NextWave Wireless Inc.
Form 10-Q
November 07, 2008

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 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 September 27, 2008

OR

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

For the transition period from to

Commission file number 000-51958

NEXTWAVE WIRELESS INC.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**20-5361360** (IRS Employer Identification No.)
12670 High Bluff Drive, San Diego, California (Address of principal executive offices)	**92130** (Zip Code)

(858) 480-3100

(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. Yes (No o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer o	Accelerated filer x	Non-accelerated filer o	Smaller reporting company o
	(Do not check if a 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 o No (

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13, or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes (No o

As of October 30, 2008, there were approximately 103,091,858 shares of the Registrant's common stock outstanding.

TABLE OF CONTENTS

PART I. Financial Information

Item 1.	Financial Statements (Unaudited) Condensed Consolidated Balance Sheets
	Consolidated Statements of Operations
	Consolidated Statements of Cash Flows
	Notes to Unaudited Interim Consolidated Financial Statements
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations
Item 3.	Quantitative and Qualitative Disclosures about Market Risk
Item 4.	Controls and Procedures

PART II. Other Information

Item 1.	Legal Proceedings
Item 1A.	Risk Factors
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds
Item 3.	Defaults Upon Senior Securities
Item 4.	Submission of Matters to a Vote of Security Holders
Item 5.	Other Information
Item 6.	Exhibits

Signatures

Index to Exhibits

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PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

NEXTWAVE WIRELESS INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except par value data)

ASSETS	**ProForma September 27, 2008 (Note 1) (unaudited)**	**September 27, 2008 (unaudited)**	**December 29, 2007**
Current assets:			
Cash and cash equivalents	$ 94,966	$ 5,966	$ 47,634
Marketable securities	1,084	1,084	113,684
Restricted cash and marketable securities	60,913	60,913	—
Accounts receivable, net of allowance for doubtful accounts of $203 and $156, at September 27, 2008 and December 29, 2007, respectively	6,473	6,473	6,941
Deferred cost of revenues	2,739	2,739	3,515
Wireless spectrum assets held for sale	141,680	141,680	—
Assets of discontinued operations	44,074	44,074	249,689
Prepaid expenses and other current assets	6,039	6,039	5,536
Total current assets	357,968	268,968	426,999
Restricted cash	—	—	75,000
Wireless spectrum licenses, net	498,257	498,257	633,881
Goodwill	39,509	39,509	40,082
Other intangible assets, net	22,799	22,799	27,247
Property and equipment, net	23,725	23,725	29,773
Other noncurrent assets	18,115	7,115	25,756
Total assets	$ 960,373	$ 860,373	$ 1,258,738
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current liabilities:			
Accounts payable	$ 10,606	$ 10,606	$ 6,001
Accrued expenses	30,839	30,839	49,226
Current portion of long-term obligations	205,140	205,140	6,745
Deferred revenue	20,850	20,850	24,696
Accrued restructuring charges	1,851	1,851	—
Liabilities of discontinued operations	65,273	65,273	80,107
Other current liabilities	7,479	7,479	2,121
Total current liabilities	342,038	342,038	168,896
Deferred income tax liabilities	102,744	102,744	103,264
Long-term obligations, net of current portion	643,242	162,054	321,651
Accrued purchase consideration and stock bonuses payable	3,032	3,032	57,903
Other noncurrent liabilities	6,855	6,855	6,273
Total liabilities	1,097,911	616,723	657,987
Commitments and contingencies			
Redeemable Series A Senior Convertible Preferred Stock, $0.001 par value; 355 shares authorized; 0, 355 and 355 shares issued and outstanding at pro forma September 27, 2008 (unaudited),	—	393,988	371,986

September 27, 2008 (unaudited) and December 29, 2007, respectively; liquidation preference of $0, $397,592 and $375,811 at pro forma September 27, 2008 (unaudited), September 27, 2008 (unaudited) and December 29, 2007, respectively			
Stockholders' equity (deficit):			
Preferred stock, $0.001 par value; 25,000 shares authorized; 355 shares designated as Series A Senior Convertible Preferred Stock; no other shares issued or outstanding	—	—	—
Common stock, $0.001 par value; 400,000 shares authorized; 103,092, 103,092 and 92,667 shares issued and outstanding at pro forma September 27, 2008 (unaudited), September 27, 2008 (unaudited) and December 29, 2007, respectively	103	103	93

Additional paid-in-capital	733,880	721,080	686,918
Accumulated other comprehensive income	12,335	12,335	12,836
Accumulated deficit	(883,856)	(883,856)	(471,082)
Total stockholders' equity (deficit)	(137,538)	(150,338)	228,765
Total liabilities and stockholders' equity (deficit)	$ 960,373	$ 860,373	$ 1,258,738

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

NEXTWAVE WIRELESS INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

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

	Three Months Ended		**Nine Months Ended**	
	September 27, 2008	**September 29, 2007**	**September 27, 2008**	**September 29, 2007**
Technology licensing and service revenues	$ 18,207	$ 10,875	$ 51,468	$ 26,381
Operating expenses:				
Cost of technology licensing and service revenues	7,246	6,151	21,449	13,649
Engineering, research and development	22,969	20,377	64,882	54,454
Sales and marketing	4,669	3,799	16,694	10,606
General and administrative	20,155	22,040	64,263	55,019
Asset impairment charges	2,244	—	2,244	—
Restructuring charges	3,818	—	3,948	—
Purchased in-process research and development costs	—	—	—	860
Total operating expenses	61,101	52,367	173,480	134,588
Gain on sale of wireless spectrum licenses	19,317	—	19,317	—
Loss from operations	(23,577)	(41,492)	(102,695)	(108,207)
Other income (expense):				
Interest income	229	4,813	2,694	12,313
Interest expense	(12,045)	(11,710)	(45,821)	(34,048)
Other income (expense), net	(1,576)	(253)	(2,812)	(70)
Total other expense, net	(13,392)	(7,150)	(45,939)	(21,805)
Loss from continuing operations before provision for income taxes and minority interest	(36,969)	(48,642)	(148,634)	(130,012)
Income tax provision	(144)	(351)	(631)	(752)
Minority interest	—	—	—	1,048
Net loss from continuing operations	(37,113)	(48,993)	(149,265)	(129,716)
Loss from discontinued operations, net of income tax provision of $797, $0, $966 and $0, respectively	(196,187)	(51,859)	(263,509)	(85,796)
Net loss	(233,300)	(100,852)	(412,774)	(215,512)
Less: Preferred stock dividends	(7,397)	(6,862)	(21,782)	(13,814)
Accretion of issuance costs on preferred stock	(75)	(69)	(220)	(139)
Net loss applicable to common shares	$ (240,772)	$ (107,783)	$ (434,776)	$ (229,465)
Net loss per common share – basic and diluted:				
Continuing operations, including preferred stock dividends and costs	$ (0.43)	$ (0.60)	$ (1.72)	$ (1.62)
Discontinued operations	(1.90)	(0.56)	(2.64)	(0.97)
Net loss per common share – basic and diluted	$ (2.34)	$ (1.17)	$ (4.35)	$ (2.60)
Weighted average shares used in per share calculation	103,092	92,468	99,851	88,413

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

5

NEXTWAVE WIRELESS INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands) (unaudited)

	Nine Months Ended September 27, 2008	September 29, 2007
OPERATING ACTIVITIES		
Net loss	$ (412,774)	$ (215,512)
Loss from discontinued operations, net of taxes	(263,509)	(85,796)
Loss from continuing operations	(149,265)	(129,716)
Adjustments to reconcile net loss to net cash used in operating activities:		
Amortization of intangible assets	14,226	7,548
Depreciation	6,676	4,170
Non-cash share-based compensation	4,129	7,031
Accretion of interest expense	16,776	15,536
Gain on sale of spectrum license	(19,317)	—
Asset impairment charges	2,244	—
Other-than-temporary impairment of marketable securities	2,721	—
In-process research and development	—	860
Minority interest	—	(1,048)
Other non-cash adjustments	450	2,262
Changes in operating assets and liabilities:		
Accounts receivable	424	3,815
Deferred cost of revenues	769	(619)
Prepaid expenses and other current assets	(795)	1,303
Other assets	(1,556)	1,993
Accounts payable and accrued liabilities	(4,841)	(3,162)
Deferred revenue	(4,641)	9,150
Other liabilities and deferred credits	3,113	573
Net cash used in operating activities-continuing operations	(128,887)	(80,304)
INVESTING ACTIVITIES		
Proceeds from maturities of marketable securities	106,385	19,273
Proceeds from sales of marketable securities	115,671	865,234
Purchases of marketable securities	(112,167)	(905,251)
Cash from sale of wireless spectrum licenses	35,774	—
Cash paid for business combinations, net of cash acquired	(268)	(84,562)
Cash paid for wireless spectrum licenses	(4,864)	(34,607)
Cash paid to acquire property and equipment	(5,779)	(8,616)
Cash advanced to our investee pursuant to convertible note agreement	(500)	—
Other, net	(698)	(500)
Net cash provided by (used in) investing activities-continuing operations	133,554	(149,029)
FINANCING ACTIVITIES		
Net cash released from restricted cash account securing long-term obligations	17,763	—
Proceeds from the sale of Series A Senior Convertible Preferred Stock, net of costs to issue	—	351,146
Proceeds from long-term debt	21,463	—
Payments on long-term obligations	(7,453)	(4,052)

Proceeds from the sale of common shares	1,737	2,175
Cash distribution paid to members	—	(2,034)
Net cash provided by financing activities-continuing operations	33,510	347,235
Cash used by discontinued operations:		
Net cash used in operating activities-discontinued operations	(74,839)	(68,435)
Net cash used in investing activities-discontinued operations	(5,721)	(9,576)
Net cash used by discontinued operations	(79,560)	(78,011)
Effect of foreign currency exchange rate changes on cash	(135)	—
Net increase (decrease) in cash and cash equivalents	(41,518)	39,891
Cash and cash equivalents, beginning of period	53,050	32,980
Cash and cash equivalents, end of period	11,532	72,871
Less cash and cash equivalents of discontinued operations, end of period	(5,566)	(5,644)
Cash and cash equivalents of continuing operations, end of period	$ 5,966	$ 67,227
Noncash investing and financing activities:		
Common stock issued for business acquisitions	$ 36,501	$ 74,522
Common stock issued under stock plans	$ 7,051	$ 2,268
Wireless spectrum licenses acquired with lease obligations	$ 8,636	$ 5,569

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

NEXTWAVE WIRELESS INC.

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation and Significant Accounting Policies

Financial Statement Preparation

The unaudited consolidated interim financial statements have been prepared by NextWave Wireless Inc. (together with its subsidiaries, “NextWave”, “we”, “our” or “us”) according to the rules and regulations of the United States Securities and Exchange Commission (“SEC”), and therefore certain information and disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted. In the opinion of management, the accompanying unaudited consolidated financial statements for the periods presented reflect all adjustments necessary to fairly state our financial position, results of operations and cash flows, including adjustments related to asset impairment write-offs and restructuring-related charges. These unaudited consolidated financial statements should be read in conjunction with our audited financial statements for the year ended December 29, 2007, included in our Annual Report on Form 10-K filed with the SEC on March 13, 2008.

The accompanying consolidated financial statements have been prepared assuming that we will continue as a going concern. This basis of accounting contemplates the recovery of our assets and the satisfaction of our liabilities in the normal course of business. During the nine months ended September 27, 2008 and September 29, 2007, we generated net losses of $412.8 million and $215.5 million, respectively, and have an accumulated deficit of $883.9 million at September 27, 2008. Cash used in operating activities by continuing operations was $128.9 million and $80.3 million for the nine months ended September 27, 2008 and September 29, 2007, respectively.

Our unrestricted cash, cash equivalents and marketable securities at September 27, 2008 totaled $7.1 million, of which $1.1 million consist of auction rate securities that we have been unable to liquidate due to weakness in the auction markets. We had a net working capital deficit of $73.1 million at September 27, 2008.

On October 9, 2008, we issued Senior-Subordinated Secured Second Lien Notes due 2010 (the "Second Lien Notes") in the aggregate principal amount of $105.3 million (Note 17). After payment of transaction-related fees and expenses, we received net proceeds of approximately $89 million to be used solely in connection with our ordinary course business operations and not for any acquisition of assets or businesses or other uses. In related transactions, we entered into amendments to our 7% Senior Secured Notes (“Senior Notes”) due July 17, 2010 in the aggregate principal amount of $350.0 million (Note 4) and issued Third Lien Subordinated Secured Convertible Notes due 2011 (“Exchange Notes”) in an aggregate principal amount of $478.3 million (Note 17) in exchange for all of our outstanding shares of Series A Senior Convertible Preferred Stock (the “Series A Preferred Stock”) which had a carrying value of $398.6 million at the time of the exchange. These related activities were consummated to satisfy the funding conditions under our Second Lien Notes commitment letter and to facilitate our global restructuring initiative. We did not receive any proceeds from the issuance of the Exchange Notes.

Additionally, in an effort to reduce our future working capital requirements, in the third quarter of 2008, we commenced the implementation of a global restructuring initiative, pursuant to which we intend to, among other things, divest our network infrastructure businesses (Note 2), pursue the sale of certain of our other businesses and assets, and complete other cost reduction actions. These initiatives were expanded on October 8, 2008 in connection with our Second Lien Notes financing by our adoption of a six-month operating budget providing for cost savings measures (the “Operating Budget”) , the appointment of an interim Chief Operating Officer and the formation of a Governance Committee of our Board of Directors with responsibilities for monitoring compliance with the Operating Budget and overseeing certain asset management activities contemplated by the Operating Budget.

We believe the completion of the asset divestiture and cost reductions actions contemplated by our Operating Budget our current cash, cash equivalents and marketable securities, projected revenues from our Multimedia segment and the proceeds from the issuance of the Second Lien Notes will allow us to meet our estimated working capital requirements at least through September 2009.

Discontinued Operations

In an effort to reduce our future working capital requirements, in September 2008, we announced our intent to divest our network infrastructure businesses, which comprise our Networks segment, either through sale, dissolution or closure. Our Networks segment includes our GO Networks, IPWireless and Cygnus subsidiaries, and our Global Services and NextWave Network Product Support strategic business units.

Several factors led to our decision to divest our network infrastructure businesses, including adverse worldwide economic conditions, which we believe have adversely affected manufacturers of telecommunications equipment and technology and caused our Networks segment to experience lower than projected contract bookings and revenues. We believe these conditions

7

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have also led to a delay in global WiMAX network deployments that will continue to impact the timing and volume of projected commercial sales of our WiMAX semiconductor products.

Pursuant to our global restructuring initiative, we are actively marketing for sale our IPWireless, GO Networks and Cygnus subsidiaries. Additionally, in October 2008, we initiated bankruptcy liquidation proceedings for three of our network infrastructure subsidiaries in Israel, Denmark and Canada which is designed to provide an orderly process for the discontinuance of operations and to advance our divestiture and cost reduction strategy. We will deconsolidate these subsidiaries upon change in control following acceptance of our bankruptcy filings in the fourth quarter of 2008.

We expect to complete the planned divestiture of our Networks segment during the fourth quarter of 2008. In October 2008, we expanded our restructuring initiative in connection with our Second Lien Notes financing through the adoption of the Operating Budget, the appointment of an interim Chief Operating Officer and the formation of a Governance Committee of our Board of Directors with responsibilities for monitoring compliance with the Operating Budget and overseeing certain asset management activities contemplated by the Operating Budget. Accordingly, we expect that additional businesses, including our Semiconductor and WiMax Telecom business units, will be classified as held for sale in the fourth quarter of 2008.

The carrying amounts of the assets and liabilities of the discontinued Networks segment held for sale are as follows:

	September 27,	**December 29, 2007**
(in thousands)	**2008**	
Cash and cash equivalents	$ 5,566	$ 5,416
Accounts receivable, net of allowance for doubtful accounts	4,322	7,847
Inventory	7,182	4,478
Deferred cost of revenues	14,284	24,326
Prepaid expenses and other current assets	2,383	4,363
Property and equipment, net	9,870	14,609
Goodwill	—	130,975
Other intangible assets, net	—	55,141
Other noncurrent assets	467	2,534
Assets of discontinued operations	$ 44,074	$ 249,689
Accounts payable	$ 17,170	$ 19,884
Accrued restructuring charges	655	—
Accrued expenses	22,264	26,043
Deferred revenue	24,351	33,371
Other liabilities	833	809
Liabilities of discontinued operations	$ 65,273	$ 80,107

The results of operations of the discontinued Networks segment are as follows:

	Three Months Ended		**Nine Months Ended**	
	September 27,	**September 29,**	**September 27,**	**September 29,**
(in thousands)	**2008**	**2007**	**2008**	**2007**
Hardware revenues	$ 19,987	$ 6,877	$ 44,509	$ 11,949
Operating expenses:				
Cost of hardware revenues	21,761	15,885	47,905	24,118
Engineering, research and development	14,958	22,487	58,784	46,606
Sales and marketing	3,592	3,947	15,069	6,425
General and administrative	4,143	3,582	11,009	7,649
Asset impairment charges	167,689	—	169,885	—

Restructuring charges	4,084	—	4,202	—
Purchased in-process research and development costs	—	11,200	—	11,200
Total operating expenses	216,227	57,101	306,854	95,998
Loss from operations	(196,240)	(50,224)	(262,345)	(84,049)
Other income (expense), net	850	(1,635)	(198)	(1,747)
Loss before provision for income taxes and minority interest	(195,390)	(51,859)	(262,543)	(85,796)
Income tax provision	(797)	—	(966)	—
Net loss	$(196,187)	$ (51,859)	$(263,509)	$ (85,796)

8

Unaudited Pro Forma Balance Sheet

The unaudited pro forma balance sheet as of September 27, 2008 reflects our issuance of the Second Lien Notes in the aggregate principal amount of $105.3 million, the related net cash proceeds thereof totaling approximately $89 million, and our issuance of the Exchange Notes for an aggregate principal amount of $478.3 million in exchange for all of our outstanding shares of our Series A Preferred Stock on October 9, 2008. The pro forma balance sheets also reflect the issuance of warrants to purchase an aggregate of 40 million shares of our common stock at an exercise price of $0.01 per share to the purchasers of the Second Lien Notes with an estimated value of $12.8 million. The unaudited pro forma balance sheet information has been prepared for comparative purposes only. Our analysis of the accounting for issuance of the Exchange Notes and common stock warrants is ongoing and therefore the information presented above may be subject to change upon completion of our analysis.

Fiscal Accounting Periods

We operate on a 52-53 week fiscal year ending on the Saturday nearest to December 31 of the current calendar year or the following calendar year. Normally, each fiscal year consists of 52 weeks, but every five or six years the fiscal year consists of 53 weeks. Fiscal year 2008 is a 52-week year ending on December 27, 2008 and the first 53-week year will occur in 2009. The three and nine month periods ended September 27, 2008 and September 29, 2007 include 13 and 39 weeks, respectively.

Use of Estimates

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States 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 date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, we evaluate our estimates, including those related to revenue recognition, income taxes and the valuation of marketable securities, share-based awards, goodwill, intangible assets and other long-lived assets. Actual results could differ from those estimates.

Principles of Consolidation

Our consolidated financial statements include the assets, liabilities and operating results of our wholly-owned and majority-owned subsidiaries as of September 27, 2008 and September 29, 2007 and for the three and nine months then ended, respectively. Minority interest for the nine months ended September 29, 2007 represents the minority shareholder’s proportionate share of the net equity in our consolidated subsidiary, Inquam Broadband Holding Ltd. We acquired the remaining interest in Inquam Broadband Holding Ltd in October 2007. All significant intercompany accounts and transactions have been eliminated in consolidation.

Strategic Investment

The equity method of accounting is used for our October 2005 investment in the preferred stock of Hughes Systique Corporation (“Hughes Systique”), an early stage software development services company. Our share of the net loss of Hughes Systique is determined by applying the equity method of accounting. Under the equity method, the investor’s share of earnings or losses is determined based on changes in the investor’s claim in the book value of the investee. Additionally, the carrying value of investments accounted for using the equity method of accounting are adjusted downward to reflect any other-than-temporary declines in value. Our share of the net losses of Hughes Systique of $0.1 million and $0.2 million for the three and nine months ended September 27, 2008 and $0.4 million and $1.1 million for the three and nine months ended September 29, 2007, respectively, is included in engineering, research and development expenses in the accompanying consolidated statements of operations. The carrying value of our preferred stock investment in Hughes Systique was $1.3 million and $1.5 million at September 27, 2008 and December 29, 2007, respectively, and is reported in other noncurrent assets in the accompanying condensed consolidated balance sheets.

In February 2008, we executed a loan agreement with Hughes Systique for 6% senior secured convertible notes, whereby we committed to make available to Hughes Systique up to $1.5 million through February 2011. All principal and interest is due three years from the date of the advance. At the maturity date or upon a default event, we have the option to convert any unpaid amounts into shares of preferred stock of Hughes Systique. During the nine months ended September 27, 2008, we advanced $0.5 million to Hughes Systique, which is reported in other noncurrent assets in the accompanying condensed consolidated balance sheets. We received a request for an additional $0.5 million advance from Hughes Systique in September 2008. We are currently in discussions with Hughes Systique to terminate the loan agreement.

Our preferred stock investment in Hughes Systique and the amounts advanced under the loan agreement represent our maximum remaining exposure to a loss.

Revenue Recognition

We have derived revenues from the following sources:

- Contracts to provide multimedia software products for mobile and home electronic devices and related royalties through our PacketVideo subsidiary;

- Sales of wireless broadband and mobile broadcast network products and services by our IPWireless and GO Networks subsidiaries, which are included in discontinued operations for all periods presented. The wireless broadband and mobile broadcast network products sold by IPWireless and GO Networks often include embedded software; and
- Customer subscriptions for the WiMAX network operated by our WiMax Telecom subsidiary, acquired in 2007 and expected to be divested in the first quarter of 2009 in compliance with our Operating Budget.

For arrangements that do not contain software or embedded software that is incidental to the arrangement, we recognize revenue in accordance with the basic principles in SEC Staff Accounting Bulletin ("SAB") No. 104, *Revenue Recognition*, when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collectibility is reasonably assured.

For software arrangements, or in cases where the software is considered more than incidental and is essential to the functionality of the hardware or the infrastructure products, revenue is recognized pursuant to American Institute of Certified Public Accountants ("AICPA") Statement of Position ("SOP") No. 97-2, *Software Revenue Recognition*, SOP No. 98-9, *A Modification of SOP 97-2 Software Revenue Recognition with Respect to Certain Transactions*, and Emerging Issues Task Force ("EITF") Issue No. 03-5, *Applicability of SOP 97-2 to Non-Software Deliverables in an Arrangement Containing More-Than-Incidental Software*. We also consider the provisions of SOP No. 81-1, *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*.

Our software arrangements can include a software or technology license, non-recurring engineering services and post-contract customer support. For these arrangements, we evaluate each deliverable in the arrangement to determine whether it represents a separate unit of accounting. If objective and reliable evidence of fair value exists ("vendor specific objective evidence") for all units of accounting in the arrangement, revenue is allocated to each unit of accounting or element based on those relative fair values. If vendor specific objective evidence of fair value exists for all undelivered elements, but not for delivered elements, the residual method would be used to allocate the arrangement consideration. To date, we have not been able to establish vendor specific objective evidence for any of the elements included in our revenue arrangements, as the software and hardware products or services have not yet been sold separately, nor has a standard price list been established. As a result, once the software or technology is delivered and the only undelivered element is services, the entire non-contingent contract value is recognized ratably over the remaining service period. Costs directly attributable to providing these services are also deferred and amortized over the remaining service period of the respective revenues.

For arrangements in which customers pay one contracted amount for multiple products and services, or a combination of products and services, we also consider the guidance provided by EITF Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables*. If elements cannot be treated as separate units of accounting under EITF Issue No. 00-21, they are combined into a single unit of accounting and the associated revenue is deferred until all combined elements have been delivered or until there is only one remaining element to be delivered. Services sold separately are generally billed on a time and materials basis at agreed-upon billing rates, and revenue is recognized as the services are performed.

We earn royalty revenues on licensed embedded multimedia products sold by our licensees. Generally, royalties are paid by licensees on a per unit or contingent usage basis. The licensees generally report and pay the royalty in the quarter subsequent to the period of delivery or usage. We recognize royalty revenues based on royalties reported by licensees. When royalty arrangements also provide for ongoing post-contract customer support that does not meet the criteria to be recognized upon delivery of the software, the royalty is recognized ratably from the date the royalty report is received through the stated remaining term of the post-contract customer support. In limited situations, we have determined that post-contract customer support revenue can be recognized upon delivery of the software because the obligation to provide post-contract customer support is for one year or less, the estimated cost of providing the post-contract customer support during the arrangement is insignificant and unspecified upgrades or enhancements offered for the particular post-contract customer support arrangement historically have been and are expected to continue to be minimal and infrequently provided. In these instances, we have accrued all the estimated costs of providing the services upfront, which to date have been insignificant.

If we receive non-refundable advanced payments from licensees that are allocable to future contracts periods or could be creditable against other obligations of the licensee to us, the recognition of the related revenue is deferred until such future periods or until such creditable obligations lapse.

In instances where we have noted extended payment terms, revenue is recognized in the period the payment becomes due. If an arrangement includes specified upgrade rights, revenue is deferred until the specified upgrade has been delivered.

We do not generally allow for product returns and we have no history of product returns. Accordingly, no allowance for returns has been provided.

The timing and amount of revenue recognition depends upon a variety of factors, including the specific terms of each arrangement and the nature of our deliverables and obligations. Determination of the appropriate amount of revenue recognized involves judgments and estimates that our management believes are reasonable.

Income Taxes

10

We recognize income tax expense based on estimates of our consolidated taxable income (loss) taking into account the various legal entities through which, and jurisdictions in which, we operate. As such, income tax expense may vary from the customary relationship between income tax expense and income (loss) before taxes.

Recent Accounting Pronouncements

In March 2008, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standard (“SFAS”) No. 161, *Disclosures about Derivative Instruments and Hedging Activities - An amendment of FASB Statement No. 133*, which requires enhanced qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. SFAS No. 161 is effective for financial statements issued for fiscal years beginning after November 15, 2008, with early adoption permitted. We will provide the disclosures required by SFAS No. 161 beginning in our fiscal year 2009 financial statements.

In December 2007, the FASB issued SFAS No. 141R, *Business Combinations.* SFAS No. 141R requires an acquirer to recognize the assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree at the acquisition date to be measured at their fair value as of that date. An acquirer is required to recognize assets or liabilities arising from all other contingencies as of the acquisition date, measured at their acquisition-date fair values, only if it is more likely than not that they meet the definition of an asset or a liability. Any acquisition-related costs are to be expensed instead of capitalized. SFAS No. 141R applies prospectively to our business combinations, if any, for which the acquisition date is on or after December 28, 2008. The impact on our consolidated financial statements from the adoption of SFAS No. 141R in fiscal year 2009 will depend on acquisitions at the time.

In June 2007, the FASB ratified EITF Issue No. 07-3, *Accounting for Nonrefundable Advance Payments for Goods or Services to Be Used in Future Research and Development Activities*. EITF Issue No. 07-3 requires non-refundable advance payments for goods and services to be used in future research and development activities to be recorded as an asset and the payments to be expensed when the research and development activities are performed. Our adoption of EITF Issue No. 07-3 in the first quarter of our 2008 fiscal year did not have a material impact on our consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*. SFAS No. 159 permits entities to choose to measure certain financial assets and liabilities and other eligible items at fair value, which are not otherwise currently required to be measured at fair value. Under SFAS No. 159, the decision to measure items at fair value is made at specified election dates on an irrevocable instrument-by-instrument basis. Entities electing the fair value option would be required to recognize changes in fair value in earnings and to expense upfront cost and fees associated with the item for which the fair value option is elected. Entities electing the fair value option are required to distinguish on the face of the statement of financial position, the fair value of assets and liabilities for which the fair value option has been elected and similar assets and liabilities measured using another measurement attribute. We have elected not to adopt SFAS No. 159 for any such instruments for the nine months ended September 27, 2008. We will continue to evaluate the election of this option throughout our 2008 fiscal year.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. SFAS No. 157 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. Under the standard, fair value measurements would be separately disclosed by level within the fair value hierarchy. Our adoption of SFAS 157 in the first quarter of our 2008 fiscal year did not have a significant impact on our consolidated financial statements, although we are now required to provide additional financial statement disclosures. The disclosures required by SFAS No. 157 in the year of adoption are provided in Note 14.

Reclassifications

Certain amounts in the previously reported financial statements have been reclassified to conform to the current period presentation.

2. Restructuring Activities

In an effort to reduce our future working capital requirements, in the third quarter of 2008, we commenced the implementation of a global restructuring initiative, pursuant to which we intend to, among other things, divest our network infrastructure businesses, pursue the sale of certain other of our businesses and assets, and complete other cost reduction actions. In October 2008, we expanded our restructuring initiative in connection with our Second Lien Notes financing through the adoption of the Operating Budget, the appointment of an interim Chief Operating Officer and the formation of a Governance Committee of our Board of Directors with responsibilities for monitoring compliance with the Operating Budget and overseeing certain asset management activities contemplated by the Operating Budget. In connection with the implementation of our global restructuring initiative, in the third quarter of 2008, we terminated 224 employees worldwide and vacated three leased facilities in the United States. We anticipate that the further implementation of our global restructuring initiative as contemplated by the Operating

11

Budget will result in the termination of an additional approximately 70 employees and vacating additional leased facilities during the fourth quarter of 2008.

The following summarizes the restructuring activity for the nine months ended September 27, 2008 and the related restructuring liabilities:

(in thousands)	**Charges to Expense**	**Cash Payments**	**Reversal of Deferred Charges**	**Balance at September 27, 2008**
Employee termination costs	$ 5,321	$ (4,215)	$ —	$ 1,106
Lease liabilities and related facility closure costs	2,056	(375)	223	1,904
Other related costs, primarily legal fees	773	(623)	—	150
Total	$ 8,150	$ (5,213)	$ 223	$ 3,160
Accrued restructuring charges:				
Current portion-continuing operations				$ 1,851
Noncurrent portion-continuing operations				654
Discontinued operations				655
Total				$ 3,160

3. Asset Impairment

Goodwill and Indefinite-Lived Intangible Assets

In connection with the implementation of our global restructuring initiative in the third quarter of 2008, we reviewed our goodwill and indefinite-lived intangible assets for impairment and determined that indicators of impairment were present for the goodwill in our Networks segment. Accordingly, in the third quarter of 2008, we performed the two-step goodwill impairment assessment prescribed by SFAS No. 142, *Goodwill and Other Intangible Assets*. The first step of the goodwill impairment assessment involves determining the fair value of the two reporting units in our Networks segment which include goodwill, IPWireless and Cygnus, to determine if their carrying value exceeds their fair value.

We began actively marketing our Cygnus reporting unit for sale in the third quarter of 2008. Although we participated in preliminary sale and/or licensing discussions involving the Cygnus intellectual property and operations, none of those discussions advanced and our efforts to sell Cygnus were ultimately unsuccessful. As a result, Cygnus was shut down and the remaining employees were terminated in early October 2008. Since we do not anticipate generating significant future cash flows from the divestiture of the Cygnus reporting unit, we have assessed the fair value of the Cygnus reporting unit as nominal.

We began actively marketing our IPWireless reporting unit for sale in the third quarter of 2008 and participated in advanced sale discussions with multiple third parties. We continue to participate in sale discussions with interested parties. The Operating Budget contemplates that we will no longer provide any funding to, or incur liabilities with respect to, IPWireless past the fourth quarter of 2008. Accordingly, if we are unable to finalize a sale of IPWireless during the fourth quarter of 2008, we anticipate shutting down the IPWireless operations and liquidating the assets and liabilities of the IPWireless UK operating entity through a bankruptcy filing. Based on the current sale discussions and our timeline for divesting the IPWireless reporting unit in order to comply with the Operating Budget, we do not anticipate generating significant future cash flows from the divestiture of the IPWireless reporting unit. Accordingly, we have assessed the fair value of the IPWireless reporting unit as nominal.

Based on the analysis, we concluded that the carrying value of the Cygnus and IPWireless reporting units exceeded their fair value.

The second step of the goodwill impairment assessment involves comparing the implied fair value of the reporting unit goodwill with the carrying amount of the goodwill in order to measure the impairment loss. We will be required to issue our financial statements for the third quarter of 2008 prior to completing the second step of the goodwill impairment test. However, based on the guidance provided by SFAS No. 5, *Accounting for Contingencies*, we believe that an impairment loss for our Cygnus and IPWireless reporting units is probable and can be reasonably estimated. Accordingly, during the third quarter of 2008, we recognized a goodwill impairment loss of $117.7 million representing our best estimate of the goodwill impairment loss for the Cygnus and IPWireless reporting units. The goodwill impairment loss is reported as an asset impairment charge in discontinued operations.

The asset impairment charge recognized in the third quarter of 2008 may be subject to adjustment upon completion of the second step of the goodwill impairment test which is anticipated to be completed during the fourth quarter of 2008.

Long-Lived Assets

In connection with the implementation of our global restructuring initiative, we reviewed our long-lived assets for impairment and determined that indicators of impairment were present for the long-lived assets in our Networks segment as well as certain other long-lived assets primarily leasehold improvements at vacated leased facilities. Accordingly, based on the guidance provided by SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, in the third quarter of 2008, we performed an assessment to determine if the carrying value of these long-lived assets was recoverable through estimated undiscounted future cash flows resulting from the use of the assets and their eventual disposition.

Included in the long-lived assets of our Networks segment is an office building we own in Nevada that we are actively marketing for sale through a national brokerage firm. In June 2008, we classified the building as an asset held for sale and ceased depreciating this asset. Additionally, in June 2008, we performed a recoverability assessment of the building and determined that the carrying value of the building exceeded its market value, less costs to sell, based primarily on the current commercial real estate market conditions in the local area. Accordingly, during the second quarter of 2008, we wrote-down the carrying value of the building to its estimated market value, less costs to sell, and recognized an impairment loss of $2.2 million, which is reported as an asset impairment charge in discontinued operations in the nine months ended September 27, 2008.

For the long-lived asset recoverability assessment performed during the third quarter of 2008, the undiscounted cash flows used to estimate the recoverability of the asset carrying values were based on the estimated future net cash flows to be generated from the sale or licensing of the assets. Based on the analysis, we concluded that the carrying value of certain of our long-lived assets was not recoverable. The impaired assets primarily consist of the amortizable purchased intangible assets of IPWireless, GO Networks and Cygnus, our Nevada office building and the equipment contained therein, and leasehold improvements at vacated facilities. Accordingly, during the third quarter of 2008, we recognized an additional impairment loss of $52.3 million, of which $50.1 million is reported as an asset impairment charge in discontinued operations and $2.2 million is reported as an asset impairment charge in continuing operations.

No assurance can be given that the underlying estimates and assumptions utilized in our determination of an asset's undiscounted future cash flows will materialize as anticipated.

Due to the expansion of our global restructuring initiative through the adoption of our Operating Budget in October 2008, we may incur additional long-lived asset impairment charges in the fourth quarter of 2008.

Other

As a result of the discontinuance of the operations at our GO Networks subsidiary, we determined that the cost of the inventory held by GO Networks is not realizable and exceeds its fair value. Additionally, we wrote-off the remaining deferred cost of revenues of GO Networks since we do not anticipate realizing the associated deferred revenues. Accordingly, as a result of the write-off of the inventory and deferred cost of revenues, we recognized a non-cash charge of $4.8 million in the third quarter of 2008, which is reported in cost of revenues in discontinued operations.

4. Net Loss Per Common Share Information

Basic and diluted net loss per common share for the three and nine months ended September 27, 2008 and September 29, 2007 is computed by dividing net loss applicable to common shares during the period by the weighted average number of common shares outstanding during the respective periods, without consideration of common stock equivalents.

The following securities that could potentially dilute earnings per share in the future are not included in the determination of diluted loss per share as they are antidilutive. The share amounts are determined using a weighted average of the shares outstanding during the respective periods and assume that the last day of the respective quarterly periods were the end dates of the contingency period for any contingently issuable shares in accordance with SFAS No. 128, *Earnings Per Share*.

	Three Months Ended		**Nine Months Ended**	
	September 27,	**September 29,**	**September 27,**	**September 29,**
(in thousands)	**2008**	**2007**	**2008**	**2007**
Series A Senior Convertible Preferred Stock	35,319	32,763	34,666	22,110
Outstanding stock options	22,139	18,314	21,882	15,524
Common stock warrants	2,436	2,436	2,436	2,522
Contingently issuable shares under advisory contract	833	833	833	833
Restricted stock	151	216	94	212

In addition to the securities listed above, we may be required to issue shares of our common stock in payment of additional purchase consideration due in connection with our 2007 acquisition of IPWireless (Note 9) and in payment of bonuses due under the IPWireless Employee Stock Bonus Plan (Note 12). As the contingencies related to these shares have not yet been met as of September 27, 2008, they have been excluded from the table above.

5. Comprehensive Loss

Comprehensive loss was as follows:

	Three Months Ended		**Nine Months Ended**
	September 27,	**September 29,**	
(in thousands)	**2008**	**2007**	