Starent Networks, Corp.
Form 10-Q
August 07, 2009
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2009

or

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

For the transition period from to

Commission File Number: 001-33511

STARENT NETWORKS, CORP.

(Exact name of registrant as specified in its charter)

Delaware	04-3527533
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

30 International Place

Tewksbury, MA 01876

(Address of principal executive offices) (zip code)

(978) 851-1100

(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ¨ Yes x No

As of August 3, 2009, there were 71,550,516 shares of the registrant s $0.001 par value per share common stock outstanding.

STARENT NETWORKS, CORP.

QUARTERLY REPORT ON FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2009

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PART I. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

STARENT NETWORKS, CORP.

CONDENSED CONSOLIDATED BALANCE SHEETS

(unaudited and in thousands, except share and per share data)

	June 30, 2009	December 31, 2008
Assets		
Current assets:		
Cash and cash equivalents	$ 389,913	$ 369,351
Accounts receivable	54,910	53,689
Inventories	50,446	48,734
Deferred tax assets, net	9,173	3,449
Prepaid expenses and other current assets	7,574	4,709
Total current assets	512,016	479,932
Property and equipment, net	36,258	29,632
Deferred tax assets, net	13,287	9,699
Other assets	8,975	8,011
Restricted cash	822	943
Total assets	$ 571,358	$ 528,217
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable	$ 9,361	$ 9,042
Accrued expenses and other current liabilities	8,369	8,164
Accrued payroll and related expenses	11,762	15,195
Accrued income taxes	10,922	1,945
Current portion of deferred revenue	139,604	141,726
Total current liabilities	180,018	176,072
Deferred revenue, net of current portion	6,995	10,959
Other long-term liabilities	2,842	2,985
Commitments and contingencies (Note 7)		
Stockholders equity:		
Preferred stock, $0.001 par value; 5,000,000 shares authorized and no shares outstanding		
Common stock, $0.001 par value; 250,000,000 shares authorized; 70,991,062 and 69,867,985 shares issued and outstanding at June 30, 2009 and December 31, 2008, respectively	71	70
Additional paid-in capital	387,002	371,655
Accumulated deficit	(5,570)	(33,524)
Total stockholders equity	381,503	338,201
Total liabilities and stockholders equity	$ 571,358	$ 528,217

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

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STARENT NETWORKS, CORP.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited and in thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Revenues:				
Product	$ 65,829	$ 52,160	$ 128,959	$ 101,047
Service	12,490	9,008	22,562	16,349
Total revenues	78,319	61,168	151,521	117,396
Cost of revenues:				
Product	9,843	9,497	19,611	18,546
Service	6,006	3,806	10,552	7,716
Total cost of revenues	15,849	13,303	30,163	26,262
Gross profit	62,470	47,865	121,358	91,134
Operating expenses:				
Research and development	16,549	12,500	30,586	24,843
Sales and marketing	16,864	16,173	33,332	35,024
General and administrative	6,691	5,931	13,377	11,087
Total operating expenses	40,104	34,604	77,295	70,954
Income from operations	22,366	13,261	44,063	20,180
Interest income	305	2,009	770	4,293
Foreign currency exchange gain (loss)	1,707	(148)	759	751
Other income (expense), net			(37)	
Income before income tax expense	24,378	15,122	45,555	25,224
Income tax expense	(9,202)	(1,346)	(17,601)	(1,795)
Net income	$ 15,176	$ 13,776	$ 27,954	$ 23,429
Net income per common share (Note 3):				
Basic	$ 0.21	$ 0.20	$ 0.40	$ 0.34
Diluted	$ 0.20	$ 0.19	$ 0.37	$ 0.32
Weighted-average shares outstanding used in computing net income per common share (Note 3):				
Basic	70,648	69,379	70,367	69,105

Diluted	75,841	74,407	75,214	74,372

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

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STARENT NETWORKS, CORP.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited and in thousands)

	Six Months Ended June 30, 2009	Six Months Ended June 30, 2008
Cash flows from operating activities:		
Net income	$ 27,954	$ 23,429
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	8,032	5,018
Share-based compensation	9,635	7,888
Loss on disposal of property and equipment	28	
Benefit from deferred income taxes, net	(9,319)	
Changes in operating assets and liabilities:		
Accounts receivable	(1,193)	17,146
Inventories	(1,683)	(11,875)
Prepaid expenses and other current assets	(2,738)	293
Other assets	40	(71)
Accounts payable	284	2,373
Accrued expenses and other current liabilities	(3,537)	(3,105)
Accrued income taxes	8,927	493
Deferred revenue	(6,180)	54,527
Net cash provided by operating activities	30,250	96,116
Cash flows from investing activities:		
Purchases of property and equipment	(14,720)	(11,215)
Proceeds from maturities of short-term investments		9,610
Investments in and advancements to unconsolidated companies	(1,000)	
Change in restricted cash	125	(130)
Net cash used in investing activities	(15,595)	(1,735)
Cash flows from financing activities:		
Proceeds from exercises of stock options	5,585	2,301
Additional expenses from public offerings		(87)
Net cash provided by financing activities	5,585	2,214
Effect of exchange rate changes on cash and cash equivalents	322	565
Net increase in cash and cash equivalents	20,562	97,160
Cash and cash equivalents, beginning of year	369,351	223,987
Cash and cash equivalents, end of year	$ 389,913	$ 321,147

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

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STARENT NETWORKS, CORP.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Overview

Business Description

Starent Networks, Corp. (Starent or the Company) was incorporated in Delaware on August 11, 2000 and is a leading provider of infrastructure hardware and software products and services that enable mobile operators to deliver multimedia services to their subscribers. The Company s products and services 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.

Basis of Presentation

The accompanying interim condensed consolidated financial statements have been prepared by the Company, are unaudited and, in the opinion of management, include all adjustments, consisting only of normal, recurring adjustments and accruals necessary for a fair statement of the Company s financial position at June 30, 2009, results of operations for the three and six months ended June 30, 2009 and 2008, and cash flows for the six months ended June 30, 2009 and 2008 in accordance with accounting principles generally accepted in the United States. Interim results are not necessarily indicative of results for any other interim period or a full year. The condensed consolidated balance sheet presented as of December 31, 2008 has been derived from the audited consolidated financial statements as of that date.

The condensed consolidated financial statements and notes are presented as permitted by Form 10-Q and do not contain all of the information that is included in the annual financial statements and notes of the Company. The condensed consolidated financial statements and notes presented herein should be read in conjunction with the financial statements and notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2008.

The Company has evaluated subsequent events through August 7, 2009, the date it filed its report on Form 10-Q for the quarter ended June 30, 2009 with the Securities and Exchange Commission (SEC), and has no material subsequent events to report.

Significant Estimates and Assumptions

The preparation of financial statements in conformity with accounting principles generally accepted (GAAP) in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the reporting periods. On an ongoing basis, the Company evaluates its estimates and judgments, including those related to revenue recognition, the realizable value of accounts receivable and inventories, valuing share-based compensation instruments, evaluating loss contingencies and valuation allowances for deferred tax assets. Actual amounts could differ from these estimates. Changes in estimates are recorded in the period in which they become known.

Reclassification

Certain prior year amounts related to the classification of foreign currency gains or losses within the operating cash flows section of the condensed consolidated statements of cash flows have been reclassified to conform to the current year presentation. These reclassifications had no impact on previously reported net cash provided by operating activities, results of operations, or any balance sheet captions.

Concentrations of Risk and Off-Balance-Sheet Risk

The Company has no significant off-balance-sheet risk such as foreign exchange contracts, option contracts or other foreign hedging arrangements. Financial instruments that potentially subject the Company to concentrations of credit risk are principally cash equivalents and accounts receivable. The Company s cash equivalents are principally maintained in a limited number of highly rated financial institutions and consisted primarily of money market funds.

The Company had two customers for the three months ended June 30, 2009 that each accounted for more than 10% of revenues and in the aggregate accounted for 85% of revenues. The Company had one customer for the six months ended June 30, 2009 that accounted for 74% of revenues. The Company had two customers for the three and six months ended June 30, 2008,

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respectively, that each accounted for more than 10% of revenues and in the aggregate accounted for 85% and 83% of revenues for each of the respective periods. At June 30, 2009, the Company had two customers that accounted for 51% of accounts receivable. At December 31, 2008, the Company had two customers that accounted for 76% of accounts receivable.

The Company relies on a single contract manufacturer to manufacture and assemble its products. The Company has no long-term supply arrangements with this manufacturer and accordingly no obligation exists for the manufacturer to supply products to the Company in specific quantities or within specific time frames.

In addition, certain of the components included in the Company s products are sourced from single or limited sources, and lead times for some of these components may be significant. The Company has no long-term contracts to purchase these components.

2. Share-Based Compensation

The Company accounts for share-based compensation in accordance with Statement of Financial Accounting Standard (SFAS) 123R, *Share-Based Payment*, which it adopted on January 1, 2006. SFAS 123R requires companies to expense the fair value of employee stock options and other forms of share-based compensation. 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, the Company will continue to apply Accounting Principles Board (APB) Opinion 25, *Accounting for Stock Issued to Employees*, and related interpretations in future periods to equity awards outstanding prior to the date of its adoption of SFAS 123R. The Company has elected to use the Black-Scholes option pricing model to determine the grant-date fair value of its share-based option awards, except in those situations where an alternative method is required. For restricted stock and restricted stock units, the quoted market price of our common stock at the time of grant is used to estimate the fair value. In accordance with SFAS 123R, the Company will recognize the compensation cost of share-based awards on a graded-vesting basis over the requisite service period of each award, which is generally the vesting period.

The fair value of options granted for the three and six months ended June 30, 2009 and 2008 was estimated at the date of grant using the following assumptions:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Risk-free interest rates	2.41%	3.26%	2.14 - 2.41%	3.01 - 3.26%
Expected dividend yield	0%	0%	0%	0%
Expected life	6.25 years	6.25 years	6.25 years	6.25 years
Expected volatility	59%	54%	58 - 59%	54 - 56%

The expected life was calculated based on the simplified method as permitted by the SEC s Staff Accounting Bulletin 110, *Share-Based Payment.* The Company currently uses the simplified method to estimate the expected term for share option grants as it does not have enough historical experience to provide a reasonable estimate due to the limited period that the Company s common stock has been publicly traded. In 2008, the Company modified its computation of expected volatility to base it on the combination of historical trading activity of the Company s common stock, the Company implied volatility, and an analysis of comparable companies from a representative peer group selected based on industry and market capitalization in order to derive an expected volatility. Prior to the modification, the computation of expected volatility was based on the historical volatility of comparable companies from a representative peer group selected based on industry and market capitalization. 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. In addition to the assumptions above, as required under SFAS 123R, management makes an estimate of expected forfeitures and is recognizing compensation costs only for those equity awards expected to vest.

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The Company s results for the periods below included share-based compensation expense classified in the following expense categories of the condensed consolidated statements of operations (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Share-based compensation included in:				
Cost of revenues	$ 545	$ 381	$ 893	$ 694
Total share-based compensation included in cost of revenues	545	381	893	694
Research and development	1,987	1,803	3,387	3,107
Sales and marketing	1,750	1,366	2,995	2,293
General and administrative	1,361	968	2,360	1,794
Total share-based compensation included in operating expenses	5,098	4,137	8,742	7,194
Total share-based compensation	$ 5,643	$ 4,518	$ 9,635	$ 7,888

3. Net Income per Common Share

Basic and diluted net income per common share is presented in conformity with SFAS 128, *Earnings per Share.* Basic net income per common share is computed by dividing net income by the weighted-average number of common shares outstanding during the period, excluding the dilutive effects of common stock equivalents. Common stock equivalents include stock options and restricted stock. Diluted net income per common share includes the dilutive effect of stock options and unvested restricted stock under the treasury stock method. The following table presents the calculation of basic and diluted net income per common share (in thousands, except per share data):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Net income	$ 15,176	$ 13,776	$ 27,954	$ 23,429
Weighted-average common shares outstanding - basic	70,648	69,379	70,367	69,105
Dilutive effect of stock options and unvested restricted stock	5,193	5,028	4,847	5,267
Weighted-average common shares outstanding - diluted	75,841	74,407	75,214	74,372
Net income per common share:				
Basic	$ 0.21	$ 0.20	$ 0.40	$ 0.34
Diluted	$ 0.20	$ 0.19	$ 0.37	$ 0.32

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The following outstanding options and unvested restricted common stock subject to repurchase were excluded from the computation of diluted net income per common share for the periods presented as their effect would have been antidilutive (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Options to purchase common stock and unvested restricted common stock subject to repurchase	1,534	2,913	1,875	2,151

4. Fair Value Measurements

On January 1, 2008, the Company adopted the provisions of SFAS 157 (SFAS 157), *Fair Value Measurements,* for its financial assets and liabilities measured at fair value on a recurring basis. On January 1, 2009, as permitted by the Financial Accounting Standards Board (FASB) Staff Position No. SFAS 157-2, *Effective Date of FASB Statement No. 157*, the Company adopted the remaining provisions of SFAS 157 for all non-financial assets and non-financial liabilities that are recognized or disclosed at fair value in the financial statements on a non-recurring basis. The adoption of this accounting pronouncement did not have a material effect on the Company s consolidated financial statements for financial and non-financial assets and liabilities and any other assets and liabilities carried at fair value.

SFAS 157 provides a framework for measuring fair value under GAAP in the United States and requires expanded disclosures regarding fair value measurements. SFAS 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. SFAS 157 also establishes a fair value hierarchy that requires an entity to maximize the use of observable inputs, where available, and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities. At June 30, 2009 and December 31, 2008, the Company s Level 1 assets and liabilities included the Company s money market funds included in cash and cash equivalents.

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. At June 30, 2009 and December 31, 2008, the Company had no Level 2 assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. At June 30, 2009 and December 31, 2008, the Company had no Level 3 assets or liabilities.

At June 30, 2009 and December 31, 2008, the Company s financial assets and liabilities that were measured at fair value on a recurring basis included money market funds of $349.6 million and $348.2 million, respectively. The money market funds were Level 1 financial assets. The Company did not have any non-financial assets or liabilities that were measured or disclosed at fair value as of June 30, 2009. As required by SFAS 157, assets and liabilities measured at fair value are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Company s assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

The carrying amounts reflected in the consolidated balance sheets for accounts receivable, other current assets, accounts payable, and accrued expenses and other current liabilities approximate fair values due to their short-term maturities.

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5. Inventories

Inventories principally include the cost of raw materials and subassemblies, the cost of third-party contract manufacturers and cost of sales deferred until such time as related revenue is recognized. Deferred costs of sales are included as a component of finished goods. Inventories consisted of the following (in thousands):

	June 30, 2009	December 31, 2008
Raw materials	$ 1,726	$ 2,656
Work in process	6,712	7,545
Finished goods	42,008	38,533
	$ 50,446	$ 48,734

6. Income Taxes

The Company s effective income tax rate was 37.7% and 38.6% for the three and six months ended June 30, 2009, respectively. The Company s effective income tax rate was 8.9% and 7.1% for the three and six months ended June 30, 2008, respectively. The effective income tax rate is based upon the estimated income for the year, the estimated composition of the income in different jurisdictions and adjustments, if any, in the applicable quarterly periods for potential tax consequences, benefits, resolution of tax audits or other tax contingencies. For the three and six months ended June 30, 2009, the effective income tax rate varied from the U.S. federal statutory tax rate of 35% primarily due to the effects of nondeductible share-based compensation and state income taxes, both partially offset by federal and state R&D tax credits. The tax rate in the first six months of 2009 was nearer the statutory tax rate than in the same period of 2008, due to the Company reversing the full valuation allowance recorded against its deferred tax assets in the third quarter of 2008. The Company s income tax provision for the three and six months ended June 30, 2008 consisted primarily of taxes owed in relation to income generated by its foreign subsidiaries. The federal and state provision for that period included amounts in relation to the Company s income generated in the U.S., reduced by the utilization of available net operating loss (NOL) carryforwards and tax credits that were recorded on the balance sheet with a full valuation allowance prior to their utilization.

7. Litigation

The Company is presently defending two lawsuits brought against it by UTStarcom, Inc. In February 2005, UTStarcom filed a complaint against the Company in the United States District Court for the Northern District of California seeking unspecified damages and injunctive relief. The complaint alleges infringement by the Company of UTStarcom s U.S. Patent No. 6,829,473, entitled Roaming and Hand-Off Support for Prepaid Billing for Wireless Data Networks, which the Company refers to as the 473 patent. In May 2005, the Company answered the complaint, denied the infringement allegations contained in the complaint, and filed counterclaims against UTStarcom seeking a declaratory judgment that the Company did not infringe the 473 patent and that the 473 patent was invalid and unenforceable. In July 2005, the Company filed an amended answer and counterclaims to the 473 patent complaint. In December 2006, UTStarcom filed a reissue patent application relating to the 473 patent. In January 2007, by agreement of the parties, the District Court stayed the case pending the outcome of UTStarcom s reissue application relating to the 473 patent. In June 2007, the Company filed a request for *inter partes* re-examination of all claims of the 473 patent with the United States Patent and Trademark Office on sixteen different grounds. In August 2007, the Patent and Trademark Office granted the Company s request for *inter partes* re-examination of all claims on all sixteen grounds. In November 2007, the Patent and Trademark Office merged the reissue and re-examination proceedings. A first office action was issued on December 22, 2008, and responses to the office action have been submitted. The Company believes that it has meritorious defenses against any resulting reissued patent, and the Company is prepared to vigorously defend the 473 patent case through trial.

In May 2007, UTStarcom filed an additional complaint against the Company and a number of its 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 the Company s patents and three of its patent applications. The complaint contains allegations, among others, that a number of former employees of a business unit UTStarcom acquired, who subsequently worked for the Company, took UTStarcom s trade secrets with them and improperly used those trade secrets to develop, manufacture and market the Company s 3G wireless products, and that such products incorporate various UTStarcom confidential technical information, including UTStarcom s proprietary virtual private network and EV-DO features. UTStarcom further alleges that the Company has disclosed UTStarcom s trade secrets in one of its patents and three of its patent applications, and that this patent and these patent applications legally belong to UTStarcom based on the inventors previous work at the business unit acquired by

UTStarcom. In August 2007, the Company and the current and former employee defendants filed their answers to the complaint. The Company also filed counterclaims for tortious interference with prospective economic advantage, malicious prosecution, a

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declaration that the patents-in-suit are invalid and not infringed, and a declaration that one of the patents-in-suit is unenforceable due to inequitable conduct. In December 2007, UTStarcom filed an amendment to the complaint, which added new claims for declaration of ownership of four more of the Company s patent applications, copyright infringement, breach of restrictive covenants against the employee and former employee defendants, and aiding and abetting the employee and former employee defendants breaches of the duty of loyalty and the employment agreements. The amendment to the complaint also added another employee as a defendant. On January 4, 2008, the Company filed a motion to dismiss, or in the alternative for a more definite statement regarding, the trade secret, copyright, breaches of restrictive covenants, and aiding and abetting claims of the amendment to the complaint. UTStarcom filed its opposition to this motion on January 22, 2008, and the Company filed its reply on January 29, 2008. On May 20, 2008 the Court granted the Company s motion, in part, and ordered UTStarcom to provide a more definite statement of its claims. On May 30, 2008, UTStarcom filed a Third Amended Complaint. On June 9, 2008, the Company moved to dismiss the trade secret, copyright, breaches of restrictive covenants, and aiding and abetting claims (Counts I, VI, and VIII-XV) of the Third Amended Complaint, for failure to comply with the Court s order to provide a more definite statement of those claims. On July 23, 2008, the Court granted the Company s motion and dismissed those claims. On August 1, 2008, UTStarcom filed a Motion for Leave to Amend the Complaint to Provide a More Definite Statement and Clarification of the 7/23 Order. On August 11, 2008, the Court granted UTStarcom leave to file a Fourth Amended Complaint. UTStarcom filed a Fourth Amended Complaint on August 27, 2008. In addition, on August 26, 2008, the Company filed a motion for summary judgment of noninfringement of U.S. Patent No. 7,173,905, which has been fully briefed. On August 27, 2008, UTStarcom filed a motion to dismiss Starent s third, fourth, and fifth counterclaims for unenforceability of the asserted patents, tortious interference with prospective economic advantage, and malicious prosecution, respectively.

The Company filed a motion to strike and dismiss the Fourth Amended Complaint on September 15, 2008. The Court granted the Company s motion to strike the Fourth Amended Complaint on September 24, 2008, and, on the same day, granted UTStarcom leave to re-file the version of the Fourth Amended Complaint which was previously attached as an exhibit to its motion for leave to amend the complaint filed on August 1, 2008. UTStarcom re-filed this version of its Fourth Amended Complaint on September 25, 2008. The Company filed a motion to dismiss certain counts of UTStarcom s latest Fourth Amended Complaint on October 14, 2008. On December 5, 2008, the Court granted UTStarcom s motion to dismiss in part, dismissing the Company s counterclaim for malicious prosecution and denying UTStarcom s motion to dismiss the Company s third and fourth counterclaims for unenforceability of the asserted patents and tortious interference with prospective economic advantage. On January 6, 2009, the Company moved to amend its counterclaims to add a claim for trade secret misappropriation against UTStarcom. The Court granted this motion, and UTStarcom answered the counterclaim on January 26, 2009. On March 20, 2009, the Company filed a motion for summary judgment on UTStarcom s copyright count. On March 24, 2009, the Court granted, in-part, the Company s and individual defendants motion to dismiss certain counts of UTStarcom s Fourth Amended Complaint, dismissing nine of UTStarcom s counts, including its counts for declaration of ownership of seven patent applications and one patent, breach of restrictive covenants prohibiting disclosure of confidential and proprietary trade secret information, breach of restrictive covenants prohibiting solicitation of Carrier Unit employees, breach of restrictive covenants prohibiting solicitation of Carrier Unit customers, breach of restrictive covenants concerning the assignment of inventions, breach of the duty of loyalty, inducement of the breach of the duty of loyalty, inducement of the breach of the employment agreements, and conspiracy to misappropriate trade secrets. The Court also dismissed, in part, UTStarcom s count for intentional interference with UTStarcom s business relations. The Court denied the Company s motion to dismiss UTStarcom s trade secret count, determining that the allegations were sufficient at the pleading stage. On April 7, 2009, UTStarcom filed a motion to reconsider the Court s dismissal of certain counts, which motion was denied by the Court on April 20, 2009. On April 21, the Company answered the Fourth Amended Complaint, and re-asserted its counterclaims. On May 22, 2009, the Company filed a motion for summary judgment of noninfringement of U.S. Patent No. 6,684,256. On June 26, 2009, the Company filed a motion for summary judgment of noninfringement of U.S. Patent No. 6,765,900. UTSI s responses to those motions are due September 4, 2009 and September 9, 2009, respectively. On June 10, 2009, the parties stipulated to a dismissal, without prejudice, of all remaining claims against fifteen of the individual defendants, and UT Starcom s claim for intentional interference against the Company. On July 10, 2009, the parties stipulated to a dismissal, with prejudice, of UTSI s copyright claim against the Company.

Discovery is proceeding. No trial date has been set. In this lawsuit, UTStarcom seeks unspecified monetary damages, punitive damages, injunctive relief, findings of misappropriation of trade secrets, patent infringement and copyright infringement, costs and attorneys fees. The Company believes it has meritorious defenses to each of UTStarcom s claims in this lawsuit and it is prepared to vigorously defend the lawsuit.

In addition, the Company is subject to other legal proceedings, claims and litigation arising in the ordinary course of business. Defending lawsuits requires significant management attention and financial resources and the outcome of any litigation, including the matters described above, is inherently uncertain. The Company does not, however, currently expect that the ultimate costs to resolve pending matters will have a material adverse effect on its consolidated financial position, results of operations or cash flows.

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8. Business Segments

SFAS 131, *Disclosures About Segments of an Enterprise and Related Information*, establishes standards for reporting information about operating segments in annual financial statements and requires selected information of segments to be presented in financial reports issued to stockholders. Operating segments are defined as components of an enterprise about which separate financial information is available and that is evaluated regularly by the chief operating decision maker, or decision making group, in determining how to allocate resources and assess performance. The Company s chief operating decision maker, as defined under SFAS 131, is the chief executive officer. The Company views its operations and manages its business as one operating segment. Revenue by geography is based on the billing address of the customer. The following tables set forth revenue and long-lived assets by geographic area (in thousands).

Revenues

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
United States and Canada	$ 66,319	$ 55,707	$ 136,278	$ 109,642
Japan	9,169	3,999	10,538	5,139
Korea	718	1,111	1,716	2,074
Rest of world	2,113	351	2,989	541
Total	$ 78,319	$ 61,168	$ 151,521	$ 117,396

Long-lived Assets

	June 30, 2009	December 31, 2008
United States	$ 27,861	$ 21,059
India	7,870	7,857
Rest of world	527	716
Total	$ 36,258	$ 29,632

9. Comprehensive Income

Comprehensive income consisted of the following (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Net income	$ 15,176	$ 13,776	$ 27,954	$ 23,429
Unrealized loss on short-term investments		(5)		(2)
Comprehensive income	$ 15,176	$ 13,771	$ 27,954	$ 23,427

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10. Recent Accounting Pronouncements

On January 1, 2009, the Company adopted FASB Staff Position (FSP) 157-2, *Effective Date of FASB Statement No. 157*. FSP 157-2 delayed the effective date of SFAS 157, *Fair Value Measurement,* for all non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually), until the beginning of the first quarter of fiscal 2009. The adoption of FSP 157-2 on January 1, 2009 did not have a material impact on the Company s consolidated financial statements.

On January 1, 2009, the Company adopted FSP EITF 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities*. This FSP provides that unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings per share pursuant to the two-class method. Upon adoption, a company is required to retrospectively adjust its earnings per share data (including any amounts related to interim periods, summaries of earnings and selected financial data) to conform to the provisions in this FSP. The adoption of FSP EITF 03-6-1 did not have a material impact on the Company s consolidated financial statements.

On January 1, 2009, SFAS 141 (revised 2007), *Business Combinations* (SFAS 141R) became effective for the Company. This statement significantly changes the accounting for business combinations in a number of areas including the treatment of contingent consideration, contingencies, acquisition costs, in process research and development and restructuring costs. In addition, under this statement, changes in deferred tax asset valuation allowances and acquired income tax uncertainties in a business combination after the measurement period will impact income tax expense. SFAS 141R may have a material impact on the Company s consolidated financial statements if or when it enters into a business combination.

On January 1, 2009, SFAS 160, *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51* became effective for the Company. This statement changes the accounting and reporting for minority interests, which will be recharacterized as noncontrolling interests and classified as a component of equity. This new consolidation method significantly changes the accounting for transactions with minority interest holders. The adoption of SFAS 160 did not have an impact on the Company s consolidated financial statements.

In June 2009, the Company adopted FSP FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments*. This FSP amends SFAS 107, *Disclosures about Fair Value of Financial Instruments*, to require disclosures about fair value of financial instruments in interim as well as in annual financial statements. This FSP also amends APB 28, *Interim Financial Reporting*, to require those disclosures in all interim financial statements. The adoption of FSP FAS 107-1 and APB 28-1 did not have a material impact on the Company s consolidated financial statements.

In June 2009, FSP FAS 157-4, *Determining Whether a Market Is Not Active and a Transaction Is Not Distressed,* became effective for the Company. FSP FAS 157-4 provides guidelines for making fair value measurements more consistent with the principles presented in SFAS 157, *Fair Value Measurement*. FSP FAS 157-4 provides additional authoritative guidance in determining whether a market is active or inactive and whether a transaction is distressed, is applicable to all assets and liabilities (i.e., financial and nonfinancial) and will require enhanced disclosures. FSP FAS 157-4 did not have an impact on the Company s consolidated financial statements.

In June 2009, FSP FAS 115-2 and FSP FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments,* became effective for the Company. FSP FAS 115-2 and FSP FAS 124-2 amends the other-than-temporary impairment guidance for debt and equity securities. The adoption of FSP FAS 115-2 and FSP FAS 124-2 did not have an impact on the Company s consolidated financial statements.

In June 2009, the Company adopted SFAS No. 165, *Subsequent Events* (SFAS 165). SFAS 165 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. The disclosures required by SFAS 165 are reflected in Note 1 of the Company s financial statements.

In June 2009, the FASB issued SFAS 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles, a replacement of SFAS No. 162*. The Codification will become effective for the Company for interim and annual periods ending after September 15, 2009. The Codification does not change U.S. GAAP, but combines all authoritative standards, such as those issued by the FASB, AICPA and EITF, into a comprehensive, topically organized online database. The Codification is expected to become the single source of authoritative U.S. GAAP applicable for all non-governmental entities, except for rules and interpretive releases of the SEC.

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

Cautionary Statement

This Quarterly Report on Form 10-Q, including the information incorporated by reference herein, contains, in addition to historical information, forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements are based on our current expectations, assumptions, estimates and projections regarding our business and industry, and we do not undertake an obligation to update our forward-looking statements to reflect future events or circumstances. We may, in some cases, use words such as project, believe, anticipate, plan, expect, estimate, intend, continue, should, would, could, potentially, will, may or similar words and expressions that convey uncertainty of future events or outcomes to identify these forward-looking statements. Forward-looking statements in this Quarterly Report on Form 10-Q may include statements about:

- our ability to attract and retain customers;
- our financial performance;
- our development activities;
- *the advantages of our technology as compared to that of others;*
- *our ability to establish and maintain intellectual property rights;*
- our ability to retain and hire necessary employees and appropriately staff our operations;
- our ability to manage growth, both in the United States and internationally;
- the spending of our proceeds from public offerings of our common stock; and
- our cash needs.

The outcome of the events described in these forward-looking statements is subject to known and unknown risks, uncertainties and other factors, including the factors set forth in Part II Item 1A Risk Factors in this Quarterly Report on Form 10-Q, that could cause actual results to differ materially from the results anticipated by these forward-looking statements. You should read these factors and the risks described in other documents that we file from time to time with the Securities and Exchange Commission, or SEC, in conjunction with the unaudited condensed consolidated financial statements and related notes included elsewhere in this Quarterly Report on Form 10-Q and in the audited consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2008.

References to Starent Networks, Corp. , registrant , we , us , our and similar pronouns refer to Starent Networks, Corp. and its consolidated subsidiaries.

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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 mobile 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 or planning to deploy next-generation wireless networks, such as third generation and fourth generation, or 3G/4G, 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 hardware 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 so they can function across a range of 2.5G, 3G and 4G mobile and wireless radio access networks.

We sell our products and services to mobile operators around the world both directly and indirectly through our relationships with original equipment manufacturers, or 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 100 mobile operators in over 45 countries.

We maintain our corporate headquarters in Tewksbury, Massachusetts, and 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, 2009, we had 917 employees worldwide. Our revenues for the year ended December 31, 2008, were $254.1 million and for the three and six months ended June 30, 2009 were $78.3 million and $151.5 million, respectively. Our net income for the year ended December 31, 2008 was $60.5 million and for the three and six months ended June 30, 2009 was $15.2 million and $28.0 million, respectively.

Revenues

Our revenues consist of both product revenues and service revenues. We derive product revenues from the sale of our hardware products and the licensing of our software. Service 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 will use a small amount of equipment for testing and trial purposes and, once testing is complete, will purchase 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.

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 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. These requirements often cause us to defer recognition of revenue for a significant period of time after shipment, as a consequence of certain features of our customer arrangements (such as customer acceptance provisions), as well as the requirement that we establish company-specific evidence of the fair values of our products and services.

The variability of our revenues directly impacts our operating results in any particular period since a significant portion of our operating costs, such as personnel costs, depreciation expense 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 as well as internal costs, such as salaries and benefits related to personnel, provisions for inventory obsolescence, related overhead and share-based compensation. 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, benefits and share-based compensation 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, the volume and costs of manufacturing our hardware products and the cost associated with implementing our products in our customer networks.

Operating Expenses

Our operating expenses consist primarily of personnel 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 reporting purposes: research and development, sales and marketing and general and administrative. The following is a brief description of the key types of expenses in each of these 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, consulting services, 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.

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

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Other Income and Expense Items

Interest Income

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

Foreign Currency Exchange Gain (Loss)

Foreign currency gain (loss) primarily consists of foreign currency transactions with international customers and our foreign subsidiaries. The functional currency of our foreign operations 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, with the exception of certain non-monetary items which are remeasured at historical rates. Revenues and expenses of these foreign subsidiaries are remeasured into U.S. dollars at the average rates in effect during the year.

Income Tax Expense

Our income tax expense consists of provisions for income taxes in both the United States and foreign jurisdictions. We provide for income taxes during interim periods based on the estimated effective tax rate for the full fiscal year and record certain discrete items in the period in which they occur, such as incremental tax deductions related to employee stock options as well as changes in tax position uncertainties.

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.

Our critical accounting policies are those that require application of management s most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods. Our critical accounting policies are described in the Management s Discussion and Analysis of Financial Condition and Results of Operations section included in our Annual Report on Form 10-K for the year ended December 31, 2008. There have been no significant changes to our critical accounting policies since December 31, 2008.

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Results of Operations

Revenues

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

	Three Months Ended June 30, 2009	Three Months Ended June 30, 2008	Period-to-Period Change $	Period-to-Period Change %	Six Months Ended June 30, 2009	Six Months Ended June 30, 2008	Period-to-Period Change $	Period-to-Period Change %
	(dollars in thousands)				(dollars in thousands)			
Revenues:								
Product	$ 65,829	$ 52,160	$ 13,669	26%	$ 128,959	$ 101,047	$ 27,912	28%
Percentage of revenues	*84%*	*85%*			*85%*	*86%*		
Service	12,490	9,008	3,482	39	22,562	16,349	6,213	38
Percentage of revenues	*16%*	*15%*			*15%*	*14%*		
Total revenues	$ 78,319	$ 61,168	$ 17,151	28%	$ 151,521	$ 117,396	$ 34,125	29%
Revenues by Customer Type:								
Direct	$ 65,262	$ 55,604	$ 9,658	17%	$ 135,467	$ 109,322	$ 26,145	24%
Percentage of revenues	*83%*	*91%*			*89%*	*93%*		
Indirect	13,057	5,564	7,493	135	16,054	8,074	7,980	99
Percentage of revenues	*17%*	*9%*			*11%*	*7%*		
Total revenues	$ 78,319	$ 61,168	$ 17,151	28%	$ 151,521	$ 117,396	$ 34,125	29%
Revenues by Geography:								
United States and Canada	$ 66,319	$ 55,707	$ 10,612	19%	$ 136,278	$ 109,642	$ 26,636	24%
Percentage of revenues	*85%*	*91%*			*90%*	*93%*		
Japan	9,169	3,999	5,170	129	10,538	5,139	5,399	105
Percentage of revenues	*12%*	*7%*			*7%*	*4%*		
Korea	718	1,111	(393)	(35)	1,716	2,074	(358)	(17)
Percentage of revenues	*1%*	*2%*			*1%*	*2%*		
Rest of world	2,113	351	1,762	502	2,989	541	2,448	452
Percentage of revenues	*3%*				*2%*			
Total revenues	$ 78,319	$ 61,168	$ 17,151	28%	$ 151,521	$ 117,396	$ 34,125	29%

Revenues increased $17.2 million, or 28%, during the three months ended June 30, 2009 compared to the same period in 2008, due to an increase in product revenues of $13.7 million and an increase in service revenues of $3.5 million. Product revenues, which include hardware and software, increased primarily due to product shipments in the United States and Canada for which we received customer acceptances and recognized revenue during the three months ended June 30, 2009 as compared to the same period in 2008. The $3.5 million increase in service revenues for the three months ended June 30, 2009 compared to the same period in 2008 was due to an increase in the amount of our products installed at mobile operators, which is generally the basis of maintenance and service fees. Direct revenues increased $9.7 million, or 17%, primarily due to increased sales to existing customers. Indirect revenues increased $7.5 million, or 135%, primarily due to increased sales to an existing customer in Japan.

Revenues increased $34.1 million, or 29%, during the six months ended June 30, 2009 compared to the same period in 2008, due to an increase in product revenues of $27.9 million and an increase in service revenues of $6.2 million. Product revenues, which include hardware and software, increased primarily due to product shipments in the United States and Canada for which we received customer acceptances and recognized revenue during the six months ended June 30, 2009 as compared to the same period in 2008. The $6.2 million increase in service revenues for the six months ended June 30, 2009 compared to the same period in 2008 was due to an increase in the amount of our products installed at mobile operators. Direct revenues increased $26.1 million, or 24%, primarily due to increased sales to existing customers. Indirect revenues increased $8.0 million, or 99%, as described above.

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Cost of Revenues and Gross Profit

The following table sets forth our cost of revenues and gross profit.

	Three Months Ended June 30,		Period-to-Period Change		Six Months Ended June 30,		Period-to-Period Change	
	2009	2008	$	%	2009	2008	$	%
	(dollars in thousands)							
Cost of revenues:								
Product	$ 9,843	$ 9,497	$ 346	4%	$ 19,611	$ 18,546	$ 1,065	6%
Percentage of related revenues	*15%*	*18%*			*15%*	*18%*		
Service	6,006	3,806	2,200	58	10,552	7,716	2,836	37
Percentage of related revenues	*48%*	*42%*			*47%*	*47%*		
Total cost of revenues	$ 15,849	$ 13,303	$ 2,546	19%	$ 30,163	$ 26,262	$ 3,901	15%
Percentage of revenues	*20%*	*22%*			*20%*	*22%*		
Gross profit:								
Product	$ 55,986	$ 42,663	$ 13,323	31%	$ 109,348	$ 82,501	$ 26,847	33%
Product gross margin	*85%*	*82%*			*85%*	*82%*		
Service	6,484	5,202	1,282	25	12,010	8,633	3,377	39
Service gross margin	*52%*	*58%*			*53%*	*53%*		
Total gross profit	$ 62,470	$ 47,865	$ 14,605	31%	$ 121,358	$ 91,134	$ 30,224	33%
Gross margin	*80%*	*78%*			*80%*	*78%*		

Product gross margin increased three percentage points to 85% during the three months ended June 30, 2009 as compared to the same period in 2008 due primarily to a higher proportion of software revenue relative to the mix of hardware and software sales in the quarter compared to the prior year. We expect product gross margin to decrease somewhat during the remainder of 2009 due to the expansion of our customer base in certain geographic areas and the reduction of the percentage of software-only transactions in future periods.

The $2.2 million increase in cost of services for the three months ended June 30, 2009 as compared to the same period in 2008 was primarily due to higher personnel costs, depreciation expense and overhead costs primarily related to the addition of 47 customer support and training personnel. Service gross margin decreased six percentage points to 52% during the three months ended June 30, 2009 as compared to the same period in 2008. The decrease in margin was due to the increase in expenses described above. We anticipate cost of services will increase during the remainder of 2009 as we continue to expand our customer support organization geographically in future periods, which may result in modestly lower service gross margins.

Product gross margin increased three percentage points to 85% during the six months ended June 30, 2009 as compared to the same period in 2008 due primarily to a higher proportion of software revenue relative to the mix of hardware and software sales during the period compared to the prior year.

The $2.8 million increase in cost of services for the six months ended June 30, 2009 as compared to the same period in 2008 was primarily due to higher personnel costs, depreciation expense and overhead costs primarily related to the increased number of customer support and training employees. Service gross margin remained consistent during the six months ended June 30, 2009 as compared to the same period in 2008.

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Operating Expenses

The following table sets forth our operating expenses.

	Three Months Ended June 30,		Period-to-Period Change		Six Months Ended June 30,		Period-to-Period Change	
	2009	2008	$	%	2009	2008	$	%
	(dollars in thousands)							
Research and development	$ 16,549	$ 12,500	$ 4,049	32%	$ 30,586	$ 24,843	$ 5,743	23%
Percentage of revenues	*21%*	*20%*			*20%*	*21%*		
Sales and marketing	16,864	16,173	691	4	33,332	35,024	(1,692)	(5)
Percentage of revenues	*22%*	*26%*			*22%*	*30%*		
General and administrative	6,691	5,931	760	13	13,377	11,087	2,290	21
Percentage of revenues	*9%*	*10%*			*9%*	*9%*		
Total operating expenses	$ 40,104	$ 34,604	$ 5,500	16%	$ 77,295	$ 70,954	$ 6,341	9%
Percentage of revenues	*51%*	*57%*			*51%*	*60%*		

Our operating expenses consist primarily of personnel 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 professional fees, consulting, travel and depreciation expenses. Personnel costs are our largest expense, representing $24.4 million and $46.1 million, or 61% and 60%, of our total operating expenses for the three and six months ended June 30, 2009, respectively. For the three and six months ended June 30, 2008, personnel costs were $21.5 million and $45.5 million, or 62% and 64%, of our total operating expenses for each of the respective periods. The changes in personnel costs are described below.

Research and development

The following table sets forth our research and development expenses.

	Three Months Ended June 30,		Period-to-Period Change		Six Months Ended June 30,		Period-to-Period Change	
	2009	2008	$	%	2009	2008	$	%
	(dollars in thousands)							
Research and development	$ 16,549	$ 12,500	$ 4,049	32%	$ 30,586	$ 24,843	$ 5,743	23%
Percentage of revenues	*21%*	*20%*			*20%*	*21%*		

Research and development expenses increased $4.0 million, or 32%, during the three months ended June 30, 2009 as compared to the same period in 2008. The increase was primarily due to increases in cash compensation of $1.7 million, primarily related to the addition of 101 employees, of which 88 were located in India; and higher depreciation expense of $1.2 million related to our capital expenditures primarily utilized in our quality assurance and customer lab testing facilities. The increase in cash compensation was partially offset by the effect of exchange rate changes.

Research and development expenses increased $5.7 million, or 23%, during the six months ended June 30, 2009 as compared to the same period in 2008. The increase was primarily due to increases in cash compensation of $2.2 million and higher depreciation expense of $2.4 million, as described above.

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 that the amount of personnel costs and depreciation expense will increase during the remainder of 2009 as we continue to add engineering and quality assurance personnel and increase our test lab facilities.

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Sales and marketing

The following table sets forth our sales and marketing expenses.

	Three Months Ended June 30,		Period-to-Period Change		Six Months Ended June 30,		Period-to-Period Change	
	2009	**2008**	**$**	**%**	**2009**	**2008**	**$**	**%**
			(dollars in thousands)					
Sales and marketing	$ 16,864	$ 16,173	$ 691	4%	$ 33,332	$ 35,024	$ (1,692)	(5)%
Percentage of revenues	*22%*	*26%*			*22%*	*30%*		

Sales and marketing expenses increased $0.7 million, or 4%, for the three months ended June 30, 2009 as compared to the same period in 2008. This increase was primarily due to higher product demonstration expenses of $1.3 million, higher share-based compensation expense of $0.4 million and increases in other operating expenses. The increases in product demonstration and other operating expenses were primarily due to expansion of our sales activities geographically. The increase in share-based compensation was primarily due 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 increases in product demonstration, share-based compensation and other operating expenses were partially offset by decreases in cash compensation expense of $0.9 million and consulting expenses of $0.6 million. The decrease in cash compensation expense was due to changes in employee compensation plans, which led to lower commissions being earned during the three months ended June 30, 2009, offset by higher cash compensation primarily related to the addition of 70 employees. The decrease in consulting expense was due primarily to changes in arrangements we have with third party consultants whose fees are earned as we receive orders from specific customers.

Sales and marketing expenses decreased $1.7 million, or 5%, for the six months ended June 30, 2009 as compared to the same period in 2008. This decrease was primarily due to decreases in cash compensation expense of $4.8 million and consulting expense of $1.5 million, as described above. The decreases in compensation and consulting expenses were offset by higher travel expenses of $0.7 million due primarily to our employee additions; higher product demonstration expenses of $2.4 million; higher share-based compensation expense of $0.7 million and higher other operating expenses, as described above.

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 sales commission portion of sales and marketing personnel costs may vary significantly if our customer orders differ materially from the quotas established for our sales personnel.

General and administrative

The following table sets forth our general and administrative expenses.

	Three Months Ended June 30,		Period-to-Period Change		Six Months Ended June 30,		Period-to-Period Change	
	2009	**2008**	**$**	**%**	**2009**	**2008**	**$**	**%**
			(dollars in thousands)					
General and administrative	$ 6,691	$ 5,931	$ 760	13%	$ 13,377	$ 11,087	$ 2,290	21%
Percentage of revenues	*9%*	*10%*			*9%*	*9%*		

General and administrative expenses increased $0.8 million, or 13%, for the three months ended June 30 2009, but decreased as a percentage of revenues, as compared to the same period in 2008. The increase was primarily due to higher cash compensation of $1.1 million, an increase in share based-compensation of $0.4 million, and an increase in consulting expenses of $0.5 million. The increase in compensation expense was primarily related to the addition of 23 employees. The increase in share-based compensation was primarily due 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 increase in consulting expenses was primarily due to information

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technology projects. The increases in compensation expense, share-based compensation and consulting expense were partially offset by a decrease in professional fees of $1.1 million. The decrease in professional fees was primarily due to the receipt of an insurance reimbursement for legal fees associated with our pending litigation.

General and administrative expenses increased $2.3 million, or 21%, for the six months ended June 30, 2009 as compared to the same period in 2008. The increase was primarily due to higher cash compensation of $1.6 million, an increase in share-based compensation expense of $0.6 million, and an increase in consulting expenses of $0.9 million, as described above. The increases were partially offset by a decrease in professional fees of $0.5 million, as described above.

We expect general and administrative expense to increase in future periods as we invest in infrastructure to support continued growth. In addition, we expect to continue to incur costs associated with pending litigation discussed in Part II Item 1 Legal Proceedings .

Interest income

The following table sets forth our interest income.

	Three Months Ended June 30,		Period-to-Period Change		Six Months Ended June 30,		Period-to-Period Change	
	2009	**2008**	**$**	**%**	**2009**	**2008**	**$**	**%**
			(dollars in thousands)				**(dollars in thousands)**	
Interest income	$ 305	$ 2,009	$ (1,704)	(85)%	$ 770	$ 4,293	$ (3,523)	(82)%

Interest income consists of income generated from the investment of our cash balances. Interest income decreased $1.7 million and $3.5 million for the three and six months ended June 30, 2009 as compared to the same periods in 2008, due primarily to lower rates of return earned on our money market investments.

Foreign Currency Exchange Gain (Losses)

The following table sets forth our foreign currency exchange gain (losses).

	Three Months Ended June 30,		Period-to-Period Change		Six Months Ended June 30,		Period-to-Period Change	
	2009	**2008**	**$**	**%**	**2009**	**2008**	**$**	**%**
			(dollars in thousands)				**(dollars in thousands)**	
Foreign currency gains (losses)	$ 1,707	$ (148)	$ 1,855	(1,253)%	$ 759	$ 751	$ 8	1%

For the three months ended June 30, 2009, we recorded foreign currency gains of $1.7 million as compared to foreign currency losses of $0.1 million in the same period of 2008. The difference was primarily due to the weakening of the U.S. dollar that occurred during the second quarter of 2009 against foreign currencies in geographic locations in which we operate.

For the six months ended June 30, 2009 and 2008, we recorded foreign currency gains of $0.8 million for each of the respective periods.

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Income tax expense

The following table sets forth our income tax expense.

	Three Months Ended June 30,		Period-to-Period Change		Six Months Ended June 30,		Period-to-Period Change	
	2009	2008	$	%	2009	2008	$	%
	(dollars in thousands)				(dollars in thousands)			
Income tax expense	$ 9,202	$ 1,346	$ 7,856	584%	$ 17,601	$ 1,795	$ 15,806	881%

For the three and six months ended June 30, 2009, our effective tax rate was 37.7% and 38.6% on pre-tax income of $24.4 million and $45.6 million, respectively, as compared to an effective tax rate of 8.9% and 7.1% on pre-tax income of $15.1 million and $25.2 million for the three and six months ended June 30, 2008, respectively. For the three and six months ended June 30, 2009, our effective income tax rate differed from the federal statutory tax rate mainly due to the effects of nondeductible share-based compensation and state tax expense, both partially offset by federal and state R&D tax credits. Our effective tax rate for the three and six months ended June 30, 2009 was nearer the statutory tax rate than in the same periods of 2008, due to the reversal of our full valuation allowance recorded against our deferred tax assets in the third quarter of 2008.

Our income tax provision for the three and six months ended June 30, 2008 consisted primarily of taxes owed in relation to the income generated by our foreign subsidiaries. The federal and state provision for those periods included amounts in relation to our income generated in the U.S., reduced by the utilization of available net operating loss (NOL) carryforwards and tax credits that were recorded on the balance sheet with a full valuation allowance prior to their utilization.

We expect our annual effective income tax rate, exclusive of discrete items, to remain relatively consistent on a quarterly basis during the remainder of 2009.

Net income

The following table sets forth our net income.

	Three Months Ended June 30,		Period-to-Period Change		Six Months Ended June 30,		Period-to-Period Change	
	2009	2008	$	%	2009	2008	$	%
	(dollars in thousands)				(dollars in thousands)			
Net income	$ 15,176	$ 13,776	$ 1,400	10%	$ 27,954	$ 23,429	$ 4,525	19%

Net income increased $1.4 million and $4.5 million for the three and six months ended June 30, 2009, respectively, compared to the same periods in 2008 due to the items discussed above.

Liquidity and Capital Resources

Resources

We funded our operations from 2000 through 2004 primarily with net proceeds of issuances of convertible preferred stock of approximately $100.0 million. Since 2005, we have funded our operations principally with cash provided by operating activities, which was driven mainly by our revenue growth. In June and November 2007, we completed public offerings of our common stock, which raised approximately $204.1 million in net proceeds.

Cash and cash equivalents. Our cash and cash equivalents at June 30, 2009 of $389.9 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 $0.8 million and $0.9 million at June 30, 2009 and December 31, 2008, respectively, was not included in cash and cash equivalents and 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:

	Six Months Ended June 30,	
	2009	2008
	(dollars in thousands)	
Net cash provided by operating activities	$ 30,250	$ 96,116
Net cash used in investing activities	$ (15,595)	$ (1,735)
Net cash provided by financing activities	$ 5,585	$ 2,214

Operating activities. Cash from operating activities consisted 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.

The following table sets forth our cash provided by operating activities:

	Six Months Ended June 30,		
	2009	2008	Change
	(dollars in thousands)		
Received from:			
Customers	$ 144,109	$ 189,157	$ (45,048)
Interest	888	5,071	(4,183)
Payments for:			
Employee compensation	(48,176)	(47,413)	(763)
Inventories	(22,052)	(29,222)	7,170
Professional and consulting fees	(7,969)	(9,718)	1,749
Other operating expenses	(18,408)	(10,536)	(7,872)
Income taxes	(18,142)	(1,223)	(16,919)
	$ 30,250	$ 96,116	$ (65,866)

For the six months ended June 30, 2009, net cash provided by operating activities was $30.3 million as compared to $96.1 million for the same period in 2008. During the six months ended June 30 2009, we received $144.1 million from our customers, a decrease of $45.0 million compared to the same period in 2008. This decrease was due primarily to the timing of billing and collections of customer orders. The decrease in cash received from interest of $4.2 million was due primarily to lower rates of return earned on our money market investments. Our cash received from customers and interest was partially offset by cash payments related to employee compensation, inventories, professional and consulting fees, income taxes and various other operating expenses, as set forth in the table above. The increase in cash paid for employee compensation of $0.8 million was due primarily to increases in salary and related expenses, partially offset by lower commission payments, as discussed above. The decrease in cash paid for inventories of $7.2 million was due primarily to lower purchases of inventory. The decrease in cash paid for professional and consulting fees was due primarily to an insurance reimbursement for legal fees associated with our litigation defense. The increase in payments for other operating expenses of $7.9 million was due primarily to increases in travel, trial and demonstration equipment, rents and other expenses due to expansion of our operations and our increased number of employees. The increase in cash paid for income taxes of $16.9 million was due primarily to estimated payments related to federal and state income taxes due to our full utilization of substantially all of our remaining NOL carryforwards in 2008. We expect cash payments for income taxes to decrease modestly in future quarters of 2009.

Investing activities. Cash from investing activities consisted primarily of capital expenditures and proceeds from maturities of short-term investments associated with our investment balances. The $15.6 million of cash used in investing activities for the six months ended June 30, 2009 consisted primarily of $14.7 million of capital expenditures and a $1.0 million advance to an unconsolidated company, partially offset by a $0.1 million decrease of restricted cash associated with our facility lease agreements. The $1.7 million of cash used in investing activities for the six months ended June 30, 2008 consisted primarily of $11.2 million of capital expenditures, partially offset by $9.6 million of maturities of short-term investments. Purchases of property and equipment for the six months ended June 30, 2009 increased $3.5 million as compared with the same period in 2008, primarily due to an increase in R&D equipment purchases for quality assurance and customer lab testing facilities.

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Financing activities. Cash from financing activities consisted primarily of proceeds received from exercises of stock options and purchases of our restricted common stock. For the six months ended June 30, 2009, cash from financing activities increased by $3.4 million as compared to the same period in 2008.

At June 30, 2009 and December 31, 2008, 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 and our cash flows from operating activities will be sufficient to finance our planned growth, enhance our products and fund anticipated capital expenditures for the foreseeable future.

We may use the net proceeds from our public offerings for working capital and other general corporate purposes and 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 revenue 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 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 complete 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 and customer service, as well as for leasehold improvements and other general purposes to support our growth. Our capital expenditures totaled $14.7 million for the six months ended June 30, 2009. We expect capital expenditures to be approximately $25-30 million for 2009, primarily related to purchases of test equipment, equipment to support product development and customer service, leasehold improvements and other general purposes to support our growth.

Contractual obligations and requirements. As of June 30, 2009, our commitments under operating leases and purchase obligations were as set forth below.

	Total	Remainder of 2009	1 - 3 Years	4 - 5 Years	More than 5 Years
		(dollars in thousands)			
Operating leases	$ 6,206	$ 1,364	$ 3,559	$ 1,283	$
Purchase obligations	18,240	17,737	503		
Total	$ 24,446	$ 19,101	$ 4,062	$ 1,283	$

The table above does not reflect unrecognized tax benefits of $3.0 million, the timing of which is uncertain.

Off-Balance-Sheet Arrangements

In the normal course of business, we may enter into agreements with our customers which require us to secure performance bonds that guarantee our execution of certain obligations under the agreements. As of June 30, 2009, we had one bank guarantee in the amount of 3.0 million ($4.2 million). The bank guarantee is required to be renewed each year during the term of the agreement, which expires in July 2013. At the end of each calendar year, both parties to the agreement will discuss waiver of the bank guarantee.

We do not have any interests in entities referred to as variable interest entities, which includes special purpose entities and other structured finance entities.

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Recent Accounting Pronouncements

On January 1, 2009, we adopted FASB Staff Position, or FSP, 157-2, *Effective Date of FASB Statement No. 157*. FSP 157-2 delayed the effective date of SFAS 157, *Fair Value Measurement,* for all non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually), until the beginning of the first quarter of fiscal 2009. The adoption of FSP 157-2 on January 1, 2009 did not have a material impact on our consolidated financial statements.

On January 1, 2009, we adopted FSP EITF 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities*. This FSP provides that unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings per share pursuant to the two-class method. Upon adoption, a company is required to retrospectively adjust its earnings per share data (including any amounts related to interim periods, summaries of earnings and selected financial data) to conform to the provisions in this FSP. The adoption of FSP EITF 03-6-1 did not have a material impact on our consolidated financial statements.

On January 1, 2009, SFAS 141 (revised 2007), *Business Combinations* (SFAS 141R), became effective for us. This statement significantly changes the accounting for business combinations in a number of areas including the treatment of contingent consideration, contingencies, acquisition costs, in process research and development and restructuring costs. In addition, under this statement, changes in deferred tax asset valuation allowances and acquired income tax uncertainties in a business combination after the measurement period will impact income tax expense. SFAS 141R may have a material impact on our consolidated financial statements if or when we enter into a business combination.

On January 1, 2009, SFAS 160, *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51* became effective for us. This statement changes the accounting and reporting for minority interests, which will be recharacterized as noncontrolling interests and classified as a component of equity. This new consolidation method significantly changes the accounting for transactions with minority interest holders. The adoption of SFAS 160 did not have an impact on our consolidated financial statements.

In June 2009, we adopted FSP FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments*. This FSP amends SFAS 107, *Disclosures about Fair Value of Financial Instruments*, to require disclosures about fair value of financial instruments in interim as well as in annual financial statements. This FSP also amends APB 28, *Interim Financial Reporting*, to require those disclosures in all interim financial statements. The adoption of FSP FAS 107-1 and APB 28-1 did not have a material impact on our consolidated financial statements.

In June 2009, FSP FAS 157-4, *Determining Whether a Market Is Not Active and a Transaction Is Not Distressed,* became effective for us. FSP FAS 157-4 provides guidelines for making fair value measurements more consistent with the principles presented in SFAS 157, *Fair Value Measurement*. FSP FAS 157-4 provides additional authoritative guidance in determining whether a market is active or inactive and whether a transaction is distressed, is applicable to all assets and liabilities (i.e., financial and nonfinancial) and will require enhanced disclosures. FSP FAS 157-4 did not have an impact on our consolidated financial statements.

In June 2009, FSP FAS 115-2 and FSP FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments,* became effective for us. FSP FAS 115-2 and FSP FAS 124-2 amends the other-than-temporary impairment guidance for debt and equity securities. The adoption of FSP FAS 115-2 and FSP FAS 124-2 did not have an impact on our consolidated financial statements.

In June 2009, we adopted SFAS No. 165, *Subsequent Events*. SFAS 165 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. The disclosures required by SFAS 165 are reflected in Note 1 of our financial statements.

In June 2009, the FASB issued SFAS 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles, a replacement of SFAS No. 162*. The Codification will become effective for the Company for interim and annual periods ending after September 15, 2009. The Codification does not change U.S. generally accepted accounting principles, or GAAP, but combines all authoritative standards, such as those issued by the FASB, AICPA and EITF, into a comprehensive, topically organized online database. The Codification is expected to become the single source of authoritative U.S. GAAP applicable for all non-governmental entities, except for rules and interpretive releases of the SEC.

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ITEM 3. 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

Our international customer transactions are predominantly denominated in either U.S. dollars or Euros. Accordingly, we have exposure to changes in the exchange rates between the U.S. dollar and the Euro. We currently do not enter into foreign currency hedging transactions. In addition, 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, with the exception of certain non-monetary items which are remeasured at historical rates. Revenues and expenses of these foreign subsidiaries are remeasured into U.S. dollars at the average rates in effect during the period. Any differences resulting from the remeasurement of assets, liabilities and operations of these subsidiaries are recorded in foreign currency gain (loss) in our consolidated statements of operations. If the foreign currency exchange rates had fluctuated by 10% as of June 30, 2009 and December 31, 2008, our foreign exchange gain or loss would have fluctuated by approximately $3.1 million and $0.6 million, respectively.

Impact of Inflation

We believe that our revenue and results of operations have not been significantly impacted by inflation during the past three fiscal years. We do not believe that our revenue and results of operations will be significantly impacted by inflation in future periods.

Interest Rate Risk

At June 30, 2009, we had unrestricted cash and cash equivalents totaling $389.9 million. At December 31, 2008, we had unrestricted cash and cash equivalents totaling $369.4 million. These amounts were invested primarily in money market funds. In periods of financial market volatility, we may hold a greater proportion of our unrestricted cash and cash equivalents in money market funds that invest solely in government securities, which may result in lower yields on these balances. 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.

ITEM 4. CONTROLS AND PROCEDURES

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of June 30, 2009. The term disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, or Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Our management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of June 30, 2009, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the fiscal quarter ended June 30, 2009 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are presently defending two lawsuits brought against us by UTStarcom, Inc. In February 2005, UTStarcom filed a complaint against us in the United States District Court for the Northern District of California seeking unspecified damages and injunctive relief. The complaint alleges infringement by us of UTStarcom s U.S. Patent No. 6,829,473, entitled Roaming and Hand-Off Support for Prepaid Billing for Wireless Data Networks, which we refer to as the 473 patent. In May 2005, we answered the complaint, denied the infringement allegations contained in the complaint, and filed counterclaims against UTStarcom seeking a declaratory judgment that we did not infringe the 473 patent and that the 473 patent was invalid and unenforceable. In July 2005, we filed an amended answer and counterclaims to the 473 patent complaint. In December 2006, UTStarcom filed a reissue patent application relating to the 473 patent. In January 2007, by agreement of the parties, the District Court stayed the case pending the outcome of UTStarcom s reissue application relating to the 473 patent. In June 2007, we filed a request for *inter partes* re-examination of all claims of the 473 patent with the United States Patent and Trademark Office on sixteen different grounds. In August 2007, the Patent and Trademark Office granted our request for *inter partes* re-examination of all claims on all sixteen grounds. In November 2007, the Patent and Trademark Office merged the reissue and re-examination proceedings. A first office action was issued on December 22, 2008, and responses to the office action have been submitted. We believe that we have meritorious defenses against any resulting reissued patent, and we are prepared to vigorously defend the 473 patent case through trial.

In May 2007, UTStarcom filed an additional complaint 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 various 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 this patent and these patent applications legally belong to UTStarcom based on the inventors previous work at the business unit acquired by UTStarcom. In August 2007, we and the current and former employee defendants filed our answers to the complaint. We also filed counterclaims for tortious interference with prospective economic advantage, malicious prosecution, a declaration that the patents-in-suit are invalid and not infringed, and a declaration that one of the patents-in-suit is unenforceable due to inequitable conduct. In December 2007, UTStarcom filed an amendment to the complaint, which added new claims for declaration of ownership of four more of our patent applications, copyright infringement, breach of restrictive covenants against the employee and former employee defendants, and aiding and abetting the employee and former employee defendants breaches of the duty of loyalty and the employment agreements. The amendment to the complaint also added another employee as a defendant. On January 4, 2008, we filed a motion to dismiss, or in the alternative for a more definite statement regarding, the trade secret, copyright, breaches of restrictive covenants, and aiding and abetting claims of the amendment to the complaint. UTStarcom filed its opposition to our motion on January 22, 2008, and we filed our reply on January 29, 2008. On May 20, 2008, the Court granted our motion, in part, and ordered UTStarcom to provide a more definite statement of its claims. On May 30, 2008, UTStarcom filed a Third Amended Complaint. On June 9, 2008, we moved to dismiss the trade secret, copyright, breaches of restrictive covenants, and aiding and abetting claims (Counts I, VI, and VIII-XV) of the Third Amended Complaint, for failure to comply with the Court s order to provide a more definite statement of those claims. On July 23, 2008, the Court granted our motion and dismissed the claims that were the subject of the motion. On August 1, 2008, UTStarcom filed a Motion for Leave to Amend the Complaint to Provide a More Definite Statement and Clarification of the 7/23 Order. On August 11, 2008, the Court granted UTStarcom leave to file a Fourth Amended Complaint. UTStarcom filed a Fourth Amended Complaint on August 27, 2008. In addition, on August 26, 2008, we filed a motion for summary judgment of noninfringement of U.S. Patent No. 7,173,905, which has been fully briefed. On August 27, 2008, UTStarcom filed a motion to dismiss our third, fourth, and fifth counterclaims for unenforceability of the asserted patents, tortious interference with prospective economic advantage, and malicious prosecution, respectively.

We filed a motion to strike and dismiss the Fourth Amended Complaint on September 15, 2008. The Court granted our motion to strike the Fourth Amended Complaint on September 24, 2008, and, on the same day, granted UTStarcom leave to re-file the version of the Fourth Amended Complaint which was previously attached as an exhibit to its motion for leave to amend the complaint filed on August 1, 2008. UTStarcom re-filed this version of its Fourth Amended Complaint on September 25, 2008. We filed a motion to dismiss certain counts of UTStarcom s latest Fourth Amended Complaint on October 14, 2008. On

December 5, 2008, the Court granted UTStarcom s motion to dismiss in part, dismissing our counterclaim for malicious prosecution and denying UTStarcom s motion to dismiss our third and fourth counterclaims for unenforceability of the asserted patents and tortious interference with prospective economic advantage. On January 6, 2009, we moved to amend our counterclaims to add a claim for trade secret misappropriation against UTStarcom. The Court granted this motion, and UTStarcom answered the counterclaim on January 26, 2009. On March 20, 2009, we filed a motion for summary judgment on UTStarcom s copyright count. On March 24, 2009, the Court granted, in-part our and the individual defendants motion to dismiss certain counts of UTStarcom s Fourth Amended Complaint, dismissing nine of UTStarcom s counts, including counts for declaration of ownership of seven patent applications and one patent, breach of restrictive covenants prohibiting disclosure of confidential and proprietary trade secret information, breach of restrictive covenants prohibiting solicitation of Carrier Unit employees, breach of restrictive covenants prohibiting solicitation of Carrier Unit customers, breach of restrictive covenants concerning the assignment of inventions, breach of the duty of loyalty, inducement of the breach of the duty of loyalty, inducement of the breach of the employment agreements, and conspiracy to misappropriate trade secrets. The Court also dismissed, in part, UTStarcom s claim for intentional interference with UTStarcom s business relations. The Court denied our motion to dismiss UTStarcom s trade secret count, determining that the allegations were sufficient at the pleading stage. On April 7, 2009, UTStarcom filed a motion to reconsider the Court s dismissal of certain counts, which motion was denied by the Court on April 20, 2009. On April 21, we answered the Fourth Amended Complaint, and re-asserted our counterclaims. On May 22, 2009, we filed a motion for summary judgment of noninfringement of U.S. Patent No. 6,684,256. On June 26, 2009, we filed a motion for summary judgment of noninfringement of U.S. Patent No. 6,765,900. UTSI s responses to those motions are due September 4, 2009, and September 9, 2009, respectively. On June 10, 2009, the parties stipulated to a dismissal, without prejudice, of all remaining claims against fifteen of the individual defendants, and UT Starcom s claim for intentional interference against us. On July 10, 2009, the parties stipulated to a dismissal, with prejudice, of UTSI s copyright claim against us.

Discovery is proceeding. No trial date has been set. In this lawsuit, UTStarcom seeks unspecified monetary damages, punitive damages, injunctive relief, findings of misappropriation of trade secrets, patent infringement and copyright infringement, costs and attorneys fees. We believe we have meritorious defenses to each of UTStarcom s claims in this lawsuit and we are prepared to vigorously defend the lawsuit.

In addition, we are subject to other legal proceedings, claims and litigation arising in the ordinary course of business. Defending lawsuits requires significant management attention and financial resources and the outcome of any litigation, including the matters described above, is inherently uncertain. We do not, however, currently expect that the ultimate costs to resolve pending matters will have a material adverse effect on our consolidated financial position, results of operations or cash flows.

ITEM 1A. RISK FACTORS

These are risks and uncertainties that could cause actual results to differ materially from the results contemplated by the forward-looking statements contained in this Quarterly Report on Form 10-Q. Because of the these factors, as well as other variables affecting our operating results, past financial performance should not be considered as a reliable indicator of future performance and investors should not use historical trends to anticipate results or trends in future periods. These risks are not the only ones facing us. Please also see Cautionary Statement in Part I, Item 2 of this Quarterly Report on Form 10-Q. The following discussion highlights certain risks which may affect future operating results. These are the risks and uncertainties we believe are most important for our existing and potential stockholders to consider. Additional risks and uncertainties not presently known to us, which we currently deem immaterial or which are similar to those faced by other companies in our industry or business in general, may also impair our business operations. If any of the following risks or uncertainties actually occurs, our business, financial condition and operating results would likely suffer.

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.

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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;
- 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;
- costs related to litigation, claims and other contingencies;
- increases in our effective tax rate due to the use of substantially all of our accumulated net operating loss carryforwards in prior periods;
- fluctuations in exchange rates; 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. For example, for the six months ended June 30, 2009, we had one customer that accounted for 74% of our revenues. We had two customers for the six months ended June 30, 2008 that each accounted for more than 10% of our revenues and in the aggregate accounted for 83% 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. 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

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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
- 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.

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 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., Huawei Technologies Co., Ltd., LM Ericsson Telephone Co., and Nokia Siemens Networks B.V., 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 either 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

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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 relationships with a number of GSM/UMTS operators, 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. Our revenues depend in part on the effective performance of these distribution relationships. By utilizing 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 generally 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 could adversely affect our business, operating results and financial condition.

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 within 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.

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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 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 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 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 mobile network infrastructure. Once a mobile network operator has deployed 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.

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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 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. 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 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

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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 may adversely affect our ability to attract or retain personnel.

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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, 2009, approximately 64% of our employees were located outside of the United States, including 467 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;
- reduced protection for intellectual property rights in some countries;
- new and different sources of competition;
- internationalization of our products to meet local customs or the needs of local marketing organizations;
- compliance with multiple, conflicting, and changing laws and regulations, including employment, tax, trade, privacy, and data protection laws and regulations;
- laws and business practices, which may vary from country to country and may favor local competitors; 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.

Our operating results and cash flows are subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the British pound sterling, the Euro and the Indian rupee. These fluctuations could negatively affect our operating results and could cause our net income or loss to vary from quarter to quarter. We do not currently engage in currency hedging activities to limit the risk of exchange rate fluctuations.

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. 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.

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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.

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 $59.7 million in 2005 to $254.1 million in 2008, and $151.5 million for the six months ended June 30, 2009 and the number of our employees increased from 200 at the beginning of 2005 to 917 as of June 30, 2009. 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, in the United States and internationally; and

- provide adequate training and supervision to maintain high quality standards.

Failure to maintain effective internal controls over financial reporting and disclosure controls and procedures could adversely affect our business and the market price of our common stock, and impair our ability to timely file our SEC reports.

The Sarbanes-Oxley Act of 2002 requires, among other things, that we maintain effective internal control over financial reporting and disclosure controls and procedures. We 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 compliance with Section 404 will continue to require that we incur substantial expense and expend significant management time on compliance-related issues. 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.

Disruptions in financial markets may adversely impact availability and cost of credit and business and consumer spending patterns.

Disruptions in the financial markets have had and may continue to have an adverse effect on the U.S. and world economy, which could negatively impact business and consumer spending patterns. Current tightening of credit in financial markets also adversely affects the ability of our customers and suppliers to obtain financing for significant purchases and operations and could result in a decrease in or cancellation of orders for our products. In particular, the availability of financing may be critical to the expansion plans of mobile operators. Further, changes in employment and consumer spending patterns may slow the adoption of data-enabled wireless devices and reduce the growth of data traffic for mobile operators, which could result in delays or cancellations of upgrades and new purchases of our products. There is no assurance that government responses to the disruptions in the financial markets will restore business and consumer confidence, stabilize the markets or increase liquidity and the availability of credit.

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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.

We are subject to U.S. laws and regulations that prohibit certain practices that may be common in certain foreign countries in which we operate; failure to adhere to these laws and regulations could negatively affect our business and operating results.

Our international operations are subject to certain U.S. laws and regulations applicable to us, including the Foreign Corrupt Practices Act. Moreover, local laws and customs in many countries differ significantly from those in the United States. In many foreign countries, particularly in those with developing economies, it is common for others to engage in business practices that are prohibited by our internal policies and procedures or United States regulations applicable to us. Although we implement policies and procedures designed to ensure compliance with these laws and policies, there can be no assurance that all of our employees, contractors and agents will not take actions in violation of them. Violations of laws or key control policies by our employees, contractors or agents could result in financial reporting problems, fines, penalties, or prohibition on the importation or exportation of our products and could adversely affect our business and operating results.

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 continue 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

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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 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. 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 which, at present, includes violations of the Illinois Trade Secrets Act, infringement of patents assigned to UTStarcom, inducement of patent infringement, intentional interference with UTStarcom s business relations and copyright infringement. With respect to these claims, 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 seven of our patent applications. In this lawsuit, UTStarcom seeks unspecified monetary damages, punitive damages, injunctive relief, findings of misappropriation of trade secrets, patent infringement and copyright infringement, costs and attorneys fees. We intend to continue to vigorously defend ourselves in this litigation. 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 pay royalties on past or future sales of our ST16 or ST40 products, may force us to limit or cease development, manufacturing and sales of the ST16 and ST40, which are our only product platforms, and may require that key employees be transferred to other positions or functions, or temporarily prohibited from working for us. This could adversely affect our business, financial condition and results of operations.

We cannot assure you that in the future other third parties will not assert that our technology violates their intellectual property rights or that we will not be the subject of a material intellectual property dispute. Regardless of the merit of any particular claim that our technology violates the intellectual property rights of others, responding to such claims may require us to:

incur substantial expenses and expend significant management efforts;

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- pay damages;
- cease making, licensing or using products that are alleged to incorporate the intellectual property of others;
- enter into potentially unfavorable royalty or license agreements in order to obtain the right to use necessary technologies; and
- expend additional development resources to redesign our products.

We may also be required to indemnify customers, distributors or systems integrators for their use of the intellectual property associated with the current suit or for other third-party products that are incorporated into our products and that infringe the intellectual property rights of others. If we are unable to resolve our legal obligations by settling or paying an infringement claim or a related indemnification claim as described above, we may be required to refund amounts that we had received under the contractual arrangement with the customers, distributors or systems integrators.

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.

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

(b) Use of Proceeds from Public Offerings of Common Stock

In June 2007, we completed an initial public offering of common stock pursuant to a Registration Statement on Form S-1 (Registration No. 333-141092) which the SEC declared effective on June 5, 2007. Pursuant to the registration statement, we registered the offering and sale of an aggregate of 12,115,067 shares of our common stock, of which 10,580,226 shares were sold by us including 1,580,226 shares sold in connection with the underwriters option described below, and 1,534,841 shares were sold by certain stockholders, at a price of $12.00 per share. The underwriters exercised their option to purchase the additional 1,580,226 shares of our common stock at the initial public offering price of $12.00 per share on June 8, 2007 and the offering closed on June 11, 2007. The underwriters for the offering were Goldman, Sachs & Co., Lehman Brothers, J.P.Morgan and Thomas Weisel Partners LLC.

We raised a total of $127.0 million in gross proceeds from the initial public offering, or approximately $116.0 million in net proceeds after deducting underwriting discounts and commissions of $8.9 million and other estimated offering costs of approximately $2.1 million. The selling stockholders received a total of approximately $18.4 million in gross proceeds from the initial public offering or approximately $17.1 million of net proceeds after deducting the underwriting discounts. We have invested the remaining net proceeds in cash and cash equivalents, primarily money-market mutual funds. None of the remaining net proceeds were paid, directly or indirectly, to directors, officers, persons owning ten percent or more of our equity securities, or any of our other affiliates.

In October 2007, we completed a public offering of common stock pursuant to a Registration Statement on Form S-1 (Registration No. 333-146717) which the SEC declared effective on October 31, 2007. Pursuant to the registration statement, we registered the offering and sale of an aggregate of 8,000,000 shares of our common stock, of which 3,880,000 shares were sold by us and 4,120,000 shares were sold by certain stockholders, at a price of $24.00 per share. The underwriters for the offering were Goldman, Sachs & Co., Lehman Brothers, J.P.Morgan and Thomas Weisel Partners LLC.

We raised a total of $93.1 million in gross proceeds from the public offering, or approximately $88.1 million in net proceeds after deducting underwriting discounts and commissions of $4.4 million and other estimated offering costs. The selling stockholders received a total of approximately $98.9 million in gross proceeds from the public offering or approximately $94.2 million of net proceeds after deducting the underwriting discounts. We have invested the remaining net proceeds in cash and cash equivalents, primarily money-market mutual funds. None of the remaining net proceeds were paid, directly or indirectly, to directors, officers, persons owning ten percent or more of our equity securities, or any of our other affiliates.

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

We held our 2009 Annual Meeting of Stockholders on May 21, 2009. At the 2009 Annual Meeting, our stockholders elected two director nominees and ratified the appointment of PricewaterhouseCoopers LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2009.

At the 2009 Annual Meeting, our stockholders elected James A. Dolce, Jr. and Kenneth A. Goldman to serve as Class II directors until our 2012 annual meeting of stockholders and until their successors are elected and qualified. In addition to the election of Mr. Dolce and Mr. Goldman, our directors Edward T. Anderson, Timothy A. Barrows and Ashraf A. Dahod continue in office for terms ending in 2010 and our directors Sean M. Dalton and Matthew J. Desch continue in office for terms ending in 2011, in each case, until his successor is elected and qualified.

The matters acted upon at the 2009 Annual Meeting, and the voting tabulation for each matter, are as follows:

(1) To elect two Class II directors to our board of directors, each to serve for a term ending in 2012, or until his respective successor has been duly elected and qualified:

Nominees for Election as a Class II Director:	Votes For	Votes Withheld
James A. Dolce, Jr.	61,318,323	2,216,881
Kenneth A. Goldman	62,752,872	782,332

(2) To ratify the selection of PricewaterhouseCoopers LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2009, which matter was approved by a vote of 62,913,378 shares voting for, 568,636 shares voting against and 53,190 shares abstaining.

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ITEM 6. EXHIBITS

The following is an index of the exhibits included in this report:

Exhibit No.	Description
10.1	Form of Restricted Stock Unit Agreement, incorporated by reference to Exhibit 10.1 to the registrant s Current Report on Form 8-K, filed with the Securities and Exchange Commission on April 23, 2009.
10.2	Form of Executive Retention Agreement, incorporated by reference to Exhibit 10.1 to the registrant s Current Report on Form 8-K, filed with the Securities and Exchange Commission on June 11, 2009.
31.1	Certification of Chief Executive Officer, pursuant to Securities Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer, pursuant to Securities Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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SIGNATURES

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

STARENT NETWORKS, CORP.
(Registrant)

Date: August 7, 2009

By: /s/ ASHRAF M. DAHOD
Ashraf M. Dahod

President and Chief Executive Officer

(Principal Executive Officer)

Date: August 7, 2009

By: /s/ PAUL J. MILBURY
Paul J. Milbury

Vice President, Operations and

Chief Financial Officer

(Principal Financial Officer)

Date: August 7, 2009

By: /s/ GEORGE W. HALE
George W. Hale

Vice President, Finance and

Corporate Controller

(Principal Accounting Officer)