

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

Quarterly Report Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934
For the Fiscal Quarter Ended July 31, 1999

or

Transition Report Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934
For the transition period from _____
to _____

Commission File Number: 0-13351

NOVELL, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

87-0393339
(I.R.S. Employer
Identification No.)

122 East 1700 South
Provo, Utah 84606
(Address of principal executive offices and zip code)

(801) 861-7000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

YES NO

As of August 31, 1999 there were 333,066,484 shares of the Registrant's Common Stock outstanding.

Part I. Financial Information, Item 1. Financial Statements

**NOVELL, INC.
CONSOLIDATED UNAUDITED CONDENSED BALANCE SHEETS**

<i>Dollars in thousands, except per share data</i>	July 31, 1999	Oct. 31, 1998
ASSETS		
Current assets		
Cash and short-term investments	\$ 992,201	\$ 1,007,167
Receivables, less allowances (\$31,880 - July; \$47,921 - October)	233,302	246,577
Inventories	2,945	3,562
Prepaid expenses	48,205	63,165
Deferred and refundable income taxes	75,958	95,343
Other current assets	18,704	19,886
Total current assets	1,371,315	1,435,700
Property, plant and equipment, net	344,750	346,196
Long-term investments	210,835	114,815
Other assets	36,681	27,401
Total assets	<u>\$ 1,963,581</u>	<u>\$ 1,924,112</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable	\$ 74,636	\$ 77,987
Accrued compensation	61,543	52,348
Accrued marketing liabilities	16,708	16,383
Other accrued liabilities	53,226	62,206
Income taxes payable	45,083	64,057
Deferred revenue	149,338	141,714
Total current liabilities	400,534	414,695
Minority interests	10,108	15,919
Shareholders' equity		
Common stock, par value \$.10 a share		
Authorized - 600,000,000 shares		
Issued - 333,995,071 shares-July		
337,592,460 shares-October	33,400	33,759
Additional paid-in capital	124,422	200,897
Retained earnings	1,407,274	1,290,337
Unearned stock compensation	(7,664)	(5,396)
Cumulative translation adjustment	(2,574)	(1,753)
Unrealized (loss) on investments	(1,919)	(24,346)
Total shareholders' equity	<u>1,552,939</u>	<u>1,493,498</u>
Total liabilities and shareholders' equity	<u>\$ 1,963,581</u>	<u>\$ 1,924,112</u>

See notes to consolidated unaudited condensed financial statements.

NOVELL, INC.
CONSOLIDATED UNAUDITED CONDENSED STATEMENTS OF INCOME

<i>Dollars in thousands, except per share data</i>	<u>Fiscal Quarter Ended</u>		<u>Nine Months Ended</u>	
	July 31, 1999	July 31, 1998	July 31, 1999	July 31, 1998
Net sales	\$ 326,808	\$ 272,016	\$ 928,266	\$ 786,308
Cost of sales	73,514	63,069	213,845	179,434
Gross profit	253,294	208,947	714,421	606,874
Operating expenses				
Sales and marketing	108,806	96,986	320,598	302,621
Product development	57,183	57,048	169,271	178,136
General and administrative	24,866	24,827	76,271	76,751
Total operating expenses	190,855	178,861	566,140	557,508
Income from operations	62,439	30,086	148,281	49,366
Other income (expense)				
Investment income	10,260	7,390	30,676	37,245
Other, net	(4,211)	(592)	(16,546)	(3,337)
Other income, net	6,049	6,798	14,130	33,908
Income before taxes	68,488	36,884	162,411	83,274
Income taxes	19,177	10,328	45,476	23,317
Net income	\$ 49,311	\$ 26,556	\$ 116,935	\$ 59,957
Weighted average shares outstanding				
Basic	334,488	353,436	335,735	352,076
Diluted	350,951	362,083	351,196	357,213
Net income per share				
Basic	\$ 0.15	\$ 0.08	\$ 0.35	\$ 0.17
Diluted	\$ 0.14	\$ 0.07	\$ 0.33	\$ 0.17

See notes to consolidated unaudited condensed financial statements.

NOVELL, INC.
CONSOLIDATED UNAUDITED CONDENSED STATEMENTS OF CASH FLOWS

<i>Dollars in thousands</i>	Nine Months Ended	
	July 31, 1999	July 31, 1998
Cash flows from operating activities		
Net income	\$ 116,935	\$ 59,957
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	47,519	59,353
Stock plans' income tax benefits	46,972	3,408
Decrease in receivables	13,275	(711)
Decrease in inventories	617	6,382
Decrease (increase) in prepaid expenses	14,960	(10,483)
Decrease in deferred and refundable income taxes	20,711	39,522
Decrease in other current assets	1,182	3,848
(Decrease) increase in current liabilities, net	(14,161)	33,518
Net cash provided from operating activities	248,010	194,794
Cash flows from financing activities		
Issuance of common stock, net	79,832	26,349
Repurchase of common stock	(203,638)	(12,427)
Net cash (used) provided from financing activities	(123,806)	13,922
Cash flows from investing activities		
Expenditures for property, plant and equipment	(50,988)	(42,617)
Purchases of short-term investments	(1,567,172)	(1,574,104)
Maturities of short-term investments	1,190,733	964,366
Sales of short-term investments	537,878	456,464
Expenditures other long-term investments	(96,021)	(59,387)
Other	(14,588)	16,773
Net cash used by investing activities	(158)	(238,505)
Total increase (decrease) in cash and cash equivalents	\$ 124,046	\$ (29,789)
Cash and cash equivalents - beginning of period	177,083	208,543
Cash and cash equivalents - end of period	301,129	178,754
Short-term investments - end of period	691,072	969,171
Cash and short-term investments - end of period	\$ 992,201	\$ 1,147,925

See notes to consolidated unaudited condensed financial statements.

NOVELL, INC.
NOTES TO CONSOLIDATED UNAUDITED CONDENSED FINANCIAL STATEMENTS

A. Quarterly Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The accompanying consolidated unaudited condensed financial statements have been prepared in accordance with the instructions to Form 10-Q but do not include all of the information and footnotes required by generally accepted accounting principles and should, therefore, be read in conjunction with the Company's fiscal 1998 Annual Report to Shareholders. These statements do include all normal recurring adjustments which the Company believes necessary for a fair presentation of the statements. The interim operating results are not necessarily indicative of the results for a full year. Certain reclassifications, none of which affected net income, have been made to the prior years' amounts in order to conform to the current year's presentation.

B. Cash and Short-term Investments

All marketable debt and equity securities are included in cash and short-term investments and are considered available-for-sale and carried at fair market value, with the unrealized gains and losses, net of tax, included in shareholders' equity. Fair market values are based on quoted market prices at end of period, where available; if quoted market prices are not available, then fair market values are based on quoted market prices of comparable instruments. Municipal securities included in short-term investments have contractual maturities from 1-5 years. Money market preferreds have contractual maturities of less than 180 days. No other short-term investments have contractual maturities. The cost of securities sold is based on the specific identification method. Such securities are anticipated to be used for current operations and are therefore classified as current assets, even though some maturities may extend beyond one year.

The following is a summary of cash and short-term investments, all of which are considered available-for-sale.

<i>(Dollars in thousands)</i>	Cost at July 31, 1999	Gross Unrealized Gains	Gross Unrealized Losses	Fair Market Value at July 31, 1999
Cash and cash equivalents				
Cash	\$ 224,346	\$ -	\$ -	\$ 224,346
Taxable money market fund	39,283	-	-	39,283
Municipal securities	37,500	-	-	37,500
Cash and cash equivalents	\$ 301,129	\$ -	\$ -	\$ 301,129
Short-term investments				
Municipal securities	\$ 417,668	\$ 1,242	\$ (196)	\$ 418,714
Money market preferreds	141,405	-	(5)	141,400
Mutual funds	120,612	-	(1,828)	118,784
Equity securities	14,510	4,083	(6,419)	12,174
Short-term investments	\$ 694,195	\$ 5,325	\$ (8,448)	\$ 691,072
Cash and short-term investments	\$ 995,324	\$ 5,325	\$ (8,448)	\$ 992,201

<i>(Dollars in thousands)</i>	Cost at Oct. 31, 1998	Gross Unrealized Gains	Gross Unrealized Losses	Fair Market Value at Oct. 31, 1998
Cash and cash equivalents				
Cash	\$ 98,444	\$ –	\$ –	\$ 98,444
Repurchase agreements	8,092	–	–	8,092
Money market fund	55,957	–	–	55,957
Municipal securities	14,590	–	–	14,590
Cash and cash equivalents	\$ 177,083	\$ –	\$ –	\$ 177,083
Short-term investments				
Municipal securities	\$ 448,195	\$ 8,027	\$ –	\$ 456,222
Money market mutual funds	95,631	–	–	95,631
Money market preferreds	181,719	–	(19)	181,700
Mutual funds	15,340	–	–	15,340
Equity securities	128,837	30,159	(77,805)	81,191
Short-term investments	\$ 869,722	\$38,186	\$ (77,824)	\$ 830,084
Cash and short-term investments	\$1,046,805	\$38,186	\$ (77,824)	\$1,007,167

During the first nine months of fiscal 1999 the Company realized gains of \$49 million and realized losses of \$56 million on the sale of securities compared to realized gains of \$11 million and realized losses of \$9 million in the first nine months of fiscal 1998.

C. Income Taxes

The Company's estimated effective tax rate for the first nine months of fiscal 1999 was 28.0%, the same as in the first nine months of fiscal 1998. The Company paid cash amounts for income taxes of \$5.5 million and \$11 million, in the first nine months of fiscal 1999 and 1998, respectively.

D. Commitments and Contingencies

The Company currently has a \$10 million unsecured revolving bank line of credit, with interest at the prime rate. The line can be used for either letter of credit or working capital purposes. The line is subject to the terms of a loan agreement containing financial covenants and restrictions, none of which are expected to significantly affect the Company's operations. At July 31, 1999 borrowings, letter of credit acceptances or commitments of approximately \$1.3 million were outstanding under such line.

The Company has an additional \$5 million line of credit with another bank which is not subject to a loan agreement. At July 31, 1999 standby letters of credit of approximately \$400,000 were outstanding under this line of credit.

In fiscal 1997, the Company entered into agreements to lease buildings being constructed on land owned by the Company in San Jose, California and in Provo, Utah. The lessor has committed to fund up to \$272 million for construction of the buildings. The leases are for a period of seven years and can be renewed for two additional five year periods, subject to the approval of the lender and the Company, at the sole discretion of each party. Rent obligations commenced during the second quarter of fiscal 1999 for San Jose and will commence upon the Company's occupation of the Provo building in fiscal 2000. Annual rent under each agreement is determined by taking the portion of the committed amount actually utilized and associated capitalized interest accrued during the construction period and multiplying this amount by the secured interest rate. If the Company does not purchase the buildings, or arrange for the sale of the buildings, at the end of the lease, the Company will guarantee the lessor no more than 85% of the residual value of the buildings. The guaranteed residual value at July 31, 1999, was approximately \$218 million. In addition, the agreement calls for the Company to maintain a specific level of restricted cash to serve as collateral for the leases and

maintain compliance with certain financial covenants. The value of restricted cash held as collateral at July 31, 1999 was approximately \$172 million, and is included in long-term investments.

In 1993, a suit was filed due to a failed contract against a company that Novell subsequently acquired. The plaintiff obtained a jury verdict against the acquired company in 1996. In May 1999, the Company settled this legal matter. The resolution of this legal matter did not have a material adverse effect on the Company's financial position, results of operations, or cash flows.

In February 1998, a suit was filed against Novell and certain of its officers and directors, alleging violation of federal securities laws. The lawsuit was brought as a purported class action on behalf of purchasers of Novell common stock from November 1, 1996 through April 22, 1997. The case is in its preliminary stages. Novell believes that the case is without merit, and intends to vigorously defend against the allegations. While there can be no assurance as to the ultimate disposition of the case, Novell does not believe that the resolution of this litigation will have a material adverse effect on its financial position, results of operations, or cash flows.

The Company is a party to a number of legal claims arising in the ordinary course of business. The Company believes the ultimate resolution of the claims will not have a material adverse effect on its financial position, results of operations, or cash flows.

E. Put Warrants

In connection with the Company's stock repurchase program, the Company sold put warrants on 15 million shares of its common stock during the third quarter of fiscal 1998, giving a third party the right to sell shares of Novell common stock to the Company at contractually specified prices. The put warrants are exercisable only at maturity, expire at various dates through July 1999, and can only be settled in shares. All 15 million of the Company's put warrant obligations expired worthless in July 1999.

Additionally, during the third quarter of fiscal 1998, the Company purchased call options on 10 million shares of its common stock, giving the Company the right to purchase shares of Novell common stock at contractually specified prices. The call options are exercisable only at maturity and expire at various dates through July 1999. The premiums received from the sale of the put warrants offset in full the cost of the call options. During the first nine months of 1999, the Company exercised all of its call options to purchase 10 million shares of Novell common stock in connection with the Company's stock repurchase program.

F. International Sales

The Company operates in one business segment and markets internationally both directly to end users and through distributors who sell to dealers and end users. For the first nine months of fiscal 1999 and fiscal 1998, sales to international customers were approximately \$421 million and \$333 million, respectively. In the first nine months of fiscal 1999 and fiscal 1998, 71% and 66%, respectively, of international sales were to European countries. No one foreign country accounted for 10% or more of total sales in either period. Except for one multi-national distributor, which accounted for 11% of total revenue in the first nine months of 1999 and 13% of total revenue in the first nine months of fiscal 1998, no customer accounted for more than 10% of total revenue in any period.

G. Net Income Per Share

	Fiscal Quarter Ended		Nine Months Ended	
	July 31, 1999	July 31, 1998	July 31, 1999	July 31, 1998
<i>Amounts in thousands, except per share data</i>				
Basic net income per share computation				
Net income	\$ 49,311	\$ 26,556	\$ 116,935	\$ 59,957
Weighted average shares outstanding	334,488	353,436	335,735	352,076
Basic net income per share	\$ 0.15	\$ 0.08	\$ 0.35	\$ 0.17
Diluted net income per share computation				
Net income	\$ 49,311	\$ 26,556	\$ 116,935	\$ 59,957
Weighted average shares outstanding	334,488	353,436	335,735	352,076
Incremental shares attributable to exercise of outstanding options (treasury stock method)	16,463	8,647	15,461	5,137
Total	350,951	362,083	351,196	357,213
Diluted net income per share	\$ 0.14	\$ 0.07	\$ 0.33	\$ 0.17

H. Comprehensive Income

In the first quarter of 1999, the Company adopted Statement of Financial Accounting Standards No. 130 (SFAS 130), "Reporting Comprehensive Income." SFAS 130 establishes new rules for the reporting and displaying of comprehensive income. SFAS 130 requires unrealized gains or losses on the Company's available-for-sale securities, unearned stock compensation and cumulative translation adjustments, which prior to adoption were only reported separately in shareholders' equity, to be included in comprehensive income. The components of comprehensive income, net of tax, for the three months and nine months ended July 31, 1999 and July 31, 1998 were as follows:

	Fiscal Quarter Ended		Nine Months Ended	
	July 31, 1999	July 31, 1998	July 31, 1999	July 31, 1998
<i>Dollars in thousands</i>				
Net income	\$ 49,311	\$ 26,556	\$ 116,935	\$ 59,957
Unrealized gain/(loss) on investments	1,554	(5,436)	22,427	(9,033)
Unearned stock compensation	(1,241)	131	(2,268)	1,163
Cumulative translation adjustment	(732)	(843)	(821)	(675)
Comprehensive income	\$ 48,892	\$ 20,408	\$ 136,273	\$ 51,412

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

Introduction

Novell is the world's leading provider of directory-enabled networking software. Novell solutions give businesses total control of their private networks and the Internet, simplifying the management of user access and identity. Novell's worldwide channel, consulting, developer, education, and technical support programs are the most extensive in the network computing industry.

Results of Operations

Net Sales	Q3		Q3		YTD	
	1999	Change	1998	1999	Change	1998
Net sales (millions)	\$327	20%	\$272	\$928	18%	\$786

Novell's products can be categorized into four areas, all within the software industry. They are directory-enabled server platforms; network infrastructure and management applications; service, education and consulting; and pre-directory products. The increase in revenue in the third quarter of 1999 and for the first nine months of fiscal 1999 compared to same periods of 1998, is a result of growth in directory-enabled server platforms; network infrastructure and management applications; and service, education and consulting, slightly offset by decreases in pre-directory products.

Revenue from the directory-enabled server platforms category, which includes NetWare 4 and NetWare 5, increased \$37 million or 27% in the third quarter of 1999 compared to the third quarter of 1998, and \$106 million or 28% in the first nine months of fiscal 1999 compared to the first nine months of 1998. The third quarter and year-to-date increase in revenue is due to strong customer acceptance of NetWare 5, which is Internet Protocol based.

The network infrastructure and management applications product category includes NetWare for SAA host connectivity products, BorderManager, NDS integration and high availability service products as well as collaboration and management products including GroupWise, ManageWise, and Z.E.N.works. Revenue from this product category was \$75 million in the third quarter of 1999 compared to \$56 million in the third quarter of 1998. This 34% increase was driven by an increase in sales of management and collaboration products, including new product revenue from Z.E.N.works, and an increase in network infrastructure products including BorderManager and NDS for NT and Solaris, somewhat offset by a decrease in mobile/remote connectivity products. In the first nine months of fiscal 1999 compared to the first nine months of fiscal 1998, network infrastructure and management applications revenue was up \$61 million or 39%. This year-to-date increase was driven by strong sales of each of the management and collaboration products, BorderManager, NetWare SAA and NDS for NT and Solaris.

Service, education and consulting, revenue, generated from customer service, educational products and courses, and consulting for network solutions, were \$49 million and \$34 million in the third quarter of 1999 and 1998, respectively. The increase in the third quarter of 1999 was a result of new directory-related consulting revenue, increased service revenue as a result of increased site licenses, and growth in education. In the first nine months of fiscal 1999 compared to the first nine months of fiscal 1998, service, education, and consulting revenue increased by \$38 million or 41% due to the same factors driving the quarter over quarter revenue growth.

Pre-directory products revenue consists of NetWare 3, non directory-enabled infrastructure products and UNIX royalties. Revenue in this category decreased to \$28 million in the third quarter of 1999 compared to \$44 million in the third quarter of 1998. Revenue in for the first nine months of 1999 decreased to \$88 million compared to \$151 million for the same period of 1998. These decreases were primarily the result of shrinking NetWare 3 and host connectivity revenue and the elimination of Tuxedo revenue, which ended in the fourth quarter of fiscal 1998. Revenue from this category is expected to continue to decline as sales of directory-enabled products continue to increase and newer versions of non-directory products are introduced.

International sales represented 45% of total sales in the first nine months of 1999 compared to 42% in the first nine

months of 1998. This change is the result of stronger sales growth in the international markets where they saw a 27% increase in revenues compared to a 12% increase in domestic revenues in the first nine months of fiscal 1999 compared to the first nine months of fiscal 1998.

Gross Profit

	Q3		Q3		YTD	
	1999	Change	1998	1999	Change	1998
Gross profit (millions)	\$253	21%	\$209	\$714	18%	\$607
Percentage of net sales	78%		77%	77%		77%

Gross profit as a percentage of sales increased slightly in the third quarter of fiscal 1999 compared to the third quarter of fiscal 1998 due to lower inventory variances and decreased royalties, offset by increased expenses, both as a percentage of net sales and in absolute dollars, associated with the ramping up the Company's consulting business. In the first nine months of fiscal 1999 compared to the first nine months of fiscal 1998, the gross margin percentage remained flat. Improvements in inventory variances and training and education costs were offset by higher service, consulting and royalty costs.

	Q3		Q3		YTD	
	1999	Change	1998	1999	Change	1998
Operating Expenses						
Sales and marketing (millions)	\$109	12%	\$97	\$321	6%	\$303
Percentage of net sales	33%		36%	35%		39%
Product development (millions)	\$ 57	0%	\$ 57	\$169	-5%	\$178
Percentage of net sales	18%		21%	18%		23%
General and administrative (millions)	\$ 25	0%	\$ 25	\$ 76	-1%	\$ 77
Percentage of net sales	8%		9%	8%		10%
Total operating expenses (millions)	\$191	7%	\$179	\$566	1%	\$558
Percentage of net sales	58%		66%	61%		71%

Sales and marketing expenses increased by \$12 million, in the third quarter of fiscal 1999 compared to the third quarter of fiscal 1998 and by \$18 million in the first nine months of fiscal 1999 compared to the first nine months of fiscal 1998.

At the same time however, sales and marketing expenses decreased as a percentage of net sales in each period of 1999. Sales and marketing expenses fluctuate as a percentage of net sales in any given period due to product promotions, advertising or other discretionary expenses.

Product development expenses remained flat in the third quarter of fiscal 1999 compared to the third quarter of fiscal 1998 and decreased by \$9 million, or 5% in the first nine months of fiscal 1999 compared to the first nine months of fiscal 1998. Product development expenses also decreased as a percentage of net sales in both comparative periods due to increased sales levels and a more efficient product development organization focused on delivering new products consistent with the Company's strategy.

General and administrative expenses remained flat in the third quarter of fiscal 1999 compared to the third quarter of fiscal 1998 and decreased slightly in the first nine months of fiscal 1999 compared to the same period of fiscal 1998. General and administrative expenses decreased as a percentage of net sales in both comparative periods as well, due to a higher revenue base and an increased focus on controlling costs.

	YTD		YTD	
	1999	Change	1998	1998
Employees	5,204	—	4,502	4,502
Annualized revenue per employee (000's)	\$253	7%	\$226	\$226

Other Income, Net	Q3		Q3		YTD	
	1999	Change	1998	1999	Change	1998
Other income, net (millions)	\$ 6	-11%	\$ 7	\$ 14	-58%	\$ 34
Percentage of net sales	2%		3%	2%		4%

The primary component of other income, net is investment income, which was \$10 million in the third quarter of fiscal 1999 compared to \$7 million in the third quarter of fiscal 1998. The increase is the result of higher net realized capital losses on the disposal of certain equity securities in the third quarter of fiscal 1998. In addition to investment income, the Company incurred immaterial losses on foreign currency and wrote off certain long-term investments in the third quarter of 1999. Year-to-date other income, net decreased primarily due to lower investment income and net realized capital losses associated with certain equity securities disposed of in fiscal 1999. Investment income was \$31 million compared to \$37 million in the first nine months of fiscal 1999 and 1998, respectively, and net realized capital losses were \$7 million compared to net realized gains of \$2 million in the first nine months of fiscal 1999 and 1998, respectively.

Income Taxes

	Q3		Q3		YTD	
	1999	Change	1998	1999	Change	1998
Income taxes (millions)	\$ 19	86%	\$ 10	\$ 45	96%	\$ 23
Percentage of net sales	6%		4%	5%		3%
Effective tax rate	28%		28%	28%		28%

The effective tax rate for fiscal 1999 is estimated to be 28%, the same as fiscal 1998.

Net Income and Net Income Per Share

	Q3		Q3		YTD	
	1999	Change	1998	1999	Change	1998
Net income (millions)	\$ 49	86%	\$ 27	\$117	95%	\$ 60
Percentage of net sales	15%		10%	13%		8%
Net income per share - basic	\$.15		\$.08	\$.35		\$.17
Net income per share - diluted	\$.14		\$.07	\$.33		\$.17

Liquidity and Capital Resources

	Q3		Q4	
	1999	Change	1998	1998
Cash and short-term investments (millions)	\$992	-1%		\$1,007
Percentage of total assets	51%			52%

Cash and short-term investments decreased by \$15 million at July 31, 1999 from \$1 billion at October 31, 1998. During the year, the Company spent \$204 million of cash for the repurchase of common stock, \$72 million to increase collateral associated with certain long-term investments, \$51 million to purchase property, plant and equipment, and \$14 million for purchases of other assets in the third quarter of 1999. These cash expenditures were offset by the \$248 million provided by operating activities and the \$80 million from the issuance of common stock.

The Company's investment portfolio includes securities with gross unrealized losses of \$3 million as of July 31, 1999. The only remaining security with material unrealized losses is Corel common stock, which was obtained in March 1996 upon the Company's sale of its personal productivity applications product line. It is the Company's intention to continue to dispose of the Corel shares over the coming periods.

The investment portfolio is diversified among security types, industry groups, and individual issuers. To achieve potentially higher returns, a limited portion of the Company's investment portfolio is invested in mutual funds, which incur market risk. The Company believes that the market risk has been limited by diversification and by use of a funds management timing service which switches funds out of mutual funds and into money market funds when preset signals occur.

The Company's principal source of liquidity has been from operations. At July 31, 1999, the Company's principal unused sources of liquidity consisted of cash and short-term investments and available borrowing capacity of approximately \$14 million under its credit facilities. The Company's liquidity needs are principally for the Company's financing of accounts receivable, capital assets, strategic investments, product development and flexibility in a dynamic and competitive operating environment.

During the first nine months of fiscal 1999, the Company has continued to generate cash from operations. The Company anticipates being able to fund its current operations and capital expenditures planned for the foreseeable future with existing cash and short-term investments together with internally generated funds. The Company believes that borrowings under the Company's credit facilities or public offerings of equity or debt securities are available if the need arises. Investments will continue in product development and in new and existing areas of technology. Cash may also be used to acquire technology through purchases and strategic acquisitions. Capital expenditures in fiscal 1999 are anticipated to be approximately \$60 million, but could be reduced if the growth of the Company is less than presently anticipated.

In June 1998, the Company announced its intent to repurchase and retire up to 10 percent, or approximately 35 million shares, of Novell common stock over the next twelve months. During the first nine months of 1999, the Company repurchased and retired approximately 13.5 million shares at a cost of approximately \$204 million. During fiscal 1998, the Company repurchased and retired approximately 21 million shares at a cost of approximately \$245 million. In July 1999, the Board of Directors authorized up to \$500 million for the repurchase of additional outstanding shares of the Company's common stock through October 31, 2000.

Future Results

The Company's future results of operations involve a number of risks and uncertainties. Among the factors that could cause actual results to differ materially from historical results are the following: business conditions and the general economy; competitive factors, such as rival operating systems, acceptance of new products and price pressures; availability of third-party compatible products at reasonable prices; risk of nonpayment of accounts or notes receivable; risks associated with foreign operations; risk of product line or inventory obsolescence due to shifts in technologies or market demand; timing of software product introductions; market fluctuations of investment securities; and litigation.

In the past, many information technology products were designed with two digit year codes that did not recognize century and millennium fields. As a result, these hardware and software products may not function or may give incorrect results beginning in the year 2000. The year 2000 issue is faced by substantially every company in the computer industry, as well as every company which relies on computer systems.

The Company has created a company-wide Year 2000 team to identify and resolve Year 2000 issues associated either with the Company's internal systems or the products and services sold by the company. As part of this effort, the Company has communicated with its main suppliers of technology products and services regarding the Year 2000 status of such products or services. The Company has identified and tested its main internal systems. Most significant Y2K updates have been installed. In 1999 the Company expects to complete implementation of needed year 2000-related modifications to its information systems. The Company has also assessed its internal non-information technology systems. Most significant Y2K updates have been installed, and the Company expects to complete needed modifications to these systems in 1999.

The Company's total cost relating to these activities has not been and is not expected to be material to the Company's financial position, results of operations, or cash flows. The Company believes that necessary modifications will be made on a timely basis. However, there can be no assurance that there will not be a delay in, or increased costs associated with, the implementation of such modifications, or that the Company's suppliers will adequately prepare for the year 2000 issue. It is possible that any such delays, increased costs, or supplier failures could have a material adverse impact on the Company's operations and financial results, by, for example, impacting the Company's ability to deliver products

or services to its customers. The Company has begun contingency planning and finalized in mid-1999 its main assessment of contingency planning for potential critical operational or performance problems related to year 2000-related issues with its information systems.

The Company's year 2000 effort has included testing products currently or recently on the Company's price list for year 2000 issues. Generally, for products that were identified as needing updates to address year 2000 issues, the Company has prepared or is preparing updates, or has removed the product from its price list. Some of the Company's customers are using product versions that the Company will not support for year 2000 issues; the Company is encouraging these customers to migrate to current product versions that are year 2000 ready.

For third party products, which the Company distributes with its products, the Company has sought information from the product manufacturers regarding the products' year 2000 readiness status. Customers who use the third-party products are directed to the product manufacturer for detailed year 2000 status information. On its year 2000 web site at www.novell.com/year2000/, the Company provides information regarding which of its products are year 2000 ready and other general information related to the Company's year 2000 efforts. The Company's total costs relating to these activities has not been and is not expected to be material to the Company's financial position or results of operations.

The Company believes its current products, with any applicable updates, are well-prepared for year 2000 date issues, and the Company plans to support these products for date issues that may arise related to the year 2000. However, there can be no guarantee that one or more current Company products do not contain year 2000 date issues that may result in material costs to the Company. Because it is in the business of selling software products, the Company's risk of being subjected to lawsuits relating to year 2000 issues with its software products is likely to be greater than that of companies in other industries. Because computer systems may involve different hardware, firmware and software components from different manufacturers, it may be difficult to determine which component in a computer system may cause a year 2000 issue. As a result, the Company may be subjected to year 2000-related lawsuits independent of whether its products and services are year 2000 ready. The outcomes of any such lawsuits and the impact on the Company cannot be determined at this time.

Novell believes that it has the product offerings, facilities, personnel, and competitive and financial resources for continued business success, but future revenues, costs, margins, product mix, and profits are all influenced by a number of factors, such as those discussed above, as well as risks described in detail in the Company's fiscal 1998 report on Form 10-K.

Part II. Other Information

Except as listed below, all information required by items in Part II is omitted because the items are inapplicable or the answer is negative.

Item 1. Legal Proceedings.

The information required by this item is incorporated herein by reference to Footnote D of the Company's financial statements contained in Part I, Item 1 of this Form 10-Q.

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

None

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits

<u>Exhibit Number</u>	<u>Description</u>
27*	Financial Data Schedule

(b) Reports on Form 8-K.

No reports on Form 8-K were filed by the Registrant during the quarter ended July 31, 1999.

*Filed herewith.

SIGNATURES

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

Novell, Inc.
(Registrant)

Date: September 10, 1999

/s/ Dr. Eric Schmidt
Dr. Eric Schmidt
Chairman of the Board and
Chief Executive Officer
(Principal Executive Officer)

Date: September 10, 1999

/s/ Dennis R. Raney
Dennis R. Raney
Chief Financial Officer
(Principal Financial Officer)

Date: September 10, 1999

/s/ Ron Foster
Ron Foster
Vice President and Corporate Controller
(Principal Accounting Officer)

SIGNATURES

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

Novell, Inc.
(Registrant)

Date: September 10, 1999

Dr. Eric Schmidt
Chairman of the Board and
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Dennis R. Raney
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(Principal Financial Officer)

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Ron Foster
Vice President and Corporate Controller
(Principal Accounting Officer)