

Starent Networks, Corp.
Form S-1
March 06, 2007

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As filed with the Securities and Exchange Commission on March 6, 2007.

Registration No. 333-

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

Form S-1

REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933

STARENT NETWORKS, CORP.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

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

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

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

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

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

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

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

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

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

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

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box.

CALCULATION OF REGISTRATION FEE

Each class of Securities to be Registered	Proposed Maximum Aggregate Offering Price(1)	Amount of Registration Fee(2)
Common Stock, par value \$0.001 per share	\$115,000,000	\$3,531

- (1) Estimated solely for the purpose of computing the registration fee in accordance with Rule 457(o) under the Securities Act of 1933, as amended.
- (2) Calculated pursuant to Rule 457(o) based on an estimate of the proposed maximum aggregate offering price.

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

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

Subject to Completion. Dated March 6, 2007

Shares

Starent Networks, Corp.

Common Stock

This is an initial public offering of shares of common stock of Starent Networks, Corp.

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

Prior to this offering, there has been no public market for the common stock. It is currently estimated that the initial public offering price per share will be between \$ and \$. We have applied to have our common stock listed on the Nasdaq Global Market under the symbol "STAR."

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

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

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

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

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

Goldman, Sachs & Co.

Lehman Brothers

JPMorgan

Thomas Weisel Partners LLC

Prospectus dated , 2007.

PROSPECTUS SUMMARY

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

Starent Networks

Overview

Starent Networks is a leading provider of infrastructure solutions that enable mobile operators to deliver multimedia services to their subscribers. We have created solutions that provide core network functions and services, including access from a wide range of radio networks to the operator's packet core network, mobility management of subscriber sessions and call control. Our solutions 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 access-independent solutions integrate multiple network functions and services needed for the delivery of advanced multimedia services, such as video, Internet access, voice-over-IP, e-mail, mobile TV, photo sharing and gaming.

Mobile operators are aggressively deploying next-generation wireless networks, such as third generation, or 3G, networks, that are capable of delivering high quality, mobile multimedia services to subscribers. In deploying these new networks, mobile operators are seeking packet-based multimedia infrastructure solutions that can deliver high performance, flexibility and simplicity and provide high reliability. We have developed our multimedia core network platform, the ST16 Intelligent Mobile Gateway, and our proprietary software specifically to address the needs of packet-based mobile networks.

We sell our hardware and software products to leading mobile operators around the world both directly and through OEMs, system integrators and distributors. Since our first commercial deployment in the first quarter of 2003, our products have been deployed by over 60 mobile operators in 25 countries. We became profitable in 2005, and in 2006 our revenues were \$94.4 million and our net income was \$3.6 million.

Industry Background

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

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

Historically, mobile operators seeking to address these challenges have been required to retrofit network infrastructure solutions originally designed for wireline networks. These solutions utilizing repurposed network switches, routers and off-the-shelf enterprise servers are unable to sufficiently satisfy the needs of mobile operators to deliver efficient and reliable multimedia services.

While routers and network switches are capable of forwarding packets of information, they lack the integrated processing power, memory and software needed to examine individual packets and apply defined business policies and subscriber services to them. To address these shortcomings, mobile operators typically connect repurposed switches and routers with numerous enterprise servers in multi-element configurations. These repurposed solutions offer limited intelligence about subscriber sessions, can result in limited network performance and reliability and can be costly to operate and upgrade.

Our Solutions

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

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

High performance. Our solutions are highly scalable to support a large number of subscribers on one platform and provide high bandwidth and throughput for improved traffic capacity and flow. In addition, our solutions provide high call transaction rates, which enhance the scalability of our products, reduce unwanted delays in network traffic and allow the subscriber to have quick access to network services.

Simple and flexible network architecture. Our solutions allow mobile operators to integrate a number of network functions and enhanced services into a single hardware platform. In addition to providing network functions such as access, mobility management and call control, our platform is also capable of integrating advanced services that are typically deployed out of line from the session stream elsewhere in the network, such as enhanced charging and billing, firewall protection, security and content filtering.

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

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

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

Our Strategy

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

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

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Increase market penetration. As mobile operators continue to increase network coverage and capacity, as well as their service offerings, they create new sales opportunities for us.

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We intend to increase our market penetration of both CDMA and GSM/UMTS operators. We believe a significant opportunity for growth is from sales to GSM/UMTS operators as they continue to transition to high-bandwidth networks.

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

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

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

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

Risks Associated with Our Business

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

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

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

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

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

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

Corporate Information

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

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

The Offering

Common stock offered by Starent Networks, Corp.	shares
Common stock offered by the selling stockholders	shares
Common stock to be outstanding after this offering	shares

Use of proceeds

We intend to use the net proceeds from this offering for working capital and other general corporate purposes, including the development of new products, sales and marketing activities and capital expenditures. We may use a portion of the proceeds for the acquisition of, or investment in, companies, technologies, products or assets that complement our business. We will not receive any proceeds from the shares sold by the selling stockholders. The selling stockholders include our president and chief executive officer. See "Use of Proceeds" for more information.

Risk Factors

You should read the "Risk Factors" section and other information included in this prospectus for a discussion of factors to consider carefully before deciding to invest in shares of our common stock.

Proposed Nasdaq Global Market symbol "STAR"

The number of shares of our common stock to be outstanding after this offering is based on the number of shares of common stock outstanding as of December 31, 2006, and excludes:

11,846,085 shares of common stock issuable upon the exercise of stock options outstanding as of December 31, 2006, at a weighted average exercise price of \$0.94 per share, of which options to purchase 4,568,075 shares of our common stock were exercisable as of December 31, 2006 with a weighted average exercise price of \$0.54 per share; and

837,863 shares of common stock available for future issuance under our equity compensation plans as of December 31, 2006.

Except as otherwise noted, all information in this prospectus:

assumes no exercise by the underwriters of their over-allotment option;

gives effect to the conversion of all outstanding shares of our convertible preferred stock into 66,432,011 shares of our common stock upon the closing of this offering; and

gives effect to the restatement of our certificate of incorporation and amendment and restatement of our bylaws prior to the closing of this offering.

SUMMARY CONSOLIDATED FINANCIAL DATA

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

	Year Ended December 31,		
	2004	2005	2006
(in thousands, except per share data)			
Statement of Operations Data:			
Revenues:			
Product	\$ 29,453	\$ 51,819	\$ 81,061
Service	4,942	7,841	13,289
Total revenues	34,395	59,660	94,350
Cost of revenues:			
Product	12,633	12,285	25,640
Service	812	1,358	2,086
Total cost of revenues	13,445	13,643	27,726
Gross profit	20,950	46,017	66,624
Operating expenses:			
Research and development	13,303	18,107	25,980
Sales and marketing	18,445	19,785	30,311
General and administrative	3,185	7,352	8,515
Total operating expenses	34,933	45,244	64,806
Income (loss) from operations	(13,983)	773	1,818
Total other income, net	95	644	2,237
Income (loss) before income tax expense	(13,888)	1,417	4,055
Income tax expense	(160)	(513)	(413)
Net income (loss)	\$ (14,048)	\$ 904	\$ 3,642
Accretion of redeemable preferred stock	(6,266)	(7,349)	(7,988)
Net income (loss) applicable to common stockholders	\$ (20,314)	\$ (6,445)	\$ (4,346)
Net income (loss) per share applicable to common stockholders, basic and diluted	\$ (2.19)	\$ (0.65)	\$ (0.41)
Weighted average shares used in computing net income (loss) per share applicable to common shareholders, basic and diluted	9,296	9,963	10,540
Pro forma net income (loss) per share (unaudited)(1):			
Basic			\$ 0.05

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Year Ended December 31,

Diluted	\$ 0.04
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Weighted average shares used in computing pro forma net income (loss)
per share (unaudited):

Basic	76,972
Diluted	82,059

(1) The pro forma net income (loss) per common share, basic and diluted, has been calculated assuming the conversion of all outstanding preferred stock into common stock upon the closing of this offering and the elimination of the accretion of redeemable preferred stock.

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The pro forma balance sheet data give effect to the conversion of all outstanding shares of preferred stock into common stock and the elimination of accretion of redeemable preferred stock as of December 31, 2006. The pro forma as adjusted balance sheet data also give effect to our sale of _____ shares of common stock offered by this prospectus at an assumed initial public offering price of \$ _____ per share, the mid-point of the estimated price range shown on the cover page of this prospectus, after deducting the estimated underwriting discount and offering expenses payable by us.

As of December 31, 2006

	Actual	Pro Forma	Pro Forma as Adjusted
	(in thousands)		
Balance Sheet Data:			
Cash, cash equivalents and short-term investments	\$ 60,154	\$ 60,154	\$
Working capital	19,305	19,305	
Total assets	104,267	104,267	
Indebtedness			
Redeemable preferred stock	130,270		
Total stockholders' equity (deficit)	(105,511)	24,759	

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RISK FACTORS

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

Risks Related to Our Business and Industry

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

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

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

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

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

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

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

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

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

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

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

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

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

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

general economic conditions in our domestic and international markets.

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

We derive a substantial portion of our revenues from a limited number of customers partly due to the nature of the mobile communications industry. During any given fiscal period, a small number of customers may account for a significant percentage of our revenues. In each of 2004, 2005 and 2006, we derived more than 90% of our revenues from our top five customers. In 2004, Verizon Wireless represented more than 40% of our revenues and Samsung Electronics and ITOCHU Techno-Solutions Corporation, also known as CTC, each represented more than 20%. In 2005, Verizon Wireless represented 40% of our revenues and CTC and Samsung each represented more than 20%. In 2006, we derived more than 40% of our revenues from our CDMA OEM relationship with Nortel Networks, of which more than half was related to one mobile operator, and more than 30% of our revenues from Verizon Wireless. We terminated our OEM relationships with Nortel Networks in December 2006. See "We recently terminated our OEM relationships with Nortel Networks. If we are unable to establish strong relationships with the mobile operators formerly serviced by Nortel Networks under our CDMA agreement or if we are unable to resolve a dispute with Nortel Networks relating to the termination of our GSM/UMTS agreement, our business will be harmed," for more information.

We do not have long-term volume purchase contracts with our customers or other commitments that ensure future sales of our products to existing customers. The loss of any key customer, or our inability to generate anticipated revenue from them, would significantly and adversely affect our business, financial condition and results of operations. In addition, a change in the timing or size of a purchase by any one of our key customers can result in significant variations in our revenue and operating results from period to period. Our operating results for the foreseeable future will continue to depend on our ability to effect sales to a small number of customers and any revenue growth will depend on our success selling additional products to our large customers and expanding our customer base to include additional customers that deploy our products in large-scale networks serving significant numbers of subscribers.

Moreover, many of our key customers are large mobile operators that have substantial purchasing power and leverage in negotiating contractual arrangements with us. These customers may require us to agree to terms and conditions that could result in increased costs and decreased revenues and 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 packet-based multimedia infrastructure solutions to mobile operators. The market for our products is relatively new and still evolving, and it is uncertain whether our products will achieve and sustain high levels of demand and market acceptance. Our success will depend to a substantial extent on the willingness of mobile operators to continue to implement packet-based,

multimedia network infrastructure. Factors that could impair the rate of growth of multimedia networks include:

lower than anticipated demand by subscribers for multimedia services;

budgetary constraints of mobile operators;

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

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-based multimedia 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 solutions;

system scalability and service integration capabilities;

system intelligence;

breadth of network interoperability, access independence and standards support;

high levels of customer support and customer interaction; and

competitive pricing.

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

Competitive products may in the future have better performance, lower prices and broader acceptance than our products. Our primary competitors include Cisco Systems, Inc., LM Ericsson Telephone Co., Nokia Corporation and UTStarcom, Inc., each of which has a longer operating history, greater name recognition, a larger customer base and significantly greater financial, technical, sales, marketing and other resources than we do. Potential customers may prefer to purchase from their existing suppliers rather than a new supplier regardless of product performance or features. In addition, many of our competitors have a broader range of products and may be able to offer concessions to potential customers on bundled purchases that we are not able to match because we currently offer only a single line of products. We also face competition from a number of companies with more limited market share generally or by geography and newer market entrants.

If our market continues to develop and expand, we could face increased competition from other established companies, as well as emerging companies. For example, OEMs, system integrators and distributors currently selling our products could market products and services that compete with our products and services. In addition, some of our competitors have made

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

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

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

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

Our future success as a provider of network infrastructure solutions 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 solutions will decrease, and we may not be able to sustain or increase our levels of revenues or profitability in the future.

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

The two principal radio access interfaces in use today for mobile communications are Code Division Multiple Access, or CDMA, and Global System for Mobile Communications/Universal Mobile Telecommunications System, or GSM/UMTS. To date, we have achieved our highest number of deployments in the CDMA market, which has transitioned faster to high-bandwidth networks.

However, significantly more operators worldwide currently utilize GSM/UMTS than CDMA technologies. In order to continue our growth, we believe it is important that we continue to expand into the GSM/UMTS market. To date, we have established a relationship with a major GSM/UMTS operator, and we intend to devote significant sales and marketing resources to further penetrate the GSM/UMTS market. If GSM/UMTS operators do not transition or delay their transition to high-bandwidth networks, or if we are unable to establish relationships with additional GSM/UMTS operators, we may not be able to grow our business as expected and our results of operations will be adversely affected.

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

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

We recently terminated our OEM relationships with Nortel Networks. If we are unable to establish strong relationships with the mobile operators formerly serviced by Nortel Networks under our CDMA agreement or if we are unable to resolve a dispute with Nortel Networks relating to the termination of our GSM/UMTS agreement, our business will be harmed.

We had two OEM agreements with Nortel Networks, one relating to the CDMA market and one relating to the GSM/UMTS market. We terminated the agreement relating to the CDMA market effective March 2007 because we were no longer strategically aligned with Nortel Networks on future packet core solutions for mobile operators and to allow specific major mobile operators to purchase directly from us. Sales to Nortel Networks, all of which were made under the CDMA agreement, accounted for more than 40% of our revenues in 2006. Nortel Networks serviced a significant number of mobile operators under this agreement in 2006, the largest of which accounted for over 50% of our sales to Nortel Networks and the largest 10 of which accounted for over 80% of our sales to Nortel Networks. Although Nortel Networks has acknowledged our right to terminate the CDMA agreement, under the terms of the agreement Nortel Networks has a right to continue to purchase our CDMA products for delivery through December 2009. The termination of the CDMA agreement could disrupt our relationships with CDMA mobile operators formerly serviced by Nortel Networks. We are currently seeking to establish direct sales relationships with some of the CDMA operators formerly serviced by Nortel Networks, including the mobile operator that

accounted for over 50% of our 2006 sales to Nortel Networks, and are currently exploring a new reseller relationship with Nortel Networks to continue to service other CDMA operators. Our business will be harmed if we are unable to establish a direct relationship with the mobile operator that accounted for the majority of our sales to Nortel Networks in 2006, or if we are unable to directly or indirectly continue selling our products to the other CDMA operators formerly serviced by Nortel Networks. In addition, our business may be adversely affected if we are unable to enter into a new CDMA reseller relationship with Nortel Networks.

We also terminated the agreement relating to the GSM/UMTS market effective December 2006 because there was a lack of strategic alignment on future packet core solutions for mobile operators between us and Nortel Networks and because there had been no sales of our products under that agreement. Although we believe we had valid grounds to terminate the GSM/UMTS agreement, Nortel Networks has disputed our right to terminate that agreement. The agreement contains provisions granting Nortel Networks the exclusive rights to sell our products to specified GSM/UMTS operators until May 2009. If we are unable to resolve the dispute regarding our termination of the GSM/UMTS agreement, Nortel Networks could seek to enjoin us from selling our products and associated services directly to these specified GSM/UMTS operators, seek indemnification for damages under the agreement and/or seek payment of commissions for sales we make to these specified GSM/UMTS operators. Depending on our sales to these specified operators, the amount of damages or commissions sought may be substantial. The growth of our business may be limited if we are enjoined from or otherwise unable to establish direct or indirect sales relationships with these GSM/UMTS mobile operators. We are currently exploring a new reseller relationship with Nortel Networks to service GSM/UMTS operators. The growth of our business may be limited if we are unable to enter into a new GSM/UMTS reseller relationship with Nortel Networks.

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

Although we were profitable in 2005 and 2006, we incurred net losses for the preceding three years. Our net losses were approximately \$25.8 million in 2002, \$26.4 million in 2003 and \$14.0 million in 2004. As a result of our net losses, we had an accumulated deficit of \$105.5 million as of December 31, 2006. We will need to generate significant revenues and limit our operating expenses and other expenditures to maintain profitability, and we cannot be sure that we will remain profitable for any substantial period of time. If we are unable to remain profitable, the market price of our common stock could decline.

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

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

The inclusion of, or the announcement of an intent to include, functionality and services perceived to be similar to those offered by our solutions 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 solutions to their network. The adoption

of these competitive products or different approaches to their network infrastructure by mobile operators could have an adverse effect on our business, operating results and financial condition.

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

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

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

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

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

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

our failure to maintain high quality support and services could have a material adverse effect on our business, operating results and financial condition.

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

Mobile operators have been aggressively upgrading their networks, and new industry standards for access technologies, such as third generation, or 3G, and more advanced fourth generation, or 4G, technologies continue to evolve. Continuing technological changes in the mobile communications industry and in the mobile network infrastructure industry could undermine our competitive position or make our products obsolete, either generally or for particular types of services. Our future success will depend upon our ability to accurately predict and respond to new technology standards. We must develop and introduce a variety of new capabilities and enhancements to our existing product offerings, as well as introduce new product offerings, to address the changing standards and technological needs of the network infrastructure market. A failure to accurately predict and respond to evolving technologies, to introduce on a timely basis new products and enhancements in response to evolving technologies and standards, or to address changing needs in our current markets or expand into new markets may cause existing and potential customers to forego purchases of our products or purchase from our competitors. The introduction of new products embodying new technologies or the emergence of new industry standards could render our existing products uncompetitive from a pricing standpoint, obsolete or unmarketable.

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

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

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

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

product enhancements that we introduce may not achieve any significant degree of market acceptance.

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

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

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

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

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

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

Shortages in components that we use in our products are possible and our ability to predict the availability of such components may be limited. Some of these components are available only from single or limited sources of supply. The process of qualifying alternate sources for components, if available at all, may be time consuming, difficult and costly. In addition, the lead times associated with certain components are lengthy and preclude rapid changes in quantity requirements and delivery schedules. Any growth in our business or the economy is likely to create greater pressures on us and our suppliers to project overall component demand accurately and to establish appropriate component inventory levels. In addition, increased demand by third parties for

the components we use in our products may lead to decreased availability and higher prices for those components. We carry very little inventory of our products and product components, and we rely on our suppliers to deliver necessary components to our contract manufacturer in a timely manner based on forecasts we provide. We generally rely on purchase orders rather than long-term contracts with our suppliers. As a result, even if available, we may not be able to secure sufficient components at reasonable prices or of acceptable quality to build products in a timely manner, which would seriously impact our ability to deliver products to our customers, and our business, operating results and financial condition would be adversely affected.

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

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

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

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

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

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

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

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

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

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

Over the last several years, we derived a significant portion of our revenues from customers outside the United States, and we continue to expand our international operations. Approximately 59% of our employees are located abroad, including 204 employees located in India. In addition, we have sales and technical support personnel in numerous countries worldwide. We expect to continue to add personnel in additional countries. Any continued expansion into international markets will require significant resources and management attention and will subject us to new regulatory, economic and political risks, and we cannot be sure that any further international expansion will be successful. Among the risks we believe are most likely to affect us with respect to our international operations are:

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

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

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

unexpected changes in regulatory requirements;

reduced protection for intellectual property rights in some countries;

new and different sources of competition;

fluctuations in exchange rates; and

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

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

operations and reduce our international sales, adversely affecting our business, operating results and financial condition.

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

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

fund our operations;

respond to competitive pressures;

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

develop new products or enhancements to existing products.

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

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

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

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

We have expanded our operations significantly since inception and anticipate that further significant expansion will be required. For example, our revenues increased from \$34.4 million in 2004 to \$94.4 million in 2006, and the number of our employees increased from 117 at the beginning of 2004 to 411 as of December 31, 2006. This growth has placed significant demands on our management, as well as our financial and operational resources. If we do not effectively

manage our future growth, the efficiency of our operations and the quality of our products could suffer, which could adversely affect our business and operating results. To effectively manage this growth, we will need to continue to:

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

expand our manufacturing capacity and scale of production;

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

provide adequate training and supervision to maintain high quality standards.

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

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

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

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

Our products are subject to United States export controls and may be exported outside the United States only with the required level of export license or through an export license exception, because we incorporate encryption technology into our products. In addition, various countries

regulate the import of certain encryption technology and have enacted laws that could limit our ability to distribute our products or could limit our customers' ability to implement our products in those countries. Changes in our products or changes in export and import regulations may create delays in the introduction of our products in international markets, prevent our customers with international operations from deploying our products throughout their networks or, in some cases, prevent the export or import of our products to certain countries altogether. Any change in export or import laws and regulations, shifts in approach to the enforcement or scope of existing laws and regulations, or change in the countries, persons or technologies targeted by such regulations, could result in decreased use of our products by, or in our decreased ability to export or sell our products to, existing or potential customers with international operations. Any decreased use of our products or limitation on our ability to export or sell our products would likely adversely affect our business, operating results and financial condition.

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

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

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

Risks Related to our Intellectual Property

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

Our success and ability to compete depends in part upon our ability to obtain protection in the United States and other countries for our products by establishing and maintaining intellectual

property rights relating to or incorporated into our technology and products. We own a variety of patents and patent applications in the United States and corresponding patents and patent applications in foreign jurisdictions. However, we have not obtained patent protection in each market in which we plan to compete. To date, our patent portfolio has not prevented other companies from competing against us, and we do not know how successful we would be if we sought to enforce our patent rights against suspected infringers. Our pending and future patent applications may not issue as patents or, if issued, may not issue in a form that will be advantageous to us. Even if issued, patents may be challenged, narrowed, invalidated or circumvented, which could limit our ability to stop competitors from marketing similar products or limit the length of term of patent protection we may have for our products. Changes in either patent laws or in interpretations of patent laws in the United States and other countries may diminish the value of our intellectual property or narrow the scope of our patent protection. Any circumstance or change that results in patent protection not being available for our products could adversely affect our business, financial condition and results of operations.

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

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

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

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

We are presently defending two patent infringement lawsuits brought by UTStarcom, Inc. In March 2004, UTStarcom filed a patent infringement lawsuit against us in the United States District Court for the Northern District of California. In February 2005, UTStarcom filed a second lawsuit asserting infringement of a different patent in the same court. In the first lawsuit, the District Court granted summary judgment in our favor finding no infringement, but UTStarcom appealed this ruling to the United States Court of Appeals for the Federal Circuit. The Court of Appeals may reverse its summary judgment ruling, and we may be forced to continue to defend ourselves in this litigation, which would require a further substantial investment of our time and financial resources. Further, if the Court of Appeals reverses the summary judgment, we may ultimately be held liable for infringement of UTStarcom's patent. The second patent lawsuit by UTStarcom has been stayed pending a reissue proceeding of the patent asserted in the case. Such a reissue proceeding may take a year or longer to complete. After the reissue proceeding, the stay of the lawsuit may 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 any of UTStarcom's patents may require us to pay substantial damages based on past sales of our ST16 and, in addition, may force us to limit or cease development, manufacturing and sales of the product. This could significantly and adversely affect our business, financial condition and results of operations.

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

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

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

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

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

We incorporate certain third-party technologies, including software programs, into our products and may need to utilize additional third-party technologies in the future. However, licenses to relevant third-party technology may not continue to be available to us on commercially reasonable terms, or at all. Therefore, we could face delays in product releases until alternative technology can be identified, licensed or developed, and integrated into our current products. These delays, if they occur, could materially adversely affect our business.

Risks Related to this Offering and Ownership of Our Common Stock

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

Prior to this offering there has been no public market for shares of our common stock, and an active public market for these shares may not develop or be sustained after this offering. The initial

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public offering price for our common stock will be determined through negotiations with the representatives of the underwriters. This price will not necessarily reflect the price at which investors in the market will be willing to buy and sell our shares following this offering. In addition, the trading price of our common stock is likely to be highly volatile and could be subject to wide fluctuations in response to various factors. Some of the factors that may cause the market price of our common stock to fluctuate include:

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

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

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

changes in market valuations of similar companies;

success of competitive products;

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

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

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

litigation involving our company, our general industry or both;

additions or departures of key personnel;

investors' general perception of us;

changes in general economic, industry and market conditions; and

changes in regulatory and other dynamics.

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

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

If our existing stockholders sell, or indicate an intention to sell, substantial amounts of our common stock in the public market after the contractual lock-up agreements described below expire, subject to extension or modification as discussed below, and other restrictions on resale lapse, the trading price of our common stock could decline below the initial public offering price. Based on shares outstanding as of December 31, 2006, upon completion of this offering, we will have outstanding _____ shares of common stock, assuming no exercise of the underwriters' over-allotment option. Of these shares, _____ shares of common stock will be subject to a 180-day contractual lock-up with the underwriters. Goldman, Sachs & Co. and Lehman Brothers Inc., acting as co-representatives of the underwriters, may permit our officers, directors, employees and current stockholders who are subject to the contractual lock-up to sell shares prior to the expiration of the lock-up agreements.

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The 180-day contractual lock-up period may be extended or reduced if we announce, or are scheduled to announce, earnings or other material news or event within 15 days before or after the last day of the 180-day lock-up period. If during the last 15 days of the 180-day contractual lock-up

period we issue an earnings release or announce material news or a material event, the contractual lock-up period will continue to apply until the expiration of the 18-day period beginning on the issuance of the earnings release or the announcement of the material news or material event. Prior to the expiration of the 180-day contractual lock-up period, if we announce that we will release earnings results during the 15-day period following the last day of the contractual lock-up period, the lock-up restrictions on resale will expire on the day 18 days prior to the scheduled earnings release so long as we issue a press release and accompanying current report on Form 8-K announcing the early release date at least three days before the early release date. If we do not publicly announce the early release date by such time, the lock-up restrictions will instead continue to apply until the expiration of the 18-day period beginning on the issuance of the earnings release.

In addition, there will also be shares of common stock subject to a 180-day contractual lock-up with us. We may release these shares from these restrictions at our discretion without the prior written consent of either Goldman, Sachs & Co. or Lehman Brothers Inc.

After each of the lock-up agreements pertaining to this offering expire 180 days from the date of this prospectus, or such shorter or longer period described above, up to an additional shares will be eligible for sale in the public market, of which are held by directors, executive officers and other affiliates and will be subject to volume limitations under Rule 144 under the Securities Act and, in certain cases, various vesting agreements. In addition, after this offering, we intend to register approximately shares of our common stock that we have issued or may issue under our equity incentive plans. Once we register these shares, they can be freely sold in the public market upon issuance, subject to the lock-up agreements, applicable vesting schedules and, for directors, executive officers and other affiliates, volume limitations under Rule 144. If these additional shares are sold, or if it is perceived that they will be sold, in the public market, the trading price of our common stock could decline.

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

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

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

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

As a new investor, you will experience substantial dilution as a result of this offering and future equity issuances.

The initial public offering price per share is substantially higher than the pro forma net tangible book value per share of our common stock outstanding prior to this offering. As a result, investors purchasing common stock in this offering will experience immediate substantial dilution of \$ per share. In addition, we have issued options to acquire common stock at prices significantly

below the initial public offering price. To the extent outstanding options are ultimately exercised, there will be further dilution to investors in this offering. This dilution is due in large part to the fact that our earlier investors paid substantially less than the initial public offering price when they purchased their shares of common stock. In addition, if the underwriters exercise their over-allotment option or if we issue additional equity securities, you will experience additional dilution.

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

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

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

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

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

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

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

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

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

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

limit who may call special meetings of stockholders;

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

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

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

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

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

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

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

our ability to attract and retain customers;

our financial performance;

our research and development activities;

the advantages of our solutions as compared to those of others;

our ability to establish and maintain intellectual property rights;

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

our estimates regarding capital requirements and needs for additional financing.

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

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

USE OF PROCEEDS

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

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

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

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

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

DIVIDEND POLICY

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

CAPITALIZATION

The following table sets forth our capitalization as of December 31, 2006:

on an actual basis;

on a pro forma basis to reflect the conversion of all outstanding preferred stock into common stock upon the closing of this offering; and

on a pro forma as adjusted basis to reflect (1) the conversion of all outstanding preferred stock into common stock upon the closing of this offering, (2) the filing of our restated certificate of incorporation prior to the closing of this offering, and (3) our issuance and sale of shares of common stock in this offering at an assumed initial public offering price of \$ per share, the mid-point of the estimated price range shown on the cover page of this prospectus, after deducting the estimated underwriting discount and offering expenses payable by us.

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

As of December 31, 2006

	Actual	Pro Forma	Pro Forma As Adjusted
(in thousands, except share and per share data)			
Redeemable preferred stock, \$0.01 par value:			
64,587,861 shares authorized, issued and outstanding, actual;			
no shares authorized, issued or outstanding, pro forma and pro			
forma as adjusted	\$ 130,270	\$	\$
Stockholders' equity (deficit):			
Preferred stock, \$0.001 par value:			
no shares authorized, issued or outstanding, actual and pro			
forma; 5,000,000 shares authorized and no shares issued or			
outstanding, pro forma as adjusted			
Common stock, \$0.001 par value:			
120,000,000 shares authorized and 11,185,008 shares issued			
and outstanding, actual; shares authorized and			
77,617,019 shares issued and outstanding pro			
forma; shares authorized and shares			
issued and outstanding, pro forma as adjusted(1)	11	78	
Additional paid-in capital		130,203	
Accumulated other comprehensive loss	(1)	(1)	
Accumulated deficit	(105,521)	(105,521)	
Total stockholders' equity (deficit)	\$ (105,511)	\$ 24,759	\$

(1)

For accounting purposes only, the number of issued and outstanding shares does not include 256,250 shares of restricted stock. These shares are subject to repurchase by us until such shares are vested. See Note 11 to our consolidated financial statements for more information.

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A \$1.00 increase (decrease) in the assumed initial public offering price of \$ would increase (decrease) each of additional paid-in capital and total stockholders' equity in the pro forma

as adjusted column by \$ million, assuming the number of shares offered by us, as set forth on the cover of this prospectus, remains the same and after deducting the estimated underwriting discount and offering expenses payable by us.

The table above does not include:

11,846,085 shares of common stock issuable upon the exercise of stock options outstanding as of December 31, 2006 at a weighted average exercise price of \$0.94 per share, of which options to purchase 4,568,075 shares were exercisable as of December 31, 2006 at a weighted average exercise price of \$0.54 per share; and

837,863 shares of common stock available for future issuance under our equity compensation plans as of December 31, 2006.

DILUTION

If you invest in our common stock, your interest will be diluted immediately to the extent of the difference between the initial public offering price per share you will pay in this offering and the pro forma as adjusted net tangible book value per share of our common stock after this offering. Our pro forma net tangible book value as of December 31, 2006 was \$24.8 million, or \$0.32 per share of common stock. Our pro forma net tangible book value per share set forth below represents our total tangible assets less total liabilities, divided by the number of shares of our common stock outstanding on December 31, 2006, and assumes the conversion of all of our outstanding preferred stock into shares of our common stock immediately prior to the closing of this offering.

After giving effect to our issuance and sale of _____ shares of common stock in this offering at an assumed initial public offering price of \$ _____ per share, the mid-point of the estimated price range shown on the cover of this prospectus, after deducting the estimated underwriting discounts and offering expenses payable by us, the pro forma as adjusted net tangible book value as of December 31, 2006 would have been \$ _____ million, or \$ _____ per share. This represents an immediate increase in net tangible book value to existing stockholders of \$ _____ per share. The initial public offering price per share will significantly exceed the net tangible book value per share. Accordingly, new investors who purchase shares of common stock in this offering will suffer an immediate dilution of their investment of \$ _____ per share. The following table illustrates this per share dilution to the new investors purchasing shares of common stock in this offering without giving effect to the over-allotment option granted to the underwriters:

Assumed initial public offering price per share	\$
Pro forma net tangible book value per share as of December 31, 2006	\$ 0.32
Increase per share attributable to sale of shares of common stock in this offering	_____
Pro forma as adjusted net tangible book value per share after the offering	_____
Dilution per share to new investors	\$ _____

A \$1.00 increase (decrease) in the assumed initial public offering price of \$ _____ per share would increase (decrease) the pro forma net tangible book value by \$ _____ million, the pro forma net tangible book value per share after this offering by \$ _____ per share and the dilution in pro forma net tangible book value per share to investors in this offering by \$ _____ per share, assuming that the number of shares offered by us, as set forth on the cover page of this prospectus, remains the same and after deducting the estimated underwriting discount and offering expenses payable by us.

If the underwriters exercise their over-allotment option in full, the pro forma as adjusted net tangible book value will increase to \$ _____ per share, representing an immediate increase to existing stockholders of \$ _____ per share and an immediate dilution of \$ _____ per share to new investors. If any shares are issued in connection with outstanding options, you will experience further dilution.

The following table summarizes, on a pro forma basis as of December 31, 2006, giving effect to the conversion of all outstanding preferred stock into common stock, the differences between the number of shares of common stock purchased from us, the total consideration paid to us, and the average price per share paid by existing stockholders and by new investors purchasing shares of common stock in this offering. The calculation below is based on an assumed initial public offering price of \$ _____ per share, the mid-point of the estimated price range shown on the cover of this

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prospectus, before the deduction of the estimated underwriting discount and offering expenses payable by us:

	Shares Purchased		Total Consideration		Average Price Per Share
	Number	%	Amount	%	
Existing stockholders	77,617,019	%	\$ 99,666,000	%	\$ 1.28
New investors					\$
Total		100%	\$	100%	

The tables above assume no exercise of options to purchase shares of common stock outstanding as of December 31, 2006. At December 31, 2006, there were 11,846,085 shares of common stock issuable upon exercise of outstanding options at a weighted average exercise price of \$0.94 per share. In addition, the table above excludes 837,863 shares of common stock available for future issuance under our option plan at December 31, 2006.

If the underwriters exercise their over-allotment option in full, the number of shares held by new investors will increase to _____, or _____ % of the total number of shares of common stock outstanding after this offering.

SELECTED CONSOLIDATED FINANCIAL DATA

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

We have derived the statement of operations data for the years ended December 31, 2004, 2005, and 2006 and the balance sheet data as of December 31, 2005 and 2006 from our audited consolidated financial statements, which are included in this prospectus. We have derived the statement of operations data for the year ended December 31, 2003 and the balance sheet data as of December 31, 2003 and 2004 from our audited consolidated financial statements, which are not included in this prospectus. We have derived the statement of operations data for the year ended December 31, 2002 and the balance sheet data as of December 31, 2002 from our unaudited consolidated financial statements, which are not included in this prospectus. Our historical results for any prior period are not necessarily indicative of results to be expected for any future period.

	Year Ended December 31,				
	2002	2003	2004	2005	2006
	(unaudited)				
	(in thousands, except per share data)				
Statement of Operations Data:					
Revenues	\$	\$ 182	\$ 34,395	\$ 59,660	\$ 94,350
Cost of revenues		410	1,109	13,643	27,726
Gross profit		(410)	20,950	46,017	66,624
Operating expenses:					
Research and development		18,500	14,748	18,107	25,980
Sales and marketing		4,417	8,289	19,785	30,311
General and administrative		1,954	3,185	7,352	8,515
Total operating expenses		24,871	34,933	45,244	64,806
Income (loss) from operations		(25,281)	(13,983)	773	1,818
Other income (expense), net		(484)	95	644	2,237
Income (loss) before income tax expense		(25,765)	(13,888)	1,417	4,055
Income tax expense			(160)	(513)	(413)
Net income (loss)	\$	(25,765)	(14,048)	\$ 904	\$ 3,642
Accretion of redeemable preferred stock		(2,723)	(6,266)	(7,349)	(7,988)
Net income (loss) applicable to common stockholders	\$	(28,488)	(20,314)	\$ (6,445)	\$ (4,346)
Net income (loss) per share applicable to common stockholders, basic and diluted	\$	(5.89)	(2.19)	\$ (0.65)	\$ (0.41)
Weighted average shares used in computing net income (loss) per share applicable to common shareholders, basic and diluted		4,834	9,296	9,963	10,540
Pro forma net income (loss) per share (unaudited)(1):					
Basic					\$ 0.05
Diluted					\$ 0.04

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Year Ended December 31,

Weighted average shares used in computing pro forma net income
(loss) per share (unaudited):

Basic	76,972
Diluted	82,059

(1)

The pro forma net income (loss) per common share, basic and diluted, has been calculated assuming the conversion of all outstanding redeemable preferred stock into common stock upon the closing of this offering and the elimination of the accretion of redeemable preferred stock.

As of December 31,

2002	2003	2004	2005	2006
------	------	------	------	------

(unaudited)

(in thousands)

Balance Sheet Data:

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

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

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

Overview

Starent Networks is a leading provider of infrastructure solutions that enable mobile operators to deliver multimedia services to their subscribers. We have created solutions that provide core network functions and services, including access from a wide range of radio networks to the operator's packet core network, mobility management of subscriber sessions and call control. Our solutions 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 access-independent solutions integrate multiple network functions and services needed for the delivery of advanced multimedia services, such as video, Internet access, voice-over-IP, e-mail, mobile TV, photo sharing and gaming.

Our solution consists of both hardware and software and can be configured to meet a number of customer needs. A typical purchase consists of our ST16, the Starent operating system and other proprietary software, and our Starent Web EMS management system. A customer typically purchases our solutions with specific capacity and functionality, and may upgrade their system over time through a combination of software and hardware purchases. We sell our solutions to mobile operators around the world both directly and indirectly through our relationships with OEMs, system integrators and distributors. Since the first commercial deployment of our products in 2003, our products have been deployed by over 60 mobile operators in 25 countries. To date, we have had the greatest success in the CDMA market, but have begun to focus on the GSM/UMTS market and received our first purchase order from one of the world's largest GSM operators in June 2006. Our revenue growth will depend on the continued acceptance of our ST16 and related applications and services, further penetration of the GSM/UMTS market, increased adoption of mobile multimedia services and continued migration to packet-based networks by mobile operators.

Since our inception in August 2000, we have raised an aggregate of approximately \$100 million through a series of equity financings, a portion of which we invested in expanding our research and development organization, building our sales force and initiating our marketing and administration operations. We have incurred significant losses to date, and as of December 31, 2006 we had an accumulated deficit of \$105.5 million. We became profitable in 2005 and were also profitable in 2006. Our profitability will be affected by additional expenses that we incur to expand sales, marketing, research and development and general and administrative capabilities in order to grow our business.

We maintain our corporate headquarters in Tewksbury, Massachusetts, and also have sales and development offices in various locations worldwide. We conduct our research and development activities at two locations in India and two locations in the United States. As of December 31, 2006, we had 411 employees worldwide. Our revenues for 2006 were \$94.4 million, our net income was \$3.6 million and we had \$63.7 million of deferred revenue as of December 31, 2006.

Revenues

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

maintenance and technical support associated with our software;

hardware repair and maintenance services; and

implementation, training and professional services.

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

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

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

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

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

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

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

Cost of Revenues

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

Gross Profit

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

Operating Expenses

Operating expenses consist of research and development, sales and marketing and general and administrative expenses.

Research and development expense consists primarily of salaries and related personnel costs, prototype costs related to the design and development of new products and enhancement of existing products, payments to suppliers for design and consulting services and costs of quality assurance and testing. Research and development activities primarily take place at two locations in the United States and two locations in India.

Sales and marketing expense consists primarily of salaries, commissions and related personnel costs, travel and other out-of-pocket expenses and marketing programs such as trade shows. Commissions are recorded as expense when earned and are not necessarily directly proportionate to the amount of revenues recorded since commissions are generally earned at the time we accept customer orders and revenue is recorded once all revenue recognition criteria have been met.

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

Other Income (Expense)

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

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

Accretion of Redeemable Preferred Stock

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

Application of Critical Accounting Policies and Use of Estimates

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

We believe that of our significant accounting policies, which are described in note 2 to the financial statements included in this prospectus, the following accounting policies involve a greater degree of judgment and complexity. Accordingly, we believe these are the most critical to fully understand and evaluate our financial condition and results of operations.

Revenue Recognition

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

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

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

undelivered elements. Revenue for the undelivered elements is then recorded as those elements are delivered. When we defer revenue in an arrangement, the related product costs are also deferred, subject to their realizability, and recognized over the same period as the related revenue.

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

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

Share-Based Compensation

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

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

For the year ended December 31, 2006, we recorded expense of \$1.7 million in connection with stock-based awards. As of December 31, 2006, we had \$5.5 million of unrecognized expense related to non-vested options. This expense is expected to be recognized over a weighted average period of 1.1 years.

As there was no public market for our common stock prior to this offering, we have determined the volatility for options granted in 2006 based on an analysis of reported data for a peer group of companies that issued options with substantially similar terms. The expected volatility of options granted has been determined using an average of the historical volatility measures of this peer group of companies. The expected volatility for options granted during the year ended December 31, 2006 was 68%. The expected life of options has been determined utilizing the "simplified" method as prescribed by the SEC's Staff Accounting Bulletin No. 107, *Share-Based*

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Payment. The expected life of options granted during the year ended December 31, 2006 was 6.25 years and the weighted average risk free interest rates ranged from 4.55% to 4.99%. The risk-free interest rate is based on a U.S. treasury instrument whose term is consistent with the expected life of the stock options. We have not paid, and do not anticipate paying, cash dividends on our shares of common stock; therefore, the expected dividend yield was assumed to be zero. In addition, SFAS 123R requires companies to utilize an estimated forfeiture rate when calculating the expense for the period. As a result, we applied an estimated forfeiture rate of 3%, based on a review of our historical forfeitures, for the year ended December 31, 2006 to determine the expense recorded in our consolidated statements of operations. If this rate changes in future periods, our stock compensation expense may increase or decrease significantly.

In accordance with APB Opinion 25, share-based compensation expense resulted from stock option grants at exercise prices that, for financial reporting purposes, were deemed to be below the estimated grant date fair value of the underlying common stock. During the years ended December 31, 2004 and 2005, we granted options to purchase 6,228,000 shares of our common stock to our employees and consultants. No compensation cost related to stock-based awards to employees was recorded for the years ended December 31, 2004 and 2005, as the exercise prices were deemed to equal or exceed the grant date fair value of common stock.

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

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

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

important developments relating to our product;

our stage of development and business strategy;

our operating results;

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

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

During 2004 and 2005, our board also considered our customer base and our prospects for future growth. The board noted that our bookings and revenues were generated almost exclusively from CDMA operators. However, because a majority of worldwide subscribers are served by GSM/UMTS operators, management and the board of directors believed it was crucial for us to penetrate the GSM/UMTS market before we could achieve a level of sustainable business growth that would enable any liquidity scenarios to be practical. At the time of each option grant during 2004 and 2005, the board considered the factors discussed above and at various points throughout this period valued our common stock between \$0.20 and \$1.10 per share.

In February 2006, our board requested that an independent firm perform a contemporaneous valuation of our common stock. Our board engaged Gordon Associates Inc., an independent third-party valuation firm, to perform this valuation. In connection with this valuation, the valuation firm considered various liquidity alternatives, but determined that the probabilities and timing of the

alternative liquidity scenarios could not be reliably estimated. The valuation firm determined that the fair value of the common stock as of February 22, 2006 was \$0.99 per share. On April 18, 2006, our board of directors considered the results of the independent valuation, as well as other factors our board deemed relevant, including that we had not yet penetrated the GSM/UMTS market, and decided to continue to value our common stock at \$1.10 per share.

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

In August 2006, our board of directors requested the valuation firm to update their February 2006 report. The valuation firm updated their valuation, which resulted in a determination that the value of our common stock as of August 30, 2006 was \$1.09 per share. On September 29, 2006, our board of directors considered the results of the August 2006 independent valuation, as well as other factors the board deemed relevant, and decided to continue to value our common stock at \$1.10 per share.

In November 2006, our board of directors requested the valuation firm to perform another valuation, which resulted in a valuation of \$3.42 per share of common stock as of November 27, 2006. The November 2006 valuation was prepared utilizing the probability weighted expected return method as prescribed by the AICPA Practice Aid, *Valuation of Privately-Held-Company Equity Securities Issued as Compensation*, referred to as the Practice Aid. This valuation took into consideration the following scenarios:

completion of an initial public offering;

sale to a strategic acquirer;

remaining private; and

liquidation at a price at or below the liquidation preference.

On December 14, 2006, our board of directors considered the results of the November 2006 valuation and determined to value our common stock at \$3.42 per share as of that date.

In connection with the preparation of our financial statements for the year ended December 31, 2006, we examined the valuations of our common stock after June 2006, the point in time of our first significant GSM/UMTS purchase order. As noted above, the \$3.42 per share value determined in the November 2006 valuation was utilized for financial reporting purposes to record share-based compensation for awards granted on December 14 and December 22, 2006. We retrospectively reviewed the August 2006 valuation for financial reporting purposes and prepared an analysis of that valuation that included the values of the alternative liquidation scenarios as determined in the November 2006 valuation. As a result of this analysis, we retrospectively determined that the fair value of our common stock for financial reporting purposes as of the June, September and October 2006 stock option grant dates was \$1.28, \$2.66, and \$2.99 per share, respectively.

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

Grants Made during the Year Ended December 31, 2006	Number of Option and Restricted Shares Granted(a)	Exercise or Purchase Price	Fair Value of Common Stock
February 2, 2006	73,000	\$ 1.10(b)	\$ 1.10
April 18, 2006	1,458,000	1.10(c)	1.10
June 15, 2006	339,000	1.10(c)	1.28(e)
September 29, 2006	1,846,000	1.10(c)	2.66(e)
October 25, 2006	36,000	1.10(c)	2.99(e)
December 14, 2006	545,500	3.42(d)	3.42
December 22, 2006	300,000	3.42(d)	3.42

- (a) Excludes an aggregate of 3,825 shares of restricted stock granted to our employees at no cost during 2006. These shares of restricted stock vested immediately upon grant. We recorded compensation expense for these stock grants based upon the fair value of our common stock on the date of grant as determined by our board of directors.
- (b) The exercise or purchase price for the award was equal to the fair value of our common stock as determined in a contemporaneous valuation by our board of directors.
- (c) The exercise or purchase price for the award was equal to the fair value of our common stock as determined in a contemporaneous valuation by our board of directors, which considered, among other factors, the then most recent common stock valuation performed by the valuation firm. The exercise price was at least equal to the fair market value as determined in the then most recent valuation.
- (d) The exercise or purchase price for the award was equal to the fair value of our common stock as determined by our board of directors, based upon a contemporaneous valuation of our common stock by the valuation firm.
- (e) Retrospectively reassessed for financial reporting purposes in connection with the preparation of our financial statements for the year ended December 31, 2006.

Inventory

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

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

Income Taxes

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

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

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

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

Research and Development Expense

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

Results of Operations

Comparison of Years Ended December 31, 2005 and 2006

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

Revenues

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

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

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Year Ended December 31,

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

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

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Product revenues, which include hardware and software sales, increased \$29.2 million from 2005 due primarily to increased sales to major mobile operators in the United States and Canada. The decrease in revenues in Japan and Korea was due primarily to the incremental deferral of approximately \$8.4 million related to Japan and \$5.5 million related to Korea, as compared to the deferral at December 31, 2005. We anticipate these deferred balances will be recognized during 2007. In addition, a portion of the decrease in revenues in Korea was due to 2005 being the final period in which revenues were recognized on a subscription basis on a contract that expired on December 31, 2005. In 2006, \$14.0 million of our indirect revenue that had been deferred at December 31, 2005 was recognized based upon us establishing VSOE for maintenance and support services for a type of customer. At that point in time, deferred revenue was adjusted to the fair value of the undelivered services in accordance with SOP 97-2.

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

Cost of Revenues and Gross Profit

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

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

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

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

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

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

Operating Expenses

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

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

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

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

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

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

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

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

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

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 payroll and related expenses, prototype and related equipment and depreciation expense to increase in 2007 as we continue to add quality assurance personnel, test enhancements to our hardware and software and increase our test lab space.

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

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

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

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

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

Consulting expenses consist primarily of sales contractors utilized in areas of the world in which we do not have employees and costs associated with marketing and customer

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studies. The \$527,000 increase in 2006 was due primarily to payments to consultants paid on a contingent basis relative to a specific customer and additional market studies.

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

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. We expect commissions to be relatively consistent in 2007 as compared to 2006 and to decrease as a percentage of revenues as we leverage our sales organization. However, commissions may vary significantly from our expectations if our customer orders differ significantly from the quotas established for our sales personnel. Despite the expected increases in sales and marketing expenses, we expect these expenses to decrease as a percentage of total revenues in future periods, as we leverage our current sales and marketing organizations.

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

Year Ended December 31,		
2005	2006	Period-to-Period Change
% of Revenues	% of Revenues	