

Starent Networks, Corp.  
Form S-1  
October 15, 2007

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As filed with the Securities and Exchange Commission on October 15, 2007.

Registration No. 333-

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

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**Form S-1**  
REGISTRATION STATEMENT  
UNDER  
THE SECURITIES ACT OF 1933

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**STARENT NETWORKS, CORP.**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**  
(State or Other Jurisdiction of  
Incorporation or Organization)

**3663**  
(Primary Standard Industrial  
Classification Code No.)  
**30 International Place**  
**Tewksbury, MA 01876**  
**(978) 851-1100**

**04-3527533**  
(I.R.S. Employer  
Identification No.)

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

**Ashraf M. Dahod**  
**President and Chief Executive Officer**  
**Starent Networks, Corp.**  
**30 International Place**  
**Tewksbury, MA 01876**  
**(978) 851-1100**

(Name, address, including zip code, and telephone number, including area code, of agent for service)

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**Approximate date of commencement of proposed sale to the public:** As soon as practicable after this Registration Statement is declared effective.

If any of the securities being registered on this Form are offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, as amended (the "Securities Act") please check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

### CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Amount to be Registered(1)	Proposed Maximum Aggregate Offering Price Per Share(2)	Proposed Maximum Aggregate Offering Price(2)	Amount of Registration Fee(3)
Common Stock, par value \$.001 per share	9,200,000	\$27.365	\$251,758,000	\$7,729

(1) Includes 1,200,000 shares of common stock to cover the underwriters' option to purchase additional shares, if any.

(2) Estimated solely for the purpose of computing the registration fee in accordance with Rule 457(c) under the Securities Act of 1933, as amended.

(3) Calculated pursuant to Rule 457(c) based on the average of the high and low sales prices reported in the consolidated reporting system of the Nasdaq Global Market on October 10, 2007.

**The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to Section 8(a), may determine.**

The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and it is not soliciting offers to buy these securities in any state where the offer or sale is not permitted.

Subject to Completion. Dated October 15, 2007

## Shares

# Starent Networks, Corp.

## Common Stock

Starent Networks is offering \_\_\_\_\_ of the shares to be sold in the offering. The selling stockholders identified in this prospectus, including our president and chief executive officer, are offering an additional \_\_\_\_\_ shares. Starent Networks will not receive any of the proceeds from the sale of the shares being sold by the selling stockholders.

Our common stock is listed on the Nasdaq Global Market under the symbol "STAR." The last reported sale price of our common stock on October 12, 2007 was \$27.42 per share.

See "Risk Factors" on page 7 to read about factors you should consider before buying shares of common stock.

Neither the Securities and Exchange Commission nor any other regulatory body has approved or disapproved of these securities or passed upon the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense.

	Per share	Total
Public offering price	\$ _____	\$ _____
Underwriting discount	\$ _____	\$ _____
Proceeds, before expenses, to Starent Networks	\$ _____	\$ _____
Proceeds, before expenses, to the selling stockholders	\$ _____	\$ _____

To the extent that the underwriters sell more than \_\_\_\_\_ shares of common stock, the underwriters have the option to purchase up to an additional \_\_\_\_\_ shares from Starent Networks at the public offering price less the underwriting discount.

The underwriters expect to deliver the shares against payment in New York, New York on \_\_\_\_\_, 2007.

**Goldman, Sachs & Co.**

**Lehman Brothers**

**JPMorgan**

**Thomas Weisel Partners LLC**

Prospectus dated \_\_\_\_\_, 2007.

## PROSPECTUS SUMMARY

*This summary highlights information contained elsewhere in this prospectus. You should read the following summary together with the more detailed information appearing in this prospectus, including our consolidated financial statements and related notes, and the risk factors beginning on page 7, before deciding whether to purchase shares of our common stock. Unless the context otherwise requires, we use the terms "Starent," "Starent Networks," "our company," "we," "us" and "our" in this prospectus to refer to Starent Networks, Corp. and its subsidiaries.*

### Starent Networks

#### Overview

Starent Networks is a leading provider of infrastructure hardware and software products and services that enable mobile operators to deliver multimedia services to their subscribers. We have created hardware and software products that provide network functions and services, including access from a wide range of radio networks to the operator's packet core network. A packet core network splits traffic into multiple pieces of data, or packets, that are routed over an Internet Protocol, or IP, network and enables mobile operators to deliver multimedia services. Our products and services also provide management of subscriber sessions moving between networks and application of billing and other session policies. Our products and services provide high performance and system intelligence by combining significant computing power, memory and traffic handling capabilities with a flexible, high availability operating system and other proprietary software. Our products integrate multiple network functions and services needed for the delivery of advanced multimedia services, such as video, Internet access, voice-over-IP, e-mail, mobile TV, photo sharing and gaming.

Mobile operators are aggressively deploying next-generation wireless networks, such as third generation, or 3G, networks, that are capable of delivering high quality, mobile multimedia services to subscribers. In deploying these new networks, mobile operators are seeking packet core network hardware and software that can deliver multimedia services with high performance and simplicity and provide high reliability. We have developed our multimedia core network platforms and our proprietary software specifically to address the needs of packet-based mobile networks. Our multimedia core network platforms consist of the ST16, which has been deployed since 2003, and our recently introduced ST40, which became generally available in the third quarter of 2007.

We sell our hardware and software products to leading mobile operators around the world both directly and through OEMs, system integrators and distributors. We believe the deployment of our products by over 60 mobile operators in 25 countries including many of the world's largest mobile operators makes Starent Networks a leading provider of infrastructure products and services that enable mobile operators to deliver multimedia services to their subscribers. We became profitable in 2005, and in 2006 our revenues were \$94.4 million and our net income was \$3.6 million, including interest income of \$2.3 million. For the six months ended June 30, 2007, our revenues were \$58.5 million and our net income was \$5.7 million, including interest income of \$1.6 million. As of June 30, 2007, we had an accumulated deficit of \$99.8 million.

#### Industry Background

Mobile operators have been aggressively upgrading their networks for a variety of reasons, including in large part due to increasing mobile subscriber demand for a wide range of multimedia services. Several factors are accelerating the growth of data-rich multimedia traffic on mobile wireless networks, including continued growth in the number of mobile subscribers worldwide, an increasingly mobile and interconnected society in which information is accessible and communications are available all the time regardless of location, and a proliferation of mobile devices designed for multimedia services.

In order to deliver a high-quality subscriber experience in this multimedia environment, mobile operators require infrastructure hardware and software products that are able to identify and manage individual communications sessions, handle significant traffic and integrate services. The hardware and software must also allow mobile operators to simplify and easily upgrade their networks, deliver quality of service, reliability and availability and support multiple radio access technologies.

Historically, mobile operators seeking to address these challenges have been required to retrofit network infrastructure hardware and software originally designed for wireline networks. These products utilizing repurposed network switches, routers and off-the-shelf enterprise servers are unable to sufficiently satisfy the needs of mobile operators to deliver efficient and reliable multimedia services. While routers and network switches are capable of forwarding packets of information, they lack the integrated processing power, memory and software needed to examine individual packets and apply defined business policies and subscriber services to them. To address these shortcomings, mobile operators typically connect repurposed switches and routers with numerous enterprise servers in multi-element configurations. These repurposed products offer limited intelligence about subscriber sessions, can result in limited network performance and reliability and can be costly to operate and upgrade.

### **Our Products and Services**

Our hardware and software products provide six key, integrated capabilities that create enhanced revenue opportunities and facilitate reduced costs for mobile operators:

*Intelligence to shape the subscriber experience.* Our products and services combine custom software with significant processing power and memory to conduct a detailed inspection of each subscriber session and to associate that session with a subscriber need, operator service requirement or operator business policy.

*High performance.* Our products are capable of handling increasing amounts of network traffic to support a large number of subscribers on one platform and provide high bandwidth and data processing rates for improved traffic capacity and flow. In addition, our products provide high call transaction rates, which enhance the ability of our products to handle increasing amounts of network traffic, reduce unwanted delays in network traffic and allow the subscriber to have quick access to network services.

*Simple and flexible network architecture.* Our products allow mobile operators to integrate a number of network functions and enhanced services into a single hardware platform. In addition to providing network functions such as access, management of subscriber sessions moving between networks and application of billing and other session policies, our platforms are also capable of integrating advanced services that are typically deployed out of line from the session stream elsewhere in the network, such as enhanced charging and billing, firewall protection, security and content filtering.

*Reliability and redundancy.* Our system architecture provides a high level of resiliency and protects the subscriber's experience because all of our platforms' system resources, including those used for redundancy, can be shared. Our platforms employ hardware redundancy as well as high-availability software techniques, such as session recovery, fault containment and state replication.

*Support multiple radio access technologies.* Our products are capable of supporting multiple radio access technologies, including CDMA and GSM/UMTS, which are the two principal radio access technologies in use today. This capability allows mobile operators to deliver a uniform service experience to subscribers from a single platform, simplifying the network and limiting operator costs.

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*Well positioned for future technology upgrades.* While designed for use in today's mobile networks, our products are also readily upgradeable to respond to evolving mobile operator environments or requirements and new technologies. Our platforms can typically provide new network functions or enhanced services through a software upgrade.

### **Our Strategy**

Our goal is to strengthen our leadership in the mobile network infrastructure market. Principal elements of our strategy include the following:

*Extend our technological leadership.* We believe we have market leading products and services today, and we will continue to invest in research and development to maintain our leadership position through the introduction of new products and enhancements to existing products.

*Increase market penetration.* As mobile operators continue to increase network coverage and capacity, as well as their service offerings, they create new sales opportunities for us. We intend to increase our market penetration of both CDMA and GSM/UMTS operators. We believe a significant opportunity for growth is from sales to GSM/UMTS operators as they continue to transition to high-bandwidth networks.

*Expand into evolving markets.* We plan to address new radio access network architectures and technologies and leverage our products' access independence the flexibility and power to deploy a single hardware platform across multiple access architectures and technologies.

*Increase the number of features.* We plan to continue to develop new features based on specific customer requests and anticipated market needs.

*Expand our sales channels.* We intend to expand our existing relationships with mobile operators, pursue new direct and OEM, system integrator and distributor relationships to sell our products and expand our direct sales force.

*Continue to offer a high level of support.* We believe one critical factor of our success has been our focused support and technical expertise. We intend to continue to offer a high level of customer support.

### **Risks Associated with Our Business**

Our business is subject to numerous risks and uncertainties, as more fully described under "Risk Factors" beginning on page 7, which you should carefully consider prior to deciding whether to invest in our common stock. For example:

we compete in new and rapidly evolving markets and have a limited operating history, which makes it difficult to predict our future operating results;

our past operating results have fluctuated significantly, and likely will continue to fluctuate significantly, which makes it difficult to predict our operating results and could cause our operating results to fall below expectations;

we depend on a limited number of customers for a substantial portion of our revenues, and the loss of a key customer or any significant adverse change in the size or terms of orders from a key customer could significantly reduce our revenues;

we rely on a single line of products focused on a single market, and if the market for those products does not develop as we anticipate, our revenues may decline or fail to grow, which would adversely affect our operating results; and

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the market in which we compete is highly competitive and competitive pressures from existing and new companies may have a material adverse effect on our business.

### **Corporate Information**

We were incorporated in Delaware in August 2000. Our principal executive offices are located at 30 International Place, Tewksbury, Massachusetts 01876, and our telephone number is (978) 851-1100. Our website address is [www.starentnetworks.com](http://www.starentnetworks.com). Information contained on our website is not incorporated by reference into this prospectus, and you should not consider information contained on our website to be part of this prospectus or in deciding whether to purchase shares of our common stock.

"Starent," "ST16," "ST40," the Starent Networks logo and other trademarks or service marks of Starent Networks appearing in this prospectus are the property of Starent Networks. This prospectus contains additional trade names, trademarks and service marks of other companies.

**The Offering**

Common stock offered by Starent Networks, Corp.	shares
Common stock offered by the selling stockholders	shares
Common stock to be outstanding after this offering	shares
Use of proceeds	We intend to use the net proceeds from this offering for working capital and other general corporate purposes, including the development of new products, sales and marketing activities and capital expenditures. We may use a portion of the proceeds for the acquisition of, or investment in, companies, technologies, products or assets that complement our business. We will not receive any proceeds from the shares sold by the selling stockholders. The selling stockholders include our president and chief executive officer. See "Use of Proceeds" for more information.
Risk Factors	You should read the "Risk Factors" section and other information included in this prospectus for a discussion of factors to consider carefully before deciding to invest in shares of our common stock.
Nasdaq Global Market symbol	"STAR"

The number of shares of our common stock to be outstanding after this offering is based on the number of shares of common stock outstanding as of June 30, 2007, and excludes:

8,446,958 shares of common stock issuable upon the exercise of stock options outstanding as of June 30, 2007, at a weighted average exercise price of \$3.43 per share, of which options to purchase 2,319,237 shares of our common stock were exercisable as of June 30, 2007 with a weighted average exercise price of \$1.14 per share; and

3,481,108 shares of common stock available for future issuance under our equity compensation plans as of June 30, 2007.

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*Except as otherwise noted, all information in this prospectus assumes no exercise by the underwriters of their option to purchase up to additional shares.*



## SUMMARY CONSOLIDATED FINANCIAL DATA

The following tables summarize the consolidated financial data for our business for the periods presented. You should read the following summary financial data in conjunction with "Selected Consolidated Financial Data," "Management's Discussion and Analysis of Financial Condition and Results of Operations," and the financial statements and related notes, all included elsewhere in this prospectus.

	Year Ended December 31,			Six Months Ended June 30,	
	2004	2005	2006	2006	2007
(unaudited)					
(in thousands, except per share data)					
<b>Statement of Operations Data:</b>					
Revenues:					
Product	\$ 29,453	\$ 51,819	\$ 81,061	\$ 29,466	\$ 49,573
Service	4,942	7,841	13,289	5,357	8,923
Total revenues	34,395	59,660	94,350	34,823	58,496
Cost of revenues:					
Product	12,633	12,285	25,640	7,294	10,754
Service	812	1,358	2,086	704	3,329
Total cost of revenues	13,445	13,643	27,726	7,998	14,083
Gross profit	20,950	46,017	66,624	26,825	44,413
Operating expenses:					
Research and development	13,303	18,107	25,980	9,705	17,651
Sales and marketing	18,445	19,785	30,311	12,745	15,936
General and administrative	3,185	7,352	8,515	3,499	6,242
Total operating expenses	34,933	45,244	64,806	25,949	39,829
Income (loss) from operations	(13,983)	773	1,818	876	4,584
Total other income, net	95	644	2,237	848	1,509
Income (loss) before income tax expense	(13,888)	1,417	4,055	1,724	6,093
Income tax expense	(160)	(513)	(413)	(143)	(407)
Net income (loss)	\$ (14,048)	\$ 904	\$ 3,642	\$ 1,581	\$ 5,686
Net income (loss) per share applicable to common stockholders:					
Basic	\$ (3.28)	\$ (0.97)	\$ (0.62)	\$ (0.35)	\$ 0.04
Diluted	\$ (3.28)	\$ (0.97)	\$ (0.62)	\$ (0.35)	\$ 0.03
Weighted average shares used in computing net income (loss) per share applicable to common shareholders:					
Basic	6,197	6,642	7,026	6,838	15,864

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	<b>Year Ended December 31,</b>			<b>Six Months Ended June 30,</b>	
Diluted	6,197	6,642	7,026	6,838	21,769

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The as adjusted balance sheet data give effect to our sale of \_\_\_\_\_ shares of common stock offered by this prospectus at an assumed public offering price of \$ \_\_\_\_\_ per share, which is the last reported sale price of our common stock on October \_\_\_\_\_, 2007 after deducting the estimated underwriting discount and offering expenses payable by us.

As of June 30, 2007

Actual	As Adjusted
(unaudited)	
(in thousands)	

### Balance Sheet Data:

Cash, cash equivalents and short-term investments	\$	157,165	\$
Working capital		139,441	
Total assets		214,709	
Indebtedness			
Total stockholders' equity		152,444	

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## RISK FACTORS

*An investment in our common stock involves a high degree of risk. In deciding whether to invest, you should carefully consider the following risk factors. Any of the following risks could have a material adverse effect on our business, financial condition, results of operations or prospects and cause the value of our common stock to decline, which could cause you to lose all or part of your investment. When determining whether to invest, you should also refer to the other information in this prospectus, including the financial statements and related notes.*

### **Risks Related to Our Business and Industry**

*We compete in new and rapidly evolving markets and have a limited operating history, which makes it difficult to predict our future operating results.*

We were incorporated in August 2000, and deployed our first commercial product in the first quarter of 2003. We have a limited operating history in an industry characterized by rapid technological change, changing customer needs, evolving industry standards and frequent introductions of new products and services. We believe our limited operating history and the characteristics of our industry make it difficult to forecast our future operating results. You should consider and evaluate our prospects in light of risks faced by companies such as ours, which include challenges in accurate financial planning as a result of limited historical data and the uncertainties resulting from a relatively limited time period in which to implement and evaluate our business strategies, as compared to companies with longer operating histories.

*Our past operating results have fluctuated significantly, and likely will continue to fluctuate significantly, which makes it difficult to predict our operating results and could cause our operating results to fall below expectations.*

Our operating results have historically fluctuated significantly from period to period and we expect our operating results to continue to fluctuate due to a variety of factors, many of which are outside of our control. As a result, comparing our operating results on a period-to-period basis may not be meaningful. You should not rely on our past results as an indication of our future performance. If our revenues or operating results fall below the expectations of investors or securities analysts or below any guidance we may provide to the market, the price of our common stock could decline.

In addition to other risk factors listed in this "Risk Factors" section, factors that may affect our operating results include:

fluctuations in demand, sales cycles and prices for our products and services;

reductions in customers' budgets for mobile network infrastructure purchases and delays in their purchasing decisions;

the timing of recognizing revenue in any given period as a result of software revenue recognition rules;

the sale of our products in the timeframes we anticipate, including the number and size of orders in each period;

the level of our customer concentration and our ability to generate purchases in any particular period from large customers;

our ability to develop, introduce and ship in a timely manner new products and product enhancements that meet customer requirements;

the timing of product releases or upgrades by us or by our competitors;

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any significant changes in the competitive dynamics of our markets, including new entrants or substantial discounting of products;

our ability to control costs, including our operating expenses and the costs of the components we purchase; and

general economic conditions in our domestic and international markets.

***We depend on a limited number of customers for a substantial portion of our revenues. The loss of a key customer or any significant adverse change in the size or terms of orders from a key customer could significantly reduce our revenues.***

We derive a substantial portion of our revenues from a limited number of customers partly due to the nature of the mobile communications industry. During any given fiscal period, a small number of customers may account for a significant percentage of our revenues. For example, in 2006 we had two customers that each accounted for more than 10% of our revenues and in the aggregate represented 83% of our revenues, and for the six months ended June 30, 2007, we had four customers that each accounted for more than 10% of our revenues and in the aggregate represented 90% of our revenues. In addition, we do not have long-term volume purchase contracts with our customers or other commitments that ensure future sales of our products to existing customers. The loss of any key customer, or our inability to generate anticipated revenue from them, would significantly and adversely affect our business, financial condition and results of operations. In addition, a change in the timing or size of a purchase by any one of our key customers can result in significant variations in our revenue and operating results from period to period. Our operating results for the foreseeable future will continue to depend on our ability to effect sales to a small number of customers and any revenue growth will depend on our success selling additional products to our large customers and expanding our customer base to include additional customers that deploy our products in large-scale networks serving significant numbers of subscribers.

Moreover, many of our key customers are large mobile operators that have substantial purchasing power and leverage in negotiating contractual arrangements with us. These customers may require us to agree to terms and conditions that could result in increased costs and decreased revenues that could adversely affect our operating results.

***We rely on a single line of products focused on a single market. If the market for those products does not develop as we anticipate, our revenues may decline or fail to grow, which would adversely affect our operating results.***

We derive, and expect to continue to derive, all of our revenues from a single line of products that provide network functions and services to mobile operators' packet core networks. The market for our products is relatively new and still evolving, and it is uncertain whether our products will achieve and sustain high levels of demand and market acceptance. Our success will depend to a substantial extent on the willingness of mobile operators to continue to implement packet-based, multimedia network infrastructure. Factors that could impair the rate of growth of multimedia networks include:

lower than anticipated demand by subscribers for multimedia services;

budgetary constraints of mobile operators;

uncertainties on the part of mobile operators as to the particular 3G or 4G access technologies they select for deployment in their networks; and

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delays in the development or availability of all the network elements necessary for the mobile operator to deploy its next-generation multimedia network.

If mobile operators do not continue to implement packet core networks, the market for our products may not continue to develop or may develop more slowly than we expect, either of which would significantly adversely affect our revenues and profitability.

***If our new platform, the ST40, does not achieve widespread market acceptance, our operating results will suffer.***

In April 2007, we announced our ST40 platform, which became generally available in the third quarter of 2007. We expect to begin recording revenues from shipments of the ST40 in the fourth quarter of 2007, and a significant portion of our anticipated revenues in the fourth quarter of 2007 and beyond are expected to be generated from sales of the ST40. The current deployments of the ST40 by our customers are in their initial stages, and we cannot assure you that the ST40 will achieve its performance specifications or meet our customers' expectations. In addition, our future sales and operating results will depend, to a significant extent, on the successful introduction and marketing of the ST40. In order to achieve market penetration for the ST40, we may be required to incur additional expenses in marketing and sales in advance of the realization of actual sales. There can be no assurance that the ST40 will achieve widespread acceptance in the market. If we incur delays in the manufacture and shipment of the ST40 or customer testing and verification takes longer than anticipated, the ST40 does not achieve our planned levels of sales or the ST40 does not achieve performance specifications, our operating results will suffer and our competitive position could be impaired.

***The market in which we compete is highly competitive and competitive pressures from existing and new companies may have a material adverse effect on our business, revenues, growth rates and market share.***

We compete in a highly competitive industry that is influenced by many factors, including customer demands for:

reliable, high performance products;

system ability to handle increasing amounts of network traffic and service integration capabilities;

system intelligence;

breadth of network interoperability, access independence and standards support;

high levels of customer support and customer interaction; and

competitive pricing.

We expect competition in the mobile network infrastructure industry to intensify significantly in the future. Other companies may introduce new products in the same markets we serve or intend to enter. This competition could result in increased pricing pressure, reduced profit margins, increased sales and marketing expenses and failure to increase, or the loss of, market share, any of which would likely seriously harm our business, operating results or financial condition.

Competitive products may in the future have better performance, lower prices and broader acceptance than our products. Our primary competitors include Cisco Systems, Inc., LM Ericsson Telephone Co., Nokia Corporation and UTStarcom, Inc., each of which has a longer operating history, greater name recognition, a larger customer base and significantly greater financial, technical, sales, marketing and other resources than we do. Potential customers may prefer to

purchase from their existing suppliers rather than a new supplier regardless of product performance or features. In addition, many of our competitors have a broader range of products and may be able to offer concessions to potential customers on bundled purchases that we are not able to match because we currently offer only a single line of products. We also face competition from a number of companies with more limited market share generally or by geography and newer market entrants.

If our market continues to develop and expand, we could face increased competition from other established companies, as well as emerging companies. For example, OEMs, system integrators and distributors currently selling our products could market products and services that compete with our products and services. In addition, some of our competitors have made acquisitions or entered into partnerships or other strategic relationships with one another to offer a more comprehensive solution than they individually had offered. We expect this trend to continue as companies attempt to strengthen or maintain their market positions in an evolving industry and as companies enter into partnerships, or are acquired. Many of the companies driving this consolidation trend have significantly greater financial, technical and other resources than we do and are better positioned to acquire and offer complementary products and technologies. The companies resulting from these possible consolidations may create more compelling product offerings and be able to offer greater pricing flexibility, making it more difficult for us to compete effectively, including on the basis of price, sales and marketing programs, technology or product functionality. Continued industry consolidation may adversely impact customers' perceptions of the viability of smaller and even medium-sized technology companies and consequently customers' willingness to purchase from such companies. These pressures could materially adversely affect our business, operating results and financial condition.

***Our sales cycles can be long and unpredictable, and our sales efforts require considerable time and expense.***

Our sales cycles typically are long and unpredictable, and our sales efforts require considerable time and expense. Our sales efforts involve educating our customers about the use and benefit of our products, including their technical capabilities and potential cost savings. Customers typically undertake a significant evaluation process before making a purchase, in some cases over twelve months. We spend substantial time and resources in our sales efforts without any assurance that our efforts will produce any sales. In addition, product purchases are frequently subject to budget constraints, multiple approvals, and unplanned administrative, processing and other delays. Our long sales cycle may cause our revenues and operating results to fluctuate significantly.

***Demand for our products depends on the rate that mobile operators expand and enhance their mobile networks in order to provide multimedia services.***

Our future success as a provider of network infrastructure products and services for mobile operators ultimately depends on the continued growth of the mobile communications industry and, in particular, the continued deployment and expansion of mobile multimedia services. Increased demand by mobile subscribers for voice communications and multimedia services delivered over mobile network systems will be necessary to justify capital expenditure commitments by mobile operators to invest in the improvement and expansion of their networks. Demand for multimedia services might not continue to increase if there is limited availability or market acceptance of mobile devices designed for such services, the multimedia content offered through mobile networks does not attract widespread interest or the quality of service available through mobile networks does not meet customer expectations. If long-term expectations for mobile multimedia services are not realized or do not support a sustainable business model, operators may not commit significant

capital expenditures to upgrade their networks to provide these services, the demand for our products and services will decrease, and we may not be able to sustain or increase our levels of revenues or profitability in the future.

***A significant portion of our future revenues depends on our ability to further penetrate the GSM/UMTS market and our failure to do so could significantly interfere with our future growth.***

The two principal radio access interfaces in use today for mobile communications are Code Division Multiple Access, or CDMA, and Global System for Mobile Communications/Universal Mobile Telecommunications System, or GSM/UMTS. To date, we have achieved our highest number of deployments in the CDMA market, which has transitioned faster to high-bandwidth networks. However, significantly more operators worldwide currently utilize GSM/UMTS than CDMA technologies. In order to continue our growth, we believe it is important that we continue to expand into the GSM/UMTS market. To date, we have established a relationship with a major GSM/UMTS operator, and we intend to devote significant sales and marketing resources to further penetrate the GSM/UMTS market. If GSM/UMTS operators do not transition or delay their transition to high-bandwidth networks, or if we are unable to establish relationships with additional GSM/UMTS operators, we may not be able to grow our business as expected and our results of operations will be adversely affected.

***We rely on OEMs, system integrators and distributors to sell some of our products, and our failure to develop and manage our distribution channels could adversely affect our business.***

For our sales to mobile operators, we rely in part on establishing and maintaining successful relationships with original equipment manufacturers, or OEMs, system integrators and distributors. A significant amount of our revenues is derived through these indirect sales. Accordingly, our revenues depend in large part on the effective performance of these distribution relationships. By relying on these indirect sales channels we may have less contact with the end users of our products, thereby potentially making it more difficult for us to establish brand awareness, ensure proper delivery and installation of our products, service ongoing customer requirements and respond to evolving customer needs. Developing relationships with qualified OEMs, system integrators and distributors and training them in our technology and product offerings requires significant time and resources. In order to develop and expand our distribution channels, we must continue to scale and improve our processes and procedures that support our OEM, system integrator and distributor relationships, including investment in systems and training. We have no minimum purchase commitments with any of our OEMs, system integrators or distributors, and our contracts with them do not prohibit them from offering products or services that compete with ours. Our competitors may be effective in providing incentives to existing and potential OEMs, system integrators and distributors to favor their products or to prevent or reduce sales of our products. Our OEMs, system integrators and distributors may choose not to offer our products exclusively or at all. Our failure to establish and maintain successful relationships with our OEMs, system integrators and distributors would likely materially adversely affect our business, operating results and financial condition.

***We terminated our OEM relationships with Nortel Networks. If we are unable to establish strong relationships with the mobile operators formerly serviced by Nortel Networks under our CDMA agreement, our business will be harmed.***

We had two OEM agreements with Nortel Networks, one relating to the CDMA market and one relating to the GSM/UMTS market. We terminated the agreement relating to the CDMA market effective March 2007 because we were no longer strategically aligned with Nortel Networks on future packet core products for mobile operators and to allow specific major mobile operators to



purchase directly from us. Under the terms of the agreement, Nortel Networks has a right to continue to purchase our CDMA products for delivery through December 2008. The termination of the CDMA agreement could disrupt our relationships with CDMA mobile operators formerly serviced by Nortel Networks. We have established direct relationships with some of the CDMA operators formerly serviced by Nortel Networks and we are currently seeking to establish additional direct sales relationships with other CDMA operators formerly serviced by Nortel Networks. We are also currently in discussions to establish a new reseller relationship with Nortel Networks to continue to service other CDMA operators. Our business may be harmed if we are unable to directly or indirectly continue selling our products to the other CDMA operators formerly serviced by Nortel Networks. In addition, our business may be adversely affected if we are unable to enter into a new CDMA reseller relationship with Nortel Networks.

We also terminated the agreement relating to the GSM/UMTS market effective December 2006 because there was a lack of strategic alignment on future packet core products for mobile operators between us and Nortel Networks and because there had been no sales of our products under that agreement. The growth of our business may be limited if we are unable to establish a direct or indirect sales relationship with other GSM/UMTS mobile operators.

***We have a significant accumulated deficit, and we may not be able to maintain profitability.***

Although we were profitable in 2005 and 2006 and for the six months ended June 30, 2007, we incurred net losses for the preceding three years. Our net losses were approximately \$25.8 million in 2002, \$26.4 million in 2003 and \$14.0 million in 2004. As a result of our net losses, we had an accumulated deficit of \$99.8 million as of June 30, 2007. We will need to generate significant revenues and control our operating expenses and other expenditures to maintain profitability. If we are unable to remain profitable, the market price of our common stock could decline.

***If network functions and services similar to those offered by our products are incorporated into existing or new mobile network infrastructure products, demand by mobile operators for our products may diminish.***

Mobile network infrastructures are continually evolving with changing industry standards and the introduction of new technologies and network elements. Network functions and services provided by our products located on the packet core network may be provided by different network elements within these networks. Other providers of mobile network infrastructure products may add network functions and services provided by our products to their existing products or offer new products with similar characteristics for different parts of the network infrastructure.

The inclusion of, or the announcement of an intent to include, functionality and services perceived to be similar to those offered by our products in competitor products within or outside the packet core network could have an adverse effect on our ability to market and sell our products. Furthermore, even if the network functions and services offered by our competitors are more limited than those provided by our products, a significant number of customers may elect to accept limited functionality or services in lieu of adding our products to their network. The adoption of these competitive products or different approaches to their network infrastructure by mobile operators could have an adverse effect on our business, operating results and financial condition.

***The applications of existing or future accounting standards could result in significant fluctuations in our operating results.***

We recognize our product software license revenue in accordance with AICPA Statement of Position, or SOP, 97-2, *Software Revenue Recognition*, and related amendments and interpretations

and SOP 98-9, *Modification of SOP 97-2, Software Revenue Recognition with Respect to Certain Transactions*. Under these accounting standards, even if we deliver products to, and collect cash from, a customer in a given fiscal period, we may be required to defer recognizing revenue from the sale of such product until a future period when all the conditions necessary for revenue recognition have been satisfied. Conditions that can cause delays in revenue recognition include software arrangements that have undelivered elements for which we have not yet established vendor specific objective evidence of fair value; requirements that we deliver services for significant enhancements or modifications to customize our software for a particular customer; or material customer acceptance criteria. Our customer contracts typically include one or more of these types of conditions. Therefore, we often must defer revenue recognition for a period of time after our products are delivered and billed to a customer, and such deferral may extend over one or more fiscal quarters. The period of deferral, if any, depends on the specific terms and conditions of each customer contract, and therefore it is difficult for us to predict with accuracy at the beginning of any fiscal period the amount of revenues that we will be able to recognize from anticipated customer shipments in that period. Moreover, any changes in interpretations and guidance as to SOP 97-2 could have a significant effect on our reported financial results.

***We may have difficulty acquiring new customers due to the high costs of switching mobile network infrastructure providers or equipment.***

Mobile network operators typically make substantial investments when deploying a mobile network infrastructure. Once a mobile network operator has deployed a mobile network infrastructure for a particular portion of their network, it is often difficult and costly to switch to another vendor's infrastructure. Unless we are able to persuasively demonstrate that our products offer performance, functionality or cost advantages that materially outweigh a customer's expense of switching from a competitor's product, it will be difficult for us to generate sales once that competitor's equipment has been deployed. Accordingly, if a customer has already deployed a competitor's product for their network infrastructure, it may be difficult for us to sell our products to that customer.

***Our ability to sell our products is highly dependent on the quality of our support and services offerings, and our failure to offer high quality support and services would have a material adverse effect on our sales and results of operations.***

Once our products are deployed within our customers' networks, our customers depend on our support organization to resolve issues relating to our products. A high level of support is critical for the successful marketing and sale of our products and future enhancements. If we, or our OEMs, system integrators or distributors, do not effectively assist our customers in deploying our products, help our customers quickly resolve post-deployment issues, and provide effective ongoing support, it would adversely affect our ability to sell our products to existing customers and could harm our reputation with potential customers. In addition, as we expand our operations internationally, our support organization will face additional challenges, including those associated with delivering support, training and documentation in languages other than English. As a result, our failure to maintain high quality support and services could have a material adverse effect on our business, operating results and financial condition.

***The mobile network infrastructure industry is, and likely will continue to be, characterized by rapid technological changes in networks and standards, which will require us to develop new products and product enhancements, and could render our existing products obsolete.***

Mobile operators have been aggressively upgrading their networks, and new industry standards for access technologies, such as third generation, or 3G, and more advanced fourth

generation, or 4G, technologies continue to evolve. Continuing technological changes in the mobile communications industry and in the mobile network infrastructure industry could undermine our competitive position or make our products obsolete, either generally or for particular types of services. Our future success will depend upon our ability to accurately predict and respond to new technology standards. We must develop and introduce a variety of new capabilities and enhancements to our existing product offerings, as well as introduce new product offerings, to address the changing standards and technological needs of the network infrastructure market. A failure to accurately predict and respond to evolving technologies, to introduce on a timely basis new products and enhancements in response to evolving technologies and standards, or to address changing needs in our current markets or expand into new markets may cause existing and potential customers to forego purchases of our products or purchase from our competitors. The introduction of new products embodying new technologies or the emergence of new industry standards could render our existing products uncompetitive from a pricing standpoint, obsolete or unmarketable.

***Our products are complex and may take longer to develop than anticipated and we may not recognize revenues from new products or product enhancements until after we have incurred significant development costs.***

Some of our products must be tailored to meet customer specifications. As a result, we often develop new features and enhancements to our products. These product enhancements often take substantial time to develop because of their complexity and because customer specifications sometimes change during the development cycle. We often do not recognize revenue from our new products or enhancements until we have incurred significant development costs, and our operating results will suffer if sales of new products or enhancements fail to meet our expectations.

***There is no assurance that our research and development investments will lead to successful new products or enhancements.***

We will continue to invest in research and development for the introduction of new products and enhancements to existing products designed to improve the capacity, data processing rates and features of our products and services. We must also continue to develop new features and functionality for our products based on specific customer requests and anticipated market needs. However, research and development in the mobile network infrastructure industry is complex, expensive and subject to uncertainty. In 2005 and 2006, our research and development expenses were \$18.1 million, or approximately 30% of our total revenues, and \$26.0 million, or approximately 28% of our total revenues, respectively; and for the six months ended June 30, 2007 these expenses were \$17.7 million, or approximately 30% of our total revenues. We believe that we must continue to dedicate a significant amount of resources to our research and development efforts to maintain our competitive position. If we continue to expend a significant amount of resources on research and development and our efforts do not lead to the successful introduction of products or product enhancements that are competitive in the marketplace, there could be a material adverse effect on our business, operating results, financial condition and market share. We may not be able to anticipate market needs and develop products and product enhancements that meet those needs, and any new products or product enhancements that we introduce may not achieve any significant degree of market acceptance.

***If our products do not interoperate with our customers' networks, installations will be delayed or cancelled, which would harm our business.***

Our products must interoperate with our customers' existing networks, which often have different specifications, utilize multiple protocol standards and products from multiple vendors, and

contain multiple generations of products that have been added over time. If we find errors in the existing software or defects in the hardware used in our customers' networks or problematic network configurations or settings, as we have in the past, we may have to modify our software or hardware so that our products will interoperate with our customers' networks. This could cause longer installation times for our products or order cancellations and could harm our relationship with existing and future customers, any of which would adversely affect our business, operating results and financial condition.

In addition, our customers may require that we demonstrate that our products interoperate with network elements offered by our competitors, and we may need our competitors' cooperation to conduct such testing and validation. Any unwillingness of our competitors to cooperate with us in performing these interoperability tests or our inability to demonstrate interoperability would likely have an adverse effect on our ability to market our products.

***Our products are highly technical and may contain undetected software or hardware errors, which could cause harm to our reputation and adversely affect our business.***

Our products are highly technical and complex. When deployed, they are critical to the mobile operator networks. Our products have contained and may contain undetected errors, defects or security vulnerabilities. Some errors in our products may only be discovered after a product has been installed and used by mobile operators. Any errors, defects or security vulnerabilities discovered in our products after commercial release could result in loss of revenues or delay in revenue recognition, loss of customers and increased service and warranty cost, any of which could adversely affect our business, operating results and financial condition. In addition, we could face claims for product liability, tort or breach of warranty, including claims relating to changes to our products made by our OEMs, system integrators or distributors. Our contracts with customers generally contain provisions relating to warranty disclaimers and liability limitations, which may be ineffective. Defending a lawsuit, regardless of its merit, is costly and may divert management's attention away from the business and adversely affect the market's perception of us and our products. In addition, if our business liability insurance coverage is inadequate or future coverage is unavailable on acceptable terms or at all, our operating results and financial condition could be adversely impacted.

***We are susceptible to shortages or price fluctuations in our supply chain. Any shortages or price fluctuations in components used in our products could delay shipment of our products, which could materially adversely affect our business.***

Shortages in components that we use in our products are possible and our ability to predict the availability of such components may be limited. Some of these components are available only from single or limited sources of supply. The process of qualifying alternate sources for components, if available at all, may be time consuming, difficult and costly. In addition, the lead times associated with certain components are lengthy and preclude rapid changes in quantity requirements and delivery schedules. Any growth in our business or the economy is likely to create greater pressures on us and our suppliers to project overall component demand accurately and to establish appropriate component inventory levels. In addition, increased demand by third parties for the components we use in our products may lead to decreased availability and higher prices for those components. We carry very little inventory of our products and product components, and we rely on our suppliers to deliver necessary components to our contract manufacturer in a timely manner based on forecasts we provide. We generally rely on purchase orders rather than long-term contracts with our suppliers. As a result, even if available, we may not be able to secure sufficient components at reasonable prices or of acceptable quality to build products in a timely manner,

which would seriously impact our ability to deliver products to our customers, and our business, operating results and financial condition would be adversely affected.

***We depend on a single contract manufacturer with whom we do not have a long-term supply contract, and changes to this relationship may result in delays or disruptions that could harm our business.***

We depend on Plexus Corp., an independent contract manufacturer, to manufacture and assemble our products. We rely on purchase orders with our contract manufacturer and do not have long-term supply arrangements in place. As a result, our contract manufacturer is not obligated to supply products to us for any specific period, quantity or price. Our orders may represent a relatively small percentage of the overall orders received by our contract manufacturer from its customers. As a result, fulfilling our orders may not be considered a priority by our contract manufacturer in the event the contract manufacturer is constrained in its ability to fulfill all of its customer obligations in a timely manner.

It is time consuming and costly to qualify and implement a contract manufacturer relationship. Therefore, if our contract manufacturer suffers an interruption in its business, or experiences delays, disruptions or quality control problems in its manufacturing operations, or we have to change or add additional contract manufacturers, our ability to ship products to our customers would be delayed and our business, operating results and financial condition would be adversely affected.

***If we fail to predict accurately our manufacturing requirements, we could incur additional costs or experience manufacturing delays that could harm our business.***

We provide demand forecasts to our contract manufacturer. If we overestimate our requirements, our contract manufacturer may assess charges or we may have liabilities for excess inventory, each of which could negatively affect our gross margins. Conversely, because lead times for required materials and components vary significantly and depend on factors such as the specific supplier, contract terms and the demand for each component at a given time, if we underestimate our requirements, our contract manufacturer may have inadequate materials and components required to produce our products, which could interrupt manufacturing of our products and result in delays in shipments and deferral or loss of revenues.

***If we fail to retain our key personnel, we may not be able to achieve our anticipated level of growth and our business could suffer.***

Our future depends, in part, on our ability to attract and retain key personnel, including the continued contributions of our executive officers and other key technical personnel, each of whom would be difficult to replace. In particular, Ashraf M. Dahod, our president, chief executive officer and chairman is critical to the management of our business and operations, as well as the development of our strategic direction. The loss of services of Mr. Dahod or other executive officers or key personnel or the inability to continue to attract qualified personnel could have a material adverse effect on our business. Mr. Dahod is not a party to an employment agreement with us and, therefore, may terminate his employment with us at any time, with no advance notice. The replacement of Mr. Dahod would involve significant time and expense and may significantly delay or prevent the achievement of our business objectives.

***Competition for our employees is intense, and we may not be able to attract and retain the highly skilled employees that we need to support our business.***

Competition for highly skilled technical personnel is extremely intense and we continue to face difficulty identifying and hiring qualified personnel in many areas of our business. In particular, we

face significant challenges hiring and retaining personnel in India for research and development activities because the market for such personnel is increasingly competitive. We may not be able to hire and retain such personnel at compensation levels consistent with our existing compensation and salary structure. Many of the companies with which we compete for hiring experienced employees have greater resources than we have and may be able to offer more attractive terms of employment. In addition, we invest significant time and expense in training our employees, which increases their value to competitors who may seek to recruit them. If we fail to retain our employees, we could incur significant expenses replacing employees and the quality of our products and services and our ability to provide such products and services could diminish, resulting in a material adverse affect on our business. Furthermore, in making employment decisions, particularly in high-technology industries, candidates often consider the value of the equity they are to receive in connection with their employment. Therefore, significant volatility in the price of our stock after this offering may adversely affect our ability to attract or retain personnel.

***Our international sales and operations subject us to additional risks that may adversely affect our operating results.***

Over the last several years, we derived a significant portion of our revenues from customers outside the United States, and we continue to expand our international operations. As of June 30, 2007, approximately 59% of our employees were located abroad, including 250 employees located in India. In addition, we have sales and technical support personnel in numerous countries worldwide. We expect to continue to add personnel in additional countries. Any continued expansion into international markets will require significant resources and management attention and will subject us to new regulatory, economic and political risks, and we cannot be sure that any further international expansion will be successful. Among the risks we believe are most likely to affect us with respect to our international operations are:

the difficulty of managing and staffing international offices and the increased travel, infrastructure and legal compliance costs associated with multiple international locations;

difficulties in enforcing contracts and collecting accounts receivable, and longer payment cycles, especially in emerging markets;

our ability to comply with differing technical standards and certification requirements outside North America;

unexpected changes in regulatory requirements;

reduced protection for intellectual property rights in some countries;

new and different sources of competition;

fluctuations in exchange rates; and

tariffs and trade barriers, import/export controls, and other regulatory or contractual limitations on our ability to sell or develop our products in certain foreign markets.

As we continue to expand our business globally, our success will depend, in large part, on our ability to anticipate and effectively manage these and other risks associated with our international operations. Our failure to manage any of these risks successfully could harm our international operations and reduce our international sales, adversely affecting our business, operating results and financial condition.

***We may need additional capital in the future, which may not be available to us on favorable terms, or at all, and may dilute your ownership of our common stock.***

We have historically relied on outside financing and cash from operations to fund our operations, capital expenditures and expansion. We may require additional capital from equity or debt financing in the future to:

take advantage of strategic opportunities including more rapid expansion of our business or the acquisition of complementary products, technologies or businesses; and

develop new products or enhancements to existing products.

We may not be able to secure timely additional financing on favorable terms, or at all. The terms of any additional financing may place limits on our financial and operating flexibility. If we raise additional funds through further issuances of equity, convertible debt securities or other securities convertible into equity, our existing stockholders could suffer significant dilution in their percentage ownership of our company, and any new securities we issue could have rights, preferences and privileges senior to those of holders of our common stock, including shares of common stock sold in this offering. If we are unable to obtain adequate financing or financing on terms satisfactory to us, if and when we require it, our ability to grow or support our business and to respond to business challenges could be significantly limited.

***We may engage in future acquisitions that could disrupt our business, cause dilution to our stockholders and harm our business, operating results or financial condition.***

While we currently have no acquisitions of other businesses pending or planned, we have, from time to time, evaluated acquisition opportunities and may pursue acquisition opportunities in the future. We have very little experience consummating acquisitions, and therefore our ability as an organization to make acquisitions is unproven. We may not be able to find suitable acquisition candidates and we may not be able to complete acquisitions on favorable terms, if at all. If we do complete acquisitions, we may not ultimately strengthen our competitive position or achieve our goals, or such acquisitions may be viewed negatively by customers, financial markets or investors. In addition, any acquisitions that we make could lead to difficulties in integrating personnel and operations from the acquired businesses and in retaining and motivating key personnel from these businesses. Acquisitions may disrupt our ongoing operations, divert management from day-to-day responsibilities, increase our expenses or adversely impact our business, operating results and financial condition. Future acquisitions may reduce our cash available for operations and other uses and could result in an increase in amortization expense related to identifiable assets acquired, potentially dilutive issuances of equity securities or the incurrence of debt, which could harm our business, operating results and financial condition.

***If we fail to manage future growth effectively, our business could be harmed.***

We have expanded our operations significantly since inception and anticipate that further significant expansion will be required. For example, our revenues increased from \$34.4 million in 2004 to \$94.4 million in 2006, and the number of our employees increased from 117 at the beginning of 2004 to 501 as of June 30, 2007. This growth has placed significant demands on our management, as well as our financial and operational resources. If we do not effectively manage our future growth, the efficiency of our operations and the quality of our products could suffer, which could adversely affect our business and operating results. To effectively manage this growth, we will need to continue to:

implement appropriate operational, financial and management controls, systems and procedures, including continued implementation of our enterprise-wide financial system;

expand our manufacturing capacity and scale of production;

expand our sales, marketing and distribution infrastructure and capabilities; and

provide adequate training and supervision to maintain high quality standards.

***We will incur significant increased costs as a result of operating as a public company, and our management will be required to devote substantial time to new compliance initiatives.***

As a public company, we have begun to incur significant legal, accounting and other expenses that we did not incur as a private company. In addition, the Sarbanes-Oxley Act of 2002, and rules subsequently implemented by the Securities and Exchange Commission and the Nasdaq Stock Market, impose additional requirements on public companies, including requiring changes in corporate governance practices. Our management and other personnel will need to devote a substantial amount of time to these compliance initiatives. Moreover, these rules and regulations will increase our legal and financial compliance costs and will make some activities more time-consuming and costly. For example, we expect these rules and regulations to make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced policy limits and coverage or incur substantial additional costs to maintain the same or similar coverage. These rules and regulations could also make it more difficult for us to attract and retain qualified persons to serve on our board of directors, our board committees or as executive officers.

In addition, the Sarbanes-Oxley Act requires, among other things, that we maintain effective internal control over financial reporting and disclosure controls and procedures. In particular, for the year ending December 31, 2008, we must perform system and process evaluation and testing of our internal control over financial reporting to allow management and our independent registered public accounting firm to report on the effectiveness of our internal control over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act. Our testing, or the subsequent testing by our independent registered public accounting firm, may reveal deficiencies in our internal control over financial reporting that are deemed to be material weaknesses. Our compliance with Section 404 will require that we incur substantial expense and expend significant management time on compliance-related issues. We will need to hire additional accounting and financial staff with appropriate public company experience and technical accounting knowledge. Moreover, if we are not able to comply with the requirements of Section 404 in a timely manner, or if we or our independent registered public accounting firm identify deficiencies in our internal control over financial reporting that are deemed to be material weaknesses, the market price of our stock could decline and we could be subject to sanctions or investigations by the Nasdaq Stock Market, the Securities and Exchange Commission or other regulatory authorities, which would require additional financial and management resources.

***We are subject to governmental export and import controls that could subject us to liability or impair our ability to compete in international markets.***

Our products are subject to United States export controls and may be exported outside the United States only with the required level of export license or through an export license exception, because we incorporate encryption technology into our products. In addition, various countries regulate the import of certain encryption technology and have enacted laws that could limit our ability to distribute our products or could limit our customers' ability to implement our products in those countries. Changes in our products or changes in export and import regulations may create delays in the introduction of our products in international markets, prevent our customers with international operations from deploying our products throughout their networks or, in some cases, prevent the export or import of our products to certain countries altogether. Any change in export or



import laws and regulations, shifts in approach to the enforcement or scope of existing laws and regulations, or change in the countries, persons or technologies targeted by such regulations, could result in decreased use of our products by, or in our decreased ability to export or sell our products to, existing or potential customers with international operations. Any decreased use of our products or limitation on our ability to export or sell our products would likely adversely affect our business, operating results and financial condition.

***Compliance with environmental matters and worker health and safety laws could be costly, and noncompliance with these laws could have a material adverse effect on our results of operations, expenses and financial condition.***

Some of our operations use substances regulated under various federal, state, local and international laws governing the environment and worker health and safety, including those governing the discharge of pollutants into the ground, air and water, the management and disposal of hazardous substances and wastes, and the cleanup of contaminated sites. Some of our products are subject to various federal, state, local and international laws governing chemical substances in electronic products. We could be subject to increased costs, fines, civil or criminal sanctions, third-party property damage or personal injury claims if we violate or become liable under environmental and/or worker health and safety laws.

In January 2003, the European Union, or EU, issued two directives relating to chemical substances in electronic products. The Waste Electrical and Electronic Equipment Directive, referred to as WEEE, requires producers of electrical goods to pay for specified collection, recycling, treatment and disposal of past and future covered products. The deadline for enacting and implementing the WEEE directive was August 13, 2004, although extensions were granted in some countries. Producers became financially responsible under WEEE related legislation beginning in August 2005. The other directive, the Restriction on the use of certain Hazardous Substances, referred to as RoHS, restricts lead and other hazardous substances in electronic equipment placed on the EU market after July 1, 2006. If we fail to comply with these directives, we may suffer a loss of revenues, be unable to sell our products in certain markets and countries, be subject to penalties and fines or suffer a competitive disadvantage. Similar legislation could be enacted in other jurisdictions, including in China, Japan or the United States, and the scope of new legislation with respect to currently unregulated substances is uncertain. Costs to comply with WEEE or RoHS related legislation or similar future legislation, if applicable, could include costs associated with modifying our products, recycling and other waste processing costs, legal and regulatory costs and insurance costs. We are currently in compliance with these directives; however, we have incurred significant costs related to compliance with current requirements. The costs to comply with current and future environmental and worker health and safety laws may have a material adverse effect on our results of operations, expenses and financial condition.

#### **Risks Related to our Intellectual Property**

***Our ability to compete and the success of our business could be jeopardized if we are unable to rely on our patent rights.***

Our success and ability to compete depends in part upon our ability to obtain protection in the United States and other countries for our products by establishing and maintaining intellectual property rights relating to or incorporated into our technology and products. We own a variety of patents and patent applications in the United States and corresponding patents and patent applications in foreign jurisdictions. However, we have not obtained patent protection in each market in which we plan to compete. To date, our patent portfolio has not prevented other companies from competing against us, and we do not know how successful we would be if we sought to enforce our patent rights against suspected infringers. Our pending and future patent

applications may not issue as patents or, if issued, may not issue in a form that will be advantageous to us. Even if issued, patents may be challenged, narrowed, invalidated or circumvented, which could limit our ability to stop competitors from marketing similar products or limit the length of term of patent protection we may have for our products. Changes in either patent laws or in interpretations of patent laws in the United States and other countries may diminish the value of our intellectual property or narrow the scope of our patent protection. Any circumstance or change that results in patent protection not being available for our products could adversely affect our business, financial condition and results of operations.

***If we are unable to protect the confidentiality of our unpatented proprietary information and know-how, the value of our technology and products could be adversely affected.***

In addition to patented technology, we rely upon unpatented proprietary technology, processes and know-how. We generally seek to protect this information in part by confidentiality agreements with our employees, consultants and third parties. These agreements may be breached, and we may not have adequate remedies for any such breach. In addition, our trade secrets may otherwise become known or be independently developed by competitors. If we are unable to protect the confidentiality of our proprietary information and know-how, the value of our technology and products could be adversely affected, which could in turn adversely affect our business, financial condition and results of operations.

***Claims by others that we infringe their proprietary technology could force us to incur significant costs.***

Third parties have asserted, and may assert in the future, claims that our products infringe patents or patent applications under which we do not hold licenses or other rights. Third parties may own or control these patents and patent applications in the United States and abroad. These third parties have brought, and could in the future bring, claims against us that would cause us to incur substantial expenses and, if successfully asserted against us, could cause us to pay substantial damages. Further, if a patent infringement suit were brought against us, we could be forced to stop or delay manufacturing or sales of the product that is the subject of the suit. In addition we could be forced to redesign the product that uses any allegedly infringing technology.

We are presently defending two patent infringement lawsuits brought by UTStarcom, Inc. In February 2005, UTStarcom filed a lawsuit asserting infringement of a patent in the United States District Court for the Northern District of California relating to a prepaid billing function we provided to one of our customers. This patent lawsuit by UTStarcom has been stayed pending a reissue proceeding of the patent asserted in the case. Such a reissue proceeding may take a year or longer to complete. After the reissue proceeding, the stay of the lawsuit likely will be lifted and the lawsuit may proceed. If this occurs, we will continue to defend ourselves in this litigation, which will require a significant investment of time and financial resources. A finding that we have infringed this patent may require us to pay damages based on our past sale of the prepaid billing function and, in addition, may force us to limit or cease development, manufacturing and sales of the prepaid billing function. This could adversely affect our business, financial condition and results of operations.

In May 2007, UTStarcom filed a lawsuit against us and a number of our employees and former employees in the United States District Court for the Northern District of Illinois alleging violations of the Illinois trade secrets act, infringement of five patents assigned to UTStarcom, intentional interference with UTStarcom's business relations and declarations of ownership relating to one of our patents and three of our patent applications. The complaint contains allegations, among others, that a number of former employees of a business unit UTStarcom acquired, who subsequently worked for us, took UTStarcom's trade secrets with them and improperly used those trade secrets

to develop, manufacture and market our 3G wireless products, and that such products incorporate UTStarcom confidential technical information, including UTStarcom's proprietary virtual private network and EV-DO features. UTStarcom further alleges that we have disclosed UTStarcom's trade secrets in one of our patents and three of our patent applications, and that these patent applications legally belong to UTStarcom based on the inventors' previous work at the business unit acquired by UTStarcom. In the lawsuit, UTStarcom seeks unspecified monetary damages, injunctive relief, declarations of ownership relating to the specified patent and patent applications owned by us, costs and attorneys fees. We will vigorously defend ourselves in this litigation and we have filed counterclaims. The defense of this lawsuit and the prosecution of our counterclaims will require significant investment of time and financial resources. A finding in UTStarcom's favor in this lawsuit may require us to pay substantial damages based on the past sales of our ST16 product, may force us to limit or cease development, manufacturing and sales of the ST16 and ST40, which are our only product platforms, may require that key employees be transferred to other positions or functions, or temporarily prohibited from working for us, and may result in the loss or assignment of ownership of a specified patent and three patent applications owned by us. This could adversely affect our business, financial condition and results of operations.

As a result of patent infringement claims, or in order to avoid potential claims, we may choose or be required to seek a license from the third party and be required to pay license fees or royalties or both. These licenses may not be available on acceptable terms, or at all. Even if we were able to obtain a license, the rights may be nonexclusive, which could result in our competitors gaining access to the same intellectual property. Ultimately, we could be forced to cease some aspect of our business operations if, as a result of actual or threatened patent infringement claims, we are unable to enter into licenses on acceptable terms. This could significantly and adversely affect our business, financial condition and results of operations.

In addition to infringement claims against us, we may become a party to other types of patent litigation and other proceedings, including interference proceedings declared by the United States Patent and Trademark Office and opposition proceedings in the European Patent Office, regarding intellectual property rights with respect to our products and technology. The cost to us of any patent litigation or other proceeding, even if resolved in our favor, could be substantial. Some of our competitors may be able to sustain the costs of such litigation or proceedings more effectively than we can because of their greater financial resources. Uncertainties resulting from the initiation and continuation of patent litigation or other proceedings could have a material adverse effect on our ability to compete in the marketplace. Patent litigation and other proceedings may also require significant commitments of time by our management.

***Our use of open source could impose limitations on our ability to commercialize our products.***

We incorporate open source software into our products. Although we monitor our use of open source software closely, the terms of many open source licenses to which we are subject have not been interpreted by United States or foreign courts, and there is a risk that such licenses could be construed in a manner that imposes unanticipated conditions or restrictions on our ability to commercialize our products. In such event, we could be required to seek licenses from third parties in order to continue offering our products, to re-engineer our products or to discontinue sales of our products, any of which could materially adversely affect our business.

***We rely on the availability of licenses for intellectual property from third parties, and if these licenses are not available to us on commercially reasonable terms, product sales and development may be delayed.***

We incorporate certain third-party technologies, including software programs, into our products and may need to utilize additional third-party technologies in the future. However, licenses

to relevant third-party technology may not continue to be available to us on commercially reasonable terms, or at all. Therefore, we could face delays in product releases until alternative technology can be identified, licensed or developed, and integrated into our current products. These delays, if they occur, could materially adversely affect our business.

**Risks Related to this Offering and Ownership of Our Common Stock**

*The market price of our common stock may be volatile, and you may not be able to resell shares of our common stock at or above the price you paid.*

The trading price of our common stock is likely to be volatile and could be subject to wide fluctuations in response to various factors. Some of the factors that may cause the market price of our common stock to fluctuate include:

fluctuations in our quarterly financial results or the quarterly financial results of companies perceived to be similar to us;

changes in estimates of our financial results or recommendations by securities analysts;

failure of any of our products to achieve or maintain market acceptance;

changes in market valuations of similar companies;

success of competitive products;

changes in our capital structure, such as future issuances of securities or the incurrence of additional debt;

announcements by us or our competitors of significant products, contracts, acquisitions or strategic alliances;

regulatory developments in the United States, foreign countries or both;

litigation involving our company, our general industry or both;

additions or departures of key personnel;

investors' general perception of us;

changes in general economic, industry and market conditions; and

changes in regulatory and other dynamics.

In addition, if the market for technology stocks or the stock market in general experiences a loss of investor confidence, the trading price of our common stock could decline for reasons unrelated to our business, financial condition or results of operations. If any of the foregoing occurs, it could cause our stock price to fall and may expose us to class action lawsuits that, even if unsuccessful, could be costly to defend and a distraction to management.

*Future sales of shares by existing stockholders could cause our stock price to decline.*

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If our stockholders sell substantial amounts of our common stock in the public market, the trading price of our common stock could decline. The perception in the public market that our stockholders might sell shares of common stock could also cause the market price of our common stock to decline. Based on shares outstanding as of June 30, 2007, upon completion of this offering, we will have outstanding \_\_\_\_\_ shares of common stock, assuming no exercise of the underwriters' option to purchase additional shares. On December 3, 2007, subject to extension or modification as discussed below, \_\_\_\_\_ shares of our common stock will become eligible for sale in the public market upon expiration of the 180-day contractual lock-up period pursuant to

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lock-up agreements entered into in connection with our initial public offering. Some of our stockholders (including some of those who entered into agreements in connection with our initial public offering) have entered into lock-up agreements in connection with this offering. After all of the agreements entered into in connection with this offering expire (which will occur 90 days after the date of the final prospectus for this offering, subject to extension or modification as discussed below), an additional \_\_\_\_\_ shares of our common stock will be eligible for sale in the public market.

The 180-day contractual lock-up period relating to our initial public offering and the 90-day contractual lock-up period relating to this offering may be extended or reduced as described below. If during the last 17 days of the relevant contractual lock-up period we issue an earnings release or announce material news or a material event, the contractual lock-up period will continue to apply until the expiration of the 18-day period beginning on the issuance of the earnings release or the announcement of the material news or material event. With respect to the 180-day contractual lock-up period entered into in connection with our initial public offering, if we announce, prior to the expiration of the contractual lock-up period, that we will release earnings results during the 15-day period following the last day of the contractual lock-up period, the lock-up restrictions on resale will be automatically extended until the expiration of the 18-day period beginning on the date of the release of the earnings results. With respect to the 90-day contractual lock-up period entered into in connection with this offering, prior to the expiration of the contractual lock-up period, if we announce that we will release earnings results during the 15-day period following the last day of the contractual lock-up period, the lock-up restrictions on resale will expire on the day 18 days prior to the scheduled earnings release so long as we issue a press release and accompanying current report on Form 8-K announcing the early release date at least three days before the early release date. If we do not publicly announce the early release date by such time, the lock-up restrictions will instead continue to apply until the expiration of the 18-day period beginning on the issuance of the earnings release. Additionally, in any event the lock-up period entered into in connection with this offering will continue through and including January 15, 2008.

In addition, 4,980,573 shares of common stock subject to a 180-day contractual lock-up with us relating to our initial public offering will become eligible for sale in the public market on December 3, 2007. We may release these shares from these restrictions at our discretion without the prior written consent of either Goldman, Sachs & Co. or Lehman Brothers Inc.

In addition, as of June 30, 2007, we had options to purchase a total of 8,446,958 shares of our common stock outstanding under our equity incentive plans, of which 2,319,237 were vested. We have filed a Form S-8 registration statement to register all of the shares issuable under our equity incentive plans. The market price of shares of our common stock may drop significantly when the restrictions on resale by our existing stockholders lapse and our stockholders are able to sell shares of our common stock into the market. A decline in the price of shares of our common stock may cause you to lose part or all of your investment in our shares of common stock.

Some of our existing stockholders have demand and incidental registration rights to require us to register with the Securities and Exchange Commission up to 45,064,641 shares of our common stock. If we register these shares of common stock, the stockholders would be able to sell those shares freely in the public market.

See the section titled "Shares Eligible for Future Sale" for a discussion of the lock-up agreements and other transfer restrictions.

***We do not currently intend to pay dividends on our common stock and, consequently, your ability to achieve a return on your investment will depend on appreciation in the price of our common stock.***

We do not expect to pay cash dividends on our common stock, including the common stock issued in this offering. Any future dividend payments are within the absolute discretion of our board of directors and will depend on, among other things, our results of operations, working capital requirements, capital expenditure requirements, financial condition, contractual restrictions, business opportunities, anticipated cash needs, provisions of applicable law and other factors that our board of directors may deem relevant. We may not generate sufficient cash from operations in the future to pay dividends on our common stock. See "Dividend Policy."

***Insiders will continue to have substantial control over us after this offering and will be able to influence corporate matters.***

Upon completion of this offering, our directors and executive officers and their affiliates will beneficially own, in the aggregate, approximately % of our outstanding common stock, assuming no exercise of the underwriters' option to purchase additional shares. As a result, these stockholders will be able to exercise significant influence over all matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions, such as a merger or other sale of our company or its assets. This concentration of ownership could limit your ability to influence corporate matters and may have the effect of delaying or preventing a third-party from acquiring control over us. For information regarding the ownership of our outstanding stock by our executive officers and directors and their affiliates, see the section titled "Principal and Selling Stockholders."

***If securities or industry analysts do not publish research or publish inaccurate or unfavorable research about our business, our stock price and trading volume could decline.***

The trading market for our common stock will depend in part on the research and reports that securities or industry analysts publish about us or our business. We do not currently have and may never obtain research coverage by securities and industry analysts. If no securities or industry analysts commence coverage of our company, the trading price for our stock would be negatively impacted. In the event we obtain securities or industry analyst coverage, if one or more of the analysts who covers us downgrades our stock or publishes inaccurate or unfavorable research about our business, our stock price would likely decline. If one or more of these analysts ceases coverage of our company or fails to publish reports on us regularly, demand for our stock could decrease, which could cause our stock price and trading volume to decline.

***Anti-takeover provisions in our charter documents and Delaware law could discourage, delay or prevent a change in control of our company and may affect the trading price of our common stock.***

We are a Delaware corporation and the anti-takeover provisions of the Delaware General Corporation Law may discourage, delay or prevent a change in control by prohibiting us from engaging in a business combination with an interested stockholder for a period of three years after the person becomes an interested stockholder, even if a change in control would be beneficial to our existing stockholders. In addition, our restated certificate of incorporation and amended and restated bylaws may discourage, delay or prevent a change in our management or control over us

that stockholders may consider favorable. Our restated certificate of incorporation and amended and restated bylaws:

authorize the issuance of "blank check" preferred stock that could be issued by our board of directors to thwart a takeover attempt;

establish a classified board of directors, as a result of which the successors to the directors whose terms have expired will be elected to serve from the time of election and qualification until the third annual meeting following their election;

require that directors only be removed from office for cause and only upon a supermajority stockholder vote;

provide that vacancies on the board of directors, including newly created directorships, may be filled only by a majority vote of directors then in office;

limit who may call special meetings of stockholders;

prohibit stockholder action by written consent, requiring all actions to be taken at a meeting of the stockholders; and

require supermajority stockholder voting to effect certain amendments to our restated certificate of incorporation and amended and restated bylaws.

For more information regarding these and other provisions, see the section titled "Description of Capital Stock Anti-Takeover Effects of Our Charter and Bylaws and Delaware Law."

***Our management will have broad discretion over the use of the proceeds we receive in this offering and might not apply the proceeds in ways that increase the value of your investment.***

Our management will have broad discretion to use the net proceeds from this offering, and you will be relying on the judgment of our management regarding the application of these proceeds. Our management might not apply the net proceeds of this offering in ways that increase the value of your investment. We expect to use the net proceeds from this offering for general corporate purposes, including working capital and capital expenditures, which may in the future include investments in, or acquisitions of, complementary businesses, services or technologies. We have not allocated these net proceeds for any specific purposes. You will not have the opportunity to influence our decisions on how to use the net proceeds from this offering.



**SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS**

This prospectus contains forward-looking statements that involve substantial risks and uncertainties. All statements, other than statements of historical facts, included in this prospectus regarding our strategy, future operations, future financial position, future revenues, projected costs, prospects, plans, objectives of management and expected market growth are forward-looking statements. The words "anticipate," "believe," "estimate," "expect," "intend," "may," "plan," "predict," "project," "will," "would" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. These forward-looking statements include, among other things, statements about:

our ability to attract and retain customers;

our financial performance;

our research and development activities;

the advantages of our products and services as compared to those of others;

our ability to establish and maintain intellectual property rights;

our ability to retain and hire necessary employees and appropriately staff our operations; and

our estimates regarding capital requirements and needs for additional financing.

We may not actually achieve the plans, intentions or expectations disclosed in our forward-looking statements, and you should not place undue reliance on our forward-looking statements. Actual results or events could differ materially from the plans, intentions and expectations disclosed in the forward-looking statements we make. We have included important factors in the cautionary statements included in this prospectus, particularly in the "Risk Factors" section, that could cause actual results or events to differ materially from the forward-looking statements that we make. Our forward-looking statements do not reflect the potential impact of any future acquisitions, mergers, dispositions, joint ventures or investments we may make.

You should read this prospectus and the documents that we have filed as exhibits to the registration statement, of which this prospectus is a part, completely and with the understanding that our actual future results may be materially different from what we expect. We do not assume any obligation to update any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

### USE OF PROCEEDS

We estimate that we will receive net proceeds from this offering of approximately \$      million, based on an assumed public offering price of \$      per share, which is the last reported sale price of our common stock on October      , 2007, after deducting the estimated underwriting discounts and commissions and offering expenses payable by us. If the underwriters exercise their option to purchase additional shares, we estimate that we will receive an additional \$      million in net proceeds. At an assumed public offering price of \$      per share, the selling stockholders will receive \$      million from their sale of our common stock in this offering, after deducting the estimated underwriting discount. We will not receive any proceeds from the sale of shares of common stock by the selling stockholders. Our president and chief executive officer is selling shares of common stock in this offering. See "Principal and Selling Stockholders."

A \$1.00 increase (decrease) in the assumed public offering price of \$      per share would increase (decrease) the net proceeds to us from this offering by \$      million and increase (decrease) the net proceeds to the selling stockholders from this offering by \$      million, assuming the number of shares offered by us and the selling stockholders, as set forth on the cover of this prospectus, remains the same.

We intend to use the net proceeds from this offering for working capital and other general corporate purposes, which may include financing our growth, developing new products, and funding capital expenditures, acquisitions and investments. In addition, the other principal purposes for this offering are to:

facilitate our future access to the public capital markets;

increase our visibility in our markets;

provide liquidity for our existing stockholders;

improve the effectiveness of our equity compensation plans in attracting and retaining key employees; and

enhance our ability to acquire other businesses, products or technologies.

We have not yet determined with any certainty the manner in which we will allocate these net proceeds. Management will retain broad discretion in the allocation and use of the net proceeds from this offering. The amounts and timing of these expenditures will vary depending on a number of factors, including the amount of cash generated by our operations, competitive and technological developments, and the rate of growth, if any, of our business. For example, if we were to expand our operations more rapidly than anticipated by our current plans, a greater portion of the proceeds would likely be used for the construction and expansion of facilities, working capital and other capital expenditures. Alternatively, if we were to engage in an acquisition that contained a significant cash component, some or all of the proceeds might be used for that purpose.

Although we may use a portion of the proceeds for the acquisition of, or investment in, companies, technologies, products or assets that complement our business, we have no present understandings, commitments or agreements to enter into any acquisitions or make any investments. We cannot assure you that we will make any acquisitions or investments in the future.

Pending specific utilization of the net proceeds as described above, we intend to invest the net proceeds of the offering in short-term investment grade and U.S. government securities.

**PRICE RANGE OF COMMON STOCK**

Our common stock commenced trading on the Nasdaq Global Market under the symbol "STAR" on June 6, 2007. The following table sets forth, for the periods indicated, the high and low reported sales prices of our common stock as reported on the Nasdaq Global Market:

	<u>High</u>	<u>Low</u>
<b>2007</b>		
Second quarter (from June 6, 2007)	\$ 17.00	\$ 13.29
Third quarter	\$ 24.11	\$ 13.55
Fourth quarter (through October 12, 2007)	\$ 29.00	\$ 21.42

As of October 12, 2007, there were 313 holders of record of our common stock. The last reported sale price of the common stock on October 12, 2007 was \$27.42 per share.

**DIVIDEND POLICY**

We have never paid or declared any cash dividends on our common stock. We currently intend to retain earnings, if any, to finance the growth and development of our business, and we do not expect to pay any cash dividends on our common stock in the foreseeable future. Payment of future dividends, if any, will be at the discretion of the board of directors and will depend on our financial condition, results of operations, capital requirements, restrictions contained in current or future financing instruments, and other factors the board deems relevant.

**CAPITALIZATION**

The following table sets forth our capitalization as of June 30, 2007:

on an actual basis; and

on an as adjusted basis to reflect our issuance and sale of \_\_\_\_\_ shares of common stock in this offering at an assumed public offering price of \$ \_\_\_\_\_ per share, which is the last reported sale price of our common stock on October \_\_\_\_\_, 2007, after deducting the estimated underwriting discount and offering expenses payable by us.

You should read this table together with our financial statements and the related notes appearing at the end of this prospectus and the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section of this prospectus.

<b>As of June 30, 2007</b>	
<b>Actual</b>	<b>As Adjusted</b>
<b>(unaudited)</b>	
<b>(in thousands, except share and per share data)</b>	

<b>Stockholders' equity:</b>		
Preferred stock, \$0.001 par value:		
5,000,000 shares authorized and no shares issued or outstanding, actual or as adjusted		
Common stock, \$0.001 par value:		
250,000,000 shares authorized, 63,969,186 shares issued and outstanding, actual and _____ shares issued and outstanding, as adjusted(1)		
	\$	64
Additional paid-in capital		252,220
Accumulated other comprehensive loss		(9)
Accumulated deficit		(99,831)
		(9)
		(99,831)
<hr/>		
<b>Total stockholders' equity</b>	<b>\$</b>	<b>152,444</b>
		<b>\$</b>

(1) For accounting purposes only, the number of issued and outstanding shares does not include 555,483 shares of restricted stock. These shares are subject to repurchase by us until such shares are vested. See Note 11 to our consolidated financial statements for more information.

A \$1.00 increase (decrease) in the assumed public offering price of \$ \_\_\_\_\_ per share would increase (decrease) each of additional paid-in capital and total stockholders' equity in the as adjusted column by \$ \_\_\_\_\_ million, assuming the number of shares offered by us, as set forth on the cover of this prospectus, remains the same and after deducting the estimated underwriting discount and offering expenses payable by us.

The table above is based on 64,524,669 shares of our common stock outstanding as of June 30, 2007 and does not include:

8,446,958 shares of common stock issuable upon the exercise of stock options outstanding as of June 30, 2007 at a weighted average exercise price of \$3.43 per share, of which options to purchase 2,319,237 shares were exercisable as of June 30, 2007 at a weighted average exercise price of \$1.14 per share; and

3,481,108 shares of common stock available for future issuance under our equity compensation plans as of June 30, 2007.



## SELECTED CONSOLIDATED FINANCIAL DATA

The following tables summarize our consolidated financial data for the periods presented. You should read the following selected consolidated financial data in conjunction with our financial statements and the related notes appearing at the end of this prospectus and the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section of this prospectus.

We have derived the statement of operations data for the years ended December 31, 2004, 2005 and 2006 and the balance sheet data as of December 31, 2005 and 2006 from our audited consolidated financial statements, which are included in this prospectus. We have derived the statement of operations data for the year ended December 31, 2003 and the balance sheet data as of December 31, 2003 and 2004 from our audited consolidated financial statements, which are not included in this prospectus. We have derived the statement of operations data for the year ended December 31, 2002 and the balance sheet data as of December 31, 2002 from our unaudited consolidated financial statements, which are not included in this prospectus. We derived the consolidated financial data for the six months ended June 30, 2006 and 2007 and as of June 30, 2007 from our unaudited consolidated financial statements, which are included elsewhere in this prospectus. In the opinion of management, the unaudited consolidated financial statements have been prepared on the same basis as our audited financial statements and include all adjustments, consisting of normal recurring adjustments and accruals, necessary for the fair statement of the financial information set forth in those statements. Our historical results for any prior period are not necessarily indicative of results to be expected for any future period.

	Year Ended December 31,					Six Months Ended June 30,	
	2002	2003	2004	2005	2006	2006	2007
	(unaudited)					(unaudited)	
	(in thousands, except per share data)						
<b>Statement of Operations Data:</b>							
Revenues	\$	\$ 182	\$ 34,395	\$ 59,660	\$ 94,350	\$ 34,823	\$ 58,496
Cost of revenues		410	1,109	13,445	13,643	27,726	7,998
Gross profit		(410)	(927)	20,950	46,017	66,624	26,825
Operating expenses:							
Research and development		18,500	14,748	13,303	18,107	25,980	9,705
Sales and marketing		4,417	8,289	18,445	19,785	30,311	12,745
General and administrative		1,954	2,470	3,185	7,352	8,515	3,499
Total operating expenses		24,871	25,507	34,933	45,244	64,806	25,949
Income (loss) from operations		(25,281)	(26,434)	(13,983)	773	1,818	876
Other income (expense), net		(484)	(8)	95	644	2,237	848
Income (loss) before income tax expense		(25,765)	(26,442)	(13,888)	1,417	4,055	1,724
Income tax expense				(160)	(513)	(413)	(143)
Net income (loss)	\$	(25,765)	\$ (26,442)	\$ (14,048)	\$ 904	\$ 3,642	\$ 1,581
Net income (loss) per share applicable to common stockholders:							
Basic	\$	(8.84)	\$ (6.39)	\$ (3.28)	\$ (0.97)	\$ (0.62)	\$ (0.35)
Diluted	\$	(8.84)	\$ (6.39)	\$ (3.28)	\$ (0.97)	\$ (0.62)	\$ (0.35)

Weighted average shares used in computing net income (loss) per share applicable to common shareholders:

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	Year Ended December 31,					Six Months Ended June 30,	
Basic	3,223	4,825	6,197	6,642	7,026	6,838	15,864
Diluted	3,223	4,825	6,197	6,642	7,026	6,838	21,769

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As of December 31,

	2002	2003	2004	2005	2006	As of June 30, 2007
	(unaudited)					(unaudited)

(in thousands)

**Balance Sheet Data:**

Cash, cash equivalents and short-term investments	\$ 13,653	\$ 2,036	\$ 20,819	\$ 37,489	\$ 60,154	\$ 157,165
Working capital	11,090	1,889	10,002	41,490	19,305	139,441
Total assets	21,412	17,262	63,892	84,353	104,267	214,709
Indebtedness			197	33		
Redeemable convertible preferred stock	56,786	64,153	97,043	122,282	130,270	
Total stockholders' equity (deficit)	(46,434)	(77,091)	(97,092)	(103,202)	(105,511)	152,444

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**MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*You should read the following discussion and analysis of our financial condition and results of operations together with our financial statements and the related notes and other financial information included elsewhere in this prospectus. Some of the information contained in this discussion and analysis or set forth elsewhere in this prospectus, including information with respect to our plans and strategy for our business and related financing, includes forward-looking statements that involve risks and uncertainties. You should review the "Risk Factors" section of this prospectus for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in the following discussion and analysis.*

**Overview**

Starent Networks is a leading provider of infrastructure hardware and software products and services that enable mobile operators to deliver multimedia services to their subscribers. We have created hardware and software products that provide network functions and services, including access from a wide range of radio networks to the operator's packet core network. Our products and services also provide management of subscriber sessions moving between networks and application of billing and other session policies. Our products and services provide high performance and system intelligence by combining significant computing power, memory and traffic handling capabilities with a flexible, high availability operating system and other proprietary software. Our products integrate multiple network functions and services needed for the delivery of advanced multimedia services, such as video, Internet access, voice-over-IP, e-mail, mobile TV, photo sharing and gaming.

Our products consist of both hardware and software and can be configured to meet a number of customer needs. A typical purchase consists of our ST16, the Starent operating system and other proprietary software, and our Starent Web EMS management system. In April 2007 we announced the ST40, which provides improved performance, capacity and functionality and became generally available in the third quarter of 2007. A customer typically purchases our products with specific capacity and functionality, and may upgrade their system over time through a combination of software and hardware purchases. We sell our products and services to mobile operators around the world both directly and indirectly through our relationships with OEMs, system integrators and distributors. Since the first commercial deployment of our products in 2003, our products have been deployed by over 60 mobile operators in 25 countries. To date, we have had the greatest success in the CDMA market, but have begun to focus on the GSM/UMTS market. We believe penetration of the GSM/UMTS market is important to our future growth since mobile operators utilizing this technology provide services to approximately 80% of the worldwide mobile voice and data services subscribers.

We received our first purchase order from one of the world's largest GSM operators in June 2006 and have expanded our relationship with this customer during 2007. We plan to continue to expand our current relationships, and to develop new relationships, with GSM/UMTS mobile operators. Many of these operators are located outside of the United States and developing these relationships requires significant time and various interoperability and verification testing. Therefore, these activities will require continued substantial investment in our sales and marketing personnel. We expect to begin recording revenues from shipments of the ST40 in the fourth quarter of 2007. Our revenue growth will depend on the acceptance of our ST40, the continued acceptance of our ST16 and applications and services related to our platforms, further penetration of the GSM/UMTS market, increased adoption of mobile multimedia services and continued migration to packet-based networks by mobile operators.

Since our inception in August 2000, we have raised an aggregate of approximately \$227 million through a series of equity financings, a portion of which we invested in expanding our research and development organization, building our sales force and initiating our marketing and administration operations. We have incurred significant losses to date, and as of June 30, 2007 we had an accumulated deficit of \$99.8 million. We became profitable in 2005 and were also profitable in 2006 and in the first half of 2007. Our profitability will be affected by additional expenses that we incur to expand sales, marketing, research and development and general and administrative capabilities in order to grow our business.

We maintain our corporate headquarters in Tewksbury, Massachusetts, and also have sales and development offices in various locations worldwide. We conduct our research and development activities at two locations in India and two locations in the United States. As of June 30, 2007, we had 501 employees worldwide. Our revenues for 2006 were \$94.4 million and \$58.5 million for the six months ended June 30, 2007, our net income for 2006 was \$3.6 million and \$5.7 million for the six months ended June 30, 2007 and we had \$63.7 million and \$40.9 million of deferred revenue as of December 31, 2006 and June 30, 2007, respectively.

### **Revenues**

Our revenues consist of both product revenues and services revenues. We derive product revenues from the sale of our hardware products and the licensing of our software. Services revenues are generated from:

maintenance and technical support associated with our software;

hardware repair and maintenance services; and

implementation, training and professional services.

We recognize revenue in accordance with Statement of Position, or SOP 97-2, *Software Revenue Recognition* and SOP 98-9, *Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions*. Accordingly, revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable and collection is probable.

Mobile operators can purchase our products and license our software in various configurations, depending on their requirements for capacity, features and protocols. Typically, a mobile operator purchases a small amount of equipment for testing and trial purposes and, once testing is complete, purchases the necessary products to meet their initial capacity and feature requirements. As their capacity requirements increase, operators may purchase additional hardware or license additional software. The level of our sales is significantly influenced by the extent to which mobile operators make capital investments to enhance and expand their networks to provide multimedia services. Mobile operators' capital investments will be influenced by the demand for multimedia services by their customers.

We offer our products and services through our direct sales force to mobile operators and indirectly through relationships with OEMs, system integrators and distributors. The OEMs, system integrators and distributors generally purchase our products after they have received a purchase order from their customers and do not maintain an inventory of our products in anticipation of sales to their customers.

In 2004, we entered into OEM agreements with Nortel Networks relating to the CDMA market and the GSM/UMTS market. Sales to Nortel Networks, all of which were made under the CDMA agreement, accounted for more than 40% of our revenues in 2006. In December 2006, we terminated both OEM agreements. Under the terms of the CDMA agreement, Nortel Networks has a

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right to continue to purchase our CDMA products for delivery through December 2008. Although the termination of the CDMA agreement could disrupt our relationships with CDMA mobile operators formerly serviced by Nortel Networks, we have established and continue seeking to establish additional direct sales relationships with other CDMA operators formerly serviced by Nortel Networks. In addition, we are currently in discussions to establish a new reseller relationship with Nortel Networks. As a result, we do not believe that the termination of the Nortel Networks OEM agreements will significantly impact our revenues.

We believe our revenues will vary significantly from period-to-period as a result of the following:

*Fluctuations in the timing of customer orders.* Mobile operators require significant lead times to incorporate changes and enhancements into their networks to ensure the various network components are interoperable. These lead times and interoperability testing requirements result in an extended sales cycle and can lead to uneven purchasing patterns. In addition, our reliance on a relatively small number of customers placing relatively few but large orders contributes to the variability of our revenues.

*The timing of revenue recognition in relation to the shipment of products.* Our products contain software which is not incidental to our products. Therefore, we recognize revenue pursuant to the requirements of SOP 97-2. Due to the requirements of this statement and its related interpretations, certain features of our customer arrangements, such as customer acceptance terms in many of our customer contracts and the need for us to establish fair values of our products and services based on facts specific to our operations, we often defer recognition of revenue for a significant period of time after shipment.

The variability of our revenues directly impacts our operating performance in any particular period since a significant portion of our operating costs, such as prototypes and related equipment and sales commissions, are either fixed in the short-term or may not vary proportionately with recorded revenues.

### ***Cost of Revenues***

Cost of revenues consists of costs of products sold and services provided. Cost of products consists primarily of payments to a third party manufacturer for purchased materials and services and internal costs, such as salaries and benefits related to personnel, provision for inventory obsolescence and related overhead. The use of an outsourced manufacturer enables us to conserve working capital, adjust to fluctuations in demand and provide for timely delivery to our customers. Cost of services consists primarily of salaries and benefits related to professional services and technical support personnel, product repair costs, depreciation and related overhead.

### ***Gross Profit***

Our gross profit has been, and will be, affected by many factors, including the demand for our products and services, the average selling price of our products, which in turn depends on the mix of product configurations sold, new product introductions, the region of the world in which our customers are located and the volume and costs of manufacturing our hardware products.

### ***Operating Expenses***

Our operating expenses consist primarily of personal costs including salaries, commissions bonuses, share-based compensation and related benefits and taxes; prototype costs related to the design and development of new products and enhancement of existing products; and consulting, travel and depreciation expenses. The expenses are classified into the following categories for

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reporting purposes: research and development, sales and marketing and general and administrative. Following is a brief description of the key types of expenses in each of the categories.

Research and development expense consists primarily of personnel costs, prototype costs, consulting services and depreciation. Research and development activities, including hardware and software development and quality assurance testing, primarily occur at two locations in the United States and two locations in India.

Sales and marketing expense consists primarily of personnel costs, travel and marketing programs such as trade shows. Commissions are a significant component of our sales personnel costs and are recorded as expense when earned which is not necessarily directly proportionate to the amount of revenues recorded since commissions are generally earned at the time we accept customer orders and revenue is recorded once all revenue recognition criteria have been met.

General and administrative expense consists primarily of personnel costs related to our executive, finance, human resource and information technology organizations, professional fees, insurance and other related overhead.

### ***Other Income (Expense)***

Other income (expense) primarily consists of interest income earned on cash and short-term investments. We have historically invested our cash in money market funds and other short-term, high-grade investments.

Other income (expense) also includes gains (losses) from foreign currency transactions of our foreign subsidiaries. The functional currency of our foreign operations is the U.S. dollar. Accordingly, all assets and liabilities, except certain long-term assets, of these international subsidiaries are remeasured into U.S. dollars using the exchange rates in effect at the balance sheet date. Revenues and expenses of these international subsidiaries are generally remeasured into U.S. dollars at the average rates in effect during the year.

### ***Accretion of Redeemable Convertible Preferred Stock***

Accretion of redeemable convertible preferred stock includes accrued dividends on each series of our preferred stock.

### **Application of Critical Accounting Policies and Use of Estimates**

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements and related disclosures require us to make estimates, assumptions and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. We evaluate our estimates and assumptions on an ongoing basis. Our actual results may differ significantly from these estimates under different assumptions or conditions.

We believe that of our significant accounting policies, which are described in note 3 to the financial statements included in this prospectus, the following accounting policies involve a greater degree of judgment and complexity. Accordingly, we believe these are the most critical to fully understand and evaluate our financial condition and results of operations.

### ***Revenue Recognition***

Generally, our revenues are generated through fulfillment of contractual arrangements that contain multiple elements, including equipment with embedded software and services, such as installation, training, consulting and maintenance and support, known as M&S. We recognize revenue in accordance with Statement of Position, or SOP 97-2, *Software Revenue Recognition* and SOP 98-9, *Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions*. Accordingly, revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable and collection is probable. Certain of these requirements, most notably the customer acceptance terms generally included in our contracts and our need to establish fair values of our products and services based on facts specific to our operations, are critical to the timing and extent of our revenue recognition. As a result of these factors, a significant majority of our contractual arrangements result in the deferral of revenue and the time period for deferral may be significant. In addition, in certain circumstances, pricing considerations must be assessed to determine whether the price is fixed or determinable.

Product revenues consist of revenues from sales of our hardware and licensing of our software. Product sales generally include a perpetual license to our software. Product revenues are generally recognized at shipment or upon customer acceptance, assuming all other revenue recognition criteria are met. Substantially all of our products have been sold in conjunction with product support services, which consist of software updates and product support. Software updates provide customers with rights to unspecified software product upgrades and to maintenance releases and patches released during the term of the support period. Revenues for support services are recognized on a straight-line basis over the service contract term, which is generally 12 to 15 months.

Pursuant to SOP 97-2 revenue is allocated to deliverables based on vendor specific objective evidence of fair value, known as VSOE, when VSOE exists. Generally, all revenues for an arrangement are deferred when VSOE does not exist for any undelivered element. However, revenue is recognized ratably over the contractual M&S period when M&S is the only undelivered element. If VSOE exists for the undelivered elements, but not the delivered elements, revenue is recognized under the residual method set forth in SOP 98-9, which provides that revenue is recognized based on the difference between the total arrangement fee and the VSOE of the undelivered elements. Revenue for the undelivered elements is then recorded as those elements are delivered. When we defer revenue in an arrangement, the related product costs are also deferred, subject to their realizability, and recognized over the same period as the related revenue.

The determination of VSOE is highly judgmental and is a key factor in determining whether revenue may be recognized or must be deferred and the extent to which it may be recognized once the various elements of an arrangement are delivered. We assess VSOE based on previous sales of products and services, the type and size of customer, renewal rates in contracts and the geographic location of the customer. We monitor VSOE on an ongoing basis. As noted above, most of our arrangements include multiple elements, some of which are delivered in or over future periods. Therefore a change in our assessment of, or our inability to establish, VSOE for products or services may result in significant variation in our revenues and operating results.

In arrangements where cash consideration is paid to a customer, the payments are recorded in accordance with EITF 01-9, *Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)*, which generally requires the consideration be recorded as a reduction of revenues.

*Share-Based Compensation*

Prior to January 1, 2006, we accounted for our stock-based awards to employees using the intrinsic value method prescribed in Accounting Principles Board, or APB, Opinion 25, *Accounting for Stock Issued to Employees*, and related interpretations. Under the intrinsic value method, compensation expense is measured on the date of the grant as the difference between the deemed fair value of our common stock and the exercise or purchase price multiplied by the number of stock options or restricted stock awards granted. In addition, through December 31, 2005, we accounted for share-based compensation expense for non-employees using the fair value method prescribed by SFAS 123, applying the Black-Scholes option-pricing model, and recorded the fair value, for financial reporting purposes, of non-employee stock options as an expense over either the vesting term of the option or the service period.

In December 2004, the Financial Accounting Standards Board, or FASB, issued SFAS 123R, *Share-Based Payment*, which requires companies to expense the fair value of employee stock options and other forms of share-based compensation. We adopted SFAS 123R effective January 1, 2006. SFAS 123R requires nonpublic companies that used the minimum value method in SFAS 123 for either recognition or pro forma disclosures to apply SFAS 123R using the prospective-transition method. As such, we will continue to apply APB Opinion 25 in future periods to equity awards outstanding prior to the date of our adoption of SFAS 123R. In accordance with SFAS 123R, we will recognize the compensation cost of stock-based awards on a graded-vesting basis over the vesting period of the award. Effective with the adoption of SFAS 123R, we have elected to use the Black-Scholes option pricing model to determine the weighted average fair value of stock options granted or modified.

For the year ended December 31, 2006 and the six months ended June 30, 2007, we recorded expense of \$1.7 million and \$4.8 million, respectively, in connection with stock-based awards. As of June 30, 2007, we had \$14.8 million of unrecognized expense related to non-vested options. This expense is expected to be recognized over a weighted average period of 1.2 years.

As there was no public market for our common stock prior to our initial public offering, we have determined the volatility for options granted after January 1, 2006 based on an analysis of reported data for a peer group of companies that issued options with substantially similar terms. The expected volatility of options granted has been determined using an average of the historical volatility measures of this peer group of companies. The expected volatility for options granted after January 1, 2006 was 64-68%. The expected life of options has been determined utilizing the "simplified" method as prescribed by the SEC's Staff Accounting Bulletin No. 107, *Share-Based Payment*. The expected life of options granted during each of the year ended December 31, 2006 and the six months ended June 30, 2007 was 6.25 years and the weighted average risk free interest rate was 4.61-4.76%. The risk-free interest rate is based on a U.S. treasury instrument whose term is consistent with the expected life of the stock options. We have not paid, and do not anticipate paying, cash dividends on our shares of common stock; therefore, the expected dividend yield was assumed to be zero. In addition, SFAS 123R requires companies to utilize an estimated forfeiture rate when calculating the expense for the period. As a result, we applied an estimated forfeiture rate of 3%, based on a review of our historical forfeitures, to determine the expense recorded in our consolidated statements of operations. If this rate changes in future periods, our stock compensation expense may increase or decrease significantly.

In accordance with APB Opinion 25, share-based compensation expense resulted from stock option grants at exercise prices that, for financial reporting purposes, were deemed to be below the estimated grant date fair value of the underlying common stock. During the years ended December 31, 2004 and 2005, we granted options to purchase 4,152,000 shares of our common stock to our employees and consultants. No compensation cost related to stock-based awards to

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employees was recorded for the years ended December 31, 2004 and 2005, as the exercise prices were deemed to equal or exceed the grant date fair value of common stock.

During 2004 and 2005, we relied on our board of directors, the members of which have extensive experience in the industry in which we operate and all but one of whom are non-employee directors, to determine a reasonable estimate of the then fair value of our common stock. Given the absence of an active market for our common stock, our board of directors determined the estimated fair value of our common stock on the date of grant based on several factors, including:

the grants involved private, early stage company securities that were not liquid;

the prices at which our convertible preferred stock was issued by us to investors in transactions in February 2004 and from May to September 2005 considering the rights, preferences and privileges of the convertible preferred stock relative to the common stock;

important developments relating to our product;

our stage of development and business strategy;

our operating results;

the likelihood of achieving a liquidity event for shares of common stock, such as an initial public offering or sale of our company, given prevailing market conditions; and

the state of the new issue market for similarly situated technology companies.

During 2004 and 2005, our board also considered our customer base and our prospects for future growth. The board noted that our bookings and revenues were generated almost exclusively from CDMA operators. However, because a majority of worldwide subscribers are served by GSM/UMTS operators, management and the board of directors believed it was crucial for us to penetrate the GSM/UMTS market before we could achieve a level of sustainable business growth that would enable any liquidity scenarios to be practical. At the time of each option grant during 2004 and 2005, the board considered the factors discussed above and at various points throughout this period valued our common stock between \$0.30 and \$1.65 per share.

In February 2006, our board requested that an independent firm perform a contemporaneous valuation of our common stock. Our board engaged Gordon Associates Inc., an independent third-party valuation firm, to perform this valuation. In connection with this valuation, the valuation firm considered various liquidity alternatives, but determined that the probabilities and timing of the alternative liquidity scenarios could not be reliably estimated. The valuation firm determined that the fair value of the common stock as of February 22, 2006 was \$1.49 per share. On April 18, 2006, our board of directors considered the results of the independent valuation, as well as other factors our board deemed relevant, including that we had not yet penetrated the GSM/UMTS market, and decided to continue to value our common stock at \$1.65 per share.

In June 2006, we received a purchase order from one of the world's largest GSM operators. This purchase order represented a significant event in our development as it provided an opportunity to enter into the GSM/UMTS market and provided credibility for our products with other GSM/UMTS operators, including our GSM customer's affiliates that operate networks in a significant number of countries in Europe.

In August 2006, our board of directors requested the valuation firm to update their February 2006 report. The valuation firm updated their valuation, which resulted in a determination that the value of our common stock as of August 30, 2006 was \$1.64 per share. On September 29, 2006, our board of directors considered the results of the August 2006 independent valuation, as

well as other factors the board deemed relevant, and decided to continue to value our common stock at \$1.65 per share.

In November 2006, our board of directors requested the valuation firm to perform another valuation, which resulted in a valuation of \$5.13 per share of common stock as of November 27, 2006. The November 2006 valuation was prepared utilizing the probability weighted expected return method as prescribed by the AICPA Practice Aid, *Valuation of Privately-Held-Company Equity Securities Issued as Compensation*, referred to as the Practice Aid. This valuation took into consideration the following scenarios:

completion of an initial public offering;

sale to a strategic acquirer;

remaining private; and

liquidation at a price at or below the liquidation preference.

On December 14, 2006, our board of directors considered the results of the November 2006 valuation and determined to value our common stock at \$5.13 per share as of that date.

In connection with the preparation of our financial statements for the year ended December 31, 2006, we examined the valuations of our common stock after June 2006, the point in time of our first significant GSM/UMTS purchase order. As noted above, the \$5.13 per share value determined in the November 2006 valuation was utilized for financial reporting purposes to record share-based compensation for awards granted on December 14 and December 22, 2006. We retrospectively reviewed the August 2006 valuation for financial reporting purposes and prepared an analysis of that valuation that included the values of the alternative liquidation scenarios as determined in the November 2006 valuation. As a result of this analysis, we retrospectively determined that the fair value of our common stock for financial reporting purposes as of the June, September and October 2006 stock option grant dates was \$1.92, \$3.99, and \$4.49 per share, respectively.

In January 2007 and again in March 2007, our board of directors requested the valuation firm to update their November 2006 valuation. The valuation firm conducted these valuation updates utilizing the probability weighted expected return method as prescribed by the Practice Aid, and considered the same scenarios as utilized in the November 2006 valuation. The valuation firm's January 2007 update resulted in a determination that the value of our common stock as of January 26, 2007 was \$5.87 per share. On February 8, 2007, our board of directors considered the results of the January 2007 independent valuation, as well as other factors the board deemed relevant, and determined to value our common stock at \$5.87 per share as of that date. The valuation firm's March 2007 update resulted in a determination that the value of our common stock as of March 19, 2007 was \$7.58 per share. On April 13, 2007, our board of directors considered the results of the March 2007 independent valuation, as well as other factors the board deemed relevant, and determined to value our common stock at \$8.25 per share as of that date.



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The following is a summary of stock option and restricted stock grants during 2006 and through April 2007:

Grants Made During 2006 and through April 2007	Number of Option and Restricted Shares Granted(a)	Exercise or Purchase Price	Fair Value of Common Stock
February 2, 2006	48,665	\$ 1.65(b)	\$ 1.65
April 18, 2006	971,970	1.65(c)	1.65
June 15, 2006	225,997	1.65(c)	1.92(e)
September 29, 2006	1,230,640	1.65(c)	3.99(e)
October 25, 2006	23,999	1.65(c)	4.49(e)
December 14, 2006	363,653	5.13(d)	5.13
December 22, 2006	199,998	5.13(d)	5.13
January 10, 2007	266,666	5.13(c)	5.13
February 8, 2007	433,333	5.87(d)	5.87
February 9, 2007	384,619	5.87(d)	5.87
March 2, 2007	47,330	5.87(d)	5.87
April 13, 2007	1,066,628	8.25(c)	8.25

- (a) Excludes an aggregate of 3,252 shares of restricted stock granted to our employees at no cost during 2006 and 2007. These shares of restricted stock vested immediately upon grant. We recorded compensation expense for these stock grants based upon the fair value of our common stock on the date of grant as determined by our board of directors.
- (b) The exercise or purchase price for the award was equal to the fair value of our common stock as determined in a contemporaneous valuation by our board of directors.
- (c) The exercise or purchase price for the award was equal to the fair value of our common stock as determined in a contemporaneous valuation by our board of directors, which considered, among other factors, the then most recent common stock valuation performed by the valuation firm. The exercise price was at least equal to the fair market value as determined in the then most recent valuation.
- (d) The exercise or purchase price for the award was equal to the fair value of our common stock as determined by our board of directors, based upon a contemporaneous valuation of our common stock by the valuation firm.
- (e) Retrospectively reassessed for financial reporting purposes in connection with the preparation of our financial statements for the year ended December 31, 2006.

As described above, the determination of the fair value of our common stock required the assessment of many quantitative and qualitative factors. Examples of these factors include the following:

our capital structure, including preferential payments, dividend rights and restrictions;

the lack of an active public market for our common and preferred stock;

industry background and information;

developments relating to our products and services;

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our financial results, both actual and forecasted; and

performance of similarly situated technology companies.

Our board of directors determined the fair value of our common stock taking into consideration these factors and the results of the various valuations prepared by our valuation firm, as indicated in the table above.

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On May 15, 2007, we, in consultation with the managing underwriters of our initial public offering, determined our estimated offering price range of \$9.00 to \$11.00 per share. The estimated initial public offering price range was based on current market conditions and updated comparable company market data, and was contingent on our continuing business execution. From February 2, 2006 through April 13, 2007, we granted share-based awards as indicated in the table above. During this period, the value of our common stock increased primarily as a result of our improved operating results, our success developing relationships with GSM/UMTS operators and the increased probability of a potential initial public offering. Based on the increased probability of a potential initial public offering, the discount used by our valuation firm for the lack of an active market for our common stock was reduced from 30% in the February 2006 valuation to 10% in the March 2007 valuation. The difference between the fair value of our common stock on each grant date and \$10.00, the mid-point of the initial estimated price range for our initial public offering filed with the SEC on May 18, 2007, declined in each quarter since the beginning of 2006.

The significant factors contributing to the difference between the fair value of our common stock as determined by our board of directors and the initial estimated price range for our initial public offering filed with the SEC on May 18, 2007 were:

a discount for lack of a public market for our common stock was not included in determining the estimated initial public offering price;

our operating results improved as revenues were \$27.6 million in the first quarter of 2007, a 92% increase over the first quarter of 2006;

the valuation firm utilized market and income approaches in their valuations while only a market comparable approach was applied in determining the estimated initial public offering price; and

companies considered in the market comparable approach used to determine the estimated initial public offering price included companies recently completing public offerings.

### ***Inventory***

We carry our inventory at the lower of historical cost or net realizable value assuming inventory items are consumed on a first-in, first-out basis. We recognize inventory losses based on obsolescence and levels in excess of forecasted demand. In these cases, inventory is written down to estimated realizable value based on historical usage and expected demand. Inherent in our estimates of market value in determining inventory valuation are estimates related to economic trends, future demand for our products and technical obsolescence of our products. If future demand or market conditions are less favorable than our projections, additional inventory write-downs could be required and would be reflected in the cost of revenues in the period the revision is made. To date, we have not been required to revise any of our assumptions or estimates used to determine our inventory valuations.

When products have been delivered, but the product revenues associated with the arrangement have been deferred as a result of not meeting the revenue recognition criteria required by SOP 97-2, we defer the related inventory costs for the delivered items.

### ***Income Taxes***

We are subject to income taxes in both the United States and foreign jurisdictions and we use estimates in determining our provisions for income taxes. We account for income taxes in accordance with SFAS 109, *Accounting for Income Taxes*, which is the asset and liability method for accounting and reporting for income taxes. Under SFAS 109, deferred tax assets and liabilities are recognized based on temporary differences between the financial reporting and income tax bases of assets and liabilities using statutory rates.

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As of December 31, 2006, we had U.S. federal net operating loss carryforwards for income tax purposes of \$63.1 million that expire beginning in 2022 and state net operating loss carryforwards of \$65.5 million that expire beginning in 2007. We also had U.S. federal tax credits of \$3.0 million that expire beginning in 2020 and state research and development credits of \$652,000 that expire beginning in 2018. The Internal Revenue Code contains provisions that limit the net operating losses and tax credit carryforwards available to be used in any given year in the event of certain circumstances, including significant changes in ownership interests, as defined.

During the year ended December 31, 2006, we recorded income tax expense of \$413,000 which consisted primarily of provisions associated with various state and foreign jurisdictions. Income tax expense related to our international subsidiaries generally results from taxable income generated by the subsidiary pursuant to intercompany service agreements. We believe the compensation associated with these service agreements is reasonable in light of the level and nature of services performed by our subsidiaries. However, if a foreign tax jurisdiction or the Internal Revenue Service were to challenge these arrangements, we could be subject to additional income tax expense either in the United States or the foreign jurisdiction.

Our income tax expense consists primarily of provisions associated with various state and foreign jurisdictions as well as federal alternative minimum tax. Income tax expense related to our international subsidiaries generally results from taxable income generated by the subsidiary pursuant to intercompany service agreements. We believe the compensation associated with these service agreements is reasonable in light of the level and nature of services performed by our subsidiaries. However, if a foreign tax jurisdiction or the Internal Revenue Service were to challenge these arrangements, we could be subject to additional income tax expense either in the United States or the foreign jurisdiction.

Due to the uncertainty surrounding the realization of our deferred tax assets, based principally on operating losses, we have provided a full valuation allowance against our various tax attributes. We will assess the level of valuation allowance required in future periods based on the available positive and negative evidence at that point in time. Should more positive than negative evidence regarding the realizability of tax attributes exist at a future point in time, the valuation allowance may be reduced or eliminated altogether. Reduction of the valuation allowance, in whole or in part, would result in a non-cash reduction in income tax expense during the period of reduction.

On January 1, 2007, we adopted the provisions of FASB Interpretation, or FIN, No. 48, *Accounting for Uncertainty in Income Taxes*, an interpretation of SFAS 109. The new standard defines the threshold for recognizing the benefits of tax return positions in the financial statements as "more-likely-than-not" to be sustained by the taxing authorities based solely on the technical merits of the position. If the recognition threshold is met, the tax benefit is measured and recognized as the largest amount of tax benefit, in our judgment, which is greater than 50% likely to be realized. We did not recognize any change in our reserves for uncertain tax positions as a result of the adoption of this standard. At the adoption date of January 1, 2007, we had approximately \$134,000 of unrecognized tax benefits the benefit of which, if recognized, would favorably affect the income tax rate in future periods. At June 30, 2007, we had a liability of approximately \$134,000 related to unrecognized tax benefits.

We recognize interest and penalties related to uncertain tax positions in income tax expense. Upon our adoption of FIN 48 and at June 30, 2007, we had an immaterial amount of accrued interest and penalties associated with our uncertain tax positions.

We have accumulated significant losses from our inception in August 2000. Since the net operating losses may potentially be utilized in future years to reduce taxable income, all of our tax years remain open to examination by the major taxing jurisdictions to which we are subject.

**Research and Development Expense**

Research and development expense includes costs incurred to develop intellectual property. Research and development costs are charged to operations as incurred. The costs to develop new software and substantial enhancements to existing software are expensed as incurred until technological feasibility has been established, at which time any additional costs would be capitalized. We have determined technological feasibility is established at the time a working model of software is completed. The time period during which costs could be capitalized, from the point of reaching technological feasibility until the time of general product release is short. Consequently, the amounts that could be capitalized are not material to our financial position or results of operations and therefore have been charged to expense as incurred.

**Results of Operations****Comparison of the Six Months Ended June 30, 2006 and 2007****Revenues**

The following table sets forth our revenues by type and geographic location of our customers.

	Six Months Ended June 30,					
	2007		2006		Period-to-Period Change	
	Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage
	(dollars in thousands)					
<b>Revenues:</b>						
Product	\$ 49,573	85%	\$ 29,466	85%	\$ 20,107	68%
Service	8,923	15	5,357	15	3,566	67
Total revenues	\$ 58,496	100%	\$ 34,823	100%	\$ 23,673	68%
<b>Revenues by Customer Type:</b>						
Direct	\$ 29,094	50%	\$ 29,886	86%	\$ (792)	(3)%
Indirect	29,402	50	4,937	14	24,465	496
Total revenues	\$ 58,496	100%	\$ 34,823	100%	\$ 23,673	68%
<b>Revenues by Geography:</b>						
United States and Canada	\$ 36,936	63%	\$ 27,353	79%	\$ 9,583	35%
Japan	13,524	23	2,144	6	11,380	531
Korea	6,273	11	324	1	5,949	1,836
Rest of world	1,763	3	5,002	14	(3,239)	(65)
Total revenues	\$ 58,496	100%	\$ 34,823	100%	\$ 23,673	68%

Revenues increased \$23.7 million, or 68%, in the six months ended June 30, 2007 as compared to the same period in 2006, primarily due to increased product sales to existing customers. Product revenues, which include hardware and software sales, increased \$20.1 million in the first half of 2007 as compared to the same period in 2006 due primarily to increased sales to major mobile operators in the United States and Canada and an increase related to the recognition of revenue in Japan deferred in prior periods since we delivered previously committed software functionality during the quarter ended June 30, 2007. The increase in revenues from Korea was due primarily to the recognition of approximately \$5.5 million that was deferred at December 31, 2006 due to the delivery of specific software functionality during the first quarter of 2007.



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*Cost of Revenues and Gross Profit*

Six Months Ended June 30,						
2007		2006		Period-to-Period Change		
Amount	% of Related Revenues	Amount	% of Related Revenues	Amount	Percentage	
(dollars in thousands)						
<b>Cost of revenues:</b>						
Product	\$ 10,754	22%	\$ 7,294	25%	\$ 3,460	47%
Services	3,329	37	704	13	2,625	373
Total cost of revenues	\$ 14,083	24%	\$ 7,998	23%	\$ 6,085	76%
<b>Gross Profit:</b>						
Product	\$ 38,819	78%	\$ 22,172	75%	\$ 16,647	75%
Services	5,594	63	4,653	87	941	20
Total gross profit	\$ 44,413	76%	\$ 26,825	77%	\$ 17,588	66%

Product gross margin increased three percentage points in the first six months of 2007 as compared to the same period in 2006 due primarily to a higher proportion of software revenue in the first quarter of 2007.

The \$2.6 million increase in cost of services was primarily due to higher personnel costs, depreciation expense and overhead costs associated with additional customer support and training personnel that were added during 2006 and in the first half of 2007. We anticipate cost of services will increase in future periods as we continue to increase the number of customer support personnel we employ and continue to expand our customer support testing facilities.

Gross profit on services increased 20% during the first six months of 2007 as a result of the increase in our installed base though the increase was at a lower rate than the growth in service revenue due to the increased costs of services described above.

We believe our overall gross margin for the remainder of 2007 will decrease somewhat from the 76% achieved in the first half of 2007.

*Operating Expenses*

Six Months Ended June 30,						
2007		2006		Period-to-Period Change		
Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage	
(dollars in thousands)						
Research and development	\$ 17,651	30%	\$ 9,705	28%	\$ 7,946	82%
Sales and marketing	15,936	27	12,745	37	3,191	25
General and administrative	6,242	11	3,499	10	2,743	78
Total operating expenses	\$ 39,829	68%	\$ 25,949	75%	\$ 13,880	53%

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*Personnel Costs.* As discussed above, personnel costs are our largest expense representing 65% of our total operating expenses for the six months ended June 30, 2007. These costs include a



cash component and a stock component. The cash component of compensation included in each expense category is set forth below.

	<b>Six Months Ended June 30,</b>		
	<b>2007</b>	<b>2006</b>	<b>Change</b>
	(dollars in thousands)		
Research and development	\$ 9,468	\$ 6,275	\$ 3,193
Sales and marketing	9,535	8,410	1,125
General and administrative	2,266	1,323	943
<b>Total cash-based compensation in operating expenses</b>	<b>\$ 21,269</b>	<b>\$ 16,008</b>	<b>\$ 5,261</b>

The increases in personnel costs above were due primarily to a higher number of employees in the six month period ended June 30, 2007 compared to the six month period ended June 30, 2006. We added 115 research and development employees, 32 sales and marketing employees and 15 general and administrative employees since June 30, 2006 resulting in total employees of 501 at June 30, 2007.

In addition to cash compensation, we provide share-based compensation to our employees which is a significant portion of our personnel costs. These charges increased significantly in the six month period ended June 30, 2007 as compared to the same period of 2006 due primarily to the increase in the fair value of our common stock at the time the share-based awards were granted and our higher number of employees. The share-based compensation included in each expense category is set forth below.

	<b>Six Months Ended June 30,</b>		
	<b>2007</b>	<b>2006</b>	<b>Change</b>
Research and development	\$ 2,141	\$ 82	\$ 2,059
Sales and marketing	993	98	895
General and administrative	1,422	44	1,378
<b>Total share-based compensation in operating expenses</b>	<b>\$ 4,556</b>	<b>\$ 224</b>	<b>\$ 4,332</b>

*Research and development.* Research and development expenses increased \$7.9 million, or 82%, in the first half of 2007 from the same period in 2006, and the percentage of these costs to revenues also increased. In addition to the increases in personnel costs of \$5.3 million described above, prototype costs were \$1.6 million higher in the first half of 2007 as compared to the same period of 2006 due primarily to the timing of testing of our ST40 platform.

We intend to continue to invest significantly in our research and development efforts, which we believe are essential to maintaining our competitive position. Accordingly, we anticipate personnel costs and depreciation expense to increase during the remainder of 2007 as we continue to add quality assurance personnel and increase our test lab facilities.

*Sales and marketing.* For the first half of 2007, sales and marketing expenses increased \$3.2 million, or 25%, as compared to the same period in 2006, but were lower as a percentage of revenues. The spending increase was due primarily to higher personnel costs of \$2.0 million, higher travel expenses of approximately \$514,000 and higher rent and facilities expense.

We anticipate continuing to increase the number of sales and marketing personnel we employ in future periods to expand our geographic presence, to address specific customer opportunities and to increase our revenues. The commission portion of sales personnel costs may vary

significantly if our customer orders differ materially from the quotas established for our sales personnel. In addition, we expect to incur additional expenses such as demonstration and interoperability testing associated with our ST40 platform in existing and new markets.

*General and administrative.* For the six months ended June 30, 2007, general and administrative expenses increased \$2.7 million, or 78%, as compared to the same period in 2006 due primarily to the higher cash and share-based personnel costs discussed above and higher consulting expenses of \$494,000 related to enhancements to our enterprise financial system.

We expect general and administrative expense to increase in future periods as we invest in infrastructure to support continued growth and incur additional costs related to operating as a publicly-traded company, including increased audit and legal fees, costs of compliance with securities and other regulations, investor relations and higher insurance premiums. In addition, we expect to incur additional costs associated with our pending litigation.

*Interest income.* Interest income consists of income generated from the investment of our cash balances and short-term investments. Interest income increased \$686,000 for the six month period ended June 30, 2007 due to higher average balances and higher rates of return during this period of 2007. In June 2007, our cash and short-term investment balance increased approximately \$116.0 million due to the receipt of the net proceeds of our initial public offering.

*Income tax expense.* For the six months ended June 30, 2007, we recorded income tax expense of \$407,000 compared to \$143,000 in the same period of 2006. The increase in the 2007 period was due primarily to us being subject to federal alternative minimum tax in 2007 and not in 2006. We anticipate that we will be subject to state and foreign income taxes and federal alternative minimum tax in future years. We have significant net operating loss carryforwards and other deferred tax assets, but have recorded a valuation allowance against them due to the uncertainty surrounding the timing and extent of realization of these tax attributes.

*Net income.* Net income increased approximately \$4.1 million for the six months ended June 30, 2007 compared to the same period of 2006 due to the items discussed above.

*Comparison of Years Ended December 31, 2005 and 2006*

	Year Ended December 31,				Period-to-Period Change	
	2005		2006		Amount	Percentage
	Amount	% of Revenues	Amount	% of Revenues		
(dollars in thousands)						
<b>Revenues:</b>						
Product	\$ 51,819	87%	\$ 81,061	86%	\$ 29,242	56%
Services	7,841	13	13,289	14	5,448	70
Total revenues	\$ 59,660	100%	\$ 94,350	100%	\$ 34,690	58
<b>Cost of revenues:</b>						
Product	\$ 12,285	21%	\$ 25,640	27%	\$ 13,355	109%
Services	1,358	2	2,086	2	728	54
Total cost of revenues	\$ 13,643	23%	\$ 27,726	29%	\$ 14,083	103
<b>Operating expenses:</b>						
Research and development	\$ 18,107	30%	\$ 25,980	28%	\$ 7,873	43%
Sales and marketing	19,785	33	30,311	32	10,526	53
General and administrative	7,352	12	8,515	9	1,163	16
Total operating expenses	\$ 45,244	76%	\$ 64,806	69%	\$ 19,562	43%

*Revenues*

The following table sets forth our revenues by type and geographic location of our customers.

	Year Ended December 31,				Period-to-Period Change	
	2005		2006		Amount	Percentage
	Amount	% of Revenues	Amount	% of Revenues		
(dollars in thousands)						
<b>Revenues by Customer Type:</b>						
Direct	\$ 27,446	46%	\$ 46,964	50%	\$ 19,518	71%
Indirect	32,214	54	47,386	50	15,172	47
Total revenues	\$ 59,660	100%	\$ 94,350	100%	\$ 34,690	58
<b>Revenues by Geography:</b>						
United States and Canada	\$ 28,691	48%	\$ 81,687	87%	\$ 52,996	185%

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Year Ended December 31,

Japan	<del>18,718</del>	<del>31</del>	<del>4,227</del>	<del>4</del>	(14,491)	(77)
Korea	11,731	20	661	1	(11,070)	(94)
Rest of world	520	1	7,775	8	7,255	1,395
	<b>_____</b>	<b>_____</b>	<b>_____</b>	<b>_____</b>	<b>_____</b>	<b>_____</b>
Total revenues	\$ 59,660	100%	\$ 94,350	100%	\$ 34,690	58%
	<b>_____</b>	<b>_____</b>	<b>_____</b>	<b>_____</b>	<b>_____</b>	<b>_____</b>

Revenues increased \$34.7 million in 2006, primarily due to increased product sales to existing customers and recognition of \$39.2 million of revenue that was deferred at December 31, 2005 as compared to the recognition in 2005 of \$33.0 million that was deferred at December 31, 2004.

Product revenues, which include hardware and software sales, increased \$29.2 million from 2005 due primarily to increased sales to major mobile operators in the United States and Canada. The decrease in revenues in Japan and Korea was due primarily to the incremental deferral of

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approximately \$8.4 million related to Japan and \$5.5 million related to Korea, as compared to the deferral at December 31, 2005. We anticipate these deferred balances will be recognized during 2007. In addition, a portion of the decrease in revenues in Korea was due to 2005 being the final period in which revenues were recognized on a subscription basis on a contract that expired on December 31, 2005. In 2006, \$14.0 million of our indirect revenue that had been deferred at December 31, 2005 was recognized based upon us establishing VSOE for maintenance and support services for a type of customer. At that point in time, deferred revenue was adjusted to the fair value of the undelivered services in accordance with SOP 97-2.

Services revenues increased \$5.4 million due primarily to increased maintenance and support services being provided on a larger installed base during 2006.

*Cost of Revenues and Gross Profit*

	Year Ended December 31,				Period-to-Period Change	
	2005		2006		Amount	Percentage
	Amount	% of Related Revenues	Amount	% of Related Revenues		
(dollars in thousands)						
<b>Cost of Revenues:</b>						
Product	\$ 12,285	24%	\$ 25,640	32%	\$ 13,355	109%
Services	1,358	17	2,086	16	728	54
Total cost of revenues	\$ 13,643	23%	\$ 27,726	29%	\$ 14,083	103%
<b>Gross Profit:</b>						
Product	\$ 39,534	76%	\$ 55,421	68%	\$ 15,887	40%
Services	6,483	83	11,203	84	4,720	73
Total gross profit	\$ 46,017	77%	\$ 66,624	71%	\$ 20,607	45%

The \$14.1 million increase in cost of revenues was attributable to the increase in hardware and software products sold during 2006 or delivered in previous periods but recognized in revenues during 2006, and higher cost of services.

Product gross margin percentage decreased 8 percentage points due primarily to the increase in the cost of products sold related to us establishing VSOE for maintenance and support for a type of customer. As described above, we recorded additional revenues in 2006 as a result of the establishment of VSOE; however, the cost of products associated with this revenue was higher because the arrangement obligated us to provide certain products free of charge. We recognized \$7.3 million of costs associated with the \$14.0 million of revenue that was recognized upon the establishment of VSOE in 2006. This cost in conjunction with lower average selling price for this OEM arrangement resulted in lower gross margin percentage.

We anticipate our direct sales relationships to contribute a higher percentage of our future revenues, which should result in a higher gross product profit percentage. However, this increase in percentage may be somewhat offset by higher customer support costs as described below.

During 2006, the \$728,000 increase in cost of services was primarily due to higher salaries, incentives and benefits, depreciation expense and overhead costs associated with additional customer support and training personnel that were added during 2006. We anticipate cost of services to increase in future periods as we continue to increase the number of customer support personnel we employ. In addition to the increased number of employees, we plan to expand our customer support testing facilities in 2007 which will increase cost of services. Many of these costs will be fixed in nature and could therefore result in lower services gross profit in the future.

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Gross profit on services increased 73% as a result of a substantial increase in maintenance, support and service revenues associated with the growth in our installed product base without a corresponding proportionate increase in costs. However, we anticipate adding additional employees and customer support testing facilities during 2007 which may reduce the services gross margin percentage in the future.

### *Operating Expenses*

	Year Ended December 31,					
	2005		2006		Period-to-Period Change	
	Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage
	(dollars in thousands)					
Research and development	\$ 18,107	30%	\$ 25,980	28%	\$ 7,873	43%
Sales and marketing	19,785	33	30,311	32	10,526	53
General and administrative	7,352	12	8,515	9	1,163	16
<b>Total operating expenses</b>	<b>\$ 45,244</b>	<b>76%</b>	<b>\$ 64,806</b>	<b>69%</b>	<b>\$ 19,562</b>	<b>43%</b>

*Research and development.* Research and development expenses consisted primarily of the following significant items:

	Year Ended December 31,					
	2005		2006		Period-to-Period Change	
	Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage
	(dollars in thousands)					
Payroll and related expenses	\$ 9,938	17%	\$ 13,702	15%	\$ 3,764	38%
Prototypes and related equipment	3,215	5	4,415	5	1,200	37
Consulting	1,485	2	2,281	2	796	54
Depreciation	1,249	2	1,867	2	618	49
Share-based compensation	230		708	1	478	208
Other	1,990	3	3,007	3	1,017	51
<b>Total research and development</b>	<b>\$ 18,107</b>	<b>30%</b>	<b>\$ 25,980</b>	<b>28%</b>	<b>\$ 7,873</b>	<b>43%</b>

Research and development expenses increased \$7.9 million or 43% in 2006 from 2005, however the percentage of these costs to revenues decreased as our revenues increased 58%. Following is a discussion of each significant item listed above:

Payroll and related expenses increased \$3.8 million due to the addition of 89 employees of which 75 were located in India and 14 of which were located in the United States. The majority of these additions were in software engineering and quality assurance to develop and test additional software products.

Prototypes and related equipment include the cost of building and testing our hardware products and the cost of our hardware products utilized to test our software products. These costs increased \$1.2 million in 2006 largely due to the increased personnel. Generally, it is necessary to provide testing equipment for a majority of the testing personnel added. In addition, prototype expense increased due to development efforts related to enhancements to our hardware.



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Consulting expense primarily consists of contract employees utilized in the development and testing of our products. These expenses increased \$796,000 in 2006 as compared to 2005 as we utilized a higher number of contractors.

Depreciation expense increased \$618,000 due primarily to capital expenditures for equipment and building improvements and expansions.

Other expenses consist primarily of office, facilities and supplies costs. The increase in these costs was due primarily to additional space required to accommodate increased personnel.

*Sales and marketing.* Sales and marketing expenses consisted primarily of the following significant items:

	Year Ended December 31,					
	2005		2006		Period-to-Period Change	
	Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage
	(dollars in thousands)					
Salaries and related expenses	\$ 8,251	14%	\$ 10,861	12%	\$ 2,610	32%
Commissions	3,350	6	10,221	11	6,871	205
Travel	3,548	6	3,398	4	(150)	(4)
Consulting	1,185	2	1,712	2	527	44
Share-based compensation	28		404		376	1,343
Other	3,423	6	3,715	4	292	9
	\$ 19,785	33%	\$ 30,311	32%	\$ 10,526	53%

Sales and marketing expenses increased \$10.5 million, or 53%, as compared to 2005, and were slightly lower as a percentage of revenues. Following is a discussion of each significant item listed above:

Salaries and related expenses increased \$2.6 million during 2006 due to the addition of sales and marketing personnel.

Our sales personnel earn a significant portion of their compensation through commissions that are generally based upon accepted customer orders and subsequent collections of amounts billed. Commissions increased \$6.9 million in 2006, as compared to 2005, due primarily to customer orders exceeding expectations primarily in the United States and Canada and 2006 customer orders exceeding 2005 orders by \$38.3 million.

Consulting expenses consist primarily of sales contractors utilized in areas of the world in which we do not have employees and costs associated with marketing and customer studies. The \$527,000 increase in 2006 was due primarily to payments to consultants paid on a contingent basis relative to a specific customer and additional market studies.

Other expense consists primarily of facilities, promotions and demonstration equipment for our customers.



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*General and administrative.* General and administrative expenses consisted primarily of the following significant items:

	Year Ended December 31,					
	2005		2006		Period-to-Period Change	
	Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage
	(dollars in thousands)					
Payroll and related expenses	\$ 2,106	4%	\$ 3,120	3%	\$ 1,014	48%
Professional fees	3,585	6	3,104	3	(481)	(13)
Consulting	482	1	736	1	254	53
Share-based compensation			504	1	504	
Other	1,179	2	1,051	1	(128)	(11)
<b>Total general and administrative</b>	<b>\$ 7,352</b>	<b>12%</b>	<b>\$ 8,515</b>	<b>9%</b>	<b>\$ 1,163</b>	<b>16%</b>

General and administrative expenses increased \$1.2 million, or 16%, in 2006 as compared to 2005, and decreased as a percentage of revenues. Following is a discussion of each significant item listed above:

Payroll and related expenses increased \$1.0 million in 2006 as compared to 2005 due primarily to additional finance and other administrative personnel and higher salaries and bonuses.

Professional fees primarily consist of legal and accounting fees. The \$481,000 decrease in these costs was due primarily to lower legal fees in 2006. In 2005, we incurred significant litigation costs related to our defense of certain patent infringement claims which were not incurred in 2006. This reduction was partially offset by higher accounting and audit fees. In 2006, we commenced an internal control reporting readiness program.

Consulting expenses primarily consist of contractors and system consultants fees. The increase of \$254,000 in 2006 was primarily due to additional finance contract employees utilized prior to permanently filling these positions and consulting related to our enterprise financial system.

*Interest income.* Interest income consists of income generated from the investment of our cash balances and short-term investments. The \$1.5 million increase was due to higher average balances during 2006 as we generated significant cash from operations and to higher rates of return on these balances.

*Income tax expense.* For the year ended December 31, 2006, we recorded income tax expense of \$413,000 versus \$513,000 in the prior year. The decrease in 2006 was due primarily to us being subject to federal alternative minimum tax in 2005 and not in 2006. We anticipate that we will be subject to state income taxes and federal alternative minimum taxes in future years. We have significant net operating loss carryforwards and other deferred tax assets, but have recorded a valuation allowance against them due to the uncertainty surrounding the timing and extent of realization of these tax attributes.

*Net income.* Net income increased approximately \$2.7 million for the year ended December 31, 2006 to \$3.6 million. This increase resulted from the items discussed above, including the increase in interest income of \$1.5 million.

*Comparison of Years Ended December 31, 2004 and 2005*

	Year Ended December 31,					
	2004		2005		Period-to-Period Change	
	Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage
(dollars in thousands)						
<b>Revenues:</b>						
Product	\$ 29,453	86%	\$ 51,819	87%	\$ 22,366	76%
Services	4,942	14	7,841	13	2,899	59
Total revenues	\$ 34,395	100%	\$ 59,660	100%	\$ 25,265	73%
<b>Cost of revenues:</b>						
Product	\$ 12,633	37%	\$ 12,285	21%	\$ (348)	(3)%
Services	812	2	1,358	2	546	67
Total cost of revenues	\$ 13,445	39%	\$ 13,643	23%	\$ 198	1%
<b>Operating expenses:</b>						
Research and development	\$ 13,303	39%	\$ 18,107	30%	\$ 4,804	36%
Sales and marketing	18,445	54	19,785	33	1,340	7
General and administrative	3,185	9	7,352	12	4,167	131
Total operating expenses	\$ 34,933	102%	\$ 45,244	76%	\$ 10,311	30%

*Revenues*

The following table sets forth our revenues by type and geographic location of our customers.

	Year Ended December 31,					
	2004		2005		Period-to-Period Change	
	Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage
(dollars in thousands)						
<b>Revenues by Customer Type:</b>						
Direct	\$ 18,856	55%	\$ 27,446	46%	\$ 8,590	46%
Indirect	15,539	45	32,214	54	16,675	107
Total revenues	\$ 34,395	100%	\$ 59,660	100%	\$ 25,265	73%

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Year Ended December 31,

**Revenues by Geography:**

United States and Canada	\$	17,102	50%	\$	28,691	48%	\$	11,589	68%
Japan		7,485	22		18,718	31		11,233	150
Korea		7,704	22		11,731	20		4,027	52
Rest of world		2,104	6		520	1		(1,584)	(75)
Total revenues	\$	34,395	100%	\$	59,660	100%	\$	25,265	73%

Revenues increased \$25.3 million in 2005, primarily due to increased product sales to existing customers and \$33.0 million of revenue recognized that was deferred at December 31, 2004 as compared to the recognition in 2004 of \$16.1 million that was deferred at December 31, 2003.

Product revenues, which include hardware and software sales, increased \$22.4 million from 2004 due primarily to increased sales to major mobile operators and the recognition of deferred

revenue mentioned above. Revenues in Japan increased in 2005 primarily due to the recognition of \$6.3 million more revenue from deferred revenue in 2005 than 2004 and a lower amount of unbilled sales in 2005 than in 2004. The revenues increase related to Korea was due primarily to the inclusion in 2005 of a full year of revenue recognized on a subscription basis for a particular customer compared to only eight months of recognition in 2004.

Services revenues increased \$2.9 million due primarily to increased maintenance and support services being provided on a larger installed base during 2005.

*Cost of Revenues and Gross Profit*

	Year Ended December 31,					
	2004		2005		Period-to-Period Change	
	Amount	% of Related Revenues	Amount	% of Related Revenues	Amount	Percentage
(dollars in thousands)						
<b>Cost of Revenues:</b>						
Product	\$ 12,633	43%	\$ 12,285	24%	\$ (348)	(3)%
Services	812	16	1,358	17	546	67
Total cost of revenues	\$ 13,445	39%	\$ 13,643	23%	\$ 198	1%
<b>Gross Profit:</b>						
Product	\$ 16,820	57%	\$ 39,534	76%	\$ 22,714	135%
Services	4,130	84	6,483	83	2,353	57
Total gross profit	\$ 20,950	61%	\$ 46,017	77%	\$ 25,067	120%

Cost of revenues was relatively unchanged in 2005 as compared to 2004 due primarily to 2004 including,

approximately \$640,000 of charges related to warranty and repair costs that largely did not occur in 2005; and

an approximate \$1.0 million addition to our excess and obsolete reserve which did not recur in 2005.

Product gross margin increased 19% due primarily to the items discussed above and our 2005 sales having higher average selling prices than 2004 sales primarily related to customers outside the United States and Canada.

During 2005, the \$546,000 increase in cost of services was primarily due to higher salaries, incentives and benefits and overhead costs associated with additional support and training personnel that were added during 2005.

Gross profit on services increased 57% in 2005 primarily as a result of higher maintenance, support and service revenues associated with the growth in our installed product base without a corresponding increase in costs.

## Operating Expenses

	Year Ended December 31,					
	2004		2005		Period-to-Period Change	
	Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage
	(dollars in thousands)					
Research and development	\$ 13,303	39%	\$ 18,107	30%	\$ 4,804	36%
Sales and marketing	18,445	54	19,785	33	1,340	7
General and administrative	3,185	9	7,352	12	4,167	131
Total operating expenses	\$ 34,933	102%	\$ 45,244	76%	\$ 10,311	30%

*Research and development.* Research and development expenses consisted primarily of the following significant items:

	Year Ended December 31,					
	2004		2005		Period-to-Period Change	
	Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage
	(dollars in thousands)					
Payroll and related expenses	\$ 7,913	23%	\$ 9,938	17%	\$ 2,025	26%
Prototypes and related equipment	633	2	3,215	5	2,582	408
Consulting	879	3	1,485	2	606	69
Depreciation	1,339	4	1,249	2	(90)	(7)
Share-based compensation	200	1	230		30	15
Other	2,339	7	1,990	3	(349)	(15)
Total research and development	\$ 13,303	39%	\$ 18,107	30%	\$ 4,804	36%

Research and development expenses increased \$4.8 million or 36% from 2004, however the percentage of these costs to revenues decreased as our revenues increased 73%. Following is a discussion of significant changes in the items listed above:

Payroll and related expenses increased \$2.0 million due to the addition of 50 employees of which 41 were located in India and 9 of which were located in the United States. The majority of these additions were in software engineering and quality assurance in order to develop and test additional software products.

Prototypes and related equipment increased \$2.6 million in 2005 driven largely by increased personnel. Generally, it is necessary to provide testing equipment for a majority of the testing personnel added.

Consulting expense increased \$606,000 in 2005 as compared to 2004 as we utilized a higher number of contractors than in 2004.



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*Sales and marketing.* Sales and marketing expenses consisted primarily of the following significant items:

	Year Ended December 31,					
	2004		2005		Period-to-Period Change	
	Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage
	(dollars in thousands)					
Salaries and related expenses	\$ 5,928	17%	\$ 8,251	14%	\$ 2,323	39%
Commissions	6,821	20	3,350	6	(3,471)	(51)
Travel	1,966	6	3,548	6	1,582	80
Consulting	1,382	4	1,185	2	(197)	(14)
Share-based compensation			28		28	
Other	2,348	7	3,423	6	1,075	46
<b>Total sales and marketing</b>	<b>\$ 18,445</b>	<b>54%</b>	<b>\$ 19,785</b>	<b>33%</b>	<b>\$ 1,340</b>	<b>7%</b>

Sales and marketing expenses increased \$1.3 million or 7% as compared to 2004; however, the percentage of these costs to revenues decreased as our revenues increased 73%. Following is a discussion of the significant changes in the items listed above:

Salaries and related expenses increased \$2.3 million during 2005 due to the addition of sales and marketing professionals. Sales professionals were added to expand our geographic presence, to address specific customer opportunities and to increase our revenues.

Our sales personnel earn a significant portion of their compensation through commissions that are generally based upon accepted customer orders and subsequent collections of amounts billed. Commission expense decreased \$3.5 million as compared to 2004 due primarily to customer orders being lower than established sales quotas.

Travel costs increased in 2005 primarily as a result of the personnel hired during the year.

Other expense consists primarily of facilities, promotions and demonstration equipment for our customers. The increase in 2005 was due primarily to higher rent and related facility expenses.

*General and administrative.* General and administrative expenses consisted primarily of the following significant items:

	Year Ended December 31,					
	2004		2005		Period-to-Period Change	
	Amount	% of Revenues	Amount	% of Revenues	Amount	Percentage
	(dollars in thousands)					
Payroll and related expenses	\$ 1,359	4%	\$ 2,106	4%	\$ 747	55%
Professional fees	1,305	4	3,585	6	2,280	175
Consulting	272	1	482	1	210	77
Other	249	1	1,179	2	930	373

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Year Ended December 31,

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Total general and administrative	\$	3,185	9%	\$	7,352	12%	\$	4,167	131%
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General and administrative expenses increased \$4.2 million or 131% as compared to 2004, and increased as a percentage of revenues. Following is a discussion of each significant item listed above:

Payroll and related expenses increased \$747,000 as compared to 2004 due primarily to additional finance and other administrative personnel and higher salaries and bonuses.

Professional fees consist primarily of legal and accounting fees. The \$2.3 million increase in these costs was due primarily to higher legal fees in 2005. In 2005, we incurred significant litigation costs related to our defense of certain patent infringement claims which were not incurred in 2004.

The increase of \$210,000 in consulting expenses in 2005 was primarily due to higher translation and finance system consulting and contractor fees.

*Interest income.* Interest income consists of income generated from the investment of our cash balances and short-term investments. The \$662,000 increase in 2005 was due to higher average cash and investment balances due primarily to the issuance of our Series E convertible preferred stock during 2005 that generated net proceeds of approximately \$17.9 million.

*Income tax expense.* For the year ended December 31, 2005, we recorded income tax expense of \$513,000 as compared to \$160,000 in 2004. The increase in 2005 was due primarily to us being subject to federal alternative minimum tax in 2005 and higher state income taxes. In 2004, income tax expense consisted primarily of taxes related to our international subsidiaries. We have significant net operating loss carryforwards and other deferred tax assets, but have recorded a valuation allowance against them due to the uncertainty surrounding the timing and extent of realization of these tax attributes.

*Net income (loss).* Net income totaled \$904,000 for the year ended December 31, 2005 as compared to a net loss of \$14.0 million for the year ended December 31, 2004. The increase in net income was due primarily to the increase in revenues, which was partially offset by higher operating expenses as discussed above.

### **Selected Quarterly Data**

The following table sets forth our unaudited quarterly consolidated statement of operations data for each of the six quarters ended June 30, 2007. In our opinion, the information presented has been prepared on the same basis as the audited consolidated financial statements included in this prospectus, and reflects all necessary adjustments, consisting only of normal recurring

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adjustments, necessary for a fair presentation of this data. The results of historical periods are not necessarily indicative of the results of operations for a full year or any future period.

For the Three Months Ended

	March 31, 2006	June 30, 2006	September 30, 2006	December 31, 2006	March 31, 2007	June 30, 2007
(dollars in thousands)						
<b>Revenues:</b>						
Product	\$ 11,722	\$ 17,744	\$ 31,642	\$ 19,952	\$ 24,452	\$ 25,121
Services	2,712	2,645	3,596	4,337	3,190	5,733
	14,434	20,389	35,238	24,289	27,642	30,854
<b>Cost of revenues:</b>						
Product	3,893	3,401	13,240	5,106	4,438	6,316
Services	341	363	429	953	1,387	1,942
	4,234	3,764	13,669	6,059	5,825	8,258
Gross profit	10,200	16,625	21,569	18,230	21,817	22,596
<b>Operating expenses:</b>						
Research and development	3,642	6,064	7,421	8,853	10,066	7,585
Sales and marketing	5,160	7,584	8,983	8,584	7,069	8,867
General and administrative	1,516	1,983	2,317	2,699	2,844	3,398
Total operating expenses	10,318	15,631	18,721	20,136	19,979	19,850
Income (loss) from operations	(118)	994	2,848	(1,906)	1,838	2,746
Other income (expense), net	420	428	645	744	710	799
Income (loss) before income tax expense	302	1,422	3,493	(1,162)	2,548	3,545
Income tax expense	(50)	(92)	(243)	(27)	(243)	(164)
Net income (loss)	\$ 252	\$ 1,330	\$ 3,250	\$ (1,189)	\$ 2,305	\$ 3,381

Consistent with our historical experience, revenues fluctuated on a quarterly basis in 2006 and 2007 due to timing of customer orders and revenue recognition in relation to the shipment of products. Revenues for the quarter ended September 30, 2006 included \$15.7 million of revenues associated with us establishing VSOE for maintenance and support for a type of customer, which did not recur in subsequent quarters. This establishment of VSOE also resulted in the recognition of significant cost of products sold of approximately \$7.6 million. These costs, in addition to this customer having lower average sales prices, resulted in reduced gross margin.

Research and development expenses increased in each quarter presented due primarily to the hiring of additional research and development personnel, which in turn resulted in higher prototype and related equipment expense. In addition, we recognized a \$2.0 million payment from a customer for professional services, which was recorded as a reduction of research and development expense in the quarter ended March 31, 2006. Research and development expenses decreased in the quarter ended June 30, 2007 due to higher prototype expenses in the

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previous quarter and a \$1.4 million reimbursement in the quarter ended June 30, 2007 related to engineering services provided to a customer.

Sales and marketing expenses increased due to the hiring of additional sales personnel and higher commissions in the quarter ended September 30, 2006.

Our net loss of \$1.2 million for the quarter ended December 31, 2006 was largely due to the recognition of \$1.2 million of share-based compensation in that period.

Our operating results may fluctuate due to a variety of factors, many of which are outside of our control. As a result, comparing our operating results on a period-to-period basis may not be meaningful. Most notably we believe our revenues will vary significantly from period to period as a result of the following:

*Fluctuations in the timing of customer orders.* Mobile operators require significant lead times to incorporate changes and enhancements into their networks to ensure the various network components are interoperable. These lead times and interoperability testing requirements result in an extended sales cycle and can lead to uneven purchasing patterns. In addition, our reliance on a relatively small number of customers contributes to the variability of revenues.

*The timing of revenue recognition in relation to the shipment of products.* Our products contain software which is not incidental to our products, therefore we recognize revenue pursuant to the requirements of SOP 97-2 as discussed above. Due to the requirements of this statement and its related interpretations, such as customer acceptance terms in most of our contracts and the need for us to establish fair values of our products and services based on facts specific to our operations, revenue recognition is often deferred for a significant period of time after shipment.

The variability in our revenues directly impacts our operating performance in any particular period since a significant portion of our operating costs, such as prototype and related equipment, share-based compensation and sales commissions, are either fixed in the short-term or may not vary proportionately with recorded revenues. Commissions are recorded at the point in time we receive a customer order and revenue is recorded at the point in time all of the criteria for revenue recognition have been met. Revenue recognition often occurs in a subsequent period. The cost for prototype and related equipment may vary based on the number of testing personnel we hire and the number of products being developed.

## **Liquidity and Capital Resources**

### ***Resources***

We funded our operations from 2000 through 2004 primarily with approximately \$100.0 million of net proceeds from issuances of convertible preferred stock. Since 2005, we have funded our operations principally with cash provided by operating activities, which was driven mainly by our revenue growth.

*Cash, cash equivalents and short-term investments.* Our cash, cash equivalents and short term investments at June 30, 2007 of \$157.2 million were held for working capital purposes and were invested primarily in money market funds. We do not enter into investments for trading or speculative purposes. Restricted cash, which totaled \$1.0 million at December 31, 2006 and \$592,000 at June 30, 2007, and was not included in cash and cash equivalents, was held as collateral for letters of credit related to vendor and lease agreements.

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Our net cash flows from operating, investing and financing activities for the periods indicated in the table below were as follows:

	Year Ended December 31,			Six Months Ended June 30,	
	2004	2005	2006	2006	2007
	(dollars in thousands)				
Net cash provided by (used in) operating activities	\$ (4,095)	\$ 2,015	\$ 31,056	\$ 10,978	\$ (10,976)
Net cash provided by (used in) investing activities	\$ (2,368)	\$ (20,488)	\$ (28,130)	\$ (6,003)	\$ 5,686
Net cash provided by (used in) financing activities	\$ 25,230	\$ 17,780	\$ 987	\$ 76	\$ 117,592

*Operating activities.* Cash from operating activities consists of significant components of the statements of operations adjusted for changes in various working capital items including deferred revenues, accounts receivable, inventories, accounts payable, prepaid expenses and various accrued expenses.

*Six months ended June 30, 2007 compared to six months ended June 30, 2006.*

For the first six months of 2007, net cash used in operating activities was \$11.0 million as compared to cash provided by operating activities of \$11.0 million in the same period in 2006. Cash received from customers decreased \$7.9 million in the first half of 2007 to \$34.4 million from \$42.3 million in the same period of 2006. This reduction was due primarily to lower accounts receivable at the beginning of the 2007 period. In addition, cash paid for payroll and related expenses increased \$7.3 million totaling \$21.5 million in 2007 compared to the same period in 2006, and cash paid for inventories was approximately \$5.4 million higher in the 2007 period as compared to 2006. The increase in payroll and related expenses was due primarily to our increased headcount as discussed above. The increase in cash paid for inventories was due primarily to our purchases of components related to the introduction of our ST40 platform.

*2005 compared to 2006.*

Net cash provided by operating activities was \$31.1 million in 2006 as compared to \$2.0 million in 2005. Cash received from customers increased \$45.0 million in 2006 to \$112.1 million from \$67.1 million in 2005 due primarily to higher shipments combined with a reduction in accounts receivable of \$4.0 million. The increase in cash receipts was partially offset by an increase in payments for payroll and related expenses of \$8.9 million, which totaled \$35.5 million in 2006. The increase in payroll and related payments was due primarily to our increased headcount and sales commissions as discussed above partially offset by an increase in our accruals for these costs. Cash paid for inventories was \$19.8 million in 2006 which was relatively consistent to the 2005 level of \$20.3 million. In addition to these significant receipts and payments, amounts paid for prototypes and related equipment, consulting, professional fees, travel and other items increased during 2006 due primarily to our higher number of personnel, increased number of locations and continued investment in infrastructure to support our growth.

2004 compared to 2005.

Net cash provided by operating activities was \$2.0 million in 2005 as compared to \$4.1 million used in operations during 2004. Cash received from customers increased \$21.2 million in 2005 to \$67.1 million from \$45.9 million in 2004 due primarily to an increase in shipments. The increase in cash receipts was partially offset by an increase in payments for payroll and related expenses of \$7.6 million, which totaled \$26.6 million in 2005 and increases in prototypes and related equipment, consulting, professional fees and travel and entertainment. The increase in payroll and related expenses was due primarily to our increased headcount in 2005. We paid approximately \$20.3 million in 2005 for inventories, which increased approximately \$1.0 million from 2004 due to higher shipments in 2005. The increase in amounts paid for prototypes and related equipment, consulting and professional fees, travel and other items increased during 2005 due primarily to our higher number of personnel, increased number of locations and continued investment in infrastructure to support our growth.

*Investing activities.* Cash from investing activities consisted primarily of capital expenditures and purchases and sales of short-term investments associated with our investment balances. The \$5.7 million of cash provided by investing activities during the first half of 2007 consisted primarily of maturities for short-term investments partially offset by \$10.1 million of capital expenditures. The \$7.6 million increase in cash used in investing activities in 2006 was due primarily to higher capital expenditures of \$6.2 million, related primarily to office expansions and equipment, and \$1.2 million of higher net purchases of short-term investments as compared to 2005. Cash used in investing activities increased \$18.1 million in 2005 as compared to 2004, \$17.4 million of which was due to higher net purchases of short-term investments and \$1.6 million of which was due to higher capital expenditures.

*Financing activities.* Cash from financing activities consisted primarily of cash received from the issuance of convertible preferred stock and sales and exercises of our equity instruments. The increase in cash provided by financing activities of \$117.6 million in the first half of 2007 was due primarily to approximately \$127.0 million of cash received from the issuance of 10,580,226 shares of our common stock at \$12.00 per share in our initial public offering reduced by approximately \$8.9 million of discounts and commissions and approximately \$2.1 million of other costs associated with the offering. The decrease in cash provided by financing activities of \$16.8 million in 2006 was due primarily to \$17.9 million less proceeds from the issuance of convertible preferred stock partially offset by higher proceeds from the sales and exercises of our restricted stock and stock options of \$965,000. Cash provided by financing activities decreased \$7.5 million in 2005 due primarily to lower proceeds from the issuance of our convertible preferred stock of \$7.0 million. At December 31, 2006 we had no long-term debt outstanding and our restricted cash was our only asset pledged as collateral.

We believe our existing cash and cash equivalents, short-term investments and cash flows from operating activities will be sufficient to finance our planned growth, enhance our products and fund anticipated capital expenditures at least through 2009.

We may use the net proceeds from this offering for working capital and other general corporate purposes, to finance accelerated growth, develop new product lines and fund acquisitions and strategic investments. These future working capital requirements will depend on many factors, including the rate of our revenues growth, our introduction of new products and enhancements and our expansion of sales and marketing and product development activities. To the extent our existing resources and the proceeds of this offering are insufficient to fund these activities we may need to raise additional funds through bank credit arrangements or public or private equity or debt financings. We also may need to raise additional funds in the event we

determine in the future to effect one or more acquisitions of businesses, technologies and products that complement our existing operations. In the event additional funding is required, we may not be able to obtain bank credit arrangements or affect an equity or debt financing on terms acceptable to us or at all.

**Requirements**

*Capital expenditures.* We have made capital expenditures primarily for testing and evaluation systems and equipment to support product development, as well as for leasehold improvements and other general purposes to support our growth. Our capital expenditures totaled \$1.7 million in 2004, \$3.4 million in 2005, \$9.6 million in 2006 and \$10.1 million in the six months ended June 30, 2007. We expect capital expenditures to be approximately \$18-20 million for the full year of 2007, primarily related to purchases of test equipment, equipment to support product development, leasehold improvements and other general purposes to support our growth.

*Contractual obligations and requirements.* As of June 30, 2007, our commitments under operating leases and purchase obligations were as set forth below. For purposes of the table below, purchase obligations are defined as agreements to purchase goods or services that are enforceable and legally binding and that specify all significant terms, including, fixed or minimum quantities to be purchased, fixed, minimum or variable pricing provisions, and the approximate timing of transactions.

	<u>Total</u>	<u>Remainder of 2007</u>	<u>1-3 Years</u>	<u>4-5 Years</u>	<u>More than 5 Years</u>
	(dollars in thousands)				
Operating leases	\$ 6,410	\$ 1,132	\$ 3,616	\$ 1,662	\$
Purchase obligations	8,547	7,772	775		
<b>Total</b>	<b>\$ 14,957</b>	<b>\$ 8,904</b>	<b>\$ 4,391</b>	<b>\$ 1,662</b>	<b>\$</b>

**Off-Balance-Sheet Arrangements**

We do not engage in any off balance sheet financing activities. We do not have any interest in entities referred to as variable interest entities, which includes special purpose entities and other structured finance entities.

**Quantitative and Qualitative Disclosures About Market Risk**

Market risk represents the risk of loss that may impact our financial position due to adverse changes in financial market prices and rates. Our market risk exposure is primarily a result of fluctuations in foreign exchange rates and interest rates. We do not hold or issue financial instruments for trading purposes.

**Foreign Currency Exchange Risk**

To date, substantially all of our international customer agreements have been denominated in U.S. dollars. Accordingly, we have limited exposure to foreign currency exchange rates and do not enter into foreign currency hedging transactions. The functional currency of our foreign operations in Europe, Asia and South America is the U.S. dollar. Accordingly, all assets and liabilities of these foreign subsidiaries are remeasured into U.S. dollars using the exchange rates in effect at the balance sheet date. Revenues and expenses of these foreign subsidiaries are remeasured into U.S. dollars at the average rates in effect during the year. Any differences resulting from the remeasurement of assets, liabilities and operations of these subsidiaries are recorded within other

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income (expense) in the consolidated statements of operations. If the foreign currency exchange rates fluctuated by 10% as of June 30, 2007, our foreign exchange gain or loss would have fluctuated by approximately \$147,000.

### ***Interest Rate Risk***

At June 30, 2007, we had unrestricted cash and cash equivalents and short-term investments totaling \$157.2 million. These amounts were invested primarily in money market funds and high quality corporate and government securities. The unrestricted cash and cash equivalents were held for working capital purposes. We do not enter into investments for trading or speculative purposes. Due to the short-term nature of these investments, we believe that we do not have any material exposure to changes in the fair value of our investment portfolio as a result of changes in interest rates. Declines in interest rates, however, would reduce future investment income.

### **Recent Accounting Pronouncements**

In July 2006, the FASB issued FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes, an interpretation of SFAS 109, Accounting for Income Taxes*, which prescribes a recognition threshold and measurement process for recording in the financial statements uncertain tax positions taken or expected to be taken in a tax return. In addition, FIN 48 provides guidance on the derecognition, classification, interest and penalties, accounting in interim periods and disclosure requirements for uncertain tax positions. The accounting provisions of FIN 48 were effective for us beginning on January 1, 2007. The adoption of FIN 48 did not have a material impact on our results of operations, financial position or cash flows.

In September 2006, the FASB issued SFAS 157, *Fair Value Measurement*, which provides guidance for using fair value to measure assets and liabilities. In addition, SFAS 157 also provides guidance for expanded information about the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value and the effect of fair value measurements on earnings. SFAS 157 applies whenever other standards require (or permit) assets or liabilities to be measured at fair value, but does not expand the use of fair value to any new circumstances. The accounting provisions of SFAS 157 will be effective for us beginning January 1, 2008. We are in the process of determining the effect the adoption of SFAS 157 will have on our consolidated financial statements.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities, Including an Amendment of FASB Statement No. 115*. SFAS 159 allows entities to measure many financial instruments and certain other assets and liabilities at fair value on an instrument-by-instrument basis (the fair value option). The fair value option represents step in the evolution of financial reporting because it considerably expands the ability of entities to select the measurement attribute for certain assets and liabilities. We will be required to adopt the provisions of SFAS 159 January 1, 2008, however earlier adoption is allowed. We will adopt this standard on January 1, 2008. We are in the process of determining the effect the adoption of SFAS 159 will have on our consolidated financial statements.

### **Change in Accountants**

Ernst & Young LLP previously served as our independent registered public accounting firm. On April 20, 2005, our board of directors dismissed Ernst & Young LLP as our registered public accounting firm. As of April 20, 2005, Ernst & Young LLP had not begun its audit of our consolidated financial statements as of and for the fiscal year ended December 31, 2004.

Ernst & Young LLP's audit reports on our consolidated financial statements as of and for the years ended December 31, 2002 and 2003 did not contain any adverse opinion or disclaimer of



opinion, nor were they qualified or modified as to uncertainty, audit scope or accounting principle except with respect to their audit report on our 2002 financial statements, which contained an explanatory paragraph to highlight a going concern uncertainty. In connection with its audits of our financial statements as of December 31, 2002 and 2003 and for the years then ended and during the interim period from January 1, 2004 through April 20, 2005, there were no disagreements with Ernst & Young LLP on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of Ernst & Young LLP, would have caused Ernst & Young LLP to make reference to the subject matter of the disagreement in connection with its audit reports related to our fiscal 2002 and 2003 consolidated financial statements. During our two fiscal years ended December 31, 2002 and 2003 and during the interim period from January 1, 2004 until April 20, 2005, there were no reportable events as defined in Item 304(a)(1)(v) of Regulation S-K.

Subsequent to our dismissal of Ernst & Young LLP, management restated its financial statements as of and for the years ended December 31, 2002 and 2003 principally related to the shifting of the recognition of approximately \$3.5 million of revenue and the related cost of revenue from 2003 to later periods. We have not consulted with Ernst & Young LLP with regard to the basis for those restatements. As described below, our 2003 financial statements as presented in this prospectus have been audited by PricewaterhouseCoopers LLP and the 2002 financial statements as presented in this prospectus are unaudited.

Also on April 20, 2005, our board of directors appointed PricewaterhouseCoopers LLP as our new independent registered public accounting firm for the fiscal year ended December 31, 2005 and engaged PricewaterhouseCoopers LLP to conduct an audit of our consolidated financial statements for the year ended December 31, 2004. In connection with this audit, PricewaterhouseCoopers LLP also audited our restated 2003 financial statements.

We did not consult with PricewaterhouseCoopers LLP on any financial or accounting reporting matters before its appointment. PricewaterhouseCoopers LLP has reported on our consolidated financial statements for each of the fiscal years ended December 31, 2003, 2004, 2005 and 2006 included in this prospectus.

We delivered a copy of this disclosure to Ernst & Young LLP on October 12, 2007 and requested that Ernst & Young LLP furnish us with a letter addressed to the SEC stating whether or not it agrees with the above statements regarding Ernst & Young LLP. Attached to the registration statement of which this prospectus is a part, as Exhibit 16.1, is a copy of the letter of Ernst & Young LLP to the SEC dated October 15, 2007.

## BUSINESS

### Overview

Starent Networks is a leading provider of infrastructure hardware and software products and services that enable mobile operators to deliver multimedia services to their subscribers. We have created hardware and software products that provide core network functions and services, including access from a wide range of radio networks to the operator's packet core network. Our products and services also provide management of subscriber sessions moving between networks and application of billing and other session policies. Our products and services provide high performance and system intelligence by combining significant computing power, memory and traffic handling capabilities with a flexible, high availability operating system and other proprietary software. Our products integrate multiple network functions and services needed for the delivery of advanced multimedia services, such as video, Internet access, voice-over-IP, e-mail, mobile TV, photo sharing and gaming.

Consumers and professionals are increasingly using mobile phones and other multimedia handheld devices to stay connected to each other, to access the Internet, to utilize business applications and for entertainment. At the same time, mobile operators are experiencing declining profits from voice services and increasing competitive pressures. To address these changes, mobile operators are deploying next-generation wireless networks, such as third generation, or 3G, networks, that are capable of delivering high quality, mobile multimedia services to subscribers. In deploying these new networks, mobile operators are seeking packet core network products and services that can deliver higher performance and functionality than has been available from products repurposed from wireline applications.

We have developed our multimedia core network platforms, the ST16 and the ST40, and our proprietary software specifically to address the needs of packet-based mobile networks. Our products are designed to provide mobile operators with new revenue opportunities while also reducing their costs. Our products possess a high degree of system intelligence that allows a mobile operator to understand the details of each subscriber session, enabling individual subscriber management and network traffic flow control. Our products also offer high performance capabilities, such as high capacity, significant data processing rates and high transaction rates, which increase the efficiency of the network and enhance the mobile subscriber's experience. To increase reliability, our platforms employ hardware redundancy and high-availability software techniques. By integrating several network functions into a single element, we allow mobile operators to simplify their networks. We designed our products to be access independent in that they can function across a range of 2.5G, 3G and 4G mobile and wireless radio access networks.

We sell our hardware and software products to leading mobile operators around the world both directly and through OEMs, system integrators and distributors. We were founded in 2000 and our products were first used commercially by a mobile operator in the first quarter of 2003. Since 2003, our products have been deployed by over 60 mobile operators in 25 countries. We were profitable in fiscal years 2005 and 2006. In 2006, our revenues were \$94.4 million and our net income was \$3.6 million, including interest income of \$2.3 million. For the six months ended June 30, 2007 our revenues and net income were \$58.5 million and \$5.7 million, respectively. As of June 30, 2007, we had an accumulated deficit of \$99.8 million.

### Industry Background

Mobile operators today are experiencing some of the most dramatic changes to their business models since the advent of mobile communications. These changes are the result of increased competition among mobile operators, the decline in average revenue per subscriber from voice communications and the rapid increase in mobile subscriber demand for a wide range of multimedia services. To address each of these trends, mobile operators are dramatically increasing

the data services provided through their networks. For example, Verizon Wireless reported for the second quarter of 2007 that data revenues were up 70.3% over the prior year period, contributing \$1.8 billion, or 19% of all service revenue in the quarter. This trend is expected to continue. Strategy Analytics, an independent research firm, forecasts that data services will account for 24% of subscriber revenue by 2011. According to Strategy Analytics, global mobile data services revenue is expected to grow 15% annually over the next five years from \$106 billion in 2006 to \$200 billion in 2011.

Several factors are accelerating the growth of data-rich multimedia traffic on mobile wireless networks. The number of mobile subscribers worldwide continues to grow as established markets experience increases in subscriber penetration and developing countries adopt mobile communications more rapidly. According to Wireless Intelligence, an independent research firm, the number of worldwide mobile connections is expected to grow 50% from 2.7 billion in 2006 to 4 billion in 2010. Another factor is our increasingly mobile and interconnected society in which information is accessible and communications are available all the time regardless of location. Moreover, as individuals and enterprises become accustomed to increased access to multimedia services on the Internet, including video, music downloads, multimedia messaging and continuous information and news, there is an increasing desire to have mobile access to these services. Also contributing to the growth in traffic is the proliferation of mobile devices designed for multimedia services, such as smart phones, personal digital assistants, laptop computers and other handheld devices.

#### *The Evolution of Mobile Voice and Data Networks*

Mobile operators have been aggressively upgrading their networks in response to the demands created by the growth in voice and multimedia services. IDC, an independent research firm, estimates that capital expenditures in the global wireless infrastructure market in 2006 were more than \$46.5 billion. In particular, mobile operators have made significant investments in upgrading from 2G to 3G radio access technologies that can provide greater bandwidth needed to increase voice capacity and deliver high bandwidth data services.

The two principal radio access interfaces in use today are Code Division Multiple Access, or CDMA, which is used primarily in the United States and Asia, and Global System for Mobile Communications/Universal Mobile Telecommunications System, or GSM/UMTS, which is used in most markets around the world. CDMA mobile operators are currently upgrading to CDMA2000 1X, 1xEV-DO Rev. 0 and 1xEV-DO Rev. A, while GSM/UMTS operators are moving to High Speed Packet Access, or HSPA. Additionally, many operators are exploring more advanced fourth generation, or 4G, access technologies, such as Mobile WiMax and Long Term Evolution/System Architecture Evolution, or LTE/SAE.

In addition to upgrading the radio access portion of their networks, mobile operators are deploying packet-based technology to supplement or replace circuit-based technology. Traditional circuit networks, which were developed for voice communications, establish a dedicated circuit for each call. However, circuit networks are relatively inefficient and do not allow for high-bandwidth multimedia services. Packet networks split traffic into multiple pieces of data, or packets, that are routed over an Internet Protocol, or IP, network, eliminating the need to establish a dedicated circuit for each call or session. The use of a packet core network increases network efficiency and lowers operating costs, while also enabling an operator to deliver multimedia services. As more multimedia services are deployed, more traffic will flow over the packet network. Over time, we expect mobile operators will convert entirely to packet networks not only for data services but also for all voice communications.

The following diagram illustrates the flow of traffic in both circuit-based and packet-based mobile networks:

As mobile operators implement more multimedia services on their packet networks, they are looking to further standardize the delivery of these services. New core network architecture standards are being developed, such as IP Multimedia Subsystem, or IMS, and Multimedia Domain, or MMD. These standards will also be implemented by wireline operators. The implementation of these new delivery architecture standards by both mobile and wireline operators will provide an opportunity for fixed-mobile convergence, which is the ability of a subscriber to have a uniform service experience as they move between a mobile network, such as a 3G network, and a wireline or a fixed wireless network, such as WiFi. With the convergence of mobile and wireline networks, telecommunications operators will be able to provide services to users irrespective of their location, access technology and communications device.

*The Need for Intelligent and Robust Network Products and Services*

As mobile networks transition to next-generation access technologies and become increasingly packet-based, many mobile operators want their networks to be "intelligent." An intelligent network provides mobile operators with the ability to inspect data packets from individual transactions in great detail. This deep packet inspection allows the mobile operator to shape each subscriber session using quality of service, bandwidth allocation and traffic flow control. This ability to actively manage network traffic flows allows mobile operators to deliver a consistent experience as subscribers roam through a mobile network or move across different types of networks. In order to offer reliable and intelligent mobile networks that provide a high quality subscriber experience and are able to handle increasing amounts of network traffic, operators require infrastructure products and services that:

*Identify and manage individual communications sessions.* The network needs to be able to identify, manage and manipulate each subscriber session by applying policy and charging decisions based on the mobile operator's business model or subscriber policies.

*Handle significant traffic.* As multimedia services dramatically increase the volume of network traffic, networks must be capable of handling this traffic without diminishing the subscriber experience. This capability will require significant computing power and data processing rates.

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*Simplify the network.* As mobile operators provide an increasing number of services and capabilities, they will need to simplify their networks so they can limit the deployment of costly new equipment each time a new service or capability is added.

*Deliver quality of service, reliability and availability.* As mobile subscribers pay a premium for advanced multimedia services, they will demand that these advanced services be of high quality, reliable and available whenever the subscriber wants to access them.

*Support multiple radio access technologies and subscriber management.* As mobile networks evolve to include different access technologies, mobile operators need the ability to provide the same services regardless of access mode and to apply common subscriber management tools, such as billing and subscriber authentication, across multiple access networks.

*Are easy to upgrade.* As networks continue to evolve rapidly, operators must be able to easily and cost effectively integrate new access technologies and services with their existing networks and increase capacity.

Historically, mobile operators deploying packet networks have been required to retrofit network infrastructure hardware and software originally designed for wireline networks. These products have included repurposed network switches, routers and off-the-shelf enterprise servers, none of which are able to sufficiently satisfy the needs of mobile operators to deliver efficient and reliable multimedia services.

While routers and network switches are capable of forwarding packets of information, they lack the integrated processing power, memory and software needed to examine individual packets and apply defined business policies and subscriber services to them. To overcome these shortcomings, mobile operators typically connect the repurposed switches and routers with numerous enterprise servers in order to provide services such as deep packet inspection, virtual private networks and firewalls. These multi-element configurations require network traffic to make multiple hops through different networks and equipment for the additional services. This can cause network traffic delays and limit subscriber and network visibility. These delays result in slower transmission speeds, a lower quality experience for the subscriber and potentially lower service use. These delays also have a significant negative impact on real-time services, such as voice and streaming video.

These multi-element configurations can also increase network complexity, resulting in a product that is difficult and expensive to scale and often costly to operate. This complexity also makes the deployment of new network functions and addition of new subscriber services time-consuming and expensive because it often requires a new configuration. Additionally, the need for redundancy to improve service reliability further increases both the complexity and the cost of these multi-element configurations. Even with additional redundancy, the complexity of these systems creates multiple potential points of failure, and engineering a multi-element product that can handle the large volumes of traffic on a typical mobile operator's network can be difficult.

### **Our Solutions**

We have introduced new, "purpose-built" network infrastructure products comprised of both high-performance hardware and software that address the specific challenges faced by mobile operators in offering multimedia services. Our products fulfill a number of network functions that enable carriers to deliver multimedia services across a range of network architectures. Unlike repurposed multi-element configurations, our integrated products and services were designed specifically to provide the high capacity, data processing rates, computer processing capability and software required to meet the needs of mobile operators in offering packet-based multimedia services.

Our hardware and software products and services provide six key, integrated capabilities that create enhanced revenue opportunities and facilitate reduced costs for mobile operators:

*Intelligence to shape the subscriber experience.* Our products' system intelligence allows mobile operators to manage each subscriber session, which is critical for creating, delivering and charging for differentiated services, while enhancing the subscriber experience. Our products combine custom software with significant processing power and memory to conduct a detailed inspection of each subscriber session and to associate that session with a subscriber need, operator service requirement or operator business policy.

*High performance.* Our products improve the performance of a mobile operator's network by enhancing the network's capabilities and efficiencies. Our products are able to handle increasing amounts of network traffic to support a large number of subscribers on one platform. They also provide high bandwidth and data processing rates for improved traffic capacity and flow, which increases network efficiency and performance. In addition, the high call transaction rates provided by our products enhance the ability of our products to handle increasing amounts of network traffic, reduce unwanted delays in network traffic and allow the subscriber to have quick access to network services.

*Simple and flexible network architecture.* Our products allow mobile operators to integrate a number of network functions and enhanced services into a single hardware platform. In addition to providing network functions such as access, management of subscriber sessions moving between networks and application of billing and other session policies, our platforms are capable of integrating advanced services, such as enhanced charging and billing, firewall protection, security and content filtering. We refer to these services as in-line services. Traditionally such services would be deployed out of line from the session stream in a server farm elsewhere in the network. By integrating both network functions and in-line services, mobile operators can simplify the design of their networks, more rapidly deploy services and improve the flow of network traffic, while also reducing costs.