external factors. The Company periodically reviews the value of acquired technology and purchased intangible assets for reasonableness in accordance with ASC 360 Property, Plant and Equipment, or ASC 360. If changes in the Company s assumptions at the time of future periodic reviews indicate that the carrying value of its acquired technology and purchased intangible assets exceeds their fair value and it determines that carrying amounts can not be recovered, it would result in impairment losses. As of March 31, 2010 and 2009, intangible assets totaled $5.1 million and $6.2 million, net of accumulated amortization of $9.7 million and $7.7 million, respectively. There has been no impairment as of March 31, 2010 or 2009.

Goodwill. In accordance with ASC 350, goodwill is not amortized but is tested for impairment annually during the Company s fourth quarter and whenever events and circumstances occur indicating that the asset might be impaired. The Company performed its annual impairment test of goodwill as of March 31, 2010 and 2009 and concluded that the fair value substantially exceeded the carrying value; therefore, the Company did not record any impairment. The Company has not recorded a goodwill impairment since it first recorded goodwill in fiscal 2001.

Valuation of Long-Lived Assets. In accordance with ASC 360, the Company reviews its long-lived assets, including property and equipment, for impairment whenever events or changes in circumstances indicate that the carrying amounts of the assets may not be fully recoverable. If the total of the expected undiscounted future net cash flows is less than the carrying amount of the asset, a loss is recognized for the difference between the fair value and carrying amount of the asset. There has been no impairment as of March 31, 2010 or 2009.

OPNET TECHNOLOGIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

March 31, 2010, 2009, and 2008

Revenue Recognition. The Company derives revenue from three primary sources: (1) product, (2) product updates, technical support and services, which include product update, certain training provided and offered on a when-and-if available basis to customers, and technical support, and (3) professional services, which include consulting and custom training services for customers without a current maintenance agreement. The Company recognizes revenue based on the provisions ASC 605-985 Software Revenue Recognition, or ASC 605-985.

Product Revenue

Product revenue represents all fees earned from granting customers perpetual and term licenses to use the Company s software as well as the hardware that it uses to deliver its ACE Live software products. It excludes revenue derived from product updates, which are included in product updates, technical support and services revenue. For the years ended March 31, 2010, 2009, and 2008, perpetual licenses represented approximately 92%, 93%, and 97% of product revenue, respectively. Product revenue is recognized when the following four criteria are met: (i) persuasive evidence of an arrangement exists, (ii) delivery of the software has occurred, (iii) the product fee is fixed or determinable, and (iv) collectibility is probable. The Company defines each of these four criteria as follows:

Persuasive evidence of an arrangement exists. For license arrangements with end-users, it is the Company s customary practice to have a written software license agreement, which is signed by both the end user and the Company, and a purchase order or equivalent. A written contract can be executed based on the customer-specific format or on the standard shrink wrap software master license agreement. For those end users who have previously negotiated a software license agreement with the Company, the initial software license agreement is used as evidence of a written contract. Sales to distributors, resellers, and value-added resellers, which the Company collectively refers to as resellers, are primarily made outside of North America and are evidenced by a master reseller agreement governing the relationship, which is signed by both the reseller and the Company, together with a purchase order on a transaction-by-transaction basis. To further evidence an arrangement, the Company s master reseller agreement requires that the reseller provide the Company copies of the end user s executed software master license agreements.

Delivery has occurred. Physical delivery of the Company s software products to end users or resellers, which are collectively referred to as customers, is generally considered to have occurred upon the transfer of media containing the Company s software products to a common carrier (usually FOB shipping point based on standard agreement terms). Software licenses may also be delivered electronically to end users. Electronic delivery is deemed to occur after end users have been provided with access codes that allow them to take immediate possession of the software. If a software arrangement includes undelivered software products or services that are essential to the functionality of delivered software products, delivery is not considered to have occurred until these software products or services are delivered.

The fee is fixed or determinable. It is the Company s policy to not provide customers the right to any adjustments or refund of any portion of their license fees paid, acceptance provisions, cancellation privileges, or rights of return. The Company s normal payment terms for its software products and services currently range from net 30 days to net 90 days and primarily vary based on the country in which an agreement is executed. Payments that extend beyond the Company s normal payment terms from the contract date but that are due within six months are generally deemed to be fixed or determinable based on its successful collection history on such arrangements, and thereby satisfy the required criteria for revenue recognition**.** Arrangements with payment terms extending beyond six months are considered not to be fixed or determinable, and revenue from such arrangements is recognized as payments become due and payable.

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Collectibility is probable. Collectibility is assessed on a customer-by-customer basis. The Company typically sells to customers for whom there is a history of successful collection. New customers are subject to a credit review process that evaluates the customer s ability to pay**.** If the Company determines from the outset of an arrangement that collectibility is not probable, revenue is recognized as cash is collected.

In instances when any of the four criteria are not met, the Company defers recognition of product revenue until the criteria are met. When the sale of the software product requires the Company to make significant enhancements, customization or modifications to the software that are essential to its functionality, product revenue and consulting fees are recognized using contract accounting under ASC 605-35 Revenue Recognition Construction-Type and Production, or ASC 605-35. The Company estimates the percentage-of-completion, under ASC 605-35, based on its estimate of total hours to complete the project as a percentage of total hours incurred and the estimated hours to complete.

The process of estimation inherent in the application of the percentage-of-completion method of accounting for revenue is subject to judgments and uncertainties and may affect the amounts of product revenue and professional services revenue under certain contracts and related expenses reported in the Company s consolidated financial statements. A number of internal and external factors can affect the Company s estimates to complete client engagements, including skill level and experience of project managers, staff assigned to engagements, and continuity and attrition level of professional services staff. Changes in the estimated stage of completion of a particular project could create variability in the Company s revenue and results of operations if it is required to increase or decrease previously recognized revenue related to a particular project or if it expects to incur a loss on the project.

All fees billed to clients for shipping and handling are classified as product revenue. All costs associated with shipping and handling are classified as cost of product revenue.

Product Update, Technical Support, and Services Revenue

Product updates, technical support and services revenue represents fees associated with the sale of product updates, training, and technical support, all provided on a when-and-if-available basis (except for technical support) under the Company s maintenance agreement. Payments for product updates, technical support and services on initial order or on renewal are generally made in advance and are nonrefundable. Product updates consist of the right to unspecified software updates on a when-and-if-available basis and are typically entered into in connection with the initial software product purchase. Product updates, technical support and services may be renewed upon expiration of the term. Customers can purchase product updates separately from technical support and services. Revenue from product updates, technical support and services is deferred and recognized as revenue on a straight-line basis over the term of the maintenance agreement.

Revenue under multiple-element arrangements, which typically include product, consulting services, training and maintenance agreements sold together, are allocated to each element in the arrangement primarily using the residual method based upon the fair value of the undelivered elements, which is specific to the Company vendor-specific objective evidence of fair value, or VSOE. This means that the Company defers revenue from the arrangement fee equivalent to the fair value of the undelivered elements. Discounts, if any, are applied to the delivered elements, usually product, under the residual method. For periodic unspecified product updates and technical support agreements, VSOE is based upon either the renewal rate specified in each contract or the price charged when sold separately. For consulting services and training for customers without a current maintenance agreement, VSOE is based upon the rates charged for these services when sold separately.