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

FORM 10-Q

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

For the quarterly period ended December 31, 2004

OR

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

For the transition period from __________ to __________

Commission File Number 000-26041

F5 NETWORKS, INC.

(Exact name of registrant as specified in its charter)

WASHINGTON	**91-1714307**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

401 Elliott Avenue West
Seattle, Washington 98119
(Address of principal executive offices and zip code)

(206) 272-5555
(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 registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☑ No ☐

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

The number of shares outstanding of the registrant's common stock as of February 4, 2005 was 36,669,190.

QUARTERLY REPORT ON FORM 10-Q

For the Quarter Ended December 31, 2004

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F5 NETWORKS, INC.
CONSOLIDATED BALANCE SHEETS
(unaudited, in thousands)

	December 31, 2004	September 30, 2004
ASSETS		
Current assets		
Cash and cash equivalents	$ 23,803	$ 24,901
Short-term investments	139,909	115,600
Accounts receivable, net of allowances of $3,269 and $3,161	28,101	22,665
Inventories	1,728	1,696
Deferred tax assets	4,619	4,494
Other current assets	8,495	5,776
Total current assets	206,655	175,132
Restricted cash	6,221	6,243
Property and equipment, net	12,969	11,954
Long-term investments	90,657	81,792
Deferred tax assets	32,966	26,886
Goodwill	50,067	50,067
Other assets, net	7,954	8,279
Total assets	$ 407,489	$ 360,353
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$ 7,746	$ 4,840
Accrued liabilities	16,537	17,668
Deferred revenue	29,046	28,064
Total current liabilities	53,329	50,572
Long-term liabilities	2,298	2,136
Commitments and contingencies		
Shareholders' equity		
Preferred stock, no par value; 10,000 shares authorized, no shares outstanding	—	—
Common stock, no par value; 100,000 shares authorized, 36,307 and 34,772 shares issued and outstanding	341,318	306,655
Accumulated other comprehensive loss	(937)	(498)
Retained earnings	11,481	1,488
Total shareholders' equity	351,862	307,645
Total liabilities and shareholders' equity	$ 407,489	$ 360,353

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

F5 NETWORKS, INC.
CONSOLIDATED INCOME STATEMENTS
(unaudited, in thousands, except per share data)

	Three months ended December 31, 2004	Three months ended December 31, 2003
Net revenues		
Products	$ 46,397	$ 26,376
Services	13,612	9,705
Total	60,009	36,081
Cost of net revenues		
Products	10,528	5,849
Services	3,386	2,462
Total	13,914	8,311
Gross profit	46,095	27,770
Operating expenses		
Sales and marketing	19,640	14,954
Research and development	6,974	5,444
General and administrative	5,006	3,347
Amortization of unearned compensation	—	10
Total	31,620	23,755
Income from operations	14,475	4,015
Other income, net	1,387	184
Income before income taxes	15,862	4,199
Provision for income taxes	5,869	398
Net income	$ 9,993	$ 3,801
Net income per share – basic	$ 0.28	$ 0.13
Weighted average shares – basic	35,577	30,159
Net income per share – diluted	$ 0.26	$ 0.11
Weighted average shares – diluted	37,818	33,121

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

F5 NETWORKS, INC.
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
FOR THE THREE MONTHS ENDED DECEMBER 31, 2004
(unaudited, in thousands)

	Common Stock		Accumulated Other Comprehensive Income / (Loss)	Retained Earnings	Total Shareholders' Equity
	Shares	Amount			
Balance, September 30, 2004	34,772	$306,655	$ (498)	$ 1,488	$ 307,645
Exercise of employee stock options	1,462	21,079	—	—	21,079
Issuance of stock under employee stock purchase plan	73	1,692	—	—	1,692
Tax benefit from employee stock transactions	—	11,892	—	—	11,892
Net income	—	—	—	9,993	—
Foreign currency translation adjustment	—	—	54	—	—
Unrealized loss on investments	—	—	(493)	—	—
Comprehensive income	—	—	—	—	9,554
Balance, December 31, 2004	36,307	$341,318	$ (937)	$11,481	$ 351,862

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

F5 NETWORKS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited, in thousands)

	Three months ended December 31, 2004	Three months ended December 31, 2003
Operating activities		
Net income	$ 9,993	$ 3,801
Adjustments to reconcile net income to net cash provided by operating activities:		
Loss on disposition of assets	7	—
Amortization of unearned compensation	–	10
Provision for doubtful accounts and sales returns	205	497
Depreciation and amortization	1,582	1,175
Deferred tax assets	(6,205)	—
Tax benefit from nonqualified stock options	11,892	—
Changes in operating assets and liabilities:		
Accounts receivable	(5,640)	1,557
Inventories	(31)	(389)
Other current assets	(1,226)	296
Other assets	(111)	(168)
Accounts payable and accrued liabilities	2,061	(845)
Deferred revenue	982	2,494
Net cash provided by operating activities	13,509	8,428
Investing activities		
Purchase of investments	(120,260)	(177,994)
Sale of investments	86,593	69,342
Investment in restricted cash	24	—
Acquisition of business	(395)	—
Purchases of property and equipment	(2,082)	(751)
Net cash used in investing activities	(36,120)	(109,403)
Financing activities		
Proceeds from public offering, net of issuance costs	—	113,636
Proceeds from the exercise of stock options	21,331	4,441
Net cash provided by financing activities	21,331	118,077
Net (decrease) increase in cash and cash equivalents	(1,280)	17,102
Effect of exchange rate differences	182	259
Cash and cash equivalents, at beginning of period	24,901	10,351
Cash and cash equivalents, at end of period	$ 23,803	$ 27,712

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

F5 NETWORKS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

1. Summary of Significant Accounting Policies

Description of Business

F5 Networks, Inc. (the Company) provides products and services to help companies efficiently and securely manage their Internet traffic. The Company's products enhance the delivery, optimization and security of application traffic on Internet-based networks. IP traffic passes through the Company's products where it is inspected and modified to ensure that it is delivered securely and in a way that optimizes the performance of both the network and the applications. The Company also offers a broad range of services such as consulting, training, installation, maintenance, and other technical support services.

Basis of Presentation

In the opinion of management, the unaudited consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, necessary for their fair presentation in conformity with accounting principles generally accepted in the United States of America. Certain information and footnote disclosures normally included in annual financial statements have been condensed or omitted in accordance with the rules and regulations of the Securities and Exchange Commission. The information included in this Form 10-Q should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2004.

Reclassification

Certain reclassifications have been made to prior year balances to conform to the current period presentation. Specifically, the Company's deferred tax liabilities have been reclassified and presented net of deferred tax assets in accordance with the provisions of Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes." The reclassifications had no impact on previously reported net income or shareholder's equity.

Revenue Recognition

The Company recognizes revenue in accordance with the guidance provided under Statement of Position (SOP) No. 97-2, "Software Revenue Recognition," and SOP No. 98-9 "Modification of SOP No. 97-2, Software Revenue Recognition, with Respect to Certain Transactions," Statement of Financial Accounting Standards (SFAS) No. 48, "Revenue Recognition When Right of Return Exists," and SEC Staff Accounting Bulletin (SAB) No. 104, "Revenue Recognition."

The Company sells products through distributors, resellers, and directly to end users. The Company recognizes product revenue upon shipment, net of estimated returns, provided that collection is determined to be probable and no significant obligations remain. In certain regions where the Company does not have the ability to reasonably estimate returns, the Company defers revenue on sales to its distributors until the Company has received information from the channel partner indicating that the distributor has sold the product to its customer. Payment terms to domestic customers are generally net 30 days. Payment terms to international customers range from net 30 to 90 days based on normal and customary trade practices in the individual markets. The Company has offered extended payment terms ranging from three to six months to certain customers, in which case, revenue is recognized when payments are made.

Whenever a software license, hardware, installation and post-contract customer support, or PCS, elements are sold together, a portion of the sales price is allocated to each element based on their respective fair values as determined when the individual elements are sold separately. Revenues from the license of software are recognized when the software has been shipped and the customer is obligated to pay for the software. When rights of return are present and the Company cannot estimate returns, the Company recognizes revenue when such rights of return lapse. Revenues for PCS are recognized on a straight-line basis over the service contract term. PCS includes rights to upgrades, when and if available, a limited period of telephone support, updates, and bug fixes. Installation revenue is recognized when the product has been installed at the customer's site. Consulting services are customarily billed at fixed rates, plus out-of-pocket expenses, and revenues are recognized when the consulting has been completed. Training revenue is recognized when the training has been completed.

Goodwill

Goodwill represents the excess purchase price over the estimated fair value of net assets acquired as of the acquisition date. The Company has adopted the requirements of Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS No. 142). SFAS No. 142 requires goodwill to be tested for impairment on an annual basis and between annual tests in certain circumstances, and written down when impaired. Goodwill of $24.2 million was recorded in connection with the acquisition of uRoam, Inc. in July 2003 while $25.9 million was recorded as a result of the MagniFire acquisition on May 31, 2004. There was no impairment of goodwill during the three months ended December 31, 2004 and 2003, respectively.

Stock-Based Compensation

The Company accounts for stock-based employee compensation arrangements in accordance with the provisions of Accounting Principles Board Opinion No. 25 ("APB No. 25"), "Accounting for Stock Issued to Employees," FASB Interpretation No. 44 ("FIN No. 44") "Accounting for Certain Transactions Involving Stock Compensation," and related interpretations and complies with the disclosure provisions of Statement of Financial Accounting Standards No. 123 ("SFAS No. 123"), "Accounting for Stock-Based Compensation." Under APB No. 25, compensation expense is based on the difference, if any, on the date of the grant, between the fair value of our stock and the exercise price of the option. The unearned compensation is being amortized in accordance with Financial Accounting Standards Board Interpretation No. 28 on an accelerated basis over the vesting period of the individual options.

Pro forma information regarding net income is required by SFAS No. 123 and has been determined as if the Company had accounted for stock options under the fair value method. For purposes of pro forma disclosures, the estimated fair value of the options is amortized over the options' vesting period. The net income and net income per share would have been adjusted to the pro forma amounts indicated below (in thousands, except per share data):

	Three months ended December 31,	
	2004	**2003**
Net income as reported	$ 9,993	$ 3,801
Add : Stock-based employee compensation expense under APB No. 25 included in reported net income, net of tax effect	—	10
Deduct : Total stock-based employee compensation expense determined under the fair value method, net of tax effect	2,746	4,967
Pro forma net income (loss)	$ 7,247	$ (1,156)
Net income (loss) per share :		
As reported – basic	$ 0.28	$ 0.13
Pro forma – basic	$ 0.20	$ (0.04)
As reported – diluted	$ 0.26	$ 0.11
Pro forma – diluted	$ 0.19	$ (0.04)

F5 NETWORKS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

Earnings Per Share

Basic net income per share is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted net income per share is computed by dividing net income by the weighted average number of common and dilutive common stock equivalent shares outstanding during the period.

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

	Three months ended December 31,	
	2004	2003
Numerator		
Net income	$ 9,993	$ 3,801
Denominator		
Weighted average shares outstanding – basic	35,577	30,159
Dilutive effect of common shares from stock options	2,241	2,962
Weighted average shares outstanding – diluted	37,818	33,121
Basic net income per share	$ 0.28	$ 0.13
Diluted net income per share	$ 0.26	$ 0.11

Approximately 0.5 million and 1.5 million of common shares potentially issuable from stock options for the three months ended December 31, 2004 and 2003, respectively, are excluded from the calculation of diluted earnings per share because the exercise price was greater than the average market price of the common stock for the respective period.

Recent Accounting Pronouncements

In March 2004, the Emerging Issues Task Force (“EITF”) reached a consensus on Issue No. 03-1, “The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments.” EITF 03-1 provides guidance on other-than-temporary impairment models for marketable debt and equity securities accounted for under SFAS No. 115, “Accounting for Certain Investments in Debt and Equity Securities,” and SFAS No. 124, “Accounting for Certain Investments Held by Not-for-Profit Organizations,” and non-marketable equity securities accounted for under the cost method. The EITF developed a basic three-step model to evaluate whether an investment is other-than-temporarily impaired. On September 30, 2004, the FASB approved the issuance of FASB Staff Position (FSP) EITF 03-1-1, which delays the effective date until additional guidance is issued for the application of the recognition and measurement provisions of EITF 03-1 to investments in securities that are impaired. The Company does not expect the adoption of EITF 03-1 to have a material effect on the Company’s results of operations or financial condition.

In December 2004, the FASB issued SFAS No. 123®, “Share-Based Payment”. This Statement revises FASB Statement No. 123, “Accounting for Stock-Based Compensation” and supersedes APB Opinion No. 25, “Accounting for Stock Issued to Employees” SFAS No. 123® focuses primarily on the accounting for transactions in which an entity obtains employee services in share-based payment transactions. SFAS No. 123® generally requires companies to recognize in the statement of operations the cost of employee services received in exchange for awards of equity instruments based on the grant-date fair value of those awards. This Statement is effective as of the first reporting period that begins after June 15, 2005. Accordingly, the Company will adopt SFAS 123® in its fourth quarter of fiscal 2005. The Company is currently evaluating the provisions of SFAS 123® including the assessment of allowable option valuation methodologies and expects that this Statement will have a material impact on its financial statements beginning in the fourth quarter.

F5 NETWORKS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

2. Commitments and Contingencies

Guarantees and Product Warranties

In the normal course of business to facilitate sales of its products, the Company indemnifies other parties, including customers, resellers, lessors, and parties to other transactions with the Company, with respect to certain matters. The Company has agreed to hold the other party harmless against losses arising from a breach of representations or covenants, or out of intellectual property infringement or other claims made against certain parties. These agreements may limit the time within which an indemnification claim can be made and the amount of the claim. In addition, the Company has entered into indemnification agreements with its officers and directors, and the Company's bylaws contain similar indemnification obligations to the Company's agents. It is not possible to determine the maximum potential amount under these indemnification agreements due to the limited history of prior indemnification claims and the unique facts and circumstances involved in each particular agreement.

The Company generally offers warranties of 90 days for hardware with the option of purchasing additional warranty coverage in increments of one year. The Company accrues for warranty costs as part of its cost of sales based on associated material product costs and technical support labor costs. The following table summarizes the activity related to product warranties during the three months ended December 31, 2004 and 2003 (in thousands):

	Three months ended December 31,	
	2004	2003
Balance, beginning of fiscal year	$ 1,062	$ 827
Provision for warranties issued	266	98
Payments	(266)	(96)
Balance, end of period	$ 1,062	$ 829

Purchase Commitments

The Company currently has arrangements with contract manufacturers and other suppliers for the manufacture of the Company's products. The arrangement with the primary contract manufacturer allows them to procure component inventory on the Company's behalf based on a rolling production forecast provided by the Company. The Company is obligated to the purchase of component inventory that the contract manufacturer procures in accordance with the forecast, unless we give notice of order cancellation in advance of applicable lead times. As of December 31, 2004, the Company was committed to purchase approximately $7.4 million of such inventory during the next quarter.

Litigation

The Company is not aware of any pending legal proceedings that, individually or in the aggregate, would have a material adverse effect on the Company's business, operating results, or financial condition. The Company may in the future be party to litigation arising in the ordinary course of business, including claims that allegedly infringe upon third-party trademarks or other intellectual property rights. Such claims, even if not meritorious, could result in the expenditure of significant financial and managerial resources.

3. Restructuring Charge

During the fiscal year 2002, the Company executed on a restructuring plan that included the discontinuation of its cache appliance business. As a result of discontinuing this line of business and other changes in the overall business, the Company incurred restructuring charges of $3.3 million for the fiscal year 2002. The restructuring charges included employee termination benefits, impaired assets, consolidation of excess facilities, and other obligations for which the Company no longer derives an economic benefit. There were no restructuring charges for the three months ended December 31, 2004 and 2003.

F5 NETWORKS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

The activity of the remaining restructuring liability included as a component of accrued liabilities on the balance sheet for the three months ended December 31, 2004 is presented below (in thousands):

	Balance at September 30, 2004	Additional Charges	Cash Payments and Write-offs	Balance at December 31, 2004
Excess facilities	$ 625	$ —	$ (66)	$ 559

The excess facilities charge was the result of the Company's decision to exit its support facility in Washington DC and was estimated based on current comparable rates for leases in the respective market. In April 2003, the excess facilities were subleased at the then current market value. Since then the difference between the lease payments and sublease income has historically been applied against the restructuring liability. During the three months ended December 31, 2004, timely receipts of sublease income were not received and the collectibility of sublease income is uncertain. If we are unable to collect further sublease income throughout the duration of the lease term, expiring in 2007, the actual loss may be increased from the original estimate and an additional restructuring charge may be required.

4. Geographic Sales and Significant Customers

The following presents revenues by geographic region (in thousands):

	Three months ended December 31, 2004	Three months ended December 31, 2003
United States	35,197	23,792
Europe	11,034	5,296
Japan	8,599	4,218
Asia Pacific	5,179	2,775
	$ 60,009	$ 36,081

The Company's customers are in diverse industries and geographic locations. Net revenues from international customers are primarily denominated in U.S. Dollars and totaled approximately $24.8 million and $12.3 million for the three months ended December 31, 2004 and 2003, respectively. One domestic distributor accounted for 16.0% and 18.5% of total net revenue for the three months ended December 31 2004 and 2003, respectively. This distributor accounted for 18.9% and 28.7% of accounts receivable as of December 31, 2004 and 2003, respectively.

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

The following Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with our consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on December 12, 2004. Our discussion may contain forward-looking statements, within the meaning of the Private Securities Litigation Reform Act of 1995, based upon current expectations. These forward-looking statements include, but are not limited to, statements about our plans, objectives, expectations and intentions and other statements that are not historical facts. Because these forward-looking statements involve risks and uncertainties, our actual results and the timing of certain events could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth under "Risk Factors" and "Business" in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2004, and elsewhere in this report.

Overview

We are a global provider of software and hardware products and services that help companies efficiently and securely manage their Internet traffic. Our products enhance the delivery, optimization and security of application traffic on Internet-based networks. We market and sell our products primarily through indirect sales channels in North America, Europe, Japan and the Asia Pacific region. Enterprise customers (Fortune 1000 or Business Week Global 1000 companies) in financial services, transportation, government and telecommunications industries continue to make up the largest percentage of our customer base.

Our management monitors and analyzes a number of key performance indicators in order to manage our business and evaluate our financial and operating performance. Those indicators include:

• *Revenues.* The majority of our revenues are derived from sales of our core products; BIG-IP Local Traffic Manager; BIG-IP Global Traffic Manager; BIG-IP ISP Traffic Manager; and FirePass SSL VPN servers. We also derive revenues from the sales of services including annual maintenance contracts, installation, training and consulting services. We carefully monitor the sales mix of our revenues within each reporting period. We believe customer acceptance rates of our new products and feature enhancements are key indicators of future trends. We also consider overall revenue concentration by customer and by geographic region as additional indicators of current and future trends.

• *Cost of revenues and gross margins.* We strive to control our cost of revenues and thereby maintain our gross margins. Significant items impacting cost of revenues are hardware costs paid to our contract manufacturers, third-party software license fees, amortization of developed technology, personnel and overhead expenses. Our margins have remained relatively stable over the past two years, however factors such as sales price, product mix, inventory obsolescence, returns, component price increases, and warranty costs could significantly impact our gross margins from quarter to quarter and represent the significant indicators we monitor on a regular basis.

• *Operating expenses.* Operating expenses are substantially driven by personnel and related overhead expenses. Existing headcount and future hiring plans are the predominant factors in analyzing and forecasting future operating expense trends. Other significant operating expenses that we monitor include marketing and promotions, travel, professional fees, computer costs related to the development of new products, facilities and depreciation expenses.

• *Liquidity and cash flows.* Our financial condition remains strong with significant cash and investments and no long term debt. The increase in cash and investments during the first quarter of fiscal 2005 was primarily due to the proceeds from the exercise of employee stock options and cash from operations. Going forward, we believe the primary driver of our cash flows will be net income from operations. Capital expenditures during the first quarter of fiscal 2005 were comprised primarily of tenant improvements and information technology infrastructure and equipment to support the growth of our core business activities.

• *Balance sheet.* We view cash, short-term and long-term investments, deferred revenue, accounts receivable balances and day’s sales outstanding as important indicators of our financial health. Deferred revenues continued to increase due to the growth in the amount of annual maintenance contracts purchased on new products and maintenance renewal contracts related to our existing product installation base. Our day’s sales outstanding for the first quarter of fiscal 2005 was 42 which we expect to maintain in the low to mid-40’s range going forward.

Critical Accounting Policies and Estimates

Our consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following critical accounting policies affect the more significant judgments and estimates used in the preparation of our financial statements. These critical accounting policies are consistent with those disclosed in our Annual Report on Form 10-K.

Revenue Recognition. We recognize revenue in accordance with the guidance provided under Statement of Position (SOP) No. 97-2, "Software Revenue Recognition," and SOP No. 98-9 "Modification of SOP No. 97-2, Software Revenue Recognition, with Respect to Certain Transactions." Statement of Financial Accounting Standards (SFAS) No. 48, "Revenue Recognition When Right of Return Exists," and SEC Staff Accounting Bulletin (SAB) No. 104, "Revenue Recognition."

We sell products through distributors, resellers, and directly to end users. We recognize product revenue upon shipment, net of estimated returns, provided that collection is determined to be probable and no significant obligations remain. In certain regions where we do not have the ability to reasonably estimate returns, we defer revenue on sales to distributors until we have received information from the channel partner indicating that the distributor has sold the product to its customer. Payment terms to domestic customers are generally net 30 days. Payment terms to international customers range from net 30 to 90 days based on normal and customary trade practices in the individual markets. We have offered extended payment terms to certain customers, in which case, revenue is recognized when payments are made.

Whenever a software license, hardware, installation and post-contract customer support, or PCS, elements are sold together, a portion of the sales price is allocated to each element based on their respective fair values as determined when the individual elements are sold separately. Revenues from the license of software are recognized when the software has been shipped and the customer is obligated to pay for the software. When rights of return are present and we cannot estimate returns, we recognize revenue when such rights of return lapse. Revenues for PCS are recognized on a straight-line basis over the service contract term. PCS includes rights to upgrades, when and if available, a limited period of telephone support, updates, and bug fixes. Installation revenue is recognized when the product has been installed at the customer's site. Consulting services are customarily billed at fixed rates, plus out-of-pocket expenses, and revenues are recognized when the consulting has been completed. Training revenue is recognized when the training has been completed.

Reserve for Doubtful Accounts. Estimates are used in determining our allowance for doubtful accounts and are based upon an assessment of selected accounts and as a percentage of our remaining accounts receivable by aging category. In determining these percentages, we evaluate historical write-offs, current trends in the credit quality of our customer base, as well as changes in the credit policies. We perform ongoing credit evaluations of our customers' financial condition and generally do not require any collateral. If there is deterioration of a major customer's credit worthiness or actual defaults are higher than our historical experience, our allowance for doubtful accounts may not be sufficient.

Reserve for Product Returns. In some instances, product revenue from distributors is subject to agreements allowing rights of return. Product returns are estimated based on historical experience and are recorded at the time revenues are recognized. Accordingly, we reduce recognized revenue for estimated future returns at the time revenue is recorded. When rights of return are present and we cannot estimate returns, revenue is recognized when such rights lapse. The estimates for returns are adjusted periodically based upon changes in historical rates of returns, inventory in the distribution channel and other related factors. It is possible that these estimates will change in the future or that the actual amounts could vary from our estimates.

Reserve for Warranties. A warranty reserve is established based on our historical experience and an estimate of the amounts necessary to settle future and existing claims on products sold as of the balance sheet date. While we believe that our warranty reserve is adequate and that the judgment applied is appropriate, such amounts estimated to be due and payable could differ materially from what will actually transpire in the future.

Accounting for Income Taxes. We utilize the liability method of accounting for income taxes pursuant to SFAS 109. Accordingly, we are required to estimate our income taxes in each of the jurisdictions in which we operate as part of the process of preparing our consolidated financial statements. This process involves estimating our actual current tax exposure, including assessing the risks associated with tax audits, together with assessing temporary differences resulting from the different treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities. Due to the evolving nature of tax rules combined with the large number of jurisdictions in which we operate, it is possible that our estimates of our tax liability could change in the future, which may result in additional tax liabilities and adversely affect our results of operations, financial condition and cash flows.

Results of Operations

	Three months ended December 31, 2004	Three months ended December 31, 2003
	(in thousands, except percentages)	
Revenues		
Net revenues		
Products	$ 46,397	$ 26,376
Services	13,612	9,705
Total	$ 60,009	$ 36,081
Percentage of net revenues		
Products	77.3%	73.1%
Services	22.7	26.9
Total	100.0%	100.0%

Net revenues. Total net revenues increased 66.3%, to $60.0 million for the three months ended December 31, 2004 from $36.1 million for the same period in the prior year. The improvement was due to increased demand for our application traffic management products, primarily sales of our new BIG-IP version 9 products, across all geographic regions. Revenues from our recently introduced application security products increased to approximately 9.0% of total net revenues. Higher services revenues resulting from our increased installed base of products contributed to the overall increase from the prior period. International revenues grew to 41.3% of total net revenues for the three months ended December 31, 2004 compared to 34.1% for the same period in the prior year. We expect international revenues will continue to represent a significant amount of total net revenues although we cannot provide assurance that international revenues as a percentage of total net revenues will remain at current levels.

Net product revenues increased 75.9%, to $46.4 million for the three months ended December 31, 2004 from $26.4 million for the same period in the prior year. Sales of our BIG-IP family of application traffic management products represented 82.4% and 87.6% of product revenues for the three months ended December 31, 2004 and 2003, respectively. The decrease was due to an increase in sales of our application security products, including FirePass, and to a lesser degree our TrafficShield products which began shipping in the current quarter.

Net services revenues increased 40.3%, to $13.6 million for the three months ended December 31, 2004 from $9.7 million for the same period in the prior year. The increase in services revenue was primarily due to increases in the purchase or renewal of maintenance contracts as our installed base of products increased.

Ingram Micro Inc., one of our domestic distributors, accounted for 16.0% and 18.5% of our total net revenues for the three months ended December 31, 2004 and 2003, respectively. The decrease as a percentage of total net revenues is due to the addition of new distributors and the increase in international revenues. Ingram Micro Inc. accounted for 18.9% of our accounts receivable as of December 31, 2004.

	Three months ended December 31,	
	2004	2003
	(in thousands, except percentages)	
Gross margin		
Cost of net revenues		
Products	$ 10,528	$ 5,849
Services	3,386	2,462
Total	13,914	8,311
Gross margin	$ 46,095	$ 27,770
Cost of net revenues (as a percentage of related revenue)		
Products	22.7%	22.2%
Services	24.9	25.4
Total	23.2	23.0
Gross margin	76.8%	77.0%

Cost of Net Product Revenues . Cost of our net product revenues consists of finished products purchased from our contract manufacturers, manufacturing overhead, freight, warranty, provisions for excess and obsolete inventory, and amortization expenses in connection with developed technology from recent acquisitions. Cost of net product revenues increased as a percentage of net product revenues to 22.7% from 22.2% in the prior period. The increase in cost of net product revenues as a percentage of net product revenues was due to higher amortization charges of $0.2 million related to the acquired technology we purchased from MagniFire Websystems, Inc., or MagniFire, during the third quarter of fiscal 2004.

Cost of Net Services Revenues . Cost of net services revenues increased in absolute dollars due to increased salary and benefits expenses as a result of an increase in professional services employee headcount. Services employee headcount at the end of December 2004 increased to 105 from 76 at the end of December 2003. Cost of net services revenues decreased as a percentage of services revenues to 24.9% from 25.4% for the same periods. The decrease in cost of net services revenues as a percentage of net services revenues is primarily the result of leveraging our existing services operating infrastructure to support the increased net services revenue.

We expect to maintain our gross margins in the near term; however, gross margins could be adversely affected by increased material costs, component shortages, excess and obsolete inventory charges and heightened sales price competition.

	Three months ended December 31,	
	2004	2003
	(in thousands, except percentages)	
Operating expenses		
Sales and marketing	$ 19,640	$ 14,954
Research and development	6,974	5,444
General and administrative	5,006	3,347
Amortization of unearned compensation	—	10
Total	$ 31,620	$ 23,755
Operating expenses (as a percentage of revenue)		
Sales and marketing	32.7%	41.4%
Research and development	11.6	15.1
General and administrative	8.3	9.3
Amortization of unearned compensation	—	—
Total	52.7%	65.8%

Sales and marketing. Sales and marketing expenses consists of salaries, commissions and related expenses of our sales and marketing staff, costs of our marketing programs, including public relations, advertising and trade shows, facilities and depreciation expenses. The decrease in sales and marketing expenses as a percentage of total net revenues is primarily the result of leveraging our existing sales and distribution infrastructure to support the increased net revenues. In absolute dollars, sales and marketing expenses increased 31.3% from the prior period. The increase was primarily due to higher salary, commission and employee benefit related expenses. The increase in commission expenses is consistent with the increase in revenue for the current period. The increased personnel costs were driven by growth in employee headcount. Sales and marketing headcount at the end of December 2004 increased to 266 from 216 at the end of December 2003. In the future, we expect to continue to increase our sales and marketing expenses to grow revenues and increase our market share.

Research and development . Research and development expenses consist of salaries and benefits for our product development personnel, prototype materials and expenses related to the development of new and improved products, facilities and depreciation expenses. Research and development expenses increased 28.1% from the prior period. The increase was attributed to higher salary and employee benefit costs. Research and development headcount at the end of December 2004 increased to 197 from 150 at the end of December 2003. The growth in employee headcount was primarily related to our acquisition of MagniFire in May of 2004 and to support the further development efforts of the new application security products. We expect to continue to increase research and development expenses as our future success is dependent on the continued enhancement of our current products and our ability to develop new, technologically advanced products that meet the changing needs of our customers.

General and administrative . General and administrative expenses consist of salaries and related expenses of our executive, finance, information technology, human resource and legal personnel, third-party professional service fees, bad debt charges, facilities and depreciation expenses. The decrease in general and administrative expenses as a percentage of total net revenues is primarily the result of leveraging our existing corporate infrastructure to support the increased net revenues. In absolute dollars, general and administrative expenses increased 49.6% from the prior period. The increase was primarily due to increased salary and benefit expenses of $0.9 million and professional service fees of $0.5 million, particularly audit and internal controls review in connection with the Sarbanes-Oxley Act of 2002. General and administrative headcount at the end of December 2004 increased to 81 from 68 at the end of December 2003.

Amortization of unearned compensation. During the current period we did not issue any stock awards below fair market value on the date of the respective grant. Accordingly we recorded no compensation expense related to stock options during the current period. As a result of new accounting rules pertaining to stock-based compensation arrangements we will incur material amortization charges for unearned stock-based compensation beginning in the fourth quarter of fiscal 2005. We are currently evaluating the provisions of the new rules, including an assessment of allowable option valuation methodologies and have not yet determined the specific impact that the new rules will have on our financial statements.

	Three months ended December 31, 2004	Three months ended December 31, 2003
	(in thousands, except percentages)	
Other income and income taxes		
Income from operations	$ 14,475	$ 4,015
Other income, net	1,387	184
Income before income taxes	15,862	4,199
Provision for income taxes	5,869	398
Net income	$ 9,993	$ 3,801
Other income and income taxes (as a percentage of revenue)		
Income from operations	24.1%	11.1%
Other income, net	2.3	0.5
Income before income taxes	26.4	11.6
Provision for income taxes	9.8	1.1
Net income	16.7%	10.5%

Other income, net. Other income, net, consists of interest income and foreign currency transaction gains and losses. The significant increase was due to interest income earned on the proceeds from our public offering completed in November of 2003.

Income taxes . We recorded a 37% provision for income taxes during the current period. In the prior comparable period when we had a valuation allowance offsetting our U.S. deferred tax assets, the provision for income taxes consisted primarily of foreign taxes related to our international operations. For the remainder of fiscal 2005, we expect to record a provision for income taxes comparable to the current period; however, our effective tax rate may fluctuate based on a number of factors including variations in estimated taxable income in our geographic locations, unforeseen changes in the valuation of our net deferred tax assets or changes in tax laws or interpretations thereof.

Financial Condition

Cash and cash equivalents, short-term investments and long-term investments were $254.4 million as of December 31, 2004 compared to $222.3 million as of September 30, 2004, representing an increase of $32.1 million. The increase was due to cash provided by operations of $13.5 million and cash received from employee stock option exercises of $21.3 million partially offset by $2.1 million used for the purchase of property and equipment and $0.4 million of cash payments to shareholders of MagniFire, which was acquired in May 2004.

Cash provided by operating activities was $13.5 million for the three months ended December 31, 2004 compared to $8.4 million for the same period in the prior year. Cash flow from operations in the three months ended December 31, 2004 resulted from increased net income combined with changes in operating assets and liabilities, as adjusted for various non-cash items including corporate tax deductions on certain employee stock option exercises and depreciation and amortization charges. Due to the significant amount of cumulative net operating losses for tax purposes we do not expect to incur or remit U.S. federal income taxes for the remainder of fiscal 2005.

Cash used in investing activities was $36.1 million for the three months ended December 31, 2004 compared to $109.4 million for the same period in the prior year. The significant amount of cash used in investing activities in the prior period was primarily due to investing the proceeds from our public offering in November 2003. Cash provided by financing activities for the three months ended December 31, 2004 was $21.3 million compared to

$118.1 million for the same period in the prior year. Our financing activities in the current period consisted of cash received from the exercise of employee stock options and purchases under our employee stock purchase plan. Financing activities in the prior period was primarily attributed to the $113.6 million net proceeds received from the November 2003 public stock offering. Based on our current operating and capital expenditure forecasts, we believe that our existing cash and investment balances together with cash generated from operations should be sufficient to meet our operating requirements for the foreseeable future.

As of December 31, 2004, our principal commitments consisted of obligations outstanding under operating leases. We lease our facilities under operating leases that expire at various dates through 2012. There have been no material changes in our principal lease commitments compared to those discussed in our Annual Report on Form 10-K for the year ended September 30, 2004. In connection with the lease agreement for our corporate headquarters we established a restricted escrow account collateralized by a $6.0 million certificate of deposit that has been included on our balance sheet as a component of restricted cash. The total amount required in escrow reduces at various dates as set forth by the lease agreement.

We outsource the manufacturing of our pre-configured hardware platforms to contract manufacturers who assemble each product to our specifications. Our agreement with our largest contract manufacturer allows them to procure component inventory on our behalf based upon a rolling production forecast. We are contractually obligated to purchase the component inventory in accordance with the forecast, unless we give notice of order cancellation in advance of applicable lead times. As of December 31, 2004, we were committed to purchase approximately $7.4 million of such inventory during the next quarter.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Management believes there have been no material changes to our quantitative and qualitative disclosures about market risk during the three month period ended December 31, 2004, compared to those discussed in our Annual Report on Form 10-K for the year ended September 30, 2004.

Item 4. Controls and Procedures

As of December 31, 2004, we carried out an evaluation, under the supervision and with the participation of the Company’s management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Exchange Act Rule 13a-15(e) and 15d-15(e). Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that our disclosure controls and procedures are effective to timely alert them to any material information relating to the Company (including its consolidated subsidiaries) that must be included in our periodic SEC filings. There have been no significant changes in the Company’s internal controls or in other factors that could significantly affect internal controls subsequent to their evaluation.

We intend to review and evaluate the design and effectiveness of our disclosure controls and procedures on an ongoing basis and to improve our controls and procedures over time and to correct any deficiencies that we may discover in the future. Our goal is to ensure that our senior management has timely access to all material financial and non-financial information concerning our business. While we believe the present design of our disclosure controls and procedures is effective to achieve our goal, future events affecting our business may cause us to modify our disclosure controls and procedures.

We are in the process of implementing the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 which requires our management to assess the effectiveness of our internal controls over financial reporting and include an assertion in our annual report as to the effectiveness of our controls. Subsequently, our independent auditors, PricewaterhouseCoopers LLP, will be required to attest to whether our assessment of the effectiveness of our internal controls over financial reporting is fairly stated in all material respects and separately report on whether it believes we maintained, in all material respects, effective internal controls over financial reporting as of September 30, 2005. We are in the process of performing the system and process documentation, evaluation and testing required for management to make this assessment and for the auditors to provide its attestation report. We have not completed this process or its assessment, and this process will require significant amounts of management time and resources. In the course of evaluation and testing, management may identify deficiencies that will need to be addressed and remediated.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

The Company is not aware of any pending legal proceedings that, individually or in the aggregate, would have a material adverse effect on the Company's business, operating results, or financial condition. The Company may in the future be party to litigation arising in the ordinary course of business, including claims that allegedly infringe upon third-party trademarks or other intellectual property rights. Such claims, even if not meritorious, could result in the expenditure of significant financial and managerial resources.

Reference is made to Item 3, Legal Proceedings in our Annual Report on Form 10-K for the year ended September 30, 2004, filed December 7, 2004 for descriptions of our legal proceedings. We continue to believe that the resolution of these legal proceedings will not have a material adverse effect on us and there have been no material developments since our 10-K filing.

Item 6. Exhibits

Exhibit Number	Exhibit Description
3.1	— Second Amended and Restated Articles of Incorporation of the Registration (1)
3.2	— Amended and Restated Bylaws of the Registrant (1)
4.1	— Specimen Common Stock Certificate (1)
31.1*	— Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2*	— Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	— Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* Filed herewith.

(1) Incorporated by reference from Registration Statement on Form S-1, File No. 333-75817.

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SIGNATURES

Pursuant to the requirements 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 this 9th day of February, 2005.

F5 NETWORKS, INC.

By: /s/ STEVEN B. COBURN

Steven B. Coburn
Chief Financial Officer
(Duly Authorized Officer and
Principal Financial and Accounting Officer)

EXHIBIT INDEX

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Exhibit 31.1

CERTIFICATIONS

I, John McAdam, certify that:

1) I have reviewed this quarterly report on Form 10-Q of F5 Networks, Inc.;

2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4) The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b. evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c. disclosed in this report any change in the registrant's internal controls over financial reporting that occurred during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal controls over financial reporting; and

5) The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 9, 2005

/s/ JOHN MCADAM

John McAdam
Chief Executive Officer and President

Exhibit 31.2

CERTIFICATIONS

I, Steven B. Coburn, certify that:

1) I have reviewed this quarterly report on Form 10-Q of F5 Networks, Inc.;

2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4) The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b. evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c. disclosed in this report any change in the registrant's internal controls over financial reporting that occurred during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal controls over financial reporting; and

5) The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 9, 2005

/s/ STEVEN B. COBURN

Steven B. Coburn
Senior Vice President, Chief Financial Officer

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of F5 Networks, Inc. (the "Company") on Form 10-Q for the period ending December 31, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), we, John McAdam, President and Chief Executive Officer and Steven Coburn, Senior Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Date: February 9, 2005

/s/ JOHN MCADAM

John McAdam

/s/ STEVEN B. COBURN

Steven B. Coburn

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to F5 Networks, Inc., and will be retained by F5 Networks, Inc., and furnished to the Securities

and Exchange Commission or its staff upon request.