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### **UNITED STATES** SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

### **FORM 10-Q**

(Mark	a One)
X	QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2005

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

For the transition period from

Commission File Number: 000-23593

### VERISIGN, INC.

(Exact name of registrant as specified in its charter)

**Delaware** 

(State or other jurisdiction of incorporation or organization)

94-3221585 (I.R.S. Employer Identification No.)

487 East Middlefield Road, Mountain View, CA

(Address of principal executive offices)

94043 (Zip Code)

Registrant's telephone number, including area code: (650) 961-7500

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 Act). YES $\boxtimes$ NO $\square$
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Class

Shares Outstanding July 31, 2005

Common stock, \$.001 par value

265,073,119

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#### PART I—FINANCIAL INFORMATION

#### ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

 $As \ required \ under \ Item \ 1 - Condensed \ Consolidated \ Financial \ Statements \ (Unaudited) \ included \ in \ this \ section \ are \ as \ follows:$ 

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#### VERISIGN, INC. AND SUBSIDIARIES

### CONDENSED CONSOLIDATED BALANCE SHEETS (In thousands, except share data)

		June 30, 2005		ecember 31, 2004
ASSETS	(	Unaudited)		
Current assets:				
Cash and cash equivalents	\$	449,579	\$	330,641
Short-term investments		431,960		406,784
Accounts receivable, (net of allowances of \$13,821 and \$11,450)		279,985		198,317
Prepaid expenses and other current assets		108,576		51,324
Deferred tax assets		18,187		19,057
Total current assets		1,288,287		1,006,123
Property and equipment, net		522,884		512,621
Goodwill		972,050		725,427
Other intangible assets, net		245,260		243,838
Restricted cash		51,444		51,518
Long-term note receivable		25,196		39,956
Other assets, net	_	13,542	_	13,391
Total long-term assets		1,830,376		1,586,751
Total assets	\$	3,118,663	\$	2,592,874
LIABILITIES AND STOCKHOLDERS' EQUITY			_	
Current liabilities:				
Accounts payable and accrued liabilities	\$	480,284	\$	382,025
Accrued restructuring costs		8,669		11,696
Deferred revenue		357,974		305,874
Total current liabilities		846,927		699,595
I and town deferred versame	_	110 260		107 505
Long-term deferred revenue  Long-term accrued restructuring costs		119,369 13,529		107,595 19,276
Other long-term liabilities		5,638		6,815
Deferred tax liabilities		23,334		31,319
	_			
Total long-term liabilities	_	161,870		165,005
Total liabilities		1,008,797		864,600
Minority interest in subsidiaries	_	38,646	_	36,277
Commitments and contingencies		30,040		30,277
Stockholders' equity:				
Preferred stock—par value \$.001 per share				
Authorized shares: 5,000,000				
Issued and outstanding shares: none		_		_
Common stock—par value \$.001 per share  Authorized shares: 1,000,000,000				
Issued and outstanding shares: 264,249,155 and 253,341,383 (excluding 7,717,017 and 6,164,017 shares held in treasury at June 30, 2005 and December 31, 2004, respectively)		264		253
Additional paid-in capital		23,548,934		23,253,111
Unearned compensation		(10,639)		(6,127)
Accumulated deficit	(	21,463,359)	(	21,553,829)
Accumulated other comprehensive loss		(3,980)		(1,411)
Total stockholders' equity	_	2,071,220	_	1,691,997
Total liabilities and stockholders' equity	\$	3,118,663	\$	2,592,874

#### VERISIGN, INC. AND SUBSIDIARIES

# CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (In thousands, except per share data) (Unaudited)

	Three Mor June		Six Mont June	
	2005	2004	2005	2004
Revenues	\$444,830	\$256,045	\$845,821	\$485,158
Costs and expenses:				
Cost of revenues	136,555	102,235	261,397	193,717
Sales and marketing	140,417	46,847	269,794	87,017
Research and development	26,974	15,253	48,991	31,960
General and administrative	49,944	38,595	92,322	73,834
Restructuring and other (reversals) charges	(133)	(3,626)	(2,008)	11,881
Amortization of other intangible assets	24,821	18,223	47,661	33,333
Acquired in-process research and development	4,300		4,300	
Total costs and expenses	382,878	217,527	722,457	431,742
Operating income	61,952	38,518	123,364	53,416
Non-operating income:	01,002	55,515	120,00	33,110
Minority interest	(1,048)	(836)	(2,176)	(1,129)
Other income, net	14,084	1,538	29,361	2,570
Income before income taxes	74,988	39,220	150,549	54,857
Income tax expense	(33,693)	(17,275)	(60,079)	(23,842)
Net income	\$ 41,295	\$ 21,945	\$ 90,470	\$ 31,015
Net income per share:				
Basic	\$ 0.16	\$ 0.09	\$ 0.35	\$ 0.13
Diluted	\$ 0.15	\$ 0.09	\$ 0.34	\$ 0.12
Shares used in per share computation:				
Basic	263,538	249,357	258,018	246,859
Diluted	272,888	253,068	266,871	250,614

See accompanying Notes to Condensed Consolidated Financial Statements.

#### VERISIGN, INC. AND SUBSIDIARIES

# CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (In thousands) (Unaudited)

Six Months Ended June 30, 2005 2004 Cash flows from operating activities: \$ 90,470 Net income \$ 31,015 Adjustments to reconcile net income to net cash provided by operating activities: Depreciation and amortization of property and equipment 42,582 42,977 Amortization of other intangible assets 47,661 33,333 Acquired in-process research and development 4,300 Provision for doubtful accounts 2,489 329 Non-cash restructuring and other charges 146 13,436 Net (gain) loss on sale and impairment of investments (96)3,667 2,176 Minority interest in net income of subsidiary 1,129 Tax benefit associated with stock options 16,337 25,345 Deferred income taxes (7,115)(818)Amortization of unearned compensation 2,722 1,467 Loss on disposal of property and equipment 186 Changes in operating assets and liabilities: Accounts receivable (14,093)(77,227)Prepaid expenses and other current assets (54,048)(2,766)Accounts payable and accrued liabilities 83,386 (36,973)Deferred revenue 59,957 47,857 Net cash provided by operating activities 213,926 145,905 Cash flows from investing activities: Purchases of investments (204,065)(148,911)Proceeds from maturities and sales of investments 178,091 289,265 Purchases of property and equipment (45,820)(35,383)Net cash paid in business combinations (18,002)(246, 356)Payment received on long-term note receivable and dividend 17,213 Merger related costs (8,216)(2,664)Other assets (3,268)(34)Net cash used in investing activities (84,067)(144,083)Cash flows from financing activities: Proceeds from issuance of common stock from option exercises and employee stock purchase plan 35,898 25,910 Repurchase of common stock (42,477)Proceeds from sale of stock from consolidated subsidiary 778 165 Payment of long-term liabilities (1,100)(2,850)Net cash (used in) provided by financing activities (7,514)23,838 Effect of exchange rate changes (3,407)(981)Net increase (decrease) in cash and cash equivalents 118,938 24,679 Cash and cash equivalents at beginning of period 330,641 301,593 Cash and cash equivalents at end of period \$ 449,579 \$ 326,272 Cash paid for income taxes, net of refunds received \$ 14,849 9,861 \$

See accompanying Notes to Condensed Consolidated Financial Statements.

#### VERISIGN, INC. AND SUBSIDIARIES

### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

#### Note 1. Basis of Presentation and Summary of Significant Accounting Policies

The accompanying interim unaudited condensed consolidated balance sheets, statements of operations and cash flows reflect all adjustments, consisting of normal recurring adjustments and other adjustments, that are, in the opinion of management, necessary for a fair presentation of the financial position of VeriSign, Inc. and its subsidiaries ("VeriSign" or the "Company"), at June 30, 2005, and the results of operations and cash flows for the interim periods ended June 30, 2005 and 2004.

The accompanying unaudited condensed consolidated financial statements have been prepared by VeriSign in accordance with the instructions for Form 10-Q pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") and, therefore, do not include all information and notes normally provided in audited financial statements and should be read in conjunction with VeriSign's consolidated financial statements for the year ended December 31, 2004 included in the annual report previously filed on Form 10-K.

The results of operations for any interim period are not necessarily indicative, nor comparable to the results of operations for any other interim period or for a full fiscal year.

#### Reclassification

Certain reclassifications have been made to prior period amounts to conform to current period presentation. VeriSign invests in market auction preferred securities ("Auction Securities") with reauction periods of 90 days or less, and the maturities of the instruments underlying the market auction preferred securities are generally more than 90 days from the date of acquisition. VeriSign previously excluded purchases and sales of Securities from the Consolidated Statements of Cash Flows because the Auction Securities were classified as cash equivalents. Purchases of investments in the Consolidated Statements of Cash Flows for the six months ended June 30, 2004 have been reclassified to include \$53.8 million of purchases of Auction Securities, and proceeds from maturities and sales of investments for the six months ended June 30, 2004 have been reclassified to include \$146.0 million of sales and maturities of Auction Securities.

#### Cash and Cash Equivalents

VeriSign considers all highly liquid investments with original maturities of three months or less at the date of acquisition to be cash equivalents. Cash and cash equivalents include money market funds, commercial paper and various deposit accounts.

#### Short-Term Investments

Highly liquid investments with original maturities greater than three months are considered short-term investments. VeriSign invests in debt and equity securities of companies for business and investment purposes.

#### Fair Value of Financial Instruments

The fair value of VeriSign's cash equivalents, short-term investments, accounts receivable, restricted cash, long-term investments, accounts payable and other long-term liabilities approximates the carrying amount, which is the amount for which the instrument could be exchanged in a current transaction between willing parties.

#### Long-Term Investments

Investments in non-public companies where VeriSign owns less than 20% of the voting stock and has no indicators of significant influence are included in other assets in the consolidated balance sheets and are

## VERISIGN, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

accounted for under the cost method. For these non-quoted investments, VeriSign regularly reviews the assumptions underlying the operating performance and cash flow forecasts based on information provided by these privately held companies. This information may be more limited, may not be as timely, and may be less accurate than information available from publicly traded companies. Assessing each investment's carrying value requires significant judgment by management. Generally, if cash balances are insufficient to sustain the investee's operations for a six-month period and there are no anticipated prospects of future funding for the investee, VeriSign considers the decline in fair value to be other-than-temporary. If it is determined that an other-than-temporary decline exists in a non-public equity security, VeriSign writes down the investment to its fair value and records the related impairment as an investment loss in its consolidated statement of operations. During the three months ended June 30, 2005, VeriSign determined that there were no other-than-temporary declines in the value of its non-public equity investments. During the three months ended June 30, 2004, VeriSign determined that the decline in value of certain of its non-public equity investments was other-than-temporary and recorded an impairment, net of realized gains, totaling \$0.3 million. During the six months ended June 30, 2005 and 2004, VeriSign recorded impairments, net of realized gains, totaling \$0.3 million, respectively.

#### Trade Accounts Receivable and Allowances for Doubtful Accounts

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. VeriSign maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. VeriSign regularly reviews the adequacy of its accounts receivable allowance after considering the size of the accounts receivable balance, each customer's expected ability to pay and its collection history with each customer. VeriSign reviews significant invoices that are past due to determine if an allowance is appropriate based on the risk category using the factors described above. For those invoices not specifically reviewed, VeriSign maintains general reserve provisions, based upon the age of the receivable. In determining these reserves, VeriSign analyzes its historical collection experience and current economic trends. If the historical data VeriSign uses to calculate the allowance for doubtful accounts does not reflect the future ability to collect outstanding receivables, additional provisions for doubtful accounts may be needed and the future results of operations could be materially affected.

#### Property and Equipment

Property and equipment are stated at cost less accumulated depreciation. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets; 40 years for buildings and three to five years for computer equipment, purchased software, office equipment, and furniture and fixtures. Leasehold improvements are amortized using the straight-line method over the lesser of the estimated useful lives of the assets or lease terms.

#### Capitalized Software

Costs incurred in connection with the development of software products are accounted for in accordance with the Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standards ("SFAS") No. 86, "Accounting for the Costs of Computer Software to Be Sold, Leased or Otherwise Marketed." Development costs incurred in the research and development of new software products, and enhancements to existing software products are expensed as incurred until technological feasibility in the form of a working model has been established. VeriSign's software has been available for general release concurrent with the establishment of technological feasibility, and accordingly no such costs have been capitalized.

Software included in property and equipment includes amounts paid for purchased software and implementation services for software used internally that has been capitalized in accordance with the American

#### VERISIGN, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Institute of Certified Public Accountants' Statement of Position ("SOP") No. 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." The following table summarizes the implementation and consulting services from third parties for internally used software as well as costs related to internally developed software which was capitalized by VeriSign during the three and six month periods ending June 30, 2005 and June 30, 2004:

		onths Ended ne 30,	Six Montl June	ths Ended ne 30,	
	2005	2004	2005	2004	
		(In thou	ısands)		
Internally used third-party software	\$ 6,174	\$ 3,650	\$12,419	\$5,365	
Internally developed software	4,346	3,220	7,492	5,068	

#### Goodwill and Other Intangible Assets

Goodwill represents the excess of costs over fair value of net assets of businesses acquired. Goodwill and other intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but instead tested for impairment at least annually in accordance with the provisions of SFAS No. 142, "Goodwill and Other Intangible Assets." SFAS No. 142 also requires that intangible assets with estimable useful lives be amortized on a straight-line basis over their respective estimated useful lives, and reviewed for impairment in accordance with SFAS No. 144, "Accounting for Impairment or Disposal of Long-Lived Assets." There was no impairment charge to goodwill and other intangible assets from the annual impairment tests conducted in the second quarter of 2005 or 2004.

#### Impairment of Long-Lived Assets

In accordance with SFAS No. 144, long-lived assets, such as property, plant and equipment, and purchased intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Such events or circumstances include, but are not limited to, a significant decrease in the fair value of the underlying business, a significant decrease in the benefits realized from an acquired business, difficulties or delays in integrating the business or a significant change in the operations of an acquired business. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds its fair value.

Goodwill and intangible assets with indefinite useful lives not subject to amortization are tested annually for impairment, and are tested for impairment more frequently if events and circumstances indicate that the asset might be impaired. For goodwill, an impairment loss is recognized when its carrying amount exceeds its implied fair value as defined by SFAS No. 142. For acquired intangible assets not subject to amortization, an impairment loss is recognized to the extent that the carrying amount of the asset exceeds its fair value. There was no impairment charge to long-lived assets during the three or six months ended June 30, 2005 and June 30, 2004.

Provision for royalty liabilities for intellectual property rights

Certain of VeriSign content services utilize intellectual property owned or held under license by others. Where VeriSign has not yet entered into a license agreement with a holder, VeriSign records a provision for royalty payments that it estimates will be due once a license agreement is concluded. VeriSign estimates the

#### VERISIGN, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

royalty payments based on the prevailing royalty rate for the type of intellectual property being utilized. VeriSign's estimates could differ materially from the actual royalties to be paid under any definitive license agreements that may be reached due to changes in the market for such intellectual property, such as a change in demand for a particular type of content, in which case VeriSign would record a royalty expense materially different than its estimate.

#### Foreign Currency Translation and Hedging Instruments

VeriSign transacts business in multiple foreign currencies. The functional currency for most of VeriSign's international subsidiaries is the U.S. Dollar. The subsidiaries' financial statements are remeasured into U.S. Dollars using a combination of current and historical exchange rates and any remeasurement gains and losses are included in operating results.

The financial statements of the subsidiaries for which the local currency is the functional currency are translated into U.S. Dollars using the current rate for assets and liabilities and a weighted-average rate for the period for revenues and expenses. This translation results in a cumulative translation adjustment that is included in accumulated other comprehensive income or (loss), which is a separate component of stockholders' equity.

VeriSign transacts business in foreign countries in U.S. Dollars as well as multiple foreign currencies. In the fourth quarter of 2003, VeriSign initiated a foreign currency risk management program, using forward currency contracts to eliminate, reduce, or transfer selected foreign currency risks. Forward contracts are limited to durations of less than 12 months. All derivatives were recorded at fair value on the balance sheet. Gains and losses resulting from changes in fair value were accounted for in operations during the periods.

#### Revenue Recognition

VeriSign derives its revenues from two reportable segments: (i) the Internet Services Group, which consists of Security Services and Naming and Directory Services; and (ii) the Communications Services Group, which consists of network connectivity and interoperability services, intelligent database services, content and application services, clearing and settlement services, and billing and payment services. Unless otherwise noted below, VeriSign's revenue recognition policies are in accordance with SEC Staff Accounting Bulletin ("SAB") No. 104, "Revenue Recognition," and Emerging Issues Task Force ("EITF") Issue No. 00-21, "Revenue Arrangements with Multiple Deliverables."

The revenue recognition policy for each of these categories is as follows:

#### **Internet Services Group**

#### Security Services

Revenues from the Security Services business are comprised of security services including managed security services and authentication services for enterprises.

Managed Security Services ("MSS"). Revenues from managed security services primarily consist of a set-up fee and a monthly service fee for the managed security service. Revenues from set-up fees are deferred and recognized ratably over the period that the fees are earned and revenues from the monthly service fees are recognized in the period in which the services are provided.

### VERISIGN, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

VeriSign also provides global security consulting services to help enterprises assess, design, and deploy network security solutions. Revenues from global security consulting services are recognized using either the percentage-of-completion method or on a time-and-materials basis as work is performed. Percentage-of-completion is based upon the ratio of hours incurred to total hours estimated to be incurred for the project. VeriSign has a history of accurately estimating project status and the hours required to complete projects. If different conditions were to prevail such that accurate estimates could not be made, then the use of the completed contract method would be required and all revenue and costs would be deferred until the project was completed. Revenues from time-and-materials are recognized as services are performed.

Authentication Services. Revenues from the sale of authentication and security services primarily consist of a set-up fee, annual managed service and per seat license fee. Revenues from the fees are deferred and recognized ratably over the term of the license, generally 12 to 36 months. Post-contract customer support ("PCS") is bundled with authentication and security services licenses and recognized over the license term.

VeriSign Affiliate PKI Software and Services. VeriSign Affiliate PKI Software and Services are for digital certificate technology and business process technology. Revenues from the VeriSign Affiliate PKI Software and Services are derived from arrangements involving multiple elements including PCS and other services. These software licenses, which do not provide for right of return, are primarily perpetual licenses for which revenues are recognized up-front once all criteria for revenue recognition have been met.

VeriSign recognizes revenues from VeriSign Affiliate PKI Software and Services in accordance with SOP 97-2, "Software Revenue Recognition," as amended by SOP 98-9, "Modification of SOP 97-2, Software Revenue Recognition with Respect to Certain Transactions," when all of the following criteria are met: (1) persuasive evidence of an arrangement exists, (2) delivery has occurred, (3) the fee is fixed or determinable and (4) collectibility is probable. VeriSign defines each of these four criteria as follows:

- *Persuasive evidence of an arrangement exists.* It is the Company's customary practice to have a written contract, which is signed by both the customer and VeriSign, or a purchase order from those customers who have previously negotiated a standard license arrangement with VeriSign.
- *Delivery has occurred*. VeriSign's software may be either physically or electronically delivered to the customer. Electronic delivery is deemed to have occurred upon download by the customer from an FTP server. Where an arrangement includes undelivered products or services that are essential to the functionality of the delivered product, delivery is not considered to have occurred until these products or services are delivered or accepted.
- The fee is fixed or determinable. It is VeriSign's policy to not provide customers the right to a refund of any portion of their paid license fees. Generally, at least 80% of the arrangement fees are due within one year or less, but VeriSign may agree to payment terms with a foreign customer based on local customs. Arrangements with payment terms extending beyond these customary payment terms are considered not to be fixed or determinable, and revenues from such arrangements are recognized as payments become due and payable.
- Collectibility is probable. Collectibility is assessed on a customer-by-customer basis. VeriSign typically sells to customers for whom there is a history
  of successful collection. New customers are subjected to a credit review process that evaluates the customer's financial position and, ultimately, their
  ability to pay. If VeriSign determines from the outset of an arrangement that collectibility is not probable based upon its credit review process, revenues
  are recognized as cash is collected.

## VERISIGN, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The Company's determination of fair value of each element in multiple-element software arrangements is based on vendor-specific objective evidence ("VSOE") of fair value. VeriSign limits its assessment of VSOE for each element to the price charged when the same element is sold separately. VeriSign has analyzed all of the elements included in its multiple-element software arrangements and determined that it has sufficient VSOE to allocate revenues to PCS and professional services components of its perpetual license arrangements. VeriSign sells its professional services separately, and has established VSOE on this basis. VSOE for PCS is determined based upon the customer's annual renewal rates for these elements. Accordingly, assuming all other revenue recognition criteria are met, revenues from perpetual licenses are recognized upon delivery using the residual method in accordance with SOP 98-9.

VeriSign's consulting services generally are not essential to the functionality of the software. The Company's software products are fully functional upon delivery and do not require any significant modification or alteration. Customers purchase these consulting services to facilitate the adoption of VeriSign's technology and dedicate personnel to participate in the services being performed, but customers may also decide to use their own resources or appoint other consulting service organizations to provide these services. Software products are billed separately and independently from consulting services, which are generally billed on a time-and-materials or milestone-achieved basis.

VeriSign also receives ongoing royalties from each digital certificate or authentication service sold by the VeriSign Affiliate to an end user. The Company recognizes the royalties from affiliates over the term of the digital certification or authentication service to which the royalty relates, which is generally 12 to 24 months.

Commerce Security Services. Revenues from commerce security services include the sale or renewal of digital certificates. These revenues are deferred and recognized ratably over the life of the digital certificate, which is generally 12 to 36 months.

Digital Brand Management Services. Revenues from digital brand management services include VeriSign's domain name registration services and its brand monitoring services. Revenues from the registration fees are deferred and recognized ratably over the registration term and the revenues from the brand monitoring services are recognized ratably over the periods in which the services are provided, which is generally one to ten years.

Secure Payments Services. Revenues from secure payments services primarily consist of a set-up fee and a monthly service fee for the transaction processing services. Revenues from set-up fees are deferred and recognized ratably over the period that the fees are earned and revenues from the monthly service fees are recognized in the period in which the services are provided. Advance customer deposits received are deferred and allocated ratably to revenue over the periods the services are provided.

#### Naming and Directory Services

VeriSign's Naming and Directory Services revenues primarily include its domain name registry services for the .com and .net gTLDs and certain ccTLDs, and managed domain name services. Domain name registration revenues consist primarily of registration fees charged to registrars for domain name registration services. Revenues from the initial registration or renewal of domain name registration services are deferred and recognized ratably over the registration term, generally one to two years and up to ten years. Fees for renewals and advance extensions to the existing term are deferred until the new incremental period commences. These fees are then recognized ratably over the new registration term, ranging from one to ten years.

## VERISIGN, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

#### **Communications Services Group**

Revenues from Communications Services business are comprised of network connectivity and interoperability services, intelligent database services, content and application services, clearing and settlement services, and billing and payment services.

#### **Network Connectivity and Interoperability Services**

Through VeriSign's network connectivity and interoperability services, VeriSign provides SS7 Connectivity and Signaling, Seamless Roaming for Wireless and Intelligent Database and Directory Services which provides for connections and services that signal and route information within and between telecommunication carrier networks.

SS7 Connectivity and Signaling. Network connectivity revenues are derived from establishing and maintaining connection to VeriSign's SS7 network and trunk signaling services. Revenues from network connectivity consist primarily of monthly recurring fees, along with trunk signaling service fees, which are charged and recognized monthly based on the number of switches to which a customer signals.

*Wireless Roaming*. Wireless roaming revenues are derived from enabling service providers to offer wireless data roaming to their subscribers. Revenues from wireless account management services and unregistered wireless roaming services are based on the revenue retained by VeriSign and recognized in the period in which such calls are processed on a per-minute or per-call basis.

#### **Intelligent Database Services**

Intelligent Database Services revenues include Number Portability, Caller Name Identification, Toll-free Database Services and TeleBlock Do Not Call, which are derived primarily from monthly database administration and database query services and are charged and recognized on a per-use or per-query basis.

#### **Content and Application Services**

Content services revenues are derived by providing content services including content, aggregation, formatting, mediation and billing and payment services. Revenues from content services primarily consist of weekly, biweekly or monthly subscriber fees. VeriSign records these revenues net of the fees from its wireless carriers in accordance with EITF No. 99-19, "*Reporting Revenue Gross as a Principal versus Net as an Agent.*" VeriSign also provides content services on a transaction basis and recognizes revenue upon delivery. VeriSign's content subscription plans allow for a specified number of content downloads per subscription period and give the customer the ability to rollover unused content downloads to future periods. VeriSign considers historical customer usage patterns to estimate and defer revenue for the number of content downloads expected to be rolled over and utilized prior to termination of the subscription plan.

Revenues from application services are derived by providing multimedia, global and short messaging services between carrier systems and devices, and across disparate networks and technologies so the carrier's customers can exchange messages outside their carrier's network. Revenues from application services primarily represent fees charged and recognized for the messaging services either based on a monthly fee or number of messages processed. VeriSign also provides consulting services to provide multimedia messaging and interoperability solutions. These fees are charged on a transaction or fixed-fee basis. The revenues associated with interoperability solutions are typically recognized over the estimated useful life, which is generally one to two years.

## VERISIGN, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

#### Clearing and Settlement Services

The Communications Services Group also offers advanced billing and customer care services to wireline and wireless carriers. VeriSign's advanced billing and customer care services include:

Wireline and Wireless Clearinghouse Services. Clearinghouse services revenues are derived primarily from serving as a distribution and collection point for billing information and payment collection for services provided by one carrier to customers billed by another. Revenues from clearinghouse services are earned based on the number of messages processed. Amounts due from customers that are related to VeriSign's telecommunications services for third-party network access, database charges and clearinghouse toll amounts that have been invoiced and remitted to the customer are included in prepaid expenses and other current assets.

#### **Billing and Payment Services**

Revenues from billing and payment services primarily represent a monthly recurring fee for every subscriber activated by VeriSign's wireless carrier customers.

#### Note 2. Stock Compensation Plans and Unearned Compensation

At June 30, 2005, VeriSign had four stock-based employee compensation plans, including two terminated plans under which options are outstanding but no further grants can be made, and two active plans. VeriSign accounts for these plans under the recognition and measurement principles of Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees." The following table illustrates the effect on net income and net income per share if VeriSign had applied the fair value recognition provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation," to stock-based employee compensation:

	Three Mor Jun	nths Ended e 30,	Six Months Ended June 30,			
	2005	2005 2004		2005 2004		2004
	<u> </u>	(In thousands, exc	ept per share data)			
Net income, as reported	\$ 41,295	\$ 21,945	\$ 90,470	\$ 31,015		
Add: Amortization of unearned compensation, net of tax	1,186	826	1,754	1,467		
Deduct: Stock-based compensation determined under the fair value method for all awards, net of						
tax	(15,828)	(31,696)	(32,218)	(65,904)		
Pro forma net income (loss)	\$ 26,653	\$ (8,925)	\$ 60,006	\$(33,422)		
Basic:						
As reported	\$ 0.16	\$ 0.09	\$ 0.35	\$ 0.13		
Pro forma stock-based compensation	(0.06)	(0.13)	(0.12)	(0.27)		
•						
Pro forma net income (loss) per share	\$ 0.10	\$ (0.04)	\$ 0.23	\$ (0.14)		
• • •						
Diluted:						
As reported	\$ 0.15	\$ 0.09	\$ 0.34	\$ 0.12		
Pro forma stock-based compensation	(0.05)	(0.13)	(0.12)	(0.26)		
1						
Pro forma net income (loss) per share	\$ 0.10	\$ (0.04)	\$ 0.22	\$ (0.14)		
\ \ / i						

## VERISIGN, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The fair value of stock options and Employee Stock Purchase Plan options was estimated on the date of grant using the Black-Scholes option-pricing model. Under the Employee Stock Purchase Plan, rights to purchase shares are only granted during the first and third quarter of each year. The following table sets forth the weighted-average assumptions used to estimate the fair value of the stock options and Employee Stock Purchase Plan options for each period presented:

		nths Ended e 30,		hs Ended e 30,
	2005	2004	2005	2004
Stock options:				
Volatility	64%	84%	71%	88%
Risk-free interest rate	3.73%	2.98%	3.67%	2.38%
Expected life	3.1 years	2.8 years	3.1 years	2.7 years
Dividend yield	zero	zero	zero	zero
Employee Stock Purchase Plan options:				
Volatility	n/a	n/a	47%	58%
Risk-free interest rate	n/a	n/a	2.24%	1.26%
Expected life	n/a	n/a	1.25 years	1.25 years
Dividend yield	n/a	n/a	zero	zero

#### Note 3. Business Combinations

On April 6, 2005, VeriSign completed its acquisition of LightSurf Technologies, Inc. ("LightSurf"), a Santa Cruz, California-based privately held provider of multimedia messaging and interoperability solutions for the wireless market. VeriSign paid approximately \$279.2 million in common stock for all of the outstanding capital stock, warrants and vested options of LightSurf. VeriSign also assumed all unvested stock options and paid certain transaction-related expenses of LightSurf. The acquisition has been accounted for as a purchase and, accordingly, the total purchase price has been allocated to the tangible and intangible assets acquired and the liabilities assumed based on their respective fair values on the acquisition date. LightSurf's results of operations have been included in the consolidated financial statements from its date of acquisition. As a result of the acquisition of LightSurf, VeriSign recorded goodwill of \$224.1 million and intangible assets of \$44.4 million, which have been assigned to the Communications Services Group segment. The goodwill represents the excess value over both tangible and intangible assets acquired. The goodwill in this transaction is attributable to the anticipated ability to offer carriers a comprehensive wireless data utility by combining LightSurf's current capabilities with VeriSign's existing communications services platforms. None of the goodwill for LightSurf is expected to be deductible for tax purposes. The overall weighted-average life of the identified amortizable assets acquired in the purchase of LightSurf is 3.2 years. These identified intangible assets will be amortized on a straight-line basis over their useful lives.

The in-process technology acquired in the LightSurf acquisition consisted primarily of research and development related to the efforts required to develop the acquired in-process technology principally relate to the completion of all planning, design, development, and test activities that are necessary to establish that the product or service can be produced to meet its design specifications including features, functions, and performance.

VeriSign determined the fair value of the acquired in-process technology by estimating the projected cash flows related to the project or service and future revenues to be earned upon commercialization of the service. VeriSign discounted the resulting cash flows back to their net present values. VeriSign based the net cash flows from such projects on its analysis of the respective markets and estimates of revenues and operating profits related to these projects.

## VERISIGN, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The allocation of the purchase price to the assets acquired and liabilities assumed based on the estimated fair value of LightSurf was as follows:

June 30, 2005	Amortization Period
(In thousands)	(Years)
\$ 19,677	_
7,225	
224,077	_
9,000	5
1,700	2.5
29,400	3-4
4,300	_
295,379	
(16,196)	
\$ 279,183	
	2005 (In thousands) \$ 19,677     7,225     224,077     9,000     1,700     29,400     4,300  295,379  (16,196)

#### Note 4. Restructuring and Other Charges

2003 Restructuring Plan

In November 2003, VeriSign initiated a restructuring plan related to the sale of its Network Solutions business and the realignment of other business units. The restructuring plan resulted in reductions in workforce, abandonment of excess facilities, disposals of property and equipment, and other charges. To date, VeriSign has recorded \$76.9 million in restructuring charges under its 2003 restructuring plan.

Net restructuring and other charges associated with the 2003 restructuring plan that were recorded during the periods ended June 30, 2005 and 2004 are as follows:

		onths Ended ne 30,	Six Months Ended June 30,		
	2005	2005 2004 2008		2004	
	· · · · · · · · · · · · · · · · · · ·	(In tho	usands)		
Workforce reduction	\$ —	\$ (645)	\$ (1)	\$ 927	
Excess facilities	(264)	(3,612)	(2,255)	(2,488)	
Exit costs	33	346	(23)	452	
Subtotal	(231)	(3,911)	(2,279)	(1,109)	
Other charges	8	884	(27)	13,589	
-					
Total restructuring and other (reversals) charges	\$ (223)	\$ (3,027)	\$(2,306)	\$12,480	

Workforce reduction. VeriSign recorded restructuring charges related to workforce reduction in accordance with SFAS No. 112, "Employers' Accounting for Postemployment Benefits an amendment of FASB Statements No. 5 and 43," since benefits were provided pursuant to a formal severance plan which used a standard formula of paying benefits based upon tenure with the Company. The accounting for these restructuring charges has met the four requirements of SFAS No. 112, which are: (i) the Company's obligation relating to employees' rights to receive compensation for future absences is attributable to employees' services already rendered; (ii) the obligation relates to rights that vest or accumulate; (iii) payment of the compensation is probable; and (iv) the amount can be reasonably estimated. VeriSign recorded workforce reduction charges of \$1.6 million in connection with a workforce reduction of approximately 35 employees during the three months ended March 31, 2004. All severance related charges will be paid by the end of 2005.

## VERISIGN, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Excess facilities. Excess facilities restructuring charges take into account the fair value of lease obligations of the abandoned space, including the potential for sublease income. Estimating the amount of sublease income requires management to make estimates for the space that will be rented, the rate per square foot that might be received and the vacancy period of each property. These estimates could differ materially from actual amounts due to changes in the real estate markets in which the properties are located, such as the supply of office space and prevailing lease rates. Changing market conditions by geographic location and considerable work with third-party leasing companies requires VeriSign to periodically review each lease and, as necessary, change its estimates on a prospective basis. During the three and six months ended June 30, 2005, VeriSign recorded a net reversal of restructuring charges of approximately \$0.3 million and \$2.3 million, respectively. During the three and six months ended June 30, 2004, VeriSign recorded a net reversal of restructuring charges of approximately \$3.6 million and \$2.5 million, respectively, for excess facilities that were abandoned relating to lease terminations and non-cancelable lease costs. These reversals were related to excess facilities primarily in connection with a decision to utilize and build a facility that VeriSign had treated as abandoned under its 2003 restructuring plan and for which it had previously recorded a restructuring charge. The net reversal was partially offset by certain taxes and lease charges.

Exit costs. VeriSign recorded other exit costs primarily relating to contract termination fees.

Other charges. Property and equipment that was disposed of or abandoned in 2004 consisted primarily of obsolete telecommunications computer software and other equipment related to the Communications Services Group segment. During the three and six months ended June 30, 2004, VeriSign recorded asset impairment charges of approximately \$0.9 million and \$13.6 million, respectively, related to a service whose cash flows did not sustain the value of the assets employed to deliver the service. Estimates were made to determine the fair market value of the assets based on third party resale values and management judgment of the fair value of similar used equipment.

At June 30, 2005, the accrued liability associated with the 2003 restructuring plan was \$15.1 million and consisted of the following:

	Rest C Dec	accrued cructuring Costs at ember 31, 2004	Restr	cross ucturing aarges	Adju Rest	ersals and stments to ructuring harges	Rest	Net ructuring d Other harges	Red	n-Cash luctions o the ccrual	Pa	Cash ayments	Rest C Ji	ccrued ructuring losts at une 30, 2005
							(In thou	sands)						
Workforce reduction	\$	1,339	\$	_	\$	(1)	`\$	(1)	\$	(100)	\$	(236)	\$	1,002
Excess facilities		20,686		13		(2,268)		(2,255)		41		(4,499)		13,973
Exit costs		108		_		(23)		(23)		_		(32)		53
											_		-	
Subtotal	\$	22,133	\$	13	\$	(2,292)	\$	(2,279)	\$	(59)	\$	(4,767)	\$	15,028
Other charges		303		_		(27)		(27)		(67)		(125)		84
											_			
Total restructuring and other charges	\$	22,436	\$	13	\$	(2,319)	\$	(2,306)	\$	(126)	\$	(4,892)	\$	15,112
											_			
Included in current portion of accrued restructuring costs	\$	8,711											\$	5,693
													_	
Included in long-term portion of accrued restructuring costs	\$	13,725											\$	9,419

#### 2002 Restructuring Plan

In April 2002, VeriSign initiated a plan to restructure its operations to rationalize, integrate and align resources. This restructuring plan included workforce reductions, abandonment of excess facilities, write-offs of abandoned property and equipment, and other charges. To date, VeriSign has recorded \$109.1 million in restructuring charges under its 2002 restructuring plan.

### VERISIGN, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Net restructuring and other charges associated with the 2002 restructuring plan that were recorded during the periods ended June 30, 2005 and 2004 are as follows:

	Enc	Three Months Ended June 30,		Ionths ded e 30,
	2005	2004	2005	2004
		(In thou	usands)	
Workforce reduction	\$ —	\$ 27	\$ —	\$ 27
Excess facilities	90	(155)	298	(155)
Exit costs	_	(471)	_	(471)
Subtotal	90	(599)	298	(599)
Other charges	_	_	_	_
-				
Total restructuring and other charges	\$ 90	\$ (599)	\$ 298	\$ (599)

*Workforce reduction.* VeriSign's 2002 restructuring plan resulted in a workforce reduction of approximately 400 employees across certain business functions, operating units, and geographic regions. Workforce reduction charges related primarily to severance and fringe benefits.

Excess facilities. Excess facilities restructuring charges take into account the fair value of lease obligations of the abandoned space, including the potential for sublease income. Estimating the amount of sublease income requires management to make estimates for the space that will be rented, the rate per square foot that might be received and the vacancy period of each property. These estimates could differ materially from actual amounts due to changes in the real estate markets in which the properties are located, such as the supply of office space and prevailing lease rates. Changing market conditions by geographic location and considerable work with third-party leasing companies requires VeriSign to periodically review each lease and, as necessary, change its estimates on a prospective basis. VeriSign recorded charges and adjustments for excess facilities that were either abandoned or downsized relating to lease terminations and non-cancelable lease costs. During the three and six months ended June 30, 2005, VeriSign recorded approximately \$0.1 million and \$0.3 million, respectively of charges related to excess facilities.

*Exit costs.* VeriSign previously recorded other exit costs consisting of the write-off of prepaid license fees associated with products that were originally intended to be incorporated into VeriSign's product offerings but were subsequently abandoned as a result of the decision to restructure.

At June 30, 2005, the accrued liability associated with the 2002 restructuring plan was \$7.1 million and consisted of the following:

	Restr Co Dece	ecrued ructuring osts at mber 31, 2004	Restr	ross ucturing arges	Adjust Restru	sals and ments to acturing arges	Restru and	Tet octuring Other arges	Redu	-Cash uctions the crual		Cash yments	Restr Co Ju	crued ucturing osts at ne 30, 2005
							(In thousa	nds)						
Workforce reduction	\$	_	\$	_	\$	_	`\$	_	\$	_	\$	_	\$	_
Excess facilities		8,386		272		26		298		(12)		(1,728)		6,944
Exit costs		150		_		_		_		(8)				142
											_			
Total restructuring charges	\$	8,536	\$	272	\$	26	\$	298	\$	(20)	\$	(1,728)	\$	7,086
Included in current portion of accrued restructuring costs	¢	2,985											¢	2,976
accrued restructuring costs	<b>J</b>	2,903											Φ	2,970
		<u> </u>												
Included in long-term portion of accrued restructuring costs	\$	5,551											\$	4,110
COSIS	Ψ	3,331											Ψ	7,110

## VERISIGN, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Cash payments totaling approximately \$45.4 million related to the abandonment of excess facilities under both restructuring plans will be paid over the respective lease terms, the longest of which extends through June 2014. The present value of future cash payments related to lease terminations due to the abandonment of excess facilities is expected to be as follows:

	Contractual Lease Payments	Anticipated Sublease Income (In thousands)	Net
2005 (remaining 6 months)	\$ 5,593	\$ (1,977)	\$ 3,616
2006	8,222	(1,373)	6,849
2007	6,288	(2,459)	3,829
2008	3,899	(2,209)	1,690
2009	3,000	(2,077)	923
2010	3,006	(2,092)	914
Thereafter	10,548	(7,452)	3,096
	\$ 40,556	\$ (19,639)	\$20,917

#### Note 5. Property and Equipment, Net

Property and equipment, net consisted of the following:

	June 30, 2005	December 31, 2004
	(In thou	isands)
Original cost	\$ 906,652	\$ 853,337
Less: accumulated depreciation and amortization	(383,768)	(340,716)
Property and equipment, net	\$ 522,884	\$ 512,621

#### Note 6. Goodwill and Other Intangible Assets

The following table summarizes the changes in the carrying amount of goodwill as allocated to the Company's operating segments during the six months ended June 30, 2005:

	Internet Services Group		nmunications Services Group	Total
		(In	thousands)	
Balance at December 31, 2004	\$189,427	\$	536,000	\$725,427
LightSurf acquisition	<u> </u>		224,077	224,077
Other acquisitions	13,657		8,889	22,546
Balance at June 30, 2005	\$203,084	\$	768,966	\$972,050

Purchased goodwill is not amortized but is subject to testing for impairment on at least an annual basis. VeriSign performed its annual impairment test as of June 30, 2005. The fair value of VeriSign's reporting units is determined using either the income or the market valuation approach or a combination thereof. Under the income approach, the fair value of the reporting unit is based on the present value of estimated future cash flows that the reporting unit is expected to generate over its remaining life. Under the market approach, the value of the reporting unit is based on an analysis that compares the value of the reporting unit to values of publicly traded companies in similar lines of business. Other intangible assets are valued using the income approach. In the application of the income and market valuation approaches, VeriSign is required to make estimates of future

#### VERISIGN, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

operating trends and judgments on discount rates and other variables. Actual future results related to assumed variables could differ from these estimates. There was no impairment charge to goodwill and other intangible assets from the annual impairment tests conducted in the second quarter of 2005 or 2004.

VeriSign's other intangible assets are comprised of:

		As of June 30, 2005			
	Gross Carrying Value	Accumulated Amortization and Impairment	Net Carrying Value		
		(In thousands)			
Customer relationships	\$281,454	\$ (171,013)	\$ 110,441		
Technology in place	157,746	(106,707)	51,039		
Carrier relationships	27,700	(4,963)	22,737		
Non-compete agreement	18,073	(8,367)	9,706		
Trade name	17,760	(3,182)	14,578		
Contracts with ICANN and customer lists	146,838	(110,079)	36,759		
Total other intangible assets	\$649,571	\$ (404,311)	\$ 245,260		

		As of December 31, 2004			
	Gross Carrying Value	Accumulated Amortization and Impairment	Net Carrying Value		
		(In thousands)			
Customer relationships	\$270,733	\$ (146,145)	\$ 124,588		
Technology in place	121,406	(99,474)	21,932		
Carrier relationships	27,700	(2,667)	25,033		
Non-compete agreement	16,220	(4,622)	11,598		
Trade name	17,828	(1,728)	16,100		
Contracts with ICANN and customer lists	146,238	(101,651)	44,587		
Total other intangible assets	\$600,125	\$ (356,287)	\$ 243,838		

Fully amortized other intangible assets are not included in the above tables. For the three months ended June 30, 2005 and 2004, amortization of other intangible assets was \$24.8 million and \$18.2 million, respectively. Amortization of other intangible assets was \$47.7 million and \$33.3 million for the six months ended June 30, 2005 and 2004, respectively. During the three months ended June 30, 2005 we expensed \$4.3 million of in-process research and development acquired in the purchase of LightSurf.

Estimated future amortization expense related to other intangible assets at June 30, 2005 is as follows:

	(In	thousands)
	_	
2005 (remaining 6 months)	\$	51,836
2006		86,122
2007		71,039
2008		18,334
2009		13,000
2010		4,721
Thereafter		208
	_	
	\$	245,260
	\$	245,260

#### VERISIGN, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

#### Note 7. Restricted Cash

Restricted cash includes \$45.0 million of cash related to a trust established during the first quarter of 2004 for VeriSign's director and officer liability self-insurance coverage. Additionally, as of June 30, 2005 and December 31, 2004, VeriSign has pledged approximately \$6.4 million, classified as restricted cash on the accompanying balance sheet, as collateral for standby letters of credit that guarantee certain of its contractual obligations, primarily relating to its real estate lease agreements, the longest of which is expected to mature in 2014.

#### Note 8. Comprehensive Income

Comprehensive income consists of net income adjusted for unrealized gains and losses on marketable securities classified as available-for-sale and foreign currency translation adjustments.

		Three Months Ended June 30,		Six Months Ended June 30,	
	2005 2004		2005	2004	
		(In tho	usands)		
Net income	\$41,295	\$21,945	\$90,470	\$31,015	
Change in unrealized gain (loss) on investments, net of tax	1,421	(3,160)	(879)	(2,777)	
Foreign currency translation adjustments	(318)	(1,704)	(1,690)	(978)	
Comprehensive income	\$42,398	\$17,081	\$87,901	\$27,260	

#### Note 9. Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consist of the following:

	June 30, 2005	December 31, 2004
	(In thou	sands)
Prepaid expenses	\$ 87,266	\$ 19,858
Other current assets	21,310	31,466
Prepaid expenses and other current assets	\$108,576	\$ 51,324

#### Note 10. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities consist of the following:

	June 30, 2005	December 31, 2004	
	(In the	ousands)	
Accounts payable	\$121,934	\$ 69,988	
Employee compensation	70,437	72,300	
Customer deposits	13,286	21,144	
Taxes	110,691	79,906	
Other	163,936	138,687	
Accounts payable and accrued liabilities	\$480,284	\$ 382,025	

#### VERISIGN, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

#### Note 11. Calculation of Net Income Per Share

Basic net income per share is computed by dividing net income (numerator) by the weighted-average number of shares of common stock outstanding (denominator) during the period. Diluted net income per share gives effect to dilutive common equivalent shares, including unvested stock options, using the treasury stock method.

The following table represents the computation of basic and diluted net income per share:

		Three Months Ended June 30,		Six Months Ended June 30,	
	2005	2004	2005	2004	
		(In thousands, exc	ept per share data)		
Basic and diluted net income per share:					
Net income	\$ 41,295	\$ 21,945	\$ 90,470	\$ 31,015	
Determination of basic and diluted shares:					
Weighted-average common shares outstanding	263,538	249,357	258,018	246,859	
Potential common shares—dilutive stock options	9,350	3,711	8,853	3,755	
Diluted weighted-average common shares outstanding	272,888	253,068	266,871	250,614	
Basic net income per share	\$ 0.16	\$ 0.09	\$ 0.35	\$ 0.13	
Diluted net income per share	\$ 0.15	\$ 0.09	\$ 0.34	\$ 0.12	
-					

For the three and six months ended June 30, 2005, VeriSign excluded 8,764,450 and 9,655,722 weighted-average stock options, respectively, with an exercise price that exceeded the average fair market value of VeriSign's common stock for the period with a weighted-average exercise price of \$73.62 and \$75.22, respectively, because their effect would have been anti-dilutive. For the three and six months ended June 30, 2004, VeriSign excluded 12,409,224 and 12,898,418 weighted-average stock options, respectively, with an exercise price that exceeded the average fair market value of VeriSign's common stock for the period with a weighted-average exercise price of \$68.70 and \$68.97 for the respective periods. Weighted-average potential common shares do not include stock options with an exercise price that exceeded the average fair market value of VeriSign's common stock for the period.

#### Note 12. Commitments and Contingencies

#### Legal proceedings

VeriSign is engaged in complaints, lawsuits and investigations arising in the ordinary course of business. VeriSign believes that it has adequate legal defenses and that the ultimate outcome of these actions will not have a material effect on VeriSign's condensed consolidated financial position and results of operations.

#### Indemnification

VeriSign enters into indemnification agreements with many of our customers and certain other business partners in the ordinary course of business. These agreements include provisions for indemnifying the customer against claims brought by third-parties that allege a VeriSign product infringes a patent, copyright or trademark, misappropriates a trade secret, or violates any other proprietary rights of that third-party. These indemnification obligations are generally subject to limits as specified in the agreement. It is not possible to estimate the maximum potential amount of future payments VeriSign could be required to make under these indemnification agreements. To date, VeriSign has not incurred significant costs to defend lawsuits or settle claims related to indemnification agreements. VeriSign has not recorded any liabilities for these indemnification agreements at June 30, 2005 or December 31, 2004.

### VERISIGN, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

At the Company's discretion and in the ordinary course of business, VeriSign subcontracts the performance of certain services. VeriSign enters into indemnification agreements that indemnify customers against damage caused by VeriSign's employees and subcontractors. These indemnification obligations are generally subject to limits as specified in the agreement. It is not possible to estimate the maximum potential amount of future payments VeriSign could be required to make under these indemnification agreements. The Company maintains insurance policies that may enable VeriSign to recover a portion of any such claim. VeriSign has not incurred significant costs to defend lawsuits or settle claims related to these indemnification agreements. VeriSign has not recorded any liabilities for these indemnification agreements at June 30, 2005 or December 31, 2004.

#### Note 13. Segment Information

Description of segments

VeriSign operates its business in two reportable segments: the Internet Services Group and the Communications Services Group.

The Internet Services Group consists of the Security Services business and Naming and Directory Services business. The Security Services business provides products and services to enterprises and organizations that want to establish and deliver secure Internet-based services for their customers and business partners, including the following types of services: enterprise security services, including VeriSign's managed security and authentication services, and e-commerce services, including Web trust and payment services. The Naming and Directory Services business provides registry services as the exclusive registry of domain names in the .com and .net gTLDs and certain ccTLDs, as well as providing certain value added services.

The Communications Services Group provides specialized managed communications services to wireline and wireless telecommunications carriers, cable companies and enterprise customers. VeriSign's managed communications service offerings include network services, intelligent database and directory services, application services, content services, and billing and payment services.

The segments were determined based primarily on how the chief operating decision maker ("CODM") views and evaluates VeriSign's operations. VeriSign's Chief Executive Officer has been identified as the CODM as defined by SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information." Other factors, including customer base, homogeneity of products, technology and delivery channels, were also considered in determining the reportable segments. Additionally, the performance of the Internet Services Group and the Communications Services Group is the measure used by the CODM for purposes of making decisions about allocating resources between the segments.

The following table reflects the results of VeriSign's reportable segments. Internal revenues and segment gross margin include transactions between segments that are intended to reflect an arm's length transfer at the best price available for comparable external transactions.

	Internet Services Group	Communications Services Group		Services Corporate		Total Segments
Three months ended June 30, 2005:						
Revenues	\$168,166	\$	276,664	\$	_	\$444,830
Cost of revenues	34,437		93,170		8,948	136,555
		_		_		
Gross margin	\$133,729	\$	183,494	\$	(8,948)	\$308,275

## VERISIGN, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

	Internet Services Group	ervices Services		Unallocated Corporate Expenses	Total Segments
			(In thousa	nds)	
Three months ended June 30, 2004:	4.00.00			•	****
Revenues	\$138,822	\$	117,223	\$ —	\$256,045
Cost of revenues	31,719		64,724	5,792	102,235
Gross margin	\$107,103	\$	52,499	\$ (5,792)	\$153,810
	Internet Services Group	Services Services Corpora		Unallocated Corporate Expenses	Total Segments
Six months anded June 20, 2005.			(In thousa	nds)	
Six months ended June 30, 2005:  Revenues	\$327,248	\$	518,573	\$ —	\$ 845,821
Cost of revenues	69,257	φ	174,558	17,582	261,397
Cost of revenues			174,550	17,502	201,557
Gross margin	\$257,991	\$	344,015	\$ (17,582)	\$ 584,424
	Internet Services Group	S	nunications ervices Group	Unallocated Corporate Expenses	Total Segments
			(In thousa	nds)	
Six months ended June 30, 2004:					
Revenues	\$268,898	\$	216,260	\$ —	\$ 485,158
Cost of revenues	60,207		122,554	10,956	193,717
Gross margin	\$208,691	\$	93,706	\$ (10,956)	\$ 291,441
Geographic information				Six Mont Jun	
		2005	2004	2005	2004
	_		(In th	ousands)	
Americas:					
United States	\$	283,439	\$ 208,508	\$ 510,988	\$ 403,452
Other (1)		4,582	4,357	10,047	9,508
Total Americas		288,021	212,865	521,035	412,960
EMEA (2)		133,381	26,791	279,610	39,450
APAC (3)		23,428	16,389	45,176	32,748
Total revenues	¢	444,830	\$ 256,045	\$ 845,821	\$ 485,158
Total revenues	Ф	777,050	Ψ 230,043	Ψ 040,041	<u> 4</u> υυ,1υ0

<sup>(1)</sup> Canada and Latin America

VeriSign operates in the United States, Europe, Japan, Australia, Brazil, South Africa, and India. In general, revenues are attributed to the country in which the contract originated. However, revenues from all digital certificates issued from the Mountain View, California facility and domain names issued from the Dulles, Virginia facility are attributed to the United States because it is impracticable to determine the country of origin.

<sup>(2)</sup> Europe, the Middle East and Africa ("EMEA")

<sup>(3)</sup> Australia, Japan and Asia Pacific ("APAC")

## VERISIGN, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following table shows a comparison of domestic and international long-term assets, which include property and equipment, net and other assets, net:

	June 30, 2005	December 31, 2004
	(In th	ousands)
Domestic long-term assets	\$510,700	\$ 502,032
International long-term assets	25,726	23,980
Total long-term assets	\$536,426	\$ 526,012

Assets are not tracked by segment and the chief operating decision maker does not evaluate segment performance based on asset utilization.

Major Customers

No customer accounted for 10% or more of consolidated revenues for the three or six months ended June 30, 2005 or June 30, 2004.

#### Note 14. Income Taxes

For the three and six months ended June 30, 2005, VeriSign recorded income tax expense of \$33.7 million and \$60.1 million, respectively. For the three and six months ended June 30, 2004, VeriSign recorded income tax expense of \$17.3 million and \$23.8 million, respectively. VeriSign has not recorded a benefit for U.S. federal and state deferred tax assets due to the uncertainty of their realization.

In assessing the realizability of deferred tax assets, management considers whether, under FAS 109 terminology, it is more likely than not that some portion or all of deferred tax assets will not be realized. The realization of deferred tax assets is based on several factors, including the Company's past earnings and the scheduling of deferred tax liabilities and projected income from operating activities. As of June 30, 2005, VeriSign does not believe it is more likely than not that the deferred tax assets relating to U.S. federal and state operations are realizable. However, depending on VeriSign's continued ability to achieve profitability, it may have sufficient evidence in the third quarter of fiscal 2005 to conclude that realization of additional deferred tax assets is more likely than not and thus realize a tax benefit in that period from a reduction of our deferred tax asset valuation allowance.

VeriSign follows FASB Interpretation ("FIN") No. 18, "Accounting for Income Taxes in Interim Periods," and APB 28, "Interim Financial Reporting" for its quarterly income tax provision. Accordingly, management's disclosure regarding the effects of the realizability of the deferred tax assets on continuing operations, goodwill, and additional paid-in capital remain materially unchanged from the disclosure provided in Note 13, "Income Taxes," in VeriSign's Form 10-K for the year ended December 31, 2004. As such, if the valuation allowance relating to deferred tax assets were released as of December 31, 2004, approximately \$240.7 million would be credited to the statement of operations, \$268.6 million would be credited to additional paid-in capital, and \$5.4 million would be credited to goodwill. However, management would continue to apply a valuation allowance of \$33.4 million to the deferred tax asset for capital loss carryforwards, and \$48.9 million to the deferred tax asset relating to the write-down of investments, due to the limited carryover life of such tax attributes These amounts do not reflect the effects to the deferred tax assets and liabilities from the acquisition of LightSurf Technologies, Inc. Had VeriSign not applied a valuation allowance and thus a zero net deferred tax asset balance relating to the acquisition of LightSurf, VeriSign would have recorded deferred tax assets of \$5.8 million and deferred tax liabilities of \$17.7 million. If VeriSign releases its valuation allowance as indicated in this footnote, the net \$11.9 million of deferred tax liability will be increased by the same amount.

#### VERISIGN, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

#### Note 15. Related Parties

VeriSign retained a 15% interest in Network Solutions' domain name registrar business after the sale to Pivotal Private Equity on November 25, 2003. The following table shows a comparison of revenue recognized from customers in which VeriSign holds an equity investment, including International Affiliates.

	Three Mon June	nths Ended e 30,	Six Mont Jun	hs Ended e 30,
	2005	2004	2005	2004
		(In tho	usands)	
Network Solutions	\$ 9,959	\$10,613	\$20,043	\$21,795
International Affiliates	2,326	2,193	4,574	4,824
Total revenues recognized from customers in which VeriSign holds an equity investment	\$12,285	\$12,806	\$24,617	\$26,619

VeriSign had \$1.0 million and \$2.8 million of trade receivables from Network Solutions at June 30, 2005 and 2004, respectively. VeriSign had \$2.3 million and \$2.6 million in trade receivables from International Affiliates at June 30, 2005 and 2004, respectively.

As part of the consideration for the Company's sale of its Network Solutions domain name registrar business, VeriSign received a \$40 million senior subordinated note that bears interest at 7% per annum for the first three years and 9% per annum thereafter and matures five years from the date of closing. During the three months ended March 31, 2005, VeriSign received a payment from Network Solutions in the amount of \$20.0 million, which included \$14.0 million to reduce the principal balance of the note receivable, \$3.8 million of interest income related to the note receivable and a dividend payment of \$2.2 million recorded in other income. The remaining principal and interest are due upon maturity. The present value of the note at June 30, 2005 was approximately \$25.2 million using a 10% market interest rate.

#### Note 16. Repurchase of Common Stock

In 2001, the Board of Directors of VeriSign authorized the use of up to \$350 million to repurchase shares of VeriSign's common stock on the open market, or in negotiated or block trades. During the three months ended June 30, 2005, 1,553,000 shares were repurchased at an aggregate cost of approximately \$42.5 million. During the three months ended March 31, 2005, no shares were repurchased. During the three months ended June 30, 2004, no shares were repurchased. At June 30, 2005, approximately \$124.8 million remained available for future repurchases under this program.

#### Note 17. Other Income, Net

The following table presents the components of other income, net for the three and six months ended June 30, 2005 and 2004:

		Three Months Ended June 30,		hs Ended e 30,
	2005	2004	2005	2004
		(In tho	usands)	
Interest income	\$ 8,725	\$2,945	\$15,734	\$ 6,676
Net foreign currency gains (losses)	5,432	(996)	5,847	(1,255)
Other, net	(73)	(411)	7,780	(2,851)
Total other income, net	\$14,084	\$1,538	\$29,361	\$ 2,570

### VERISIGN, INC. AND SUBSIDIARIES

#### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Interest income is derived principally from the investment of our surplus cash balances. Foreign currency gains and losses include foreign currency transaction gains and losses, realized gains and losses on hedging contracts and unrealized gains and losses on hedging contracts.

#### Note 18. Resolution of Tariff Dispute

During the three months ended March 31, 2005, VeriSign completed a settlement of litigation with a telecommunications carrier, resolving disputes over certain tariff charges for SS7 traffic that VeriSign passed through to telecommunications carriers who purchased its SS7 services. Under the settlement, the carrier refunded and/or credited certain amounts to VeriSign and VeriSign refunded and/or credited certain amounts to its customers. As a result of the settlement, VeriSign recorded other income of approximately \$6.0 million during the first quarter of 2005.

#### Note 19. Foreign Currency and Hedging Instruments

VeriSign conducts business throughout the world and transacts in multiple foreign currencies. As VeriSign continues to expand its international operations, the Company is increasingly exposed to foreign currency risks. In the fourth quarter of 2003, VeriSign initiated a foreign currency risk management program designed to mitigate foreign exchange risks associated with the monetary assets and liabilities of its operations that are denominated in non-functional currencies. The primary objective of this hedging program is to minimize the gains and losses resulting from fluctuations in exchange rates. The Company does not enter into foreign currency transactions for trading or speculative purposes, nor does it hedge foreign currency exposures in a manner that entirely offsets the effects of changes in exchange rates. The program may entail the use of forward or option contracts, and in each case, these contracts are limited to a duration of less than 12 months.

At June 30, 2005, VeriSign held forward contracts in notional amounts totaling approximately \$64.5 million to mitigate the impact of exchange rate fluctuations associated with certain foreign currencies. All hedge contracts were recorded at fair market value on the balance sheet and in earnings at year end 2004 and for the first six months of 2005. The Company attempts to limit its exposure to credit risk by executing foreign exchange contracts with high-quality financial institutions.

#### **Note 20.** Recent Accounting Pronouncements

In December 2004, the FASB issued SFAS No. 123R, "Share-Based Payment," which requires the measurement of all employee share-based payments to employees, including grants of employee stock options, using a fair-value-based method and the recording of such expense in their consolidated statements of operations. The accounting provisions of SFAS 123R are effective for fiscal years beginning after June 15, 2005. VeriSign is required to adopt SFAS 123R in the first quarter of 2006. The pro forma disclosures previously permitted under SFAS 123 no longer will be an alternative to financial statement recognition. Although the Company has not yet determined whether the adoption of SFAS 123R will result in amounts that are similar to the current pro forma disclosures under SFAS 123, VeriSign is evaluating the requirements under SFAS 123R and expects the adoption to have a significant adverse impact on their consolidated statements of operations and net income per share. See Note 2, "Stock Compensation Plans and Unearned Compensation" above for further information regarding the pro forma net income (loss) and net income (loss) per share amounts, for the three and six months ended June 30, 2005 and 2004, as if VeriSign had used a fair-value-based method similar to the methods required under SFAS 123R to measure compensation expense for employee stock incentive awards.

In December 2004, the FASB issued FASB Staff Position No. FAS 109-1 ("FAS 109-1"), "Application of FASB Statement No. 109, "Accounting for Income Taxes," to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004." The American Jobs Creation Act ("AJCA")

## VERISIGN, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

introduces a special 9% tax deduction on qualified production activities. FAS 109-1 clarifies that this tax deduction should be accounted for as a special tax deduction in accordance with SFAS 109. Pursuant to the AJCA, VeriSign will not be able to claim this tax benefit until the first quarter of fiscal 2006. The Company does not expect the adoption of these new tax provisions to have a material impact on their condensed consolidated financial position, results of operations or cash flows.

In December 2004, the FASB issued FASB Staff Position No. FAS 109-2 ("FAS 109-2"), "Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creations Act of 2004." The AJCA introduces a limited time 85% dividends received deduction on the repatriation of certain foreign earnings to a U.S. taxpayer (repatriation provision), provided certain criteria are met. FAS 109-2 provides accounting and disclosure guidance for the repatriation provision. The Company does not expect the adoption of these new tax provisions to have a material impact on their condensed consolidated financial position, results of operations or cash flows.

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections* ("SFAS 154") which replaces APB Opinion No. 20 *Accounting Changes* and SFAS No. 3, *Reporting Accounting Changes in Interim Financial Statements—An Amendment of APB Opinion No. 28*. SFAS 154 requires retrospective application to prior periods' financial statements of a voluntary change in accounting principal unless it is not practicable. SFAS 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005 and is required to be adopted by the Company in the first quarter of fiscal 2006. Although the Company will continue to evaluate the application of SFAS 154, management does not currently believe adoption will have a material impact on the Company's results of operations or financial position.

In March 2005, the FASB issued FASB Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations" (FIN 47). FIN 47 clarifies that the term conditional asset retirement obligation as used in FASB Statement No. 143, "Accounting for Asset Retirement Obligations," refers to a legal obligation to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. The obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and (or) method of settlement. Uncertainty about the timing and (or) method of settlement of a conditional asset retirement obligation should be factored into the measurement of the liability when sufficient information exists. FIN 47 also clarifies when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation. FIN 47 is effective no later than the end of fiscal years ending after December 15, 2005. The Company does not expect the adoption of this statement to have a material impact on their results of operations, financial position or cash flows.

#### Note 21. Subsequent Events

On July 14, 2005, VeriSign announced that it has completed its acquisition of iDefense, a Reston, Virginia-based privately held security intelligence firm. VeriSign paid approximately \$40 million in cash for all outstanding capital stock and vested options of iDefense. VeriSign also assumed all outstanding unvested stock options of iDefense. Payment of up to \$10 million of additional consideration may be made in the future, if additional contractual conditions are met.

On August 2, 2005, the Board of Directors of VeriSign authorized the use of up to \$500 million to repurchase shares of VeriSign's common stock on the open market, or in negotiated or block trades.

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

#### **Forward-Looking Statements**

You should read the following discussion in conjunction with the interim unaudited condensed consolidated financial statements and related notes.

Except for historical information, this Report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1934 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements involve risks and uncertainties, including, among other things, statements regarding our anticipated costs and expenses and revenue mix. Forward-looking statements include, among others, those statements including the words "expects," "anticipates," "intends," "believes" and similar language. Our actual results may differ significantly from those projected in the forward-looking statements. Factors that might cause or contribute to such differences include, but are not limited to, those discussed in the section "Factors That May Affect Future Results of Operations." You should carefully review the risks described in other documents we file from time to time with the Securities and Exchange Commission, including the Quarterly Reports on Form 10-Q or Current Reports on Form 8-K that we file in 2005 and our Annual Report on Form 10-K for the year ended December 31, 2004, which was filed on March 16, 2005. You are cautioned not to place undue reliance on the forward-looking statements, which speak only as of the date of this Quarterly Report on Form 10-Q. We undertake no obligation to publicly release any revisions to the forward-looking statements or reflect events or circumstances after the date of this document.

#### Overview

VeriSign, Inc. is a leading provider of intelligent infrastructure services that enable people and businesses to find, connect, secure, and transact across complex global networks. Since 2004, our business consisted of two reportable segments: the Internet Services Group and the Communications Services Group. Prior to 2004, our business included an additional reportable segment, the Network Solutions domain name registrar business, which was sold in November 2003.

During the second quarter of 2005, IT spending, domain name registrations and renewals and e-commerce activity in the U.S., Europe and Japan continued to improve and led to growth in revenues and deferred revenues for our Internet Services Group. The Internet Services Group recorded revenues of \$168.2 million during the second quarter. Communications Services Group revenues for the period were \$276.7 million. Content services contributed approximately \$174.7 million of revenues to the Communications Services Group's results. Revenues from communications services, which include our network services and database products, and revenues from commerce services, which include our billing and payments services and clearing and settlement services, together accounted for \$101.9 million of the Communications Services Group's revenues in the period

We derive the majority of our revenues and cash flows from a relatively small number of products and services sold primarily in the United States, Europe and Japan. In the Internet Services Group, more than 88% of the revenues during the second quarter of 2005 were derived from the sale of web certificates, payment services, managed authentication and security services, registry services and managed security services. In the Communications Services Group, 86% of the revenues were derived from the sale of calling name services, billing services, SS7 connectivity, signaling services, and content services during the same period.

#### Critical accounting policies and significant management estimates

The discussion and analysis of our financial condition and results of operations are based upon our condensed consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On an ongoing basis, management evaluates its estimates,

including those related to revenue recognition, allowance for doubtful accounts, long-lived assets, restructuring, royalty liabilities, and deferred taxes. Management bases its estimates on historical experience and on various assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily available from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following critical accounting policies affect our more significant judgments and estimates used in preparing our condensed consolidated financial statements:

#### Revenue recognition

We recognize revenue in accordance with current generally accepted accounting principles. Revenue recognition requirements are complex rules which require us to make judgments and estimates. In applying our revenue recognition policy we must determine which portions of our revenue are recognized currently and which portions must be deferred. In order to determine current and deferred revenue, we make judgments and estimates with regard to the products and services to be provided. Our assumptions and judgments regarding products and services could differ from actual events.

Revenues from our consulting services are recognized using either the percentage-of-completion method or on a time-and-materials basis as work is performed. Percentage-of-completion is based upon the ratio of hours incurred to total hours estimated to be incurred for the project. We have a history of accurately estimating project status and the hours required to complete projects. If different conditions were to prevail such that accurate estimates could not be made, then the use of the completed contract method would be required and all revenue and costs would be deferred until the project was completed. Revenues from time-and-materials are recognized as services are performed.

#### Allowance for doubtful accounts

We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. We regularly review the adequacy of our accounts receivable allowance after considering the size of the accounts receivable balance, each customer's expected ability to pay, and our collection history with each customer. We review significant invoices that are past due to determine if an allowance is appropriate based on the risk category using the factors described above. In addition, we maintain a general reserve by applying a percentage based on the age of the receivable. We also monitor our accounts receivable for concentration to any one customer, industry or geographic region. We require all acquired companies to adopt our credit policies. The allowance for doubtful accounts represents our best estimate, but changes in circumstances relating to accounts receivable may result in a requirement for additional allowances in the future. As of June 30, 2005, the allowance for doubtful accounts represented approximately 5% of total accounts receivable, or approximately \$13.8 million. A change of 1% in our estimate would amount to approximately \$2.9 million.

#### Valuation of long-lived intangible assets including goodwill

Our long-lived assets consist primarily of goodwill, other intangible assets and property and equipment. We review, at least annually, goodwill resulting from purchase business combinations for impairment in accordance with Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets." We review long-lived assets, including certain identifiable intangibles, for impairment whenever events or changes in circumstances indicate that we will not be able to recover the asset's carrying amount in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." Such events or circumstances include, but are not limited to, a significant decrease in the fair value of the underlying business or asset, a significant decrease in the benefits realized from the acquired business, difficulty and delays in integrating the business or a significant change in the operations of the acquired business or use of an asset.

Recoverability of long-lived assets other than goodwill is measured by comparison of the carrying amount of an asset to estimated undiscounted cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds its fair value.

Goodwill and other intangible assets, net of accumulated amortization, totaled approximately \$1,217 million at June 30, 2005, which was comprised of \$972 million of goodwill and \$245 million of other intangible assets. Other intangible assets include customer relationships, technology in place, carrier relationships, non-compete agreements, trade names, contracts with ICANN and customer lists. Factors we consider important which could trigger an impairment review include, but are not limited to, significant under-performance relative to expected historical or projected future operating results, significant changes in the manner of our use of our acquired assets, significant changes in the strategy of our overall business, or significant negative economic trends. If this evaluation indicates that the value of an intangible asset may be impaired, an assessment of the recoverability of the net carrying value of the asset over its remaining useful life is made. If this assessment indicates that an intangible asset is not recoverable, based on the estimated undiscounted future cash flows or other comparable market valuations of the entity or technology acquired over the remaining amortization period, the net carrying value of the related intangible asset will be reduced to fair value and the remaining amortization period may be adjusted. Any such impairment charge could be significant and could have a material adverse effect on our reported financial statements. It is our policy to engage third party valuation consultants to assist us in the measurement of the fair value of our long-lived intangible assets, including goodwill. There was no impairment charge to goodwill and other intangible assets from the annual impairment tests conducted in the second quarter of 2005 or 2004.

#### Restructuring and other charges

In November 2003, we initiated a restructuring plan related to the sale of our Network Solutions business and the realignment of other business units. In April 2002, we initiated plans to restructure our operations to more fully rationalize, integrate and align our resources. Both plans resulted in reductions in workforce, abandonment of excess facilities, disposal of property and equipment and other charges. We expect these restructuring plans to be completed in 2014 upon the expiration of our lease obligations for abandoned facilities. Restructuring charges take into account the fair value of lease obligations of the abandoned space, including the potential for sublease income. Estimating the amount of sublease income requires management to make estimates for the space that will be rented, the rate per square foot that might be received and the vacancy period of each property. These estimates could differ materially from actual amounts due to changes in the real estate markets in which the properties are located, such as the supply of office space and prevailing lease rates. Changing market conditions by location and considerable work with third-party leasing companies require us to periodically review each lease and change our estimates on a prospective basis, as necessary. Such estimates will likely be revised in the future. If sublease rates continue to change in these markets, or if it takes longer than expected to sublease these facilities, the actual lease expense could exceed this estimate by an additional \$20.3 million over the next ten years relating to our restructuring plans.

#### Provision for royalty liabilities for intellectual property rights

Certain of our content services utilize intellectual property owned or held under license by others. Where we have not yet entered into a license agreement with a holder, we record a provision for royalty payments that we estimate will be due once a license agreement is concluded. We estimate the royalty payments based on the prevailing royalty rate for the type of intellectual property being utilized. Our estimates could differ materially from the actual royalties to be paid under any definitive license agreements that may be reached due to changes in the market for such intellectual property, such as a change in demand for a particular type of content, in which case we would record a royalty expense materially different than our estimate.

#### Income taxes

We determine deferred tax assets and liabilities at the end of each year based on the future tax consequences that can be attributed to net operating loss and credit carryovers and differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, using the tax rate expected to be

in effect when the taxes are actually paid or recovered. The recognition of deferred tax assets is reduced by a valuation allowance if it is likely that the benefits will not be realized. The ultimate realization of deferred tax assets depends on the generation of future taxable income during the periods in which those temporary differences become deductible. We consider past performance, expected future taxable income and prudent feasible tax planning strategies in assessing the amount of the valuation allowance. Our forecast of expected future taxable income is based over such future periods that we believe can be reasonably estimated. Changes in market conditions that differ materially from our current expectations and changes in future tax laws in the U.S. and in international jurisdictions may cause us to change our judgments of future taxable income. These changes, if any, may require us to adjust our existing tax valuation allowance higher or lower than the amount we have recorded.

In addition, the calculation of tax liabilities involves significant judgment in estimating the impact of uncertainties in the application of complex tax laws. Resolution of these uncertainties in a manner inconsistent with our expectations could have a material impact on our results of operations. We account for income tax contingencies in accordance with SFAS No. 5, "Accounting for Contingencies."

#### **Employee Stock Options**

**Option Program Description** 

Our stock option program is a broad-based, long-term retention program that is intended to contribute to the success of the Company by attracting, retaining and motivating talented employees and to align employee interests with the interests of our existing stockholders. Stock options may be granted to eligible employees when they first join VeriSign and there is the potential for grants on an annual basis for eligible employees deemed by management to be key contributors. Additionally, stock options may be awarded if there is a significant change in an employee's responsibilities or as a result of a promotion. The compensation committee of the Board of Directors may grant additional options to executive officers and key employees for other reasons. Currently, we grant options from three stock option plans: the 1998 Equity Incentive Plan and the 2001 Stock Incentive Plan which are broad-based plans, under which options may be granted to all employees, consultants, independent contractors and advisors of VeriSign other than non-employee directors, and the 1998 Directors Stock Plan, under which options are granted automatically under a pre-determined formula to non-employee directors. Under these plans the participants may be granted options to purchase shares of VeriSign stock and substantially all of our employees and directors participate in at least one of our plans. Options issued under the 1998 Equity Incentive Plan and 2001 Stock Incentive Plan generally vest as to 25% of the shares on the first anniversary of the date of grant and as to 6.25% of the shares each of the next 12 quarters. Options issued under the 1998 Directors Stock Option Plan vest as to 6.25% of the shares each quarter after the date of grant, provided the optionee continues as a director or, if VeriSign so specifies in the grant, as a consultant of VeriSign.

We recognize that stock options dilute existing stockholders and have attempted to control the number of options granted while remaining competitive with our compensation packages. The potential dilution percentage is calculated as the new option grants for the year, net of options forfeited by employees leaving the Company, divided by the total outstanding shares at the beginning of the year. Please refer to the table below for the maximum potential dilution from options granted for the six months ended June 30, 2005 and for the years ended December 31, 2004 and 2003. This maximum potential dilution will only result if all options are exercised. Many of these options, which have up to a 10-year exercise period, have exercise prices substantially higher than the market price of our common stock as reported on the Nasdaq National Market. At June 30, 2005, approximately 28% of our stock options had exercise prices in excess of the closing price of our common stock as reported on the Nasdaq National Market.

All stock option grants to executive officers are made after a review by, and with the approval of the compensation committee of the Board of Directors. All stock option grants to non-executive officers are determined by VeriSign's chief executive officer in accordance with guidelines approved by the compensation committee. All members of the compensation committee are independent directors, as defined in the applicable

rules for issuers traded on The Nasdaq Stock Market. See the "Report of the Compensation Committee" appearing in our proxy statement dated April 26, 2005 for further information concerning the policies of our compensation committee regarding the use of stock options.

#### Distribution and Dilutive Effect of Options

The following table provides information about stock options granted for the six months ended June 30, 2005 and for the years ended December 31, 2004 and 2003, to our chief executive officer and the four most highly compensated executive officers, other than the chief executive officer, who were serving as executive officers at the end of 2004. These officers are referred to together as the Named Executive Officers. Please refer to the section entitled "Executive Options" below for the Named Executive Officers.

Employee and Executive Option Grants for the six months ended June 30, 2005 and for the years ended December 31, 2004 and 2003 are as follows:

	Six Months Ended June 30, 2005	2004	2003
	(Sh	ares in thousands)	
Shares subject to options granted	1,966	9,156	13,199
Less options cancelled	(1,802)	(4,574)	(5,838)
Net shares subject to options granted	164	4,582	7,361
Common shares outstanding at beginning of period	253,341	241,829	237,510
Net options granted during the period as a percentage of outstanding common shares	0.1%	1.9%	3.1%
Options granted to Named Executive Officers during the period as a percentage of total options granted	0.0%	12.8%	8.0%
Options held by Named Executive Officers as a percentage of total options outstanding	26.1%	28.1%	23.4%

Option grants to Named Executive Officers vary from year to year depending on individual achievements and future potential in leading the Company. For additional information about our employee stock option plan activity for the fiscal years 2004 and 2003, please refer to Note 12 to the Notes to Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended December 31, 2004, which was filed on March 16, 2005.

#### General Option Information

The following table summarizes option activity for the six months ended June 30, 2005 and for the years ended December 31, 2004 and 2003:

	Six Months Ended June 30, 2005 2004			2003					
	Shares	A E	eighted- werage xercise Price	Shares	A	Veighted- Average Exercise Price	Shares	A E	eighted- werage xercise Price
Outstanding at beginning of period	32,878,169	\$	33.74	31,999,664	\$	36.87	26,960,479	\$	47.41
Assumed in business combinations	1,546,527		3.88	687,659		4.79	_		_
Granted	1,965,573		27.96	9,156,123		20.20	13,199,316		13.45
Exercised	(2,624,053)		10.46	(4,391,205)		11.04	(2,321,981)		9.05
Cancelled	(1,801,811)		71.40	(4,574,072)		45.98	(5,838,150)		43.66
Outstanding at end of period	31,964,405		31.73	32,878,169		33.74	31,999,664		36.87
Exercisable at end of period	16,788,701		43.33	17,085,569		48.19	18,156,403		48.05
Weighted-average fair value of options granted during the period		\$	13.96		\$	10.80		\$	9.00

The following table sets forth a comparison of the number of shares subject to our options whose exercise prices were below the closing price of our common stock on June 30, 2005 ("In-the-Money" options) to the number of shares subject to options whose exercise prices were equal to or greater than the closing price of our common stock on such date ("Out-of-the-Money" options).

In-the-Money and Out-of-the-Money option information as of June 30, 2005:

	Exercisable		Unexercisable			Total			
	Shares	1	Veighted- Average Exercise Price	Shares	A	eighted- Average Exercise Price	Shares	I	Veighted- Average Exercise Price
In-the-Money	9,386,924	\$	14.28	13,671,931	\$	17.21	23,058,855	\$	16.02
Out-of-the-Money (1)	7,401,777		80.18	1,503,773		34.11	8,905,550		72.40
Total options outstanding	16,788,701	\$	43.33	15,175,704	\$	18.89	31,964,405	\$	31.73

(1) Out-of-the-Money options are those options with an exercise price of our common stock at or above the closing price of \$28.76 on June 30, 2005, as reported by the Nasdaq National Market.

#### **Executive Options**

For the first six months of 2005, no options were granted to the Named Executive Officers. The following table sets forth for each of our Named Executive Officers the shares acquired and the value realized on the exercise of stock options during the first six months of 2005 and the number and value of exercisable and unexercisable options on June 30, 2005.

Option Exercises and Remaining Holdings as of June 30, 2005 of Named Executive Officers:

	Number of Shares		Number of Securities Underlying Unexercised Options at June 30, 2005  Exercisable Unexercisable		Values of Unexo Money O <sub>l</sub> June 30,	otions at
Name	Acquired on Exercise	Value Realized			Exercisable	Unexercisable
Stratton D. Sclavos	_	\$ —	4,226,654	1,420,760	\$ 35,778,924	\$ 9,047,212
Dana L. Evan	45,506	1,035,835	647,396	221,250	2,098,113	1,479,338
Quentin P. Gallivan	218,914	3,296,567	465,000	198,750	_	1,429,163
Robert J. Korzeniewski	25,000	448,250	368,750	198,750	1,631,113	1,429,163
Judy Lin	25,000	504,375	412,771	175,729	3,160,188	1,253,997

(1) Option values are based on the closing price of our common stock of \$28.76 as reported by the Nasdaq National Market on June 30, 2005, net of the option exercise price.

The following table sets forth information about our common stock that may be issued upon the exercise of options, warrants and rights under all of our existing equity compensation plans as of June 30, 2005.

	Equi	<b>Equity Compensation Plan Information</b>							
	(A)		(B)	(C) Number of securities remaining available					
Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	exerc outstan	ted-average ise price of ding options, ts and rights	for future issuance under equity compensation plans (excluding securities reflected in column (A))					
Equity compensation plans approved by stockholders	12,402,329	\$	51.90	22,404,151(1)					
Equity compensation plans not approved by stockholders	17,682,217(2)(3)		19.34	11,552,170					
Total	30,084,546	\$	32.76	33,956,321					

- (1) Includes 8,036,062 shares available for purchase under VeriSign's 1998 Employee Stock Purchase Plan ("Purchase Plan"). The Purchase Plan contains an "evergreen" provision whereby the aggregate number of shares available for issuance increase automatically on January 1 of each year by 1% of VeriSign's outstanding shares of common stock on each immediately preceding December 31.
- (2) Includes securities to be issued upon exercise of outstanding options under VeriSign's 2001 Stock Incentive Plan ("Incentive Plan"). The Incentive Plan contains an "evergreen" provision whereby the aggregate number of shares available for issuance increase automatically on January 1 of each year by 2% of VeriSign's outstanding shares of common stock on each immediately preceding December 31.
- (3) Does not include options to purchase an aggregate of 1,879,859 shares of common stock with a weighted-average exercise price of \$15.22 that were assumed in business combinations.

#### **Results of Operations**

#### Revenues

We have two reportable segments: the Internet Services Group and the Communications Services Group. A comparison of revenues for the three and six months ended June 30, 2005 and 2004 is presented below.

	2005	2004	Change
		(Dollars in thousands)	
Three months ended:			
Internet Services Group	\$168,166	\$138,822	21%
Communications Services Group	276,664	117,223	136%
Total revenues	\$444,830	\$256,045	74%
Six months ended:			
Internet Services Group	\$327,248	\$268,898	22%
Communications Services Group	518,573	216,260	140%
Total revenues	\$845,821	\$485,158	74%

Total revenues increased \$188.8 million and \$360.7 million for the three and six months ended June 30, 2005, respectively, compared to the same periods last year, primarily due to the increase in Communications Services Group revenues attributable to content services.

#### Internet Services Group

Internet Services Group revenues increased \$29.3 million and \$58.4 million for the three and six months ended June 30, 2005, respectively, primarily due to an increase in security services revenues of \$15.3 and \$33.0 for the respective periods as a result of increased managed security services revenues and as a result of a higher installed base of digital certificates, and an increase in the number of active online merchants in our secured payment services business. In addition, our naming and directory services revenues increased approximately \$14.0 million and \$25.3 million for the respective periods, as a result of an increase in the number of active domain names ending in .com and .net under management.

The following table compares active domain names ending in .com and .net managed by our naming and directory services business, the approximate installed base of Web site digital certificates in our commerce site services business and the approximate number of active online merchants in our secured payments services business as of June 30, 2005 and 2004:

	June 30, 2005	June 30, 2004	% Change
Active domain names ending in .com and .net	44.2 million	34.0 million	30%
Installed base of Web site digital certificates	471,000	430,000	10%
Active online merchants	143,500	112,000	28%

We expect Internet Services Group revenues will continue to grow during the third quarter of 2005 as demand for our Naming and Directory Services and Security Services is expected to grow.

#### Communications Services Group

Communications Services Group revenues increased approximately \$159.4 million and \$302.3 million for the three and six months ended June 30, 2005, respectively, primarily due to an increase in revenues of \$160.0 million and \$303.7 million from content services for the respective periods. Commerce revenues, which include our billing and payments services and clearing and settlement services, decreased approximately \$7.5 million and \$15.4 million for the three and six months ended June 30, 2005, compared with the same periods last year, due to consolidation of certain billing services customers and reduced pricing on contracts, partially offset by carrier subscriber growth. Communications revenues, which include our network services and data base products, increased approximately \$6.9 million and \$14.0 million for the three and six months ended June 30, 2005, compared with the same periods last year, as a result of an increase in transaction volumes offset by lower prices for some services.

The following table shows a comparison of the approximate number of quarterly database queries as of June 30, 2005 and 2004:

	2005	2004	Change
Quarterly database queries	14.4 billion	12.2 billion	18%

Compared to the second quarter of 2005, we expect Communication Services Group revenues to decrease during the third quarter due to seasonality and subscriber churn in our mobile content business.

#### Revenues by Geographic Region

Our revenues are broken out into three geographic regions consisting of the Americas, EMEA and APAC. The following tables show a comparison of our revenues by geographic region for the three and six months ended June 30, 2005 and 2004:

es by geographic region for the three and six months ended June 30, 2003 and 2004.	Three Mor June			
	2005	2004	% Change	
	(D	Pollars in thousands)		
Americas:	,	·		
United States	\$283,439	\$208,508	36%	
Other (1)	4,582	4,357	5%	
Total Americas	288,021	212,865	35%	
EMEA (2)	133,381	26,791	398%	
APAC (3)	23,428	16,389	43%	
Total revenues	\$444,830	\$256,045	74%	
		Six Months Ended June 30,		
			% Change	
	2005	e 30,		
Americas:	2005 (D	2004 Oollars in thousands)	Change —	
United States	2005 (D \$510,988	2004 2004 Pollars in thousands) \$403,452	Change	
	2005 (D	2004 Oollars in thousands)	Change —	
United States	\$510,988 10,047	2004  2004  Collars in thousands)  \$403,452  9,508	Change	
United States Other (1)  Total Americas	2005 (D \$510,988	2004 2004 Pollars in thousands) \$403,452	27% 6%	
United States Other (1)	\$510,988 10,047 521,035	2004  2004  Collars in thousands)  \$403,452  9,508  412,960	27% 6% 26%	
United States Other (1)  Total Americas EMEA (2)	\$510,988 10,047 521,035 279,610	2004  2004  Collars in thousands)  \$403,452  9,508  412,960  39,450	27% 6% 26% 609%	

<sup>(1)</sup> Canada and Latin America

<sup>(2)</sup> Europe, the Middle East and Africa ("EMEA")

<sup>(3)</sup> Australia, Japan and Asia Pacific ("APAC")

Revenues increased \$75.2 million and \$108.1 million in the Americas region in the three and six months ended June 30, 2005, respectively, compared to the same periods last year, primarily due to increased content service and naming and directory service revenues in the U.S. Revenues in the EMEA region increased \$106.6 million and \$240.2 million in the same periods primarily related to revenues from content services. APAC revenues increased \$7.0 million and \$12.4 in the three months and six months ended June 30, 2005, compared to the same periods last year, primarily due to increases in the sales of enterprise security services by VeriSign Japan along with the growth of our content services in the APAC region.

# Costs and Expenses

Total costs and expenses increased \$165.4 million and \$290.7 million for the three and six months ended June 30, 2005 as compared to the same period last year. Cost of revenues increased \$34.3 million and \$67.7 million during the three and six months ended June 30, 2005 as compared to the same periods last year, primarily as a result of increased revenues and an increase in the number of employees. Sales and marketing increased \$93.6 million and \$182.8 million during the three and six months ended June 30, 2005 as compared to the same periods last year, primarily as a result of increased advertising to promote the Jamba! and Jamster brands.

The following table shows a comparison of our employee base by function as of the end of each quarter presented:

	June 30, 2005	June 30, 2004	% Change
Employee headcount:			
Cost of revenues	1,598	1,431	12%
Sales and marketing	788	613	29%
Research and development	762	371	105%
General and administrative	613	551	11%
Total	3,761	2,966	27%

Primarily as a result of growth in our content services business, we have added over 790 employees to our employee headcount since June 30, 2004. Excluding the effects of any future acquisitions or dispositions, we expect our employee headcount to increase for the remainder of 2005 across all business units and corporate services.

### Cost of revenues

Cost of revenues consists primarily of costs related to providing digital certificate enrollment and issuance services, payment services, operational costs for the domain name registration business, customer support and training, consulting and development services, operational costs related to the management and monitoring of our clients' network security infrastructures, content licensing costs, carrier costs for our SS7 and IP-based networks and costs of facilities and computer equipment used in these activities.

A comparison of cost of revenues for the three and six months ended June 30, 2005 and 2004 is presented below:

	2005	2004	% Change
		(Dollars in thousands)	
Three months ended:			
Cost of revenues	\$136,555	\$102,235	34%
Percentage of revenues	31%	40%	
Six months ended:			
Cost of revenues	\$261,397	\$193,717	35%
Percentage of revenues	31%	40%	

Cost of revenues increased \$34.3 million and \$67.7 million for the three and six months ended June 30, 2005, respectively, as compared to the same periods last year. Direct cost of revenues increased approximately \$13.6 million and \$31.2 million for the three and six months ended June 30, 2005 as compared to the same period last year. Salary and employee benefit costs increased approximately \$6.5 million and \$16.9, for the respective periods, primarily as a result of an increase in the number of employees. Contract and professional services expenses increased \$5.0 million and \$6.7 million for the respective periods.

As a percentage of revenues, cost of revenues decreased for the three and six months ended June 30, 2005 compared to the same period last year primarily due to increased revenues from our content services, which generally have lower costs of revenues as a percentage of revenue than our other services.

We expect cost of revenues to increase in absolute dollars as revenues continue to grow for the remainder of 2005. We expect cost of revenues as a percentage of revenues to decrease during the remainder of 2005.

#### Sales and marketing

Sales and marketing expenses consist primarily of costs related to sales, marketing, and policy activities. These expenses include salaries, sales commissions, sales operations and other personnel-related expenses, travel and related expenses, trade shows, costs of lead generation, costs of computer and communications equipment and support services, facilities costs, consulting fees and costs of marketing programs, such as Internet, television, radio, print, and direct mail advertising costs.

A comparison of sales and marketing expenses for the three and six months ended June 30, 2005 and 2004 is presented below:

	2005	2004	% Change
		Dollars in thousands)	
Three months ended:	· ·		
Sales and marketing	\$140,417	\$46,847	200%
Percentage of revenues	32%	18%	
Six months ended:			
Sales and marketing	\$269,794	\$87,017	210%
Percentage of revenues	32%	18%	

Sales and marketing expenses increased approximately \$93.6 million and \$182.8 million for the three and six months ended June 30, 2005, respectively, as compared to the same periods last year. Sales and marketing expenses for content services accounted for approximately \$87.3 million and \$157.4 million of the increases compared to the respective periods last year. This was primarily attributable to increased advertising to promote content services. Salary and employee benefit costs and employee travel expenses accounted for approximately \$3.4 million and \$18.9 million of the increase for the three and six months ended June 30, 2005 as compared to the same periods last year, primarily as a result of an increase in the number of employees.

As a percentage of revenues, sales and marketing expenses increased for the three and six months ended June 30, 2005 compared to the same period last year primarily due to increased direct media advertising and marketing of our content services.

We expect sales and marketing expenses to decrease in absolute dollars and decrease as a percentage of revenues in the third quarter of 2005.

#### Research and development

Research and development expenses consist primarily of costs related to research and development personnel, including salaries and other personnel-related expenses, consulting fees and the costs of facilities, computer and communications equipment and support services used in service and technology development.

A comparison of research and development expenses for the three and six months ended June 30, 2005 and 2004 is presented below:

	2005	2004	% Change ———
	(1	Dollars in thousands)	
Three months ended:			
Research and development	\$26,974	\$15,253	77%
Percentage of revenues	6%	6%	
Six months ended:			
Research and development	\$48,991	\$31,960	53%
Percentage of revenues	6%	7%	

Research and development expenses increased approximately \$11.7 million and \$17.0 million for the three and six months ended June 30, 2005 as compared to the same periods last year. Increased salary and employee benefit costs, primarily related to content services accounted for approximately \$8.8 million and \$13.2 million of the increase for the respective periods. Also contributing to the increases were increased contract and professional services fees of \$1.2 million and \$1.3 million, as compared to the same periods last year.

As a percentage of revenues, research and development expenses were unchanged for the three months ended June 30, 2005 compared to the same period last year. As a percentage of revenues, research and development expenses decreased for the six months ended June 30, 2005 compared to the same period last year primarily due to increased revenues from our content services. We believe that rapid development of new and enhanced services and technologies are necessary to maintain our leadership position in the marketplace. Accordingly, we intend to continue to recruit experienced research and development personnel both domestically and internationally and to make other investments in research and development. We expect research and development expenses to increase modestly in absolute dollars and remain relatively constant as a percentage of revenues during the remainder of 2005.

#### General and administrative

General and administrative expenses consist primarily of salaries and other personnel-related expenses for our executive, administrative, legal, finance, information technology and human resources personnel, facilities, computer and communications equipment, management information systems, support services, professional services fees, certain tax and license fees and bad debt expense.

A comparison of general and administrative expenses for the three and six months ended June 30, 2005 and 2004 is presented below:

	2005	2004	Change
		Dollars in thousands)	
Three months ended:			
General and administrative	\$49,944	\$38,595	29%
Percentage of revenues	11%	15%	
Six months ended:			
General and administrative	\$92,322	\$73,834	25%
Percentage of revenues	11%	15%	

General and administrative expenses increased approximately \$11.3 million and \$18.5 million for the three and six months ended June 30, 2005 as compared to the same periods last year. Increases in the number of employees employed by our content services business accounted for approximately \$5.7 million and \$10.4

million of the increase for the three and six months ended June 30, 2005, respectively. Increased costs for contracted professional services accounted for approximately \$4.9 million and \$7.7 million of the increase for the respective periods.

As a percentage of revenues, general and administrative expenses decreased for the three and six months ended June 30, 2005 compared to the same period last year primarily due to increased revenues from our content services, which generally have lower general and administrative expenses as a percentage of revenues than other services, coupled with our ability to leverage existing general and administrative costs.

We expect general and administrative expenses to decrease in absolute dollars and decrease as a percentage of overall revenues during the remainder of 2005.

Restructuring and other (reversals) charges

Below is a comparison of the restructuring and other (reversals) charges under the 2003 and 2002 restructuring plans for the three and six months ended June 30, 2005 and 2004:

	2005	2004	% Change
		Dollars in thousands)	
Three months ended:			
Restructuring and other (reversals) charges	\$ (133)	\$ (3,626)	(96)%
Percentage of revenues	0%	(1)%	
Six months ended:			
Restructuring and other (reversals) charges	\$(2,008)	\$11,881	(117)%
Percentage of revenues	0%	2%	

The changes in restructuring and other (reversals) charges are primarily due to the timing of our restructuring initiatives.

2003 Restructuring Plan. In November 2003, we initiated a restructuring plan related to the sale of our Network Solutions business and the realignment of other business units. During the three months and six months ended June 30, 2005, we recorded a net reversal of restructuring charges of approximately \$0.2 million and \$2.3 million, respectively. These reversals were primarily related to excess facilities primarily in connection with a decision to utilize and build out a facility that we had treated as abandoned under our 2003 restructuring plan and for which we had previously recorded a restructuring charge. The net reversals were partially offset by certain taxes and lease charges. During the three and six months ended June 30, 2004, we recorded asset impairment charges of approximately \$0.9 million and \$13.6 million, respectively, related to a service whose cash flows did not sustain the value of the assets employed to deliver the service. Estimates were made to determine the fair market value of the assets based on third party resale values and management judgment of the fair value of similar used equipment. During the three months ended June 30, 2004, we recorded a reversal of \$3.0 million of excess restructuring charges taken in prior quarters primarily due to a change in lease obligations for a facility and adjustments to our original estimated charges as compared to actual payments for severance and fringe benefits.

2002 Restructuring Plan. In April 2002, we initiated a restructuring plan to restructure our operations to rationalize, integrate and align resources. During the three months and six months ended June 30, 2005, we recorded approximately \$0.1 million and \$0.3 million, respectively of charges related to excess facilities. During the three and six months ended June 30, 2004, we reversed \$0.6 million in excess facilities and exit costs.

See Note 4 to the Notes to Condensed Consolidated Financial Statements for further information.

Amortization of other intangible assets

A comparison of amortization of other intangible assets for the three and six months ended June 30, 2005 and 2004 is presented below:

	2005	2004	Change
	(I	ollars in thousands)	
Three months ended:			
Amortization of other intangible assets	\$24,821	\$18,223	36%
Percentage of revenues	6%	7%	
Six months ended:			
Amortization of other intangible assets	\$47,661	\$33,333	43%
Percentage of revenues	6%	7%	

SFAS No. 142 requires that purchased goodwill and certain indefinite-lived intangibles be tested for impairment on at least an annual basis. SFAS No. 144 requires that long-lived assets, including intangible assets with finite lives, be reviewed for impairment whenever events or circumstances indicate that there has been a decline in the fair value of an asset. We completed our last annual impairment testing in the second quarter of 2005 and recorded no impairment charges.

Amortization of other intangible assets increased approximately \$6.6 million and \$14.3 million for the three and six months ended June 30, 2005, respectively, as compared to the same periods last year primarily due to amortization related to intangible assets for the acquisitions of Jamba! in June of 2004, LightSurf in April of 2005 and other acquisitions in the first quarter of 2004. Amortization of assets acquired from Jamba! accounted for approximately \$4.1 million and \$10.6 million of the increase for the three and six months ended June 30, 2005, respectively. Amortization of intangible assets acquired from LightSurf accounted for approximately \$2.9 million of the increase for the three and six months ended June 30, 2005.

Acquired in-process research and development

During the three months ended June 30, 2005, we expensed in-process research and development acquired in the purchase of LightSurf. See Note 3 to the Notes to Condensed Consolidated Financial Statements for further information.

# Minority interest

Minority interest represents the portion of net income belonging to minority shareholders of our consolidated subsidiaries.

A comparison of minority interest for the three and six months ended June 30, 2005 and 2004 is presented below:

	2005	2004	Change
		Dollars in thousands)	
Three months ended:			
Minority interest	\$(1,048)	\$ (836)	(25)%
Percentage of revenues	0.2%	0.3%	
Six months ended:			
Minority interest	\$(2,176)	\$(1,129)	(93)%
Percentage of revenues	0.3%	0.2%	

Minority interest increased during the three and six months ended June 30, 2005 primarily from increased net income from our VeriSign Japan subsidiary. In June 2004, we acquired the remaining 49% minority interest in VeriSign Australia, which is now a wholly-owned subsidiary.

#### Other income, net

Other income, net consists primarily of interest earned on our cash, cash equivalents, short-term and long-term investments, gains and losses on the sale or impairment of equity investments, and the net effect of foreign currency transaction gains and losses.

A comparison of other income, net for the three and six months ended June 30, 2005 and 2004 is presented below:

	2005	2004	% Change
	(Dol	lars in thousands)	
Three months ended:			
Other income	\$14,084	\$1,538	816%
Percentage of revenues	3%	0.6%	
Six months ended:			
Other income	\$29,361	\$2,570	1,042%
Percentage of revenues	3%	0.5%	

Other income increased approximately \$12.5 million and \$26.8 million during the three and six months ended June 30, 2005 as compared to the same periods last year. Increased net gains recognized on foreign currency hedging accounted for \$6.4 million and \$7.1 million of the increase for the three and six months ended June 30, 2005, respectively, compared to the same periods last year. Interest income increased \$5.7 million and \$9.0 million during the respective periods, compared to the same periods last year, primarily as a result of higher cash balances and slightly higher interest rates during the six months ended June 30, 2005. In addition, we recorded a gain of approximately \$6.0 million related to the resolution of a dispute with a telecommunications carrier customer in the three months ended March 31, 2005. In addition, impairment of investments, net of realized gains, decreased \$3.7 million during the three and six months ended June 30, 2005, compared to the same periods last year. See Note 17 to the Notes to Condensed Consolidated Financial Statements for further information.

### Income tax expense

For the quarter ended June 30, 2005, we recorded income tax expense of \$33.7 million, compared to \$17.3 million for the same period in 2004. For the six months ended June 30, 2005, we recorded income tax expense of \$60.1 million, compared to \$23.8 million for the same period in 2004. The increases were primarily due to increased taxable net income. We have not recorded a benefit for U.S. federal and state deferred tax assets due to the uncertainty of their realization.

In assessing the realizability of deferred tax assets, management considers whether, under FAS 109 terminology, it is more likely than not that some portion or all of deferred tax assets will not be realized. The realization of deferred tax assets is based on several factors, including the Company's past earnings and the scheduling of deferred tax liabilities and projected income from operating activities. Currently, management does not believe it is more likely than not that the deferred tax assets relating to U.S. federal and state operations are realizable. However, depending on our continued ability to achieve profitability, we may have sufficient evidence in the third quarter of fiscal 2005 to conclude that realization of additional deferred tax assets is more likely than not and thus realize a tax benefit in that period from a reduction of our deferred tax asset valuation allowance.

VeriSign follows FIN 18, "Accounting for Income Taxes in Interim Periods," and APB 28, "Interim Financial Reporting" for its quarterly income tax provision. Accordingly, management's guidance regarding the effects of the realizability of the deferred tax assets on continuing operations, goodwill, and additional paid-in capital remain materially unchanged from the guidance provided in Note 13, "Income Taxes," in our Form 10-K for the year ended December 31, 2004. As such, if the valuation allowance relating to deferred tax assets were

released as of December 31, 2004, approximately \$240.7 million would be credited to the statement of operations, \$268.6 million would be credited to additional paid-in capital, and \$5.4 million would be credited to goodwill. However, management would continue to apply a valuation allowance of \$33.4 million to the deferred tax asset for capital loss carryforwards, and \$48.9 million to the deferred tax asset relating to the write-down of investments, due to the limited carryover life of such tax attributes. These amounts do not reflect the effects to the deferred tax assets and liabilities from the acquisition this quarter of LightSurf Technologies, Inc. Had we not applied a valuation allowance and thus a zero net deferred tax asset balance relating to the acquisition of Lightsurf, we would have recorded deferred tax assets of \$5.8 million and deferred tax liabilities of \$17.7 million. If we release our valuation allowance, as described above,, the net \$11.9 million of deferred tax liability will be recorded and goodwill will be increased by the same amount.

## **Liquidity and Capital Resources**

	June 30, 2005	December 31, 2004	% Change
	(	Dollars in thousands)	ı
Cash and cash equivalents	\$449,579 `	\$ 330,641	36%
Short-term investments	431,960	406,784	6%
Subtotal	\$881,539	\$ 737,425	20%
Restricted cash	51,444	51,518	0%
Total	\$932,983	\$ 788,943	18%
	Six Month June 2005		\$ Change
	June	30,	
Cash flows provided by (used in)	2005	2004 (In thousands)	Change
Operating activities	2005 \$213,926	2004 (In thousands) \$ 145,905	Change \$ 68,021
Operating activities Investing activities	2005 \$213,926 (84,067)	2004 (In thousands) \$ 145,905 (144,083)	\$ 68,021 60,016
Operating activities Investing activities Financing activities	\$213,926 (84,067) (7,514)	2004 (In thousands) \$ 145,905 (144,083) 23,838	\$ 68,021 60,016 (31,352)
Operating activities Investing activities	2005 \$213,926 (84,067)	2004 (In thousands) \$ 145,905 (144,083)	\$ 68,021 60,016

At June 30, 2005, our principal source of liquidity was \$881.5 million of cash, cash equivalents and short-term investments, consisting principally of commercial paper, medium term investment-grade corporate notes, corporate bonds and notes, U.S. government and agency securities and money market funds.

Working capital increased \$134.8 million over the periods presented primarily due to net cash provided by operating activities.

Net cash provided by operating activities of approximately \$213.9 million for the six months ended June 30, 2005 consisted primarily of net income of \$90.5 million adjusted for non-cash items totaling \$111.4 million, including depreciation and amortization of property and equipment of approximately \$42.6 million, amortization of other intangible assets of approximately \$47.7 million, expensing of acquired in-process research and development of approximately \$4.3 million and \$12.1 million provided by working capital.

Net cash used in investing activities of approximately \$84.1 million for the six months ended June 30, 2005 was primarily attributed to net investment purchases of \$26.0 million, purchases of property and equipment of \$45.8 million and net cash paid in business combinations of \$18.0 million, partially offset by a \$17.2 million payment by Network Solutions for partial payment of principal on a note receivable. This note receivable is described in Note 15 of the Notes to Condensed Consolidated Financial Statements.

Net cash used in financing activities of approximately \$7.5 million for the six months ended June 30, 2005 was primarily related to proceeds of approximately \$35.9 from issuance of common stock from option exercises and our employee stock purchase plan, offset by repurchases of common stock of \$42.5 million.

Our planned capital property and equipment expenditures for 2005 are anticipated to be approximately \$110 million, of which we spent approximately \$45.8 million during the six months ended June 30, 2005, primarily for computer and communications equipment and computer software within all areas of the Company. Our most significant expenditures will be focused on productivity, cost improvement and market development initiatives for the Internet Services Group and the Communications Services Group. Other capital property and equipment expenditures will be for productivity and cost improvement initiatives for corporate services.

Future operating lease payments include payments related to leases on excess facilities included in VeriSign's restructuring plans. The restructuring liability is included on the balance sheet as accrued restructuring costs. Amounts related to the lease terminations due to the abandonment of excess facilities will be paid over the respective lease terms, the longest of which extends through 2014. If sublease rates decrease in these markets, or if it takes longer than expected to sublease these facilities, the actual lease expense could exceed this estimate by an additional \$20.3 million over the next nine years relating to our restructuring plans. The present value of future cash payments that will be made over the next nine years related to the abandonment of excess facilities is approximately \$20.9 million. See Note 4 of the Notes to Condensed Consolidated Financial Statements.

In 2001, our Board of Directors authorized the use of up to \$350 million to repurchase shares of our common stock on the open market, or in negotiated or block trades. During the three months ended June 30, 2005, 1,553,000 shares were repurchased at an aggregate cost of approximately \$42.5 million. During the three months ended June 30, 2004, no shares were repurchased. At June 30, 2005, approximately \$124.8 million remained available for future repurchases under this program.

We believe our existing cash, cash equivalents and short-term investments and operating cash flows, will be sufficient to meet our working capital and capital expenditure requirements.

We believe existing cash and short-term investments, together with funds generated from operations should be sufficient to meet operating requirements. Our philosophy regarding the maintenance of a balance sheet with a large component of cash, cash equivalents and short-term investments reflects our views on potential future capital requirements relating to expansion of our businesses, acquisitions, and share repurchases. We regularly assess our investment management approach in view of our current and potential future needs.

#### **Factors That May Affect Future Results of Operations**

In addition to other information in this Form 10-Q, the following risk factors should be carefully considered in evaluating us and our business because these factors currently have a significant impact or may have a significant impact on our business, operating results or financial condition. Actual results could differ materially from those projected in the forward-looking statements contained in this Form 10-Q as a result of the risk factors discussed below and elsewhere in this Form 10-Q.

# Our operating results may fluctuate and our future revenues and profitability are uncertain.

Our operating results have varied and may fluctuate significantly in the future as a result of a variety of factors, many of which are outside our control. These factors include the following:

- the long sales and implementation cycles for, and potentially large order sizes of, some of our security and communications services and the timing and execution of individual customer contracts;
- volume of domain name registrations and customer renewals in our registry services business;

- · the mix of all our services sold during a period;
- · our success in marketing and market acceptance of our services by our existing customers and by new customers;
- · changes in marketing expenses related to promoting and distributing our services;
- customer renewal rates and turnover of customers of our services;
- continued development of our direct and indirect distribution channels for our security services and communications services (including our content services), both in the U.S. and abroad;
- changes in the level of spending for information technology-related products and services by enterprise customers;
- · our success in assimilating the operations, products, services and personnel of any acquired businesses;
- · the seasonal fluctuations in consumer use of communications services, including our content services;
- the timing and execution of individual customer contracts, particularly large contracts;
- the impact of price changes in our communications services, security services and payment services or our competitors' products and services;
- the impact of Statement of Financial Accounting Standards No. 123R that will require us to record a charge to earnings for employee stock option grants; and
- · general economic and market conditions as well as economic and market conditions specific to the telecommunications and Internet industries.

Our operating expenses may increase. If an increase in our expenses is not accompanied by a corresponding increase in our revenues, our operating results will suffer, particularly as revenues from some of our services are recognized ratably over the term of the service, rather than immediately when the customer pays for them, unlike our sales and marketing expenditures, which are expensed in full when incurred.

Due to all of the above factors, our revenues and operating results are difficult to forecast. Therefore, we believe that period-to-period comparisons of our operating results will not necessarily be meaningful, and you should not rely upon them as an indication of future performance. Also, operating results may fall below our expectations and the expectations of securities analysts or investors in one or more future periods. If this were to occur, the market price of our common stock would likely decline.

# Our operating results may be adversely affected by the uncertain geopolitical environment and unfavorable economic and market conditions.

Adverse economic conditions worldwide have contributed to downturns in the telecommunications and technology industries in the past and could impact our business in the future, resulting in:

- reduced demand for our services as a result of a decrease in information technology and telecommunications spending by our customers;
- · increased price competition for our products and services; and
- higher overhead costs as a percentage of revenues.

Recent political turmoil in many parts of the world, including terrorist and military actions, may continue to put pressure on global economic conditions. If the economic and market conditions in the United States and globally do not continue to improve, or if they deteriorate, we may experience material adverse impacts on our business, operating results, and financial condition as a consequence of the above factors or otherwise.

#### Our limited operating history under our current business structure may result in significant fluctuations of our financial results.

In April 2005 and May 2005, we completed our acquisitions of LightSurf Technologies, Inc. and R4 Global Solutions, respectively. In February 2004 and June 2004, we completed our acquisitions of Guardent, Inc. and Jamba!, respectively. Between 2000 and 2003, we completed several acquisitions, including our acquisitions of Network Solutions, Illuminet Holdings and H.O. Systems. In November 2003, we sold our Network Solutions domain name registrar business. LightSurf, Jamba!, Network Solutions, Illuminet Holdings and H.O. Systems operated in different businesses from our then-current business. Therefore, we have only a limited operating history on which to base an evaluation of our consolidated business and prospects. Our success will depend on many factors, many of which are not entirely under our control, including, but not limited to, the following:

- · the successful integration of acquired companies;
- the use of the Internet and other Internet Protocol, or IP, networks for electronic commerce and communications;
- · the extent to which digital certificates and domain names are used for electronic commerce or communications;
- growth in the number of Web sites;
- growth in wireless networks and communications;
- growth in demand for our services;
- · the continued evolution of electronic and mobile commerce as a viable means of conducting business;
- · the competition for any of our services;
- the perceived security of electronic commerce and communications over the Internet and other IP networks;
- the perceived security of our services, technology, infrastructure and practices;
- the significant lead times before a new product or service begins generating revenues;
- · the varying rates at which telecommunications companies, telephony resellers and Internet service providers use our services;
- the success in marketing and overall demand for our content services to consumers and businesses;
- the loss of customers through industry consolidation, or customer decisions to deploy in-house or competitor technology and services; and
- our continued ability to maintain our current, and enter into additional, strategic relationships.

#### To address these risks we must, among other things:

- · successfully market our services to new and existing customers;
- attract, integrate, train, retain and motivate qualified personnel;
- · respond to competitive developments;
- · successfully introduce new services; and
- · successfully introduce enhancements to our services to address new technologies and standards and changing market conditions.

#### We have faced difficulties assimilating, and may incur costs associated with, acquisitions.

We made several acquisitions in the last five years and may pursue additional acquisitions in the future. We have experienced difficulty in, and in the future may face difficulties, integrating the personnel, products, technologies or operations of companies we acquire. Assimilating acquired businesses involves a number of other risks, including, but not limited to:

- the potential disruption of our ongoing business;
- · the potential impairment of relationships with our employees, customers and strategic partners;
- the need to manage more geographically-dispersed operations, such as our offices in the states of Kansas, Illinois, Massachusetts, Pennsylvania, Rhode Island, Texas, Virginia, and Washington, and in Australia, Europe, India, Japan, South Africa and South America;
- greater than expected costs, unknown liabilities and the diversion of management's resources from other business concerns involved in identifying, completing and integrating acquisitions;
- the inability to retain the key employees of the acquired businesses;
- · adverse effects on the existing customer relationships of acquired companies;
- our inability to incorporate acquired technologies successfully into our operations infrastructure;
- the difficulty of assimilating the operations and personnel of the acquired businesses;
- · the potential incompatibility of business cultures;
- additional regulatory requirements;
- any perceived adverse changes in business focus;
- entering into markets and acquiring technologies in areas in which we have little experience, as is the case with our acquisition of Jamba!;
- the need to incur debt, which may reduce our cash available for operations and other uses, or issue equity securities, which may dilute the ownership interests of our existing stockholders; and
- the inability to maintain uniform standards, controls, procedures and policies.

If we are unable to successfully address any of these risks for future acquisitions, our business could be harmed.

Additionally, there is risk that we may incur additional expenses associated with an impairment of a portion of goodwill and other intangible assets due to changes in market conditions for acquisitions. Under generally accepted accounting principles, we are required to evaluate goodwill for impairment on an annual basis and to evaluate other intangible assets as events or circumstances indicate that such assets may be impaired. These evaluations could result in further impairments of goodwill or other intangible assets.

# The expansion of our international operations subjects our business to additional economic risks that could have an adverse impact on our revenues and business.

International revenues accounted for approximately 36% of our total revenues for the three months ended June 30, 2005. As a result of the growth of our content services and other businesses outside the U.S., we expect that international revenues will continue to increase in absolute monetary terms and as a percentage of revenues. We intend to expand our international operations and international sales and marketing activities. For example, we expect to expand our operations and marketing activities throughout Asia, Europe, India, and Latin America

and we currently have facilities and over 500 employees in Germany. Expansion in these international markets has required and will continue to require significant management attention and resources. We may also need to tailor some of our other services for a particular market and to enter into international distribution and operating relationships. We have limited experience in localizing our services and in developing international distribution or operating relationships. We may not succeed in expanding our services into international markets. Failure to do so could harm our business. In addition, there are risks inherent in doing business on an international basis, including, among others:

- · competition with foreign companies or other domestic companies entering the foreign markets in which we operate;
- differing and uncertain regulatory requirements;
- · legal uncertainty regarding liability and compliance with foreign laws;
- · export and import restrictions on cryptographic technology and products incorporating that technology;
- tariffs and other trade barriers and restrictions;
- · difficulties in staffing and managing foreign operations;
- longer sales and payment cycles;
- problems in collecting accounts receivable;
- currency fluctuations, as our international revenues from Europe, South Africa, Japan, South America and Australia are not denominated in U.S. Dollars;
- potential problems associated with adapting our content services to technical conditions existing in different countries;
- the necessity of developing foreign language portals and products for our content services;
- · difficulty of authenticating customer information for digital certificates, payment services and other purposes;
- political instability;
- failure of foreign laws to protect our U.S. proprietary rights adequately;
- · more stringent privacy policies in foreign countries;
- additional vulnerability from terrorist groups targeting American interests abroad;
- · seasonal reductions in business activity; and
- potentially adverse tax consequences.

#### Our failure to manage past and future growth in our business could harm our business.

Between December 31, 1995 and June 30, 2005, we grew from 26 to approximately 3,760 employees. This was achieved through internal growth, as well as acquisitions. During this time period, we opened new sales offices and significantly expanded our U.S. and non-U.S. operations. To successfully manage past growth and any future growth, we will need to continue to implement additional management information systems, continue the development of our operating, administrative, financial and accounting systems and controls and maintain close coordination among our executive, engineering, accounting, finance, marketing, sales and operations organizations. Any failure to manage growth effectively could harm our business.

The business environment is highly competitive and, if we do not compete effectively, we may suffer price reductions, reduced gross margins and loss of market share.

Competition in Security Services. Our security services are targeted at the rapidly evolving market for Internet security services, including network security, authentication, validation and secure payment services, which enable secure electronic commerce and communications over wireline and wireless IP networks. The market for security services is intensely competitive, subject to rapid change and significantly affected by new product and service introductions and other market activities of industry participants.

Principal competitors generally fall within one of the following categories: (1) companies such as RSA Security, Inc. and Entrust Technologies, which offer software applications and related digital certificate products that customers operate themselves; (2) companies such as Geo Trust and Digital Signature Trust Company (a subsidiary of Identrus) that primarily offer digital certificate and certification authority, or CA, related services; and (3) companies focused on providing a bundled offering of products and services such as BeTrusted. We also experience competition from a number of smaller companies, and we believe that our primary long-term competitors may not yet have entered the market. Furthermore, Netscape and Microsoft have introduced software products that enable the issuance and management of digital certificates, and we believe that other companies could introduce similar products.

In addition, browser companies that embed our interface technologies or otherwise feature them as a provider of digital certificate products and services in their Web browsers or on their Web sites could also promote our competitors or charge us substantial fees for promotions in the future.

We face competition in our payment services business from companies such as CyberSource, Authorize.Net (a division of Lightbridge) and First Data Corporation among others.

Competition in Managed Security Services. Consulting companies or professional services groups of other companies with Internet expertise are current or potential competitors to our managed security services. These companies include large systems integrators and consulting firms, such as Accenture, formerly Andersen Consulting, IBM Global Services and Lucent NetCare. We also compete with security product companies that offer managed security services in addition to other security services, such as Symantec and ISS, as well as a number of providers such as Ubizen and RedSiren that offer managed security services exclusively. Telecommunications providers, such as MCI which recently acquired NetSec, a provider of managed security services, are also potential competitors. In addition, we compete with some companies that have developed products that automate the management of IP addresses and name maps throughout enterprise-wide intranets, and with companies with internally developed systems integration efforts.

Competition in Communications Services. The market for communications services is extremely competitive and subject to significant pricing pressure. Competition in this area arises from two primary sources. Incumbent carriers provide competing services in their regions. In addition, we face direct competition on a nationwide basis from unregulated companies, including Syniverse Technologies and other carriers such as Southern New England Telephone Diversified Group, a unit of SBC Communications. Our wireless billing and payment services also are subject to competition from providers such as Boston Communications Group, Amdocs, and Convergys Corporation. We are also aware of major Internet service providers, software developers and smaller entrepreneurial companies that are or may in the future be focusing significant resources on developing and marketing products and services that may compete directly with ours. Furthermore, customers are increasingly likely to deploy internally developed communications technologies and services which may reduce the demand for technologies and services from third party providers such as VeriSign and further increase competitive pricing pressures.

Competition in Content Services. The market for content services is extremely competitive. Competitors include developers of content and entertainment products and services in a variety of domestic and international markets, such as Infospace, Itouch, Wisdom Entertainment, Arvato mobile, Monstermob and Buongiorno/

Vitaminic. This business also faces competition from mobile network operators such as Cingular, Verizon Wireless, Sprint, T-Mobile, Vodafone, O<sub>2</sub>, Orange, E-Plus and Telefónica, as well as Internet portal operators such as Yahoo!, AOL, T-Online and Google. Additional competitors are handset manufacturers such as Nokia and software providers such as Microsoft. As the market for wireless entertainment and information products matures, mobile phone companies, broadcasters, music publishers, other content providers or others may begin to develop competing products or services.

Competition in Registry Services. ICANN has introduced several registry service providers for new gTLDs that directly compete with the services we provide for the .com and .net gTLDs, as well as with the ccTLDs offered by us. The gTLDs .biz and .info were launched in 2001 and the gTLDs .name, .pro, .aero, .museum and .coop were launched in 2002 and 2003. Domain names registrations and other services within these gTLDs are available through ICANN accredited registrars. In addition, we currently face competition from the over 240 ccTLD registry operators who compete directly for the business of entities and individuals that are seeking to establish a Web presence.

We also face competition from service providers that offer outsourced domain name registration, resolutions and other DNS services to organizations that require a reliable and scalable infrastructure. Among the competitors are UltraDNS, NeuLevel, Affilias, Register.com and Tucows.com.

Competition in Digital Brand Management Services. We face competition from companies providing services similar to some of our Digital Brand Management Services. In the monitoring services, registration and domain name asset management area of our business, our competition comes primarily from ICANN accredited registrars and various smaller companies providing similar services.

Several of our current and potential competitors have longer operating histories and significantly greater financial, technical, marketing and other resources than we do and therefore may be able to respond more quickly than we can to new or changing opportunities, technologies, standards and customer requirements. Many of these competitors also have broader and more established distribution channels that may be used to deliver competing products or services directly to customers through bundling or other means. If such competitors were to bundle competing products or services for their customers, the demand for our products and services might be substantially reduced and the ability to distribute our products successfully and the utilization of our services would be substantially diminished. New technologies and the expansion of existing technologies may increase the competitive pressure.

New technologies and the expansion of existing technologies may increase competitive pressure. We cannot assure that competing technologies developed by others or the emergence of new industry standards will not adversely affect our competitive position or render our security services or technologies noncompetitive or obsolete. In addition, our markets are characterized by announcements of collaborative relationships involving our competitors. The existence or announcement of any such relationships could adversely affect our ability to attract and retain customers. As a result of the foregoing and other factors, we may not be able to compete effectively with current or future competitors, and competitive pressures that we face could materially harm our business.

# Our communications services business depends in part on the acceptance of our SS7 network and the telecommunications industry's continuing use of SS7 technology.

Our future growth in our communications services business depends, in part, on the commercial success and reliability of our SS7 network. Our SS7 network is a vital component of our intelligent network services and has been a significant source of revenues for our Communications Services Group. Our communications services business will suffer if our target customers do not use our SS7 network. Our future financial performance will also depend on the successful development, introduction and customer acceptance of new and enhanced SS7-based services. We are not certain that our target customers will choose our particular SS7 network solution or continue to use our SS7 network. In the future, we may not be successful in marketing our SS7 network or any new or enhanced services.

The inability of our customers to successfully implement our signaling and network services with their existing systems could adversely affect our business

Significant technical challenges exist in our signaling and network services business because many of our customers:

- purchase and implement SS7 network services in phases;
- deploy SS7 connectivity across a variety of telecommunication switches and routes; and
- integrate our SS7 network with a number of legacy systems, third-party software applications and engineering tools.

Customer implementation currently requires participation by our order management and our engineering and operations groups, each of which has limited resources. Some customers may also require us to develop costly customized features or capabilities, which increase our costs and consume a disproportionate share of our limited customer service and support resources. Also, we typically charge one-time flat rate fees for initially connecting a customer to our SS7 network and a monthly recurring flat rate fee after the connection is established. If new or existing customers have difficulty deploying our products or require significant amounts of our engineering service support, we may experience reduced operating margins. Our customers' ability to deploy our network services to their own customers and integrate them successfully within their systems depends on our customers' capabilities and the complexity involved. Difficulty in deploying those services could reduce our operating margins due to increased customer support and could cause potential delays in recognizing revenues until the services are implemented.

Our failure to achieve or sustain market acceptance of our communications services at desired pricing levels and industry consolidation could adversely impact our revenues and cash flow.

The telecommunications industry is characterized by significant price competition. Competition and industry consolidation in our communications services could result in significant pricing pressure and an erosion of our market share. Pricing pressure from competition could cause large reductions in the selling price of our services. For example, our competitors may provide customers with reduced communications costs for Internet access or private network services, reducing the overall cost of services and significantly increasing pricing pressures on us. We would need to offset the effects of any price reductions by increasing the number of our customers, generating higher revenues from enhanced services or reducing our costs, and we may not be able to do so successfully. We believe that the business of providing network connectivity and related network services will see increased consolidation in the future. Consolidation could decrease selling prices and increase competition in these industries, which could erode our market share, revenues and operating margins in our Communications Services Group. Consolidation in the telecommunications industry has led to the merging of many companies, including AT&T Wireless and Price Communications, both customers of our Communications Services Group, and there have been recent announcements of proposed mergers involving other of our customers, including, MCI and Nextel. Our business could be harmed if these mergers result in the loss of customers by our Communications Services Group. Furthermore, customers may choose to deploy internally developed communications technologies and services thereby reducing the demand for technologies and services we offer which could harm our business.

Our content services business depends on agreements with many different third parties, including wireless carriers and content providers. If these agreements are terminated or not renewed, or are amended to require us to change the way our content services are offered to customers, our business could be harmed.

Our content services business depends on our ability to enter into and maintain agreements with many different third parties including:

- · Wireless carriers and other mobile phone service providers, upon which this business is highly dependent for billing its customers; and
- Developers, music publishers and other providers of content, upon which this business is substantially dependent for content such as ring tones and games.

These agreements are typically for a short term, or are otherwise terminable upon short notice, and in the case of agreements with carriers, other mobile phone service providers and content developers, are non-exclusive. If these third parties reduce their commitment to us, terminate their agreements with us or enter into similar agreements with our competitors, the results of operations of our Communications Services Group could be materially harmed. For example, because we depend on wireless carriers to bill customers for our services, a loss of any of these relationships, or our failure to enter into new relationships with additional wireless carriers on commercially reasonable terms, could prevent us from billing and receiving revenues from customers. This business could also be harmed if we are unable to enter into additional agreements with third parties on commercially reasonable terms.

Some wireless carriers have implemented more detailed enrollment procedures before their customers can purchase content services such as those we offer. Similar enrollment procedures or other requirements affecting content services may be adopted by other wireless carriers or by trade associations seeking to establish industry-wide standards, and could adversely affect subscriber growth and renewal rates in our content services business.

# Our content services business is dependent on third parties offering attractive content and technology on acceptable terms.

Only some of our content services are developed internally. We also receive content, such as ring tones, games and logos from third parties. If the market for mobile entertainment and information continues to develop positively, content providers might try to raise their prices. Some providers insist on charging fixed fees for their content regardless of revenues, so if we fail to achieve anticipated revenues, we would achieve lower margins for our content services. There is no assurance that we will be able to timely purchase content having the requisite quality in the future and on commercially reasonable terms. Should we be unable to acquire attractive content from third parties and on acceptable terms, this could adversely affect our content services business.

# Our customer subscription agreements for our content services are typically cancelable and our business could be harmed if we fail to retain current customers or if we fail to obtain significant numbers of new customers to replace customers who cancel or fail to renew.

Our content services are typically sold as fixed weekly or monthly subscriptions. Our customers for these services may cancel their subscriptions for our service at the end of each service period and in fact, many customers elect to do so. We have limited historical data with respect to rates of customer subscription renewals, so we cannot accurately predict customer renewal rates. Our customers' subscription and renewal rates may decline or fluctuate as a result of a number of factors, including their dissatisfaction with the service, pricing pressure, changes in preferences and trends, competitive services, adverse coverage in the news media, changes in the way we advertise our services or other reasons. If our customers cancel or fail to renew their subscriptions for our content services or if we fail to obtain significant numbers of new customers to replace customers who cancel or fail to renew, our revenue could decline and our content services business will suffer.

#### Our business depends on the continued growth of the Internet and adoption and continued use of IP networks.

Our future success depends, in part, on continued growth in the use of the Internet and IP networks. If the use of and interest in the Internet and IP networks does not grow, our business would be harmed. To date, many businesses and consumers have been deterred from utilizing the Internet and IP networks for a number of reasons, including, but not limited to:

- · potentially inadequate development of network infrastructure;
- security concerns, particularly for online payments, including the potential for merchant or user impersonation and fraud or theft of stored data and information communicated over IP networks;
- privacy concerns, including the potential for third parties to obtain personally identifiable information about users or to disclose or sell data without notice to or the consent of such users;

- · other security concerns such as attacks on popular Web sites by "hackers";
- inconsistent quality of service;
- · inability to integrate business applications on IP networks;
- · the need to operate with multiple and frequently incompatible products;
- · limited bandwidth access; and
- government regulation.

The widespread acceptance of the Internet and IP networks will require a broad acceptance of new methods of conducting business and exchanging information. Organizations that already have invested substantial resources in other methods of conducting business may be reluctant to adopt new methods. Also, individuals with established patterns of purchasing goods and services and effecting payments may be reluctant to change.

A number of states, as well as the U.S. Congress, have been considering various initiatives that could permit sales and use taxes on Internet sales. If any of these initiatives are adopted, it could substantially impair the growth of electronic commerce and therefore hinder the growth in the use of the Internet and IP networks, which could harm our business.

# Many of our target markets are evolving, and if these markets fail to develop or if our products and services are not widely accepted in these markets, our business could suffer.

We target our security services at the market for trusted and secure electronic commerce and communications over IP and other networks. As a result of our acquisition of Jamba!, our Communications Services Group is also targeting the consumer market for content services. Our Naming and Directory Services business unit is developing managed services designed to work with the EPCglobal Network and radio frequency identification, or RFID, technology. These are rapidly evolving markets that may not continue to grow. Even if these markets grow, our services may not be widely accepted. Accordingly, the demand for our services is very uncertain. The factors that may affect the level of market acceptance and, consequently, our services include the following:

- market acceptance of products and services based upon technologies other than those we use;
- · public perception of the security of our technologies and of IP and other networks;
- the introduction and consumer acceptance of new generations of mobile handsets;
- the introduction and acceptance of RFID technology and the EPCglobal Network;
- · the ability of the Internet infrastructure to accommodate increased levels of usage; and
- government regulations affecting electronic commerce and communications over IP networks.

If the market for electronic commerce and communications over IP and other networks does not grow or these services are not widely accepted in the market, our business would be materially harmed.

# Governmental regulation and the application of existing laws may slow business growth, increase our costs of doing business and create potential liability.

The growth and development of the Internet has led to new laws and regulations, as well as the application of existing laws to the Internet and wireless communications. Application of these laws can be unclear. The costs of complying or failure to comply with these laws and regulations could limit our ability to operate in our markets, expose us to compliance costs and substantial liability and result in costly and time-consuming litigation.

Foreign, federal or state laws could have an adverse impact on our business. For example, recent laws include those designed to restrict the on-line distribution of certain materials deemed harmful to children and impose additional restrictions or obligations for on-line services when dealing with minors. Such legislation may impose significant additional costs on our business or subject us to additional liabilities.

Due to the nature of the Internet, it is possible that the governments of other states and foreign countries might attempt to regulate Internet transmissions or prosecute us for violations of their laws. We might unintentionally violate such laws, such laws may be modified and new laws may be enacted in the future. Any such developments could increase the costs of regulatory compliance for us, force us to change our business practices or otherwise materially harm our business.

#### Our inability to react to changes in our industry and successfully introduce new products and services could harm our business.

The emerging nature of the Internet, other communications networks, content, digital certificate, domain name registration and payment services markets, and their rapid evolution, require us continually to improve the performance, features and reliability of our services, particularly in response to competitive offerings. In particular, the market for entertainment and information is characterized by changing technology, developing industry standards, changing customer preferences and trends (which also vary from country to country), and the constant introduction of new products and services. In order to remain competitive, we must continually improve our access technology and software, support the latest transmission technologies, and adapt our products and services to changing market conditions and customer preferences. When entertainment products are placed on the market, it is difficult to predict whether they will become popular.

The communications network services industry is also characterized by rapid technological change and frequent new product and service announcements. Significant technological changes could make our technologies obsolete and other changes in our markets, particularly content, could result in some of our other products and services losing market share. Accordingly, we must continually improve the responsiveness, reliability and features of our services and develop new features, services and applications to meet changing customer needs in our target markets. For example, we sell our SS7 network services primarily to traditional telecommunications companies that rely on traditional voice networks. Many emerging companies are providing convergent Internet protocol-based network services. Our future success could also depend upon our ability to provide products and services to these Internet protocol-based telephony providers, particularly if IP-based telephony becomes widely accepted. We cannot assure that we will be able to adapt to these challenges or respond successfully or in a cost-effective way to adequately meet them. Our failure to do so would adversely affect our ability to compete and retain customers or market share.

### New products and services developed or introduced by us may not result in any significant revenues.

We must commit significant resources to develop new products and services before knowing whether our investments will result in products and services the market will accept. The success of new products and services depends on several factors, including proper new definition and timely completion, introduction and market acceptance. For example, our selection in January 2004 by EPCglobal, a not-for-profit standards organization, to operate the Object Naming Service as the root directory for the EPCglobal Network, may not increase our revenues in the foreseeable future. There can be no assurance that we will successfully identify new product and service opportunities, develop and bring new products and services to market in a timely manner, or achieve market acceptance of our products and services, or that products, services and technologies developed by others will not render our products, services or technologies obsolete or noncompetitive. Our inability to successfully market new products and services may harm our business.

# Issues arising from our agreements with ICANN and the Department of Commerce could harm our registry business.

The Department of Commerce, or DOC, has adopted a plan for a phased transition of the DOC's responsibilities for the domain name system to the Internet Corporation for Assigned Names and Numbers, or

ICANN. As part of this transition, our registry agreement with ICANN was replaced by three new agreements on May 25, 2001, one for .com, one for .net and one for .org. The term of the .com registry agreement extends until November 10, 2007 with a 4-year renewal option. The .net registry services were subject to a competitive bidding process administered by ICANN. Our bid was determined by the outside evaluators selected by ICANN to be the top bid and VeriSign and ICANN have executed a new .net registry agreement that extends until June 30, 2011. The .org registry agreement terminated on December 31, 2002, and the .org registry services were transitioned to a new registry operator selected by ICANN during 2003. We face risks from this transition to ICANN, which include the following:

- ICANN could adopt or promote policies, procedures or programs that are unfavorable to our role as the registry operator of the .com and .net top-level domains or that are inconsistent with our current or future plans;
- the DOC or ICANN could terminate our agreements to be the registry for the .com or .net gTLDs if they find that we are in violation of our agreements with them;
- if our agreements to be the registry for the .com or .net top-level domains are terminated, it could have an adverse impact on our business;
- the DOC's or ICANN's interpretation of provisions of our agreements with either of them could differ from ours;
- the DOC could revoke its recognition of ICANN, as a result of which the DOC would take the place of ICANN for purposes of the various agreements described above, and could take actions that are harmful to us;
- the U.S. Government could refuse to transfer certain responsibilities for domain name system administration to ICANN due to security, stability or
  other reasons, resulting in fragmentation or other instability in domain name system administration; and
- our registry business could face legal or other challenges resulting from our activities or the activities of registrars.

On August 27, 2004, we filed a lawsuit against ICANN in the Superior Court of the State of California County of Los Angeles. The lawsuit alleges that ICANN overstepped its contractual authority and improperly attempted to regulate our business in violation of ICANN's charter and its agreements with us. We cannot predict the affect this lawsuit will have on our relationship with ICANN.

#### Challenges to ongoing privatization of Internet administration could harm our domain name registry business.

Risks we face from challenges by third parties, including other domestic and foreign governmental authorities, to our role in the ongoing privatization of the Internet include:

- legal, regulatory or other challenges could be brought, including challenges to the agreements governing our relationship with the DOC or ICANN, or
  to the legal authority underlying the roles and actions of the DOC, ICANN or us;
- Congress has held several hearings in which various issues about the domain name system and ICANN's practices have been raised and Congress
  could take action that is unfavorable to us;
- · ICANN could fail to maintain its role, potentially resulting in instability in domain name system administration; and
- some foreign governments and governmental authorities have in the past disagreed with, and may in the future disagree with, the actions, policies or programs of ICANN, the U.S. Government and us relating to the domain name system. These foreign governments or governmental authorities may take actions or adopt policies or programs that are harmful to our business.

As a result of these challenges, it may be difficult for us to introduce new services in our domain name registry business and we could also be subject to additional restrictions on how this business is conducted.

#### If we encounter system interruptions, we could be exposed to liability and our reputation and business could suffer.

We depend on the uninterrupted operation of our various systems, secure data centers and other computer and communication networks. Our systems and operations are vulnerable to damage or interruption from:

- power loss, transmission cable cuts and other telecommunications failures;
- damage or interruption caused by fire, earthquake, and other natural disasters;
- · computer viruses or software defects; and
- · physical or electronic break-ins, sabotage, intentional acts of vandalism, terrorist attacks and other events beyond our control.

Most of our systems are located at, and most of our customer information is stored in, our facilities in Mountain View, California and Kawasaki, Japan, both of which are susceptible to earthquakes, Providence, Rhode Island; Dulles, Virginia; Lacey, Washington; Overland Park, Kansas, Melbourne, Australia and Berlin, Hamburg and Verl, Germany. Any damage or failure that causes interruptions in any of these facilities or our other computer and communications systems could materially harm our business.

In addition, our ability to issue digital certificates, our domain name registry services and other of our services depend on the efficient operation of the Internet connections from customers to our secure data centers and from our customers to the shared registration system. These connections depend upon the efficient operation of Internet service providers and Internet backbone service providers, all of which have had periodic operational problems or experienced outages in the past.

A failure in the operation of our domain name zone servers, the domain name root servers, or other events could result in the deletion of one or more domain names from the Internet for a period of time. A failure in the operation of our shared registration system could result in the inability of one or more other registrars to register and maintain domain names for a period of time. A failure in the operation or update of the master database that we maintain could result in the deletion of one or more top-level domains from the Internet and the discontinuation of second-level domain names in those top-level domains for a period of time. Any of these problems or outages could decrease customer satisfaction, which could harm our business.

# If we experience security breaches, we could be exposed to liability and our reputation and business could suffer.

We retain certain confidential customer information in our secure data centers and various registration systems. It is critical to our business strategy that our facilities and infrastructure remain secure and are perceived by the marketplace to be secure. Our domain name registry operations also depend on our ability to maintain our computer and telecommunications equipment in effective working order and to reasonably protect our systems against interruption, and potentially depend on protection by other registrars in the shared registration system. The root zone servers and top-level domain name zone servers that we operate are critical hardware to our registry services operations. Therefore, we may have to expend significant time and money to maintain or increase the security of our facilities and infrastructure.

Despite our security measures, our infrastructure may be vulnerable to physical break-ins, computer viruses, and attacks by hackers or similar disruptive problems. It is possible that we may have to expend additional financial and other resources to address such problems. Any physical or electronic break-in or other security breach or compromise of the information stored at our secure data centers and domain name registration systems may jeopardize the security of information stored on our premises or in the computer systems and networks of our customers. In such an event, we could face significant liability and customers could be reluctant to use our services. Such an occurrence could also result in adverse publicity and therefore, adversely affect the market's perception of the security of electronic commerce and communications over IP networks as well as of the security or reliability of our services.

# The reliance of our network connectivity and interoperability services and content services on third-party communications infrastructure, hardware and software exposes us to a variety of risks we cannot control.

The success of our network connectivity and interoperability services and content services depends on our network infrastructure, including the capacity leased from telecommunications suppliers. In particular, we rely on AT&T, MCI, Sprint and other telecommunications providers for leased long-haul and local loop transmission capacity. These companies provide the dedicated links that connect our network components to each other and to our customers. Our business also depends upon the capacity, reliability and security of the infrastructure owned by third parties that is used to connect telephone calls. Specifically, we currently lease capacity from regional providers on six of the 16 mated pairs of SS7 signal transfer points that comprise our network.

We have no control over the operation, quality or maintenance of a significant portion of that infrastructure or whether or not those third parties will upgrade or improve their equipment. We depend on these companies to maintain the operational integrity of our connections. If one or more of these companies is unable or unwilling to supply or expand its levels of service to us in the future, our operations could be severely interrupted. In addition, rapid changes in the telecommunications industry have led to the merging of many companies. These mergers may cause the availability, pricing and quality of the services we use to vary and could cause the length of time it takes to deliver the services that we use to increase significantly.

Our signaling and SS7 services rely on links, equipment and software provided to us from our vendors, the most important of which are gateway equipment and software from Tekelec and Agilent Technologies, Inc. We cannot assure you that we will be able to continue to purchase equipment from these vendors on acceptable terms, if at all. If we are unable to maintain current purchasing terms or ensure product availability with these vendors, we may lose customers and experience an increase in costs in seeking alternative suppliers of products and services.

# Capacity limits on our technology and network hardware and software may be difficult to project and we may not be able to expand and upgrade our systems to meet increased use.

If traffic from our telecommunication and content customers through our network increases, we will need to expand and upgrade our technology and network hardware and software. We may not be able to expand and upgrade, in a timely manner, our systems and network hardware and software capabilities to accommodate increased traffic on our network. If we do not appropriately expand and upgrade our systems and network hardware and software, we may lose customers and revenues.

#### We rely on third parties who maintain and control root zone servers and route Internet communications.

We currently administer and operate only two of the 13 root zone servers. The others are administered and operated by independent operators on a volunteer basis. Because of the importance to the functioning of the Internet of these root zone servers, our registry services business could be harmed if these volunteer operators fail to maintain these servers properly or abandon these servers, which would place additional capacity demands on the two root zone servers we operate.

Further, our registry services business could be harmed if any of these volunteer operators fail to include or provide accessibility to the data that it maintains in the root zone servers that it controls. In the event and to the extent that ICANN is authorized to set policy with regard to an authoritative root server system, as provided in our registry agreement with ICANN, it is required to ensure that the authoritative root will point to the top-level domain zone servers designated by us. If ICANN does not do this, our business could be harmed.

# Undetected or unknown defects in our services could harm our business and future operating results.

Services as complex as those we offer or develop frequently contain undetected defects or errors. Despite testing, defects or errors may occur in our existing or new services, which could result in loss of or delay in revenues, loss of market share, failure to achieve market acceptance, diversion of development resources, injury

to our reputation, tort or warranty claims, increased insurance costs or increased service and warranty costs, any of which could harm our business. The performance of our services could have unforeseen or unknown adverse effects on the networks over which they are delivered as well as on third-party applications and services that utilize our services, which could result in legal claims against us, harming our business. Furthermore, we often provide implementation, customization, consulting and other technical services in connection with the implementation and ongoing maintenance of our services, which typically involves working with sophisticated software, computing and communications systems. Our failure or inability to meet customer expectations in a timely manner could also result in loss of or delay in revenues, loss of market share, failure to achieve market acceptance, injury to our reputation and increased costs.

### Services offered by our Internet Services Group rely on public key cryptography technology that may compromise our system's security.

Services offered by our Internet Services Group depend on public key cryptography technology. With public key cryptography technology, a user is given a public key and a private key, both of which are required to perform encryption and decryption operations. The security afforded by this technology depends on the integrity of a user's private key and that it is not lost, stolen or otherwise compromised. The integrity of private keys also depends in part on the application of specific mathematical principles known as "factoring." This integrity is predicated on the assumption that the factoring of large numbers into their prime number components is difficult. Should an easy factoring method be developed, the security of encryption products utilizing public key cryptography technology would be reduced or eliminated. Furthermore, any significant advance in techniques for attacking cryptographic systems could also render some or all of our existing PKI services obsolete or unmarketable. If improved techniques for attacking cryptographic systems were ever developed, we would likely have to reissue digital certificates to some or all of our customers, which could damage our reputation and brand or otherwise harm our business. In the past there have been public announcements of the successful attack upon cryptographic keys of certain kinds and lengths and of the potential misappropriation of private keys and other activation data. This type of publicity could also hurt the public perception as to the safety of the public key cryptography technology included in our digital certificates. This negative public perception could harm our business.

# Some of our security services have lengthy sales and implementation cycles.

We market many of our security services directly to large companies and government agencies and we market our communications services to large telecommunication carriers. The sale and implementation of our services to these entities typically involves a lengthy education process and a significant technical evaluation and commitment of capital and other resources. This process is also subject to the risk of delays associated with customers' internal budgeting and other procedures for approving large capital expenditures, deploying new technologies within their networks and testing and accepting new technologies that affect key operations. As a result, the sales and implementation cycles associated with certain of our services can be lengthy, potentially lasting from three to nine months. Our quarterly and annual operating results could be materially harmed if orders forecasted for a specific customer for a particular quarter are not realized.

# Failure of VeriSign Affiliates to follow our security and trust practices or to maintain the privacy or security of confidential customer information could have an adverse impact on our revenues and business.

We have licensed to VeriSign Affiliates our Processing Center platform, which is designed to replicate our own secure data centers and allows the affiliate to offer back-end processing of PKI services for enterprises. The VeriSign Processing Center platform provides a VeriSign Affiliate with the knowledge and technology to offer PKI services similar to those offered by us. It is critical to our business strategy that the facilities and infrastructure used in issuing and marketing digital certificates remain secure and we are perceived by the marketplace to be secure. Although we provide the VeriSign Affiliate with training in security and trust practices, network management and customer service and support, these practices are performed by the affiliate and are outside of our control. Any failure of a VeriSign Affiliate to maintain the privacy or security of confidential

customer information could result in negative publicity and therefore, adversely affect the market's perception of the security of our services as well as the security of electronic commerce and communication over IP networks generally.

# We rely on our intellectual property, and any failure by us to protect, or any misappropriation of, our intellectual property could harm our business.

Our success depends on our internally developed technologies, patents and other intellectual property. Despite our precautions, it may be possible for a third party to copy or otherwise obtain and use our trade secrets or other forms of our intellectual property without authorization. Furthermore, the laws of foreign countries may not protect our proprietary rights in those countries to the same extent U.S. law protects these rights in the United States. In addition, it is possible that others may independently develop substantially equivalent intellectual property. If we do not effectively protect our intellectual property, our business could suffer. In the future, we may have to resort to litigation to enforce our intellectual property rights, to protect our trade secrets or to determine the validity and scope of the proprietary rights of others. This type of litigation, regardless of its outcome, could result in substantial costs and diversion of management and technical resources.

We also license third-party technology that is used in our products and services, to perform key functions. These third-party technology licenses may not continue to be available to us on commercially reasonable terms or at all. Our business could suffer if we lost the rights to use these technologies. A third-party could claim that the licensed software infringes a patent or other proprietary right. Litigation between the licensor and a third-party or between us and a third-party could lead to royalty obligations for which we are not indemnified or for which indemnification is insufficient, or we may not be able to obtain any additional license on commercially reasonable terms or at all. The loss of, or our inability to obtain or maintain, any of these technology licenses could delay the introduction of our Internet infrastructure services until equivalent technology, if available, is identified, licensed and integrated. This could harm our business.

# We could become subject to claims of infringement of intellectual property of others, which could be costly to defend and which could harm our business.

Claims relating to infringement of intellectual property of others or other similar claims have been made against us in the past and could be made against us in the future. In addition, we use content such as music, games and logos, as part of our content services. It is possible that we could become subject to additional claims for infringement of the intellectual property of third parties. Any claims, with or without merit, could be time-consuming, result in costly litigation and diversion of technical and management personnel, cause delays or require us to develop non-infringing technology or enter into royalty or licensing agreements. Royalty or licensing agreements, if required, may not be available on acceptable terms or at all. If a successful claim of infringement were made against us, we could be required to pay damages or have portions of our business enjoined. If we could not develop non-infringing technology or license the infringed or similar technology on a timely and cost-effective basis, our business could be harmed.

In addition, legal standards relating to the validity, enforceability, and scope of protection of intellectual property rights in Internet-related businesses are uncertain and still evolving. Because of the growth of the Internet and Internet-related businesses, patent applications are continuously and simultaneously being filed in connection with Internet-related technology. There are a significant number of U.S. and foreign patents and patent applications in our areas of interest, and we believe that there has been, and is likely to continue to be, significant litigation in the industry regarding patent and other intellectual property rights.

# We must establish and maintain strategic and other relationships.

One of our significant business strategies has been to enter into strategic or other similar collaborative relationships in order to reach a larger customer base than we could reach through our direct sales and marketing efforts. We may need to enter into additional relationships to execute our business plan. We may not be able to enter into additional, or maintain our existing, strategic relationships on commercially reasonable terms. If we

fail to enter into additional relationships, we would have to devote substantially more resources to the distribution, sale and marketing of our security services and communications services than we would otherwise.

Our success in obtaining results from these relationships will depend both on the ultimate success of the other parties to these relationships and on the ability of these parties to market our services successfully.

Furthermore, our ability to achieve future growth will also depend on our ability to continue to establish direct seller channels and to develop multiple distribution channels. Failure of one or more of our strategic relationships to result in the development and maintenance of a market for our services could harm our business. If we are unable to maintain our relationships or to enter into additional relationships, this could harm our business.

# Principal and interest on the Network Solutions note may never be repaid.

As consideration for our sale of our Network Solutions domain name registrar business on November 25, 2003, we received a \$40 million senior subordinated note from Network Solutions that matures over five years from the date of the closing of the sale. The note is subordinated to a term loan made by the senior lender to the Network Solutions business in the principal amount of \$40 million as of the closing date. We received a payment of \$17.8 million, comprised of both principal and interest, on the note from Network Solutions in March 2005. In addition to the note, we also hold a 15% interest in the Network Solutions business. We may never be repaid for the remaining amount owed under the promissory note and we may never realize any value from our membership interest.

# We depend on key personnel to manage our business effectively and may not be successful in attracting and retaining such personnel.

We depend on the performance of our senior management team and other key employees. Our success also depends on our ability to attract, integrate, train, retain and motivate these individuals and additional highly skilled technical and sales and marketing personnel, both in the U.S. and abroad. In addition, our stringent hiring practices for some of our key personnel, which consist of background checks into prospective employees' criminal and financial histories, further limit the number of qualified persons for these positions.

We have no employment agreements with any of our key executives that prevent them from leaving VeriSign at any time. In addition, we do not maintain key person life insurance for any of our officers or key employees. The loss of the services of any of our senior management team or other key employees or failure to attract, integrate, train, retain and motivate additional key employees could harm our business.

# Compliance with rules and regulations concerning corporate governance is costly and could harm our business.

The Sarbanes-Oxley Act mandates, among other things, that companies adopt new corporate governance measures and imposes comprehensive reporting and disclosure requirements, sets stricter independence and financial expertise standards for audit committee members and imposes increased civil and criminal penalties for companies, their chief executive officers and chief financial officers and directors for securities law violations. For example, Section 404 of the Sarbanes-Oxley Act requires companies to do a comprehensive and costly evaluation of their internal controls. In addition, the Nasdaq Stock Market has adopted additional comprehensive rules and regulations relating to corporate governance. These laws, rules and regulations have increased the scope, complexity and cost of our corporate governance, reporting and disclosure practices, and our compliance efforts have required significant management attention. It has become more difficult and more expensive for us to obtain director and officer liability insurance, and we have been required to accept reduced coverage and incur substantially higher costs to obtain the reduced level of coverage. Further, our board members, chief executive officer and chief financial officer could face an increased risk of personal liability in connection with the performance of their duties. As a result, we may have difficulty attracting and retaining qualified board members and executive officers, which could harm our business.

# Regulations related to equity compensation will adversely affect our operating results and negatively impact our ability to attract and retain key personnel.

Since our inception, we have used stock options and other long-term equity incentives as a fundamental component of our employee compensation packages. We believe that stock options and other long-term equity incentives directly motivate our employees to maximize long-term stockholder value and, through the use of vesting, encourage employees to remain with VeriSign. The Financial Accounting Standards Board ("FASB") recently issued Statement of Financial Accounting Standards ("SFAS") No. 123R, "Share-Based Payment," which supersedes SFAS No. 123, "Accounting for Stock-Based Compensation," that will require us to record a charge to earnings for employee stock option grants beginning in the first quarter of 2006. This change will have a material, negative impact on our reported earnings. Recording a charge for employee stock options and the employee stock purchase plan under SFAS No. 123 would have increased after tax charges by approximately \$14.6 million and \$30.9 million for the three months ended June 30, 2005 and 2004, respectively, and approximately \$30.5 million and \$64.4 million for the six months ended June 30, 2005 and 2004, respectively. In addition, regulations adopted by the Nasdaq Stock Market requiring stockholder approval for stock option plans could make it more difficult for us to grant options to employees in the future. To the extent that new policies or regulations make it more difficult or expensive to grant options to employees, we may incur increased cash compensation costs or find it difficult to attract, retain and motivate employees, either of which could materially harm our business.

# We have anti-takeover protections that may delay or prevent a change in control that could benefit our stockholders.

Our amended and restated certificate of incorporation and bylaws contain provisions that could make it more difficult for a third-party to acquire us without the consent of our board of directors. These provisions include:

- · our stockholders may take action only at a meeting and not by written consent;
- our board must be given advance notice regarding stockholder-sponsored proposals for consideration at annual meetings and for stockholder nominations for the election of directors;
- · we have a classified board of directors, with the board being divided into three classes that serve staggered three-year terms;
- · vacancies on our board may be filled until the next annual meeting of stockholders only by majority vote of the directors then in office; and
- · special meetings of our stockholders may be called only by the chairman of the board, the president or the board, and not by our stockholders.

VeriSign has also adopted a stockholder rights plan that may discourage, delay or prevent a change of control and make any future unsolicited acquisition attempt more difficult. Under the rights plan:

- The rights will become exercisable only upon the occurrence of certain events specified in the plan, including the acquisition of 20% of VeriSign's outstanding common stock by a person or group.
- Each right entitles the holder, other than an "acquiring person," to acquire shares of VeriSign's common stock at a 50% discount to the then prevailing market price.
- VeriSign's Board of Directors may redeem outstanding rights at any time prior to a person becoming an "acquiring person," at a price of \$0.001 per right. Prior to such time, the terms of the rights may be amended by VeriSign's Board of Directors without the approval of the holders of the rights.

## Changes in, or interpretations of, tax rules and regulations may adversely affect our effective tax rates.

We are subject to income taxes in both the United States and numerous foreign jurisdictions. Significant judgment is required in determining our worldwide provision for income taxes. In the ordinary course of our business, there are many transactions and calculations where the ultimate tax determination is uncertain. We are

subject to audit by various tax authorities. Although we believe our tax estimates are reasonable, the final determination of tax audits and any related litigation could be materially different than that which is reflected in historical income tax provisions and accruals. Should additional taxes be assessed as a result of an audit or litigation, an adverse effect on our income tax provision and net income in the period or periods for which that determination is made could result.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's market risk profile has not changed significantly from that described in the 2004 Form 10-K.

#### **Equity investments**

We invest in debt and equity securities of technology companies for investment purposes. In most instances, we invest in the equity and debt securities of private companies for which there is no public market, and therefore, carry a high level of risk. These companies are typically in the early stage of development and are expected to incur substantial losses in the near-term. Therefore, these companies may never become publicly traded. Even if they do, an active trading market for their securities may never develop and we may never realize any return on these investments. During the three months ended June 30, 2005, we determined that there were no other-than-temporary declines in the value of our non-public equity investments. During the three months ended June 30, 2004, we determined that the decline in value of certain of our non-public equity investments was other-than-temporary and recorded an impairment, net of realized gains, totaling \$0.3 million. During the six months ended June 30, 2005 and 2004, VeriSign recorded impairments, net of realized gains, totaling \$(0.1) million and \$3.6 million, respectively. Due to the inherent risks associated with investments, we may incur future losses on the sale or impairment of our investments.

#### Interest rate sensitivity

The primary objective of our cash management activities is to preserve principal with the additional goals of maintaining appropriate liquidity and driving after-tax returns. Some of the securities that we have invested in may be subject to interest rate risk. This means that a change in prevailing interest rates may cause the principal amount of the investment to fluctuate. For example, if we hold a security that was issued with a fixed interest rate at the then-prevailing rate and the prevailing interest rate later rises, the principal amount of our investment will probably decline in value. To minimize interest rate risk, we maintain our portfolio of cash equivalents and short-term investments in a variety of securities, including commercial paper, medium-term notes, corporate bonds and notes, U.S. government and agency securities and money market funds. In general, money market funds are not subject to interest rate risk because the interest paid on such funds fluctuates with the prevailing interest rate. As of June 30, 2005, 37% of our investments subject to interest rate risk mature in less than one year. If market interest rates were to increase immediately and uniformly by 10 percent from levels at June 30, 2005, this would not materially change the fair market value of our portfolio.

The following table presents the amounts of our cash equivalents and short-term investments that are subject to interest rate risk by range of expected maturity and weighted-average interest rates as of June 30, 2005. This table does not include money market funds because those funds are not subject to interest rate risk.

	Maturing in				
	Six Months or Less	Six Months to One Year	More than One Year	Total	Estimated Fair Value
	·		(In thousands)		
Included in cash and cash equivalents	\$ 93,727	\$ —	\$ —	\$ 93,727	\$ 93,772
Weighted-average interest rate	3.14%	_	_		
Included in short-term investments	\$ 28,958	\$ 92,132	\$315,287	\$436,377	\$431,960
Weighted-average interest rate	4.47%	3.11%	3.82%		
Included in restricted cash	\$ —	\$ —	\$ 51,444	\$ 51,444	\$ 51,444
Weighted-average interest rate	_	_	3.69%		

#### Foreign exchange risk management

We conduct business throughout the world and transact in multiple foreign currencies. As we continue to expand our international operations we are increasingly exposed to currency exchange rate risks. In the fourth quarter of 2003, we initiated a foreign currency risk management program designed to mitigate foreign exchange risks associated with the monetary assets and liabilities of our operations that are denominated in non-functional currencies. The primary objective of this hedging program is to minimize the gains and losses resulting from fluctuations in exchange rates. We do not enter into foreign currency transactions for trading or speculative purposes, nor do we hedge foreign currency exposures in a manner that entirely offsets the effects of changes in exchange rates. The program may entail the use of forward or option contracts and, in each case, these contracts are limited to a duration of less than 12 months.

At June 30, 2005, we held forward contracts in notional amounts totaling approximately \$64.5 million to mitigate the impact of exchange rate fluctuations associated with certain foreign currencies. All hedge contracts are recorded at fair market value. We attempt to limit our exposure to credit risk by executing foreign exchange contracts with high-quality financial institutions.

# ITEM 4. CONTROLS AND PROCEDURES

Under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934). Based on this evaluation, our chief executive officer and chief financial officer, as of June 30, 2005, concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) are effective to ensure that information required to be disclosed by us in this report was recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms for this report.

There was no change in our internal control over financial reporting during the fiscal quarter covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Our management, including our chief executive officer and chief financial officer, does not expect that our disclosure controls and procedures or our internal controls will prevent all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within VeriSign have been detected.

#### PART II—OTHER INFORMATION

#### ITEM 1. LEGAL PROCEEDINGS

On September 7, 2001, NetMoneyIN, an Arizona corporation, filed a complaint styled as a First Amended Complaint alleging patent infringement against VeriSign and several other previously-named defendants in the United States District Court for the District of Arizona asserting infringement of U.S. patent Nos. 5,822,737 and 5,963,917. NetMoneyIN filed a second amended complaint on October 15, 2002, alleging infringement by VeriSign and several other defendants of a third U. S. patent (No. 6,381,584) in addition to the two patents previously asserted. The second amended complaint dropped some of the originally-named defendants and added others. On August 27, 2003, NetMoneyIN filed a third amended complaint alleging direct infringement of the same three patents by VeriSign and several other previously-named defendants. In this complaint, NetMoneyIN dropped its claim of active inducement of infringement by VeriSign. Some of the other current defendants include IBM, BA Merchant Services, Wells Fargo Bank, Cardservice International, InfoSpace, E-Commerce Exchange and Paymentech. VeriSign filed an answer denying any infringement and asserting that the three asserted patents are invalid and later filed an amended answer asserting, in addition, that the asserted patents are unenforceable due to inequitable conduct before the U.S. Patent and Trademark Office. The complaint alleges that VeriSign's Payflow payment products and services directly infringe certain claims of NetMoneyIN's three patents and requests the Court to enter judgment in favor of NetMoneyIN, a permanent injunction against the defendants' alleged infringing activities, an order requiring defendants to provide an accounting for NetMoneyIN's damages, to pay NetMoneyIN such damages and three times that amount for any willful infringers, and an order awarding NetMoneyIN attorney fees and costs. NetMoneyIN has recently dropped its allegations of infringement of the '584 patent. Also, the original lead counsel for NetMoneyIN has withdrawn from the case, and NetMoneyIN has hired new counsel. Fact discovery is now closed and the Court has held a Markman hearing and taken the patent claim construction issues under advisement. VeriSign has filed a motion seeking summary judgment of no indirect infringement under 35 U.S.C. Sections 271 b and 271 c (i.e., no inducement of others to infringe and no contributory infringement). Several other defendants have filed similar motions. Briefing is not yet complete on these motions. While we cannot predict the outcome of this lawsuit, VeriSign believes that the allegations are without merit.

Beginning in May of 2002, several class action complaints were filed against VeriSign and certain of its current and former officers and directors in the United States District Court for the Northern District of California. These actions were consolidated under the heading In re VeriSign, Inc. Securities Litigation, Case No. C-02-2270 JW(HRL), on July 26, 2002. The consolidated action seeks unspecified damages for alleged violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, and Rule 10b-5 promulgated thereunder, on behalf of a class of persons who purchased VeriSign stock from January 25, 2001 through April 25, 2002. An amended consolidated complaint was filed on November 8, 2002. On April 14, 2003, the court granted in part and denied in part the defendants' motion to dismiss the amended and consolidated complaint. On May 5, 2004, plaintiffs filed a second amended complaint that is substantially identical to the amended consolidated complaint except that it purports to add a claim under Sections 11 and 15 of the Securities Act of 1933 on behalf of a subclass of persons who acquired shares of VeriSign pursuant to the registration statement and prospectus filed October 10, 2001 and amended October 26, 2001 for the acquisition of Illuminet Holdings, Inc. by VeriSign.

Parallel derivative actions have also been filed against certain of VeriSign's current and former officers and directors in state courts in California and Delaware. VeriSign is named as a nominal defendant in these actions. Several of these derivative actions were filed in Santa Clara County Superior Court of California and these actions have since been consolidated under the heading In re VeriSign, Inc. Derivative Litigation, Case No. CV 807719.

The consolidated derivative action seeks unspecified damages for alleged breaches of fiduciary duty and violations of the California Corporations Code. Defendants' demurrer to these claims was granted with leave to amend on February 4, 2003. Plaintiffs have indicated their intention to file an amended complaint. Another

derivative action was filed in the Court of Chancery New Castle County, Delaware, Case No. 19700-NC, alleging similar breaches of fiduciary duty. Defendants' motion to dismiss these claims was granted by the Court of Chancery with prejudice on September 30, 2003.

VeriSign and the individual defendants dispute all of these claims.

On August 27, 2004, VeriSign filed a lawsuit against ICANN in the Superior Court of the State of California Los Angeles County. The lawsuit alleges that ICANN breached its .com Registry Agreement with VeriSign, including, without limitation, by overstepping its contractual authority and improperly attempting to regulate our business. The complaint seeks, among other things, specific performance of the .com Registry Agreement, an injunction prohibiting ICANN from improperly regulating VeriSign, and monetary damages. On November 12, 2004, ICANN filed an answer denying VeriSign's claims and a cross-complaint against VeriSign for declaratory relief and breach of the .com Registry Agreement, alleging that VeriSign's introduction of new services breached the .com Agreement. ICANN seeks a declaration from the court that it has acted in compliance with the parties' contractual obligations with regard to the .com registry; that VeriSign has breached the parties' agreement through VeriSign's actions with respect to, among other things, SiteFinder; and that ICANN has the right to terminate the .com registry agreement if VeriSign offers "Registry Services" without ICANN's approval, including among others SiteFinder. On December 28, 2004, VeriSign filed an answer denying the claims in ICANN's cross-complaint and a cross-complaint against ICANN for breach of contract, violation of the unfair competition laws, and declaratory relief, alleging, among other things, that ICANN's accreditation of "thread" registrars is improper and causes direct injury to VeriSign. On February 14, 2005, ICANN filed an answer to VeriSign's cross-complaint denying VeriSign's allegations. VeriSign cannot predict the outcome of this lawsuit or the affect it will have on our relationship with ICANN.

On or about November 12, 2004, ICANN filed a Request for Arbitration before the International Chamber of Commerce International Court of Arbitration (the "ICC") alleging that VeriSign violated its .net Registry Agreement with ICANN when, among other things, VeriSign operated the SiteFinder service without ICANN approval. ICANN seeks a declaration from the ICC that it has acted in compliance with the parties' contractual obligations with regard to the .net registry; that VeriSign has breached the parties' agreement through VeriSign's actions with respect to, among other things, SiteFinder; and that ICANN has the right to terminate the .net registry agreement if VeriSign offers "Registry Services" without ICANN's approval, including among others SiteFinder. ICANN also seeks a declaration that, in evaluating VeriSign's bid to become the "successor" registry operator for the .net top level domain after the term of the current agreement expires on or about June 30, 2005, ICANN is entitled to consider VeriSign's alleged breaches of the existing .net agreement. VeriSign cannot predict the outcome of this action or the affect this lawsuit will have on our relationship with ICANN.

On January 18, 2005, VeriSign filed a request for arbitration before the ICC against ICANN regarding the process by which ICANN solicited and reviewed bids from companies, including VeriSign, to become the "successor" registry operator for the .net top level domain after the current registry agreement expires on or about June 30, 2005. VeriSign alleges that the "request for proposal" ("RFP") process constitutes a breach of the current .net registry agreement because, among other things, the RFP process fails to constitute an open and transparent process by which ICANN can reasonably select the best qualified successor to operate the .net registry and does not constitute a valid "consensus policy" as defined in the current .net agreement. ICANN has not yet responded to our arbitration request. On June 8, 2005, ICANN announced that it had selected VeriSign as the "successor" registry operator for the .net top level domain, and ICANN and VeriSign have entered into a contract to confirm that selection. VeriSign anticipates that its selection as the .net registry operator will resolve its request for arbitration.

On February 14, 2005, Southeast Texas Medical Associates, LLP filed a putative class action lawsuit in the Superior Court of California, alleging violations of the unfair competition laws, breach of express warranty and unjust enrichment relating to our Secure Site Pro SSL certificates. The complaint is brought on behalf of a class of persons who purchased the Secure Site Pro certificate from February 2001 to present. VeriSign disputes these claims. While we cannot predict the outcome of this matter, VeriSign believes that the allegations are without merit.

On March 8, 2005, plaintiff Charles Ford filed a putative class action lawsuit in the Superior Court of California, County of San Diego, alleging fraud, negligent misrepresentation, false advertising, and violations of the California Consumers Legal Remedies Act and unfair competition laws relating to marketing and advertising of mobile phone "ringtones" and other content by VeriSign's subsidiaries, Jamster International Sarl and Jamba! GmbH. The complaint is brought on behalf of classes of persons who responded to advertising by sending a text message on their mobile phones or registered over the Internet to purchase ringtone or other content. On April 18, 2005, VeriSign removed the action to the federal district court for the Southern District of California. VeriSign disputes the claims in this action. While we cannot predict the outcome of this matter, VeriSign believes that the allegations are without merit.

On April 11, 2005, Prism Technologies, LLC filed a complaint against VeriSign in the U.S. District Court for the District of Delaware alleging that VeriSign's "Go Secure suite of application and related hardware and software products and its Unified Authentication solution and related hardware and software products" infringe U.S. Patent No. 6,516,416, entitled "Subscription Access System for Use With an Untrusted Network." Prism Technologies seeks judgment in favor of Prism Technologies, a permanent injunction from infringement, damages in an amount not less than a reasonable royalty, attorneys' fees and costs. Prism Technologies has also named RSA Security, Inc., Netegrity, Inc. Computer Associates International, Inc and Johnson & Johnson as codefendants. VeriSign responded on June 6, 2005 by filing a counterclaim for declaratory relief and an answer denying any infringement and asserting that the patent is invalid. The Court has not yet scheduled an initial scheduling conference or entered a scheduling order. While we cannot predict the outcome of this matter, VeriSign believes that the allegations are without merit and intends to vigorously defend against them.

On June 2, 2005, the company received an access letter from the U.S. Federal Trade Commission (FTC) for information to determine whether VeriSign, using the trade name Jamster, was engaging in unfair or deceptive acts or practices in violation of Section 5 of the Federal Trade Commission Act in its advertising, offering and billing for mobile content services and products.

We currently are responding to inquiries in the United Kingdom by the Independent Committee for the Supervision of Standards of Telephone Information Services and the Advertising Standards Authority, two advertising industry regulatory bodies reviewing the television and print advertising practices of Jamba! and Jamster.

VeriSign is involved in various other investigations, claims and lawsuits arising in the normal conduct of its business, none of which, in our opinion will harm its business. VeriSign cannot assure that it will prevail in any litigation. Regardless of the outcome, any litigation may require VeriSign to incur significant litigation expense and may result in significant diversion of management attention.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

# **Unregistered Sales of Equity Securities**

On April 6, 2005, we issued an aggregate of 9,083,074 shares of our common stock in connection with the acquisition of LightSurf Technologies, Inc. The offer and sale of these securities were effected without registration in reliance on the exemption afforded by Section 3(a)(10) of the Securities Act of 1933, as amended. The issuance was approved, after a hearing upon the fairness of the terms and conditions of the transaction, by the California Department of Corporations under authority to grant such approval as expressly authorized by the laws of the State of California.

#### **Share Repurchases**

# ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plans or Programs
April 1 – 30, 2005	<u> </u>	_	_	\$ 167.2 million
May 1 – 31, 2005	1,553,000	\$ 27.35	1,553,000	124.8 million
June 1 – 30, 2005	<del>_</del>	_	_	_
Total	1,553,000	\$ 27.35	1,553,000	\$ 124.8 million

On April 26, 2001, VeriSign announced that the Board of Directors authorized the repurchase of up to \$350 million of the Company's common stock for cash in open market, negotiated or block transactions.

# ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The 2005 Annual Meeting of Stockholders was held on May 26, 2005 at our corporate offices, located at 487 East Middlefield Road, Mountain View, California. Two proposals were voted on at the meeting. The results of each proposal are as follows.

Proposal No. 1 to elect three (3) Class I directors to serve for a three-year term expiring at the Annual Meeting of Stockholders in 2008 was approved by the stockholders. The nominees received the following votes:

	For	Withheld
Scott G. Kriens	208,102,825	15,735,228
Len J. Lauer	205,108,391	18,729,662
Stratton D. Sclavos	211,233,873	12,604,180

Incumbent Class II directors Roger H. Moore, Edward A. Mueller and William A. Roper, Jr. are currently serving for a term expiring at the Annual Meeting of Stockholders in 2006. Incumbent Class III directors, D. James Bidzos, William L. Chenevich, Gregory L. Reyes and Louis A. Simpson are currently serving for a term expiring at the Annual Meeting of Stockholders in 2007.

In Proposal No. 2, stockholders ratified the appointment of KPMG LLP as independent auditors of VeriSign for the fiscal year ending December 31, 2004. This proposal received the following votes:

	Votes
For	223,176,830
Against Abstain	579,235
Abstain	81,988

Abstentions and broker non-votes were included in the determination of the number of shares represented at the meeting for purposes of determining the presence of a quorum at the Annual Meeting of Stockholders. Abstentions had the same effect as a vote against Proposal No. 2.

# ITEM 6. EXHIBITS

(a) Index to Exhibits

Exhibit Number	Exhibit Description	Filed Herewith
31.01	Certification of President, Chief Executive Officer and Chairman of the Board pursuant to Exchange Act Rule 13a-14(a).	X
31.02	Certification of Executive Vice President of Finance and Administration and Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a).	X
32.01	Certification of President, Chief Executive Officer and Chairman of the Board pursuant to Exchange Act Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350). *	X
32.02	Certification of Executive Vice President of Finance and Administration and Chief Financial Officer pursuant to Exchange Act Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350). *	X

<sup>\*</sup> As contemplated by SEC Release No. 33-8212, these exhibits are furnished with this Quarterly Report on Form 10-Q and are not deemed filed with the Securities and Exchange Commission and are not incorporated by reference in any filing of VeriSign, Inc. under the Securities Act of 1934, whether made before or after the date hereof and irrespective of any general incorporation language in such filings.

Date: August 08, 2005

Date: August 08, 2005

# **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.

By: /s/ STRATTON D. SCLAVOS

Stratton D. Sclavos
Chairman of the Board,
President and Chief Executive Officer
(Principal Executive Officer)

By: /s/ DANA L. EVAN

Dana L. EVAN

Executive Vice President of

Dana L. Evan
Executive Vice President of
Finance and Administration and
Chief Financial Officer
(Principal Financial and Accounting Officer)

# **EXHIBITS**

As required under Item 6—Exhibits, the exhibits filed as part of this report are provided in this separate section. The exhibits included in this section are as follows:

Exhibit Number	Exhibit Description	
31.01	Certification of President, Chief Executive Officer and Chairman of the Board pursuant to Exchange Act Rule 13a-14(a).	
31.02	Certification of Executive Vice President of Finance and Administration and Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a).	
32.01	Certification of President, Chief Executive Officer and Chairman of the Board pursuant to Exchange Act Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350).*	
32.02	Certification of Executive Vice President of Finance and Administration and Chief Financial Officer pursuant to Exchange Act Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350).*	

<sup>\*</sup> As contemplated by SEC Release No. 33-8212, these exhibits are furnished with this Quarterly Report on Form 10-Q and are not deemed filed with the Securities and Exchange Commission and are not incorporated by reference in any filing of VeriSign, Inc. under the Securities Act of 1933 or the Securities Act of 1934, whether made before or after the date hereof and irrespective of any general incorporation language in such filings.

# CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER PURSUANT TO EXCHANGE ACT RULE 13a-14(a)/15d-14(a) AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

- I, Stratton D. Sclavos, certify that:
- 1. I have reviewed this quarterly report on Form 10-Q of VeriSign, 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(s) 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) 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
  - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
- 5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, 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: August 08, 2005	By:	/s/ STRATTON D. SCLAVOS
		Stratton D. Sclavos
		President Chief Executive Officer

and Chairman of the Board

# CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER PURSUANT TO EXCHANGE ACT RULE 13a-14(a)/15d-14(a) AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

- I, Dana L. Evan, certify that:
- 1. I have reviewed this quarterly report on Form 10-Q of VeriSign, 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(s) 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) 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
  - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
- 5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, 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: August 08, 2005

By: /s/ DANA L. EVAN

Dana L. Evan

Executive Vice President of Finance and Administration and Chief Financial Officer

# CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

- I, Stratton D. Sclavos, President, Chief Executive Officer and Chairman of the Board of Directors of VeriSign, Inc. (the "Company"), do hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:
- 1. the Quarterly Report on Form 10-Q of the Company for the fiscal quarter ended June 30, 2005, as filed with the Securities and Exchange Commission (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 results of operations of the Company.

Date: August 08, 2005

/s/ STRATTON D. SCLAVOS

Stratton D. Sclavos
President, Chief Executive Officer and Chairman
of the Board
(Principal Executive Officer)

# CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

- I, Dana L. Evan, Executive Vice President of Finance and Administration and Chief Financial Officer of VeriSign, Inc. (the "Company"), do hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:
- 1. the Quarterly Report on Form 10-Q of the Company for the fiscal quarter ended June 30, 2005, as filed with the Securities and Exchange Commission (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 results of operations of the Company.

Date: August 08, 2005	/s/ Dana L. Evan
	Dana L. Evan
	Executive Vice President of Finance and

Executive Vice President of Finance and Administration and Chief Financial Officer (Principal Financial Officer)