OPNET TECHNOLOGIES INC
Form 10-Q
November 14, 2001

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

Form 10-Q

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

For the quarterly period ended September 30, 2001

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	7373	52-1483235
(State or other jurisdiction of incorporation or organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification No.)

7255 Woodmont Avenue
Bethesda, MD 20814
(Address of principal executive office)

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrants were required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

At November 9, 2001, there were outstanding 18,993,132 shares of common stock of the registrant.

TABLE OF CONTENTS

2

PART I. FINANCIAL INFORMATION

ITEM 1. Consolidated Financial Statements

OPNET Technologies, Inc.
Consolidated Balance Sheets
(in thousands, except per share data)
(unaudited)

	September 30, 2001	March 31, 2001
ASSETS		
Current assets:		
Cash and cash equivalents	$59,257	$62,623
Accounts receivable, net of $42 and $113 in allowance for doubtful accounts at September 30 and		

March 31, 2001, respectively	5,965	4,515
Unbilled accounts receivable	2,070	1,406
Refundable income taxes	94	332
Deferred income taxes	420	546
Prepaid expenses and other current assets	2,045	2,486
Total current assets	69,851	71,908
Deferred income taxes	141	-
Property and equipment, net	7,261	6,891
Investment in affiliate	446	-
Intangible assets, net	1,800	2,000
Goodwill and assembled workforce	10,921	10,704
Other assets:		
Deposits	44	75
Loan to officer	-	231
Purchased software, net	508	464
Total assets	$90,972	$92,273
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 829	$ 514
Accrued liabilities	2,636	7,146
Accrued income taxes	213	93
Deferred revenue	7,454	7,681
Total current liabilities	11,132	15,434
Deferred rent	226	59
Deferred revenue	339	311
Deferred taxes	-	15
Total liabilities	11,697	15,819
Commitments and contingencies		
Stockholders' equity:		
Preferred stock-par value $0.001; 5,000 shares authorized; 160 designated as Series A, No shares issued and outstanding at September 30 and March 31, 2001	-	-
Common stock-par value $0.001; 100,000 authorized; 25,112 and 24,901 shares issued at September 30 and March 31, 2001, respectively; 18,978 and 18,767 shares outstanding at September 30 and March 31, 2001, respectively	25	25
Additional paid-in capital	71,255	70,708
Deferred compensation	(135)	(180)
Retained earnings	12,236	9,999
Accumulated other comprehensive (loss) income	(6)	2
Treasury stock - 6,134 shares at September 30 and March 31, 2001	(4,100)	(4,100)
Total stockholders' equity	79,275	76,454
Total liabilities and stockholders' equity	$90,972	$92,273

See notes to consolidated financial statements.

OPNET Technologies, Inc.
Consolidated Statements of Operations
(unaudited)

	Three Months Ended September 30,		Six Months Ended September 30,	
	2001	2000	2001	2000
Revenues:				
Software licenses	$ 6,585	4,314	$13,115	$ 7,967
Services	4,690	3,456	9,290	6,237
Total revenues	11,275	7,770	22,405	14,204
Cost of revenues:				
Software licenses	160	124	270	301
Services	1,440	1,127	2,959	2,114
Total cost of revenues	1,600	1,251	3,229	2,415
Gross profit	9,675	6,519	19,176	11,789
Operating expenses:				
Research and development	3,298	1,946	6,452	3,628
Sales and marketing	4,154	3,282	8,323	5,997
General and administrative	1,090	792	2,075	1,452
Amortization of acquired technology	112	-	212	-
Total operating expenses	8,654	6,020	17,062	11,077
Income from operations	1,021	499	2,114	712
Interest and other income	517	677	1,168	813
Income before provision for income taxes	1,538	1,176	3,282	1,525
Provision for income taxes	476	435	1,045	560
Net income	1,062	741	2,237	965
Accretion of transaction costs on redeemable convertible preferred stock	-	(2)	-	(6)
Net income applicable to common shares	$ 1,062	$ 739	$ 2,237	$ 959
Basic net income applicable per common share	$ 0.06	$ 0.05	$ 0.12	$ 0.06
Diluted net income per common share	$ 0.05	$0.04	$ 0.11	$ 0.06
Weighted average common shares outstanding (basic)	18,952	16,296	18,881	14,801

Weighted average common shares outstanding (diluted)	19,861	18,042	20,025	16,333

See notes to consolidated financial statements.

4

OPNET Technologies, Inc.
Consolidated Statements of Cash Flows
(unaudited)

	Six Months Ended September 30,
	2001
	(in thousands)
Cash flows from operating activities:	
Net income	$ 2,237
Adjustments to reconcile net income to net cash (used in) provided by operating activities:	
Depreciation and amortization	985
Deferred income taxes	(30)
Tax benefit from exercise of nonqualified stock options	53
Expense related to employee stock options	45
Equity loss from affiliate	3
Changes in assets and liabilities:	
Accounts receivable	(2,345)
Prepaid expenses and other current assets	597
Loans to employees	231
Refundable income taxes	238
Deposits	31
Accounts payable	315
Accrued liabilities	(2,478)
Accrued income taxes	120
Deferred revenue	(199)
Deferred rent	167
Net cash (used in) provided by operating activities	(30)
Cash flows from investing activities:	
Acquisition	(1,156)
Investment in affiliate	(461)
Purchase of software	(123)
Purchase of property and equipment	(2,082)
Net cash used in investing activities	(3,822)
Cash flows from financing activities:	
Proceeds from sale of common stock	-
Costs incurred for initial public offering	-
Proceeds from exercise of common stock options	285
Proceeds from issuance of common stock under employee stock purchase plans	209

Net cash provided by financing activities	494
Effect of exchange rate changes on cash and cash equivalents	(8)
Net (decrease) increase in cash and cash equivalents	(3,366)
Cash and cash equivalents, beginning of period	62,623
Cash and cash equivalents, end of period	$59,257

See notes to consolidated financial statements.

OPNET Technologies, Inc.
Notes to Consolidated Financial Statements
(unaudited)

1. Basis of Presentation and Nature of Operations

OPNET Technologies, Inc. ("OPNET", the "Company", "we" or "us") provides intelligent network management software solutions that enable organizations to optimize the performance and maximize the availability of communications networks and networked applications. The OPNET product suite combines predictive modeling and a comprehensive understanding of networking technologies to enable network professionals to more effectively design and deploy networks, provision services, diagnose network and application performance problems, predict the impact of network changes, and efficiently plan capital investments. OPNET is headquartered in Bethesda, Maryland and has offices in Boston, Cary, Dallas, Santa Clara, Paris, France and Oxford, United Kingdom.

The accompanying consolidated financial statements include the results of OPNET Technologies, Inc. and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. The interim financial statements included herein are unaudited and have been prepared in accordance with generally accepted accounting principles ("GAAP") and applicable rules and regulations of the Securities and Exchange Commission (the "SEC") regarding interim financial reporting. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Accordingly, these interim financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes thereto contained in the Company's Annual Report on Form 10-K for the year ended March 31, 2001, filed with the SEC. The March 31, 2001 consolidated balance sheet included herein was derived from the audited financial statements as of that date, but does not include all disclosures including notes required by generally accepted accounting principles. In the opinion of management, these interim financial statements reflect all adjustments of a normal and recurring nature necessary to present fairly the Company's results for the interim periods. The preparation of financial statements in conformity with GAAP requires management to make certain estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities as of the date of the financial statements, as well as the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimates. In addition, the Company's operating results for the three and six months ended September 30, 2001 may not be indicative of the operating results for the full fiscal year or any other future period.

On March 30, 2001, OPNET Development Corp., a wholly owned subsidiary of the Company, acquired substantially all of the assets and operations of the NetMaker Division of Make Systems, Inc. ("NetMaker") using the purchase method of accounting. NetMaker offers a sophisticated suite of products that address the operational and engineering needs of traditional and next-generation network service providers. The results of NetMaker's operations have been included in the accompanying consolidated statements of operations from the date of acquisition.

2. Credit Agreements

In June 2000, the Company entered into a $5.0 million line of credit facility with a commercial bank. The line of credit allowed the Company to use the funds for corporate borrowings and the issuance of letters of credit up to a maximum of $5.0 million. The Company used the facility to issue a letter of credit for approximately $3.4 million to satisfy the security deposit requirements for its new corporate office facilities lease. The Company renewed the credit facility for an additional year, and it will now expire in June 2002. Interest is payable monthly, based on LIBOR plus the applicable margin ranging from 2% to 2.5% as stated in the loan agreement. The credit facility is collateralized by certain assets of the Company and there are also certain financial ratios and conditions that the Company must maintain under the terms of the loan agreement, as well as certain covenants with which the Company must comply. As of September 30, 2001, the Company had no balance outstanding under its line of credit.

3. Stockholders' Equity

During the three and six months ended September 30, 2001, the Company received proceeds of approximately $73,000 and $285,000 and issued 86,862 and 191,406 shares of Common Stock, respectively, pursuant to employee exercises of stock options. During the six months ended September 30, 2001, employees purchased 19,111 shares of Common Stock under the 2000 Employee Stock Purchase Plan, resulting in further proceeds to the Company of approximately $209,000.

6

4. Net Income Per Common Share

In February 1997, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standard ("SFAS") No. 128, Earnings Per Share. This statement requires dual presentation of basic and diluted earnings per share on the face of the income statement. In April 2001, the Emerging Issues Task Force issued an interpretation, Topic No. D-95, "Effect of Participating Convertible Securities on the Computation of Basic Earnings Per Share" which stipulates that participating convertible securities should be included in the computation of basic earnings per share. The Company has restated basic earnings per share for the three and six months ended September 30, 2000 in accordance with this interpretation. The effect on basic earnings per share was a $0.01 reduction for the six months ended September 30, 2000. Basic earnings per share is to be computed by dividing net income available to common shareholders by the weighted average number of common shares and participating preferred shares outstanding for the period. Diluted earnings per share reflect, the potential dilution that could occur if securities or other contracts to issue common shares were exercised or converted into common shares.

	Three Months Ended September 30, 2001	2000
	(in thousands, except	
Income (Numerator):		
Net income applicable to common shares	$ 1,062	$ 739
Plus:		
Accretion of transaction costs on redeemable convertible preferred stock	-	2
Net income (basic and diluted)	$ 1,062	$ 741
Shares (Denominator):		
Weighted average shares outstanding	18,952	15,399
Plus:		
Participating redeemable convertible preferred stock	-	897
Weighted average common shares outstanding (basic)	18,952	16,296
Plus:		
Effect of other dilutive securities - options	909	1,746
Weighted average shares outstanding (diluted)	19,861	18,042
Net income per common share:		
Basic net income per common share	$ 0.06	$ 0.05
Diluted net income per common share	0.05	0.04

5. Business Segment and Geographic Area Information

The Company operates in one industry segment, the development and sale of computer software programs and related services. For the six months ended September 30, 2001, there were no sales to any customers within a single country except for the United States where such sales accounted for 10% or more of total revenues. Substantially all assets were held in the United States for the quarter ended September 30, 2001 and the fiscal year ended March 31, 2001.

7

6. Supplemental Cash Flow Information

	Six Months Ended September 30, 2001	2000
	(in thousands)	
Supplemental disclosure of cash flow information:		
Cash paid during the year for income taxes	$ 651	$ 9

Supplemental disclosure of non cash activities:

Accrued tenant allowance	$ 359	$ -
Post-closing acquisition adjustments	$ 217	$ -
Conversion of preferred stock	$ -	$6,954
Accrued offering costs	$ -	$ 799
Accretion on preferred stock	$ -	$ 6

7. Comprehensive Income

In June 1997, the FASB issued SFAS No. 130, Reporting Comprehensive Income. This statement requires the Company to report and display certain information related to comprehensive income and its components. Comprehensive income includes net income and foreign currency translation adjustments. For the three and six months ended September 30, 2001, comprehensive income for the Company was $1.1 million and $2.2 million, and included accumulated foreign currency translation losses of approximately $2,000 and $8,000, respectively.

8. Investment in Affiliate

The Company applies the equity method of accounting for investments in business entities in which the Company does not have significant control but has an ownership interest between 20% and 50%. The Company consolidates all majority-owned and controlled subsidiaries.

In August 2001, the Company entered into an agreement with Comsof N.V., a Belgium company and the owner of WDM NetDesign B.V.B.A. ("WDM NetDesign"), through which the companies will collaborate on the development of optical network planning products. Under the agreement, OPNET acquired a 20% interest in WDM NetDesign for consideration of $399,000 and purchased an option for consideration of $1,000 to acquire all remaining shares of WDM NetDesign. If the Company exercises the option, OPNET will acquire the remaining shares for a total consideration of approximately $1.3 million to be paid in cash or a combination of cash and OPNET common stock. The option expires in December 2001.

The Company accounted for the investment in WDM NetDesign using the equity method. Included in the carrying amount of the WDM NetDesign investment is assembled workforce of $68,000 and acquired technology of approximately $352,000 that is being amortized on a straight-line basis over a period of five years. The purchase price allocation is preliminary and subject to adjustment.

The Company's share in WDM NetDesign's losses for the three and six months ended September 30, 2001 was $3,000.

9. New Accounting Pronouncements

In July 2001, the FASB issued SFAS No. 141, Business Combinations, and SFAS No. 142, Goodwill and Other Intangible Assets. SFAS No. 141 requires business combinations initiated after June 30, 2001 to be accounted for using the purchase method of accounting, and that certain acquired intangible assets in a business combination be separately identified and recognized as assets apart from goodwill. SFAS No. 142 requires that goodwill and certain other intangible assets will no longer be amortized and instead will be subject to periodic evaluation for impairment. In addition, the Statement includes provisions for the reclassification of certain existing recognized intangibles as goodwill.

The Company has elected for early adoption of SFAS Nos. 141 and 142, which is permitted for entities with fiscal years beginning after March 15, 2001. As a result, the Company has not amortized approximately $10.0 million of goodwill and $1.0 million of assembled workforce acquired in connection with the NetMaker acquisition, which was consummated on March 30, 2001. In accordance with SFAS No. 142, the Company had six months from the initial date of adoption to complete its transitional impairment test. The Company has completed this test and determined that no potential impairment existed. During the six months ended September 30, 2001, goodwill was adjusted by approximately $217,000 for modifications to initial purchase accounting estimates.

Acquired technology is being amortized on a straight-line basis over a period of five years and amortization of acquired technology was $112,000 and $212,000 for the three and six months ended September 30, 2001, respectively. We expect amortization expense of approximately $470,000 in each of the fiscal years ended March 31, 2002, 2003, 2004, 2005 and 2006, relating to the acquired technology.

Information regarding the Company's goodwill and intangible assets is as follows:

	As of September 30, 2001	
	Gross Carrying Amount	Accumulate Amortizati
	(in thousands)	
Intangible assets subject to amortization:		
Acquired technology	$2,352	$212
Intangible assets not subject to amortization:		
Goodwill	9,971	
Assembled workforce	1,018	
Total	$10,989	

Included in the above as components of investment in affiliate (see Note 8) are the following: acquired technology of $352,000, accumulated amortization of acquired technology of $12,000 and assembled workforce of $68,000.

In June 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations". SFAS 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. SFAS No. 143 is effective for fiscal years beginning after June 15, 2002. The Company is in the process of evaluating the impact of implementing SFAS No. 143.

In August 2001, the Financial Accounting Standards Board issued SFAS No. 144, "Accounting for the Impairment of Long-Lived Assets" which supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of" and the accounting and reporting provisions of APB No. 30, "Reporting the Results of Operations - Reporting and Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions," for the disposal of a segment of business. This Statement is effective for fiscal years beginning after December 15, 2001. SFAS No. 144 retains many of the provisions of SFAS No. 121, but addresses certain implementation issues associated with that Statement. The Company is currently evaluating the impact of implementing SFAS No. 144.

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis relates to the financial condition and results of operations of the Company for the three and six months ended September 30, 2001, and should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" contained in the Company's Annual Report on Form 10-K for the year ended March 31, 2001, filed with the SEC.

This report contains forward-looking statements that involve substantial risks and uncertainties. The statements contained in this report that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. You can identify these statements by forward-looking words such as "anticipate," "believe," "could," "estimate," "expect," "intend," "may," "plan," "potential," "should," "will," and "would" or similar words. You 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 or control accurately. The factors listed below in the section captioned "Certain Factors That May Affect Future Results," as well as any cautionary language contained herein, 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. Further, any forward-looking statement speaks only as of the date on which such statement is made, and we undertake no obligation to publicly update or revise any forward-looking information.

Overview

We provide intelligent network management software products and related services. Our product suite consists of four primary software products: OPNET IT Guru, OPNET Modeler, OPNET Netbiz, and our newest product, OPNET ServiceProvider Guru (released in June 2001). We sell our OPNET suite of products to service providers, including telecommunications carriers; ISPs and ASPs; large and medium-sized enterprises; and network equipment manufacturers. We market our product suite in North America primarily through a direct sales force and, to a lesser extent, several resellers and original equipment manufacturers. Internationally, we market our products primarily through our international subsidiaries and third-party distributors.

We sold our first products in 1987. Our operations, including acquisitions, have been financed principally through cash provided by operations, a venture financing in September 1997 and the proceeds of our initial public offering in August 2000. In August 1998, we introduced our OPNET IT Guru and OPNET Netbiz products. In June 2001, we released OPNET ServiceProvider Guru and began a new marketing and sales strategy to focus on this product.

We generate revenues principally from licensing our software products and providing related services, including maintenance and technical support, consulting, and training.

Our software license revenues consist of perpetual and term license sales of our software products and royalty income. Software license revenues are recognized upon delivery, provided that fees are fixed and determinable, no significant modifications to the product are required, and collection of the related receivable is probable. Where significant modifications are required, software license revenues are recognized along with consulting fees on a percentage-of-completion basis as the modifications are performed. We allow customers to evaluate our software before purchase, and therefore it is our policy not to allow returns.

Our service revenues consist of fees from maintenance and technical support agreements, consulting services, and training. The maintenance agreements covering our products provide for technical support and periodic unspecified product upgrades. Beginning in July 2001, our customers have been able to separately purchase periodic unspecified product upgrades without purchasing technical support. Customers purchasing technical support will be required to also purchase periodic unspecified product upgrades. Revenue related to periodic unspecified product upgrades are now classified as software license revenue. Revenue related to technical support will continue to be classified as service revenue. Revenues for both technical support and periodic unspecified product upgrades will continue to be deferred and recognized ratably over the support period. The impact of this change on software license revenue was minimal for the three months ended September 30, 2001. We offer consulting services primarily to provide product customization and enhancements. Consulting services are generally performed under fixed-price agreements and recognized as the work is performed on a percentage-of-completion basis. We provide classroom and on-site training to our customers on a daily fee basis.

10

Software license revenues and service revenues for which payment has been received, but that do not yet qualify for recognition as revenues, are reflected as deferred revenues.

Results of Operations

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

	Three Months Ended September 30,		Six Months Septembe
	2001	2000	2001
Revenues:			
Software licenses	58.4%	55.5%	58.5%
Services	41.6	44.5	41.5
Total revenues	100.0	100.0	100.0
Cost of revenues:			
Software licenses	1.4	1.6	1.2
Services	12.8	14.5	13.2
Total cost of revenues	14.2	16.1	14.4
Gross profit	85.8	83.9	85.6
Operating expenses:			
Research and development	29.2	25.0	28.8
Sales and marketing	36.8	42.3	37.1
General and administrative	9.7	10.2	9.3
Amortization of acquired technology	1.0	-	1.0

Total operating expenses	76.7	77.5	76.2
Income from operations	9.1	6.4	9.4
Interest and other income	4.5	8.7	5.2
Income before provision for income taxes	13.6	15.1	14.6
Provision for income taxes	4.2	5.6	4.6
Net income	9.4%	9.5%	10.0%

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

	Three Months Ended September 30,		Six Months Ended September 30,	
	2001	2000	2001	2
Cost of software license revenues	2.4%	2.9%	2.1%	3
Cost of service revenues	30.7	32.6	31.9	33

Comparison of Three Months Ended September 30, 2001 and 2000

Revenues

Total revenues increased 45.1% to $11.3 million for the three months ended September 30, 2001 from $7.8 million for the three months ended September 30, 2000. We believe that the percentage increase in our total revenues achieved in this period is not necessarily indicative of future results. Software license revenues were 58.4% and 55.5% of total revenues for the three months ended September 30, 2001 and 2000, respectively.

Software License Revenues. Software license revenues increased 52.6% to $6.6 million for the three months ended September 30, 2001 from $4.3 million for the three months ended September 30, 2000. The increase was primarily attributable to the substantial growth in overall demand for our suite of products, revenue contribution by our newest product, OPNET ServiceProvider Guru which was released in June 2001, and revenue related to our broadening portfolio of modules for OPNET IT Guru and OPNET Modeler products. Additional contributors to the growth in software license revenues include an increase in the average transaction size, expansion of our marketing and direct sales force and the continued growth of our international presence.

Service Revenues. Service revenues increased 35.7% to $4.7 million for the three months ended September 30, 2001 from $3.5 million for the three months ended September 30, 2000. This growth in service revenues was primarily a result of increased renewals of technical support contracts by our installed base of customers, increased technical support contracts related to new license sales, and growing demand for consulting services, primarily for the customization of our OPNET Netbiz product.

Cost of Revenues

Cost of software license revenues consists primarily of royalties, media, manuals, and distribution costs. Cost of service revenues consists primarily of personnel-related costs in providing technical support, consulting, and training to customers. Gross margin on software license revenues is substantially higher than gross margin on service revenues, reflecting the low materials, packaging, and other costs of software products compared with the relatively high personnel costs associated with providing services. Cost of service revenues varies based upon the relative mix of technical support, consulting, and training services.

Cost of Software License Revenues. Cost of software license revenues increased 29.0% to $160,000 for the three months ended September 30, 2001 from $124,000 for the three months ended September 30, 2000. Gross margin on software license revenues increased to 97.6% for the three months ended September 30, 2001 from 97.1% for the three months ended September 30, 2000. The increase in margin was primarily due to a reduction in the level of sales requiring royalty payments under our March 1999 agreement with Cadence Design Systems that required us to pay a 50% royalty for specified sales of OPNET Modeler to the portion of Cadence's customer base that uses an existing Cadence product. This agreement ended on March 31, 2001. We expect that gross margin on software license revenues will decline slightly in future periods due to anticipated royalty costs for new licensing arrangements entered into during the three months ended September 30, 2001.

Cost of Service Revenues. Cost of service revenues increased 27.8% to $1.4 million for the three months ended September 30, 2001 from $1.1 million for the three months ended September 30, 2000. Gross margin on service revenues increased to 69.3% for the three months ended September 30, 2001 from 67.4% for the three months ended September 30, 2000. This improvement in margin is primarily due to a higher level of profitability in consulting services, as well as increased volume of maintenance services that provide higher gross margins than consulting services.

Operating Expenses

Research and Development. Research and development expenses consist primarily of salaries, related benefits, and other engineering-related costs. Research and development expenses increased 69.5% to $3.3 million for the three months ended September 30, 2001 from $1.9 million for the three months ended September 30, 2000. As a percentage of total revenues, research and development expenses increased to 29.2% for the three months ended September 30, 2001 from 25.0% for the three months ended September 30, 2000. These increases are primarily due to increased staffing levels as result of the NetMaker acquisition in March 2001, increased costs of research and development programs related to the development of new products, including the release of OPNET ServiceProvider Guru in June 2001, and sustaining and upgrading our

existing products. We believe that a significant level of research and development investment will be required to maintain our competitive advantage and expect that the dollar amount of these expenditures will continue to grow in future periods.

Sales and Marketing. Sales and marketing expenses increased 26.6% to $4.2 million for the three months ended September 30, 2001 from $3.3 million for the three months ended September 30, 2000. This increase was primarily due to a substantial increase in the size of our direct sales force, increased commissions associated with the growth in revenues, and an overall increase in the level of advertising, tradeshow and other marketing activities. As a percentage of total revenues, sales and marketing expenses decreased to 36.8% for the three months ended September 30, 2001 from 42.3% for the three months ended September 30, 2000. This decrease as a percentage of total revenues resulted from a proportionally smaller increase in costs associated with developing market awareness for our newer products relative to the higher level of revenues for the three months ended September 30, 2001. We intend to continue to expand our global sales and marketing infrastructure and, accordingly, expect the dollar amount of our sales and marketing expenses to increase in the future.

General and Administrative. General and administrative expenses consist primarily of salaries, related benefits, and fees for recruiting, legal, accounting, and other services. General and administrative expenses increased 37.6% to $1.1 million for the three months ended September 30, 2001 from $792,000 for the three months ended September 30, 2000. The increased level of spending was primarily due to additional personnel costs and other expenses associated with the expansion of our supporting infrastructure. As a percentage of total revenues, general and administrative expenses decreased to 9.7% for the three months ended September 30, 2001 from 10.2% for the three months ended September 30, 2000. We expect that the dollar amount of general and administrative expenses will increase as we expand our operations.

Amortization of Acquired Technology. In connection with the NetMaker acquisition and our investment in WDM NetDesign, we recorded acquired technology of $2.0 million and $352,000 respectively, which is being amortized on a straight-line basis over a period of five years. Amortization of acquired technology for the three months ended September 30, 2001 was $112,000.

Interest and Other Income

Interest and other income decreased to $517,000 for the three months ended September 30, 2001 from $677,000 for the three months ended September 30, 2000. The decrease is primarily driven by a reduction in interest income earned on the proceeds from our initial public offering due to the decline in interest rates throughout the quarter, offset by fees associated with our $3.4 million letter of credit outstanding at September 30, 2001.

Provision for Income Taxes

The provision for income taxes increased to $476,000 for the three months ended September 30, 2001 from $435,000 for the three months ended September 30, 2000. Our effective tax rate for the three months ended September 30, 2001 was 30.9% compared to 37.0% for the three months ended September 30, 2000. This increase in the provision and corresponding decrease in the effective tax rate is primarily due to the growth in operating income partially offset by an increased percentage of research and development tax credits available to us.

Comparison of Six Months Ended September 30, 2001 and 2000

Revenues

Total revenues increased 57.7% to $22.4 million for the six months ended September 30, 2001 from $14.2 million for the six months ended September 30, 2000. Software license revenues were 58.5% and 56.1% of total revenues for the six months ended September 30, 2001 and 2000, respectively. As mentioned under the comparison of quarterly results, we believe that the percentage increase in our total revenues achieved this period is not necessarily indicative of future results.

Software License Revenues. Software license revenues increased 64.6% to $13.1 million for the six months ended September 30, 2001 from $8.0 million for the six months ended September 30, 2000. The increase was primarily attributable to the substantial growth in overall demand for our suite of products, including our new OPNET ServiceProvider Guru product, and broadening portfolio of related models and modules, increase in the average transaction size, expansion of our marketing and direct sales force and the continued growth of our international presence.

Service Revenues. Service revenues increased 48.9% to $9.3 million for the six months ended September 30, 2001 from $6.2 million for the six months ended September 30, 2000. This growth in service revenues was primarily a result of increased renewals of technical support contracts by our installed base of customers, increased technical support contracts related to new license sales, and growing demand for consulting services, primarily for the customization of our OPNET Netbiz product.

Cost of Revenues

Cost of Software License Revenues. Cost of software license revenues decreased 10.3% to $270,000 for the six months ended September 30, 2001 from $301,000 for the six months ended September 30, 2000. Gross margin on software license revenues increased to 97.9% for the six months ended September 30, 2001 from 96.2% for the six months ended September 30, 2000. The decrease in costs of software license revenues and the related increase in margin was primarily due to a reduction in the level of sales requiring royalty payments under our March 1999 agreement with Cadence Design Systems which ended on March 31, 2001.

Cost of Service Revenues. Cost of service revenues increased 40.0% to $3.0 million for the six months ended September 30, 2001 from $2.1 million for the six months ended September 30, 2000. Gross margin on service revenues increased to 68.1% for the six months ended September 30, 2001 from 66.1% for the six months ended September 30, 2000. This improvement in margin is primarily due to a higher level of profitability in consulting services, as well as increased volume of maintenance services that provide higher gross margins than consulting services.

Operating Expenses

Research and Development. Research and development expenses increased 77.8% to $6.5 million for the six months ended September 30, 2001 from $3.6 million for the six months ended September 30, 2000. As a percentage of total revenues, research and development expenses increased to 28.8% for the six months ended September 30, 2001 from 25.5% for the six months ended September 30, 2000. The increase as a percentage of total revenues is primarily due to increased staffing levels as result of the NetMaker acquisition in March 2001, increased costs of research and development programs related to the development of new products, and sustaining and upgrading our existing products.

Sales and Marketing. Sales and marketing expenses increased 38.8% to $8.3 million for the six months ended September 30, 2001 from $6.0 million for the six months ended September 30, 2000. This increase was primarily due to a substantial increase in the size of our direct sales force, increased commissions associated with the growth in revenues, and an overall increase in our sales and marketing efforts. As a percentage of total revenues, sales and marketing expenses decreased to 37.1% for the six months ended September 30, 2001 from 42.3% for the six months ended September 30, 2000.

General and Administrative. General and administrative expenses increased 42.9% to $2.1 million for the six months ended September 30, 2001 from $1.5 million for the six months ended September 30, 2000. The increased level of spending was primarily due to additional personnel costs and other expenses associated with the expansion of our supporting infrastructure. As a percentage of total revenues, general and administrative expenses decreased to 9.3% for the six months ended September 30, 2001 from 10.2% for the six months ended September 30, 2000.

Amortization of Acquired Technology. In connection with the NetMaker acquisition and our investment in WDM NetDesign, we recorded acquired technology of $2.0 million and $352,000 respectively, which is being amortized on a straight-line basis over a period of five years. Amortization of acquired technology for the six months ended September 30, 2001 was $212,000.

Interest and Other Income

Interest and other income increased to $1.2 million for the six months ended September 30, 2001 from $813,000 for the six months ended September 30, 2000. The increase was primarily due to a full six months of interest income earned on the proceeds from our initial public offering for the period ended September 30, 2001, compared to only two months of interest income earned for the comparable period in the prior year as the initial public offering was completed in August 2000. This increase was offset by a decline in interest rates for the six months ended September 30, 2001.

Provision for Income Taxes

The provision for income taxes increased to $1.0 million for the six months ended September 30, 2001 from $560,000 for the six months ended September 30, 2000. Our effective tax rate for the six months ended September 30, 2001 was 31.8% compared to 36.7% for the six months ended September 30, 2000. This increase in the provision and corresponding decrease in the effective tax rate is primarily due to the growth in operating income partially offset by an increased percentage of research and development tax credits available to us.

Liquidity and Capital Resources

Since inception, we have funded our operations primarily through cash provided by operating activities. In September 1997, we raised $7.0 million in venture financing, of which we used $3.4 million to repurchase stock from our existing stockholders. In August 2000, we completed our initial public offering in which we raised approximately $54.1 million, net of underwriting discounts and commissions and estimated offering expenses paid by us. As of September 30, 2001, we had cash and cash equivalents totaling $59.3 million.

Cash used in operating activities was $30,000 for the six months ended September 30, 2001. Cash used in operating activities is primarily derived from net income, as adjusted for depreciation and amortization offset by increased accounts receivable and accrued liability balances as a result of the growth in our business. Cash used in investing activities was $3.8 million for the six months ended September 30, 2001. The funds were used primarily to purchase property and equipment for our new corporate headquarters in Bethesda, Maryland, to pay the costs incurred for the NetMaker acquisition and to pay for our investment in WDM NetDesign. Cash provided by financing activities was $494,000 for the six months ended September 30, 2001, reflecting the proceeds received from the exercise of stock options and the sale of common stock under our 2000 Employee Stock Purchase Plan.

We have a $5.0 million revolving line of credit with a commercial bank, which expires in June 2002. Borrowings under this line of credit bear interest an annual rate equal to LIBOR plus 2% to 2.5%. We have currently used $3.4 million of this facility for a letter of credit that secures the lease for our new headquarters in Bethesda, Maryland.

We expect to experience growth in our working capital needs for the foreseeable future as we execute our business plan. We anticipate that operating activities, as well as planned capital expenditures, will constitute a material use of our cash resources. We may utilize cash resources to further expand our new headquarters facility or to fund acquisitions or investments in complementary businesses, technologies, or products.

We believe that our current cash and cash equivalents and cash generated from operations, along with available borrowings under our line of credit, will be sufficient to meet our anticipated cash requirements for working capital and capital expenditures for at least the next 12 months.

Certain Factors That May Affect Future Results

The following important factors, among others, could cause actual results to differ materially from those indicated by forward-looking statements made in this Quarterly Report on Form 10-Q and presented elsewhere by management from time to time.

Our operating results may fluctuate significantly as a result of factors outside of our control, 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 revenues 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:

- the timing of large orders;
- changes in the mix of our sales, including the mix between higher margin software products and somewhat lower margin services and maintenance, and the proportion of our license 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;
- general economic conditions, which can affect our customers' purchasing decisions and the length of our sales cycle;
- changes in our pricing policies or those of our competitors; and
- the timing and size of potential acquisitions by us.

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 revenues in any quarter depend 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 revenues than we expect, we probably will not be able to reduce our operating expenses quickly in response. Therefore, any significant shortfall in revenues or delay of customer orders could have an immediate adverse effect 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.

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

We derive all of our revenues from the sale of products and services that are designed to allow our customers to manage the performance of networks and applications. Accordingly, if the market for intelligent network management software does not continue to grow, we could face declining revenues, which could ultimately lead to our becoming unprofitable. The market for intelligent network management software solutions is in an early stage of development. 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 solutions, decide to invest in the management of their networks, and, in particular, adopt and continue to use our software solutions.

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

A key element of our strategy is to increase sales to service providers, and our future performance will be significantly dependent upon increased adoption by service providers of our software products, including OPNET ServiceProvider Guru. Accordingly, the failure of our products to perform favorably in the service provider environment or to gain wider adoption by service providers could have a negative effect on our business and future operating results.

If our newest products, OPNET IT Guru, OPNET Netbiz and OPNET ServiceProvider Guru, do not gain widespread market acceptance, our revenues might not increase and could even decline

We expect to derive a substantial portion of our revenues in the future from OPNET IT Guru and OPNET Netbiz, both of which were released in August 1998, and OPNET ServiceProvider Guru, which was released in June 2001. Our business depends on customer acceptance of these products and our revenues may not increase, or may decline, if our target customers do not adopt and expand their use of OPNET IT Guru, OPNET Netbiz and OPNET ServiceProvider Guru. To date, we have not achieved widespread market acceptance of either OPNET IT Guru or OPNET Netbiz, and we have only recently begun shipping OPNET ServiceProvider Guru. In addition, if our OPNET Modeler product, which we have been selling since 1987, encounters declining sales, which could occur for a variety of reasons, including market saturation, and sales of our newer products do not grow at a rate sufficient to offset the shortfall, our revenues would decline.

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 sales force to increase revenues. 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 revenues and grow our business could be compromised. Our sales people require a long period of time to become productive, typically three to six 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 sales force growth targets. Further, we may not generate sufficient sales to offset the increased expense resulting from growing our sales force or we may be unable to manage a larger sales force.

Our ability to increase our sales will 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 effectively market and sell our products, or we lose existing distributor relationships, we might not be able to increase our revenues. 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 rapid 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 will 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 revenues 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 revenues 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 revenues could fall. Advances in network management technology, software engineering, 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. In addition, the introduction and adoption of future network technologies or application architectures could reduce or eliminate the need for predictive network management software.

If we fail to retain our key personnel and attract and retain additional qualified personnel, we might not be able to sustain our revenue growth

Our future success and our ability to sustain our revenue growth 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, and Alain J. Cohen, our president and chief technology officer, could 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 large numbers of 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.

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

We plan to continue 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:

- greater difficulty in accounts receivable collection and longer collection periods;
- political and economic instability;
- difficulty in attracting distributors that will market and support our products effectively;
- 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; and
- the effects of currency fluctuations.

Expanding our OPNET Netbiz consulting services business will be costly and may not result in any compensating increase in sales or profitability

We have been aggressively expanding our consulting services delivered in conjunction with sales of OPNET Netbiz. The significant additional expenditures and operational resources required to expand our OPNET Netbiz consulting services business will place additional strain on our management, financial, and operational resources and may make it more difficult for us to maintain profitability. If OPNET Netbiz does not achieve significant market acceptance, our customers will not engage our consulting services organization to assist with consulting, custom development, implementation support, and training for OPNET Netbiz. In addition, we may be unable to attract or retain a sufficient number of the highly qualified consulting services personnel that we expect the expansion of our consulting services business will require.

We face intense competition, which could cause us to lose sales, resulting in lower revenues and profitability

The intense and increasing competition in our market could cause us to lose sales, which could result in lower revenues and could cause us to become unprofitable. The market for intelligent network management software is evolving rapidly and is highly competitive. We believe that this market is likely to become more competitive as the demand for intelligent network management solutions continues to increase. Many of our current and 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 will develop and market solutions that compete with our products in the future.

OPNET Modeler, OPNET IT Guru, and OPNET ServiceProvider Guru currently face or potentially will face competition from several sources, including:

- software vendors with intelligent network management offerings and application performance diagnosis solutions, such as Compuware;

- consultants who offer intelligent network management advisory services; and

- customers who develop their own intelligent network management capabilities, either internally or through outsourcing.

OPNET Netbiz competes with solutions designed to facilitate and automate sales processes in general.

If the Internet infrastructure does not grow as currently anticipated, sales of our OPNET Netbiz product may not grow and our revenues may decline

Our OPNET Netbiz product addresses a new and emerging market for sales process automation, including over the Internet, by service providers and network equipment manufacturers. The failure of this market to develop, or a delay in the development of this market, would reduce demand for OPNET Netbiz and cause our revenues to decline. The success of OPNET Netbiz depends substantially upon the widespread adoption of the Internet as a primary medium for commerce and business applications. Moreover, critical issues concerning the commercial use of the Internet, such as security, reliability, cost, accessibility, and quality of service, remain unresolved and may negatively affect the growth of Internet use or the attractiveness of commerce and business communication over the Internet.

Potential errors in our products and our inability to correct those errors could harm our reputation and could cause our customers to 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;
- 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 will 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.

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 revenues by decreasing demand for our products, 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 revenues by decreasing demand for our products. 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 revenues. 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 cease or delay 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, if 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.

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

In March 2001, we completed the NetMaker acquisition and in August 2001 we acquired a 20% interest in WDM NetDesign. We may continue to acquire or make investments in companies, products, or technologies if opportunities arise. Any acquisitions 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 acquired 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, we could experience significant delays in product releases or shipments, which could result in lost revenues and significant additional expense.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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 marketable securities are stated at amortized cost plus accrued interest, which approximates fair value. Cash equivalents and marketable securities consist primarily of money instruments and U.S. Treasury bills. 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 marketable securities.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

None.

ITEM 2. Changes in Securities and Use of Proceeds

On August 7, 2000, the Company closed an initial public offering of its Common Stock (the "Offering"). The shares of Common Stock sold in the Offering were registered under the Securities Act on a Registration Statement on Form S-1 (No. 333-32588) (the "Registration Statement") that was declared effective by the Securities and Exchange Commission on August 1, 2000, and the Offering commenced on that date.

After deducting the underwriting discounts and commissions and the estimated Offering expenses, the net proceeds to the Company from the Offering were approximately $54.1 million.

The Company intends to use the net proceeds of the Offering for general corporate purposes, including working capital and capital expenditures. From the date of the Offering through September 30, 2001, the Company used approximately $4.8 million of the net proceeds for capital expenditures and leasehold improvements related to its new headquarters facility in Bethesda, Maryland. The Company also used approximately $6.2 million of the net proceeds for the NetMaker acquisition and acquisition-related expenses, and $461,000 for the investment in WDM NetDesign. The Company has not allocated any of the remaining net proceeds to any identifiable uses. The Company may also use a portion of the net proceeds to acquire businesses, products, or technologies that are complementary to its business. Pending their use, the Company invests the net proceeds in investment grade, interest-bearing securities. None of these amounts were paid directly or indirectly to any director, officer, general partners of the Company or their associates, persons owning 10% or more of any class of equity securities of the Company, or any affiliate of the Company.

ITEM 3. Defaults Upon Senior Securities

None.

ITEM 4. Submission of Matters to a Vote of Security Holders

At the Annual Meeting of Stockholders of the Company held on September 11, 2001, (i) the Company's nominee for Class I Director for the ensuing three years was elected, (ii) the amendment and restatement of the Company's 2000 Stock Incentive Plan and the continuance of the Company's 2000 Stock Incentive Plan, as amended and restated, were approved and (iii) the selection of Deloitte & Touche LLP as the Company's independent auditors for the current fiscal year was ratified.

With respect to the election of the Class I Director, the voting was as follows:

Nominee	For	Withheld
Bruce R. Evans	15,782,727	353,603

With respect to the approval of the amendment and restatement of the Company's 2000 Stock Incentive Plan and the approval of the continuance of the Company's 2000 Stock Incentive Plan, as amended and restated, the voting was as follows:

For	10,965,651
Against	4,170,528

Abstain	11,127

With respect to the ratification of the selection of Deloitte & Touche LLP as the Company's independent auditors for the current fiscal year, the voting was as follows:

For	15,691,156
Against	440,117
Abstain	5,057

ITEM 5. Other Information

None.

ITEM 6. Exhibits and Reports on Form 8-K

A. Exhibits: See Exhibit Index

B. Reports on Form 8-K

None.

SIGNATURES

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

OPNET TECHNOLOGIES, INC.
(Registrant)

By: /s/ Marc A. Cohen

Name: Marc A. Cohen
Title: Chairman and
Chief Executive Officer
(Principal Financial and
Accounting Officer)

Date: November 14, 2001

OPNET Technologies, Inc.
EXHIBIT INDEX

Exhibit Number	Description
10.1	Amended and Restated 2000 Stock Incentive Plan