VONAGE HOLDINGS CORP
Form S-1/A
May 23, 2006

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**As filed with the Securities and Exchange Commission on May 23, 2006**

**Registration No. 333-131659**

# UNITED STATES
# SECURITIES AND EXCHANGE COMMISSION

**WASHINGTON, D.C. 20549**

**AMENDMENT NO. 7**
**TO**

# FORM S-1

**REGISTRATION STATEMENT**
**UNDER**
**THE SECURITIES ACT OF 1933**

# VONAGE HOLDINGS CORP.

(Exact name of registrant as specified in its charter)

| **Delaware** | **4813** | **11-3547680** |
|---|---|---|
| (State of Incorporation) | (Primary Standard Industrial Classification Code Number) | (I.R.S. Employer Identification No.) |

**23 Main Street**
**Holmdel, New Jersey 07733**
**(732) 528-2600**

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

**John S. Rego**
**Executive Vice President,**
**Chief Financial Officer and Treasurer**
**Vonage Holdings Corp.**
**23 Main Street**
**Holmdel, New Jersey 07733**
**(732) 528-2600**
(Name, address, including zip code, and telephone number, including area code, of agent for service)

***With copies to:***

| | |
|---|---|
| **James S. Scott, Sr., Esq.**<br>**Stephen T. Giove, Esq.**<br>**Ferdinand J. Erker, Esq.**<br>**Shearman & Sterling LLP**<br>**599 Lexington Avenue**<br>**New York, New York 10022-6069**<br>**(212) 848-4000** | **John T. Gaffney, Esq.**<br>**Erik R. Tavzel, Esq.**<br>**Cravath, Swaine & Moore LLP**<br>**Worldwide Plaza**<br>**825 Eighth Avenue**<br>**New York, New York 10019**<br>**(212) 474-1000** |

**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 to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act, check the following box. o

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

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

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

**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 of 1933 or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to said 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 an offer to buy these securities in any state where the offer or sale is not permitted.**

**SUBJECT TO COMPLETION, DATED MAY 23, 2006**

**PROSPECTUS**

## 31,250,000 Shares

# Vonage Holdings Corp.

## Common Stock

This is the initial public offering of shares of our common stock. All of the 31,250,000 shares of common stock are being sold by us.

Prior to this offering, there has been no public market for our common stock. We currently expect the initial public offering price to be between $16.00 and $18.00 per share. Our common stock has been approved for listing on the New York Stock Exchange under the symbol "VG," subject to official notice of issuance.

**Investing in our common stock involves a high degree of risk. See "Risk Factors" beginning on page 8 to read about risk factors you should consider before buying shares of our common stock.**

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

| | Per Share | Total |
|---|---|---|
| Public offering price | $ | $ |
| Underwriting discount | $ | $ |
| Proceeds, before expenses, to us | $ | $ |

We have granted the underwriters an option to purchase up to 4,687,500 additional shares of common stock to cover over-allotments.

The underwriters expect to deliver the shares to purchasers on or about , 2006.

**Citigroup** **Deutsche Bank Securities** **UBS Investment Bank**

**Bear, Stearns & Co. Inc.**

**Piper Jaffray** **Thomas Weisel Partners LLC**

Prospectus dated , 2006

**You should rely only on information contained in this prospectus or in any related free writing prospectus filed with the Securities and Exchange Commission and used or referred to in an offering to you of these securities. We have not authorized anyone to provide you with different information. We are not making an offer of these securities in any state where the offer is not permitted. You should not assume that the information contained in this prospectus is accurate as of any date other than the date on the front of this prospectus.**

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Until , 2006 ( days after the date of this prospectus), all dealers that buy, sell or trade our common stock, whether or not participating in this offering, may be required to deliver a prospectus. This is in addition to the dealers' obligation to deliver a prospectus when acting as underwriters and with respect to their unsold allotments or subscriptions.

## PROSPECTUS SUMMARY

*The following summary is qualified in its entirety by the more detailed information and financial statements and notes appearing elsewhere in this prospectus. Before making an investment, prospective investors should read this entire prospectus carefully, especially the information set forth under the heading "Risk Factors."*

**Our Company**

We are a leading provider of broadband telephone services with over 1.6 million subscriber lines as of April 1, 2006. Utilizing our innovative Voice over Internet Protocol, or VoIP, technology platform, we offer feature-rich, low-cost communications services that offer users an experience similar to traditional telephone services. While customers in the United States currently represent over 95% of our subscriber lines, we continue to expand internationally, having launched our service in Canada in November 2004 and in the United Kingdom in May 2005. Since our U.S. launch in October 2002, we have experienced rapid subscriber line growth. For example, we more than tripled our subscriber lines during 2005.

We offer our customers a variety of service plans, each of which has a fixed monthly fee. Each of our service plans includes a full suite of features typically offered by traditional telephone service providers, such as call waiting, caller ID and call forwarding. In addition, we offer several enhanced features at no additional charge that are not typically offered by traditional circuit-switched telephone service providers, such as area code selection, web- and e-mail-based voicemail and an account management website that allows customers to add or change their features online. We also offer a number of premium services for an additional fee, such as toll free numbers, fax numbers and virtual phone numbers. We offer low international per minute calling rates for calls to locations outside the United States, Puerto Rico and Canada. We believe the combination of these factors allows us to offer an attractive value proposition to our customers.

Our customers can make and receive calls using a standard telephone plugged into a portable Vonage-enabled device that can be used almost anywhere a broadband Internet connection is available. We transmit these calls using VoIP technology, which converts voice signals into digital data packets for transmission over the Internet. We provide our service by using our customers' existing broadband Internet connections, eliminating the need for us to build or lease costly "last-mile" connections. In addition, our network is based on internally developed software and industry-standard servers, rather than the more expensive switches used by traditional telephone service providers. This network design enables us to monitor, maintain and expand our network quickly and efficiently while realizing capital and operating cost savings.

We have invested heavily to build a strong brand that helps drive our subscriber growth. During 2005 and the first three months of 2006, we spent an aggregate of $331.7 million on marketing. We employ an integrated marketing strategy that includes extensive television, online, print and radio advertising, a customer referral program and a range of other promotions, all designed to build our brand, attract new customers and retain existing customers. For example, according to Nielsen//NetRatings, an independent Internet media and market research firm, we were the top advertiser on the Internet from January 2005 through the first quarter of 2006 based on estimated spending and impressions. We employ a broad distribution strategy and acquire customers through our websites, our toll free numbers and our presence in leading retail outlets, including Best Buy, Circuit City, CompUSA and RadioShack stores.

We have experienced rapid revenue growth since our inception. Our revenues were $18.7 million in 2003, $79.7 million in 2004, $269.2 million in 2005 and $118.9 million for the three months ended March 31, 2006. While our revenues have grown rapidly, we have experienced increasing net losses, primarily driven by our increase in marketing expenses. For the period from inception through March 31, 2006, our accumulated deficit was $467.4 million. For 2005 and the three months ended March 31, 2006, our net loss was $261.3 million and $85.2 million, respectively, and our marketing expenses were $243.4 million and $88.3 million, respectively. To grow our revenue and customer base and enhance awareness of our brand, we have chosen to spend significant amounts on our marketing activities, and we intend to continue to do so. While this strategy will have the effect of delaying or preventing us from generating net income in the near term, we believe that our focus on growth will better position us as a strong competitor in the long term. As of March 31, 2006, our debt consisted of $253.4 million of convertible notes (principal amount of $253.6 less unamortized discount of $0.2 million) and $24.9 million of capital leases.

**Our Market Opportunity**

VoIP communications are carried as data packets and require a broadband Internet connection that has sufficient bandwidth to deliver the data uninterrupted. As a result, broadband penetration has been a key driver of VoIP's expansion to date. We believe that as broadband adoption becomes even more prevalent worldwide, consumers will increasingly look to use their high-speed Internet connections for more of their voice, video and data communications. Many independent market research analysts believe that the growth rate in new VoIP subscribers over the next few years will exceed the growth rate for new broadband subscribers. For example, several such analysts have estimated that the approximately 0.9 to 1.5 million U.S. or North American consumer VoIP users in 2004 will grow to between 8.2 and 15.3 million by the end of 2007. As a leading provider of broadband telephone services using VoIP, we believe we are well positioned to benefit from the growth expected in this marketplace. However, the VoIP market may not grow as expected, and our business might not benefit from any actual growth that does occur.

**Our Strengths**

We believe we have the following strengths:

- Leading VoIP Market Position and VoIP Brand in the United States
- Attractive Customer Value Proposition
- Innovative, Low-Cost Technology Platform
- Strong Direct and Retail Distribution Channels
- Loyal Customer Base

**Our Strategy**

We believe that our strong brand identity and reputation for quality communications services are instrumental to building our customer base. Our core business strategy is to enhance our brand image and the quality of our services in order to attract new customers. As we build on our leading brand and above-mentioned strengths, our additional business strategies are to:

- Develop Attractive, Innovative Features and Products
- Expand our Direct and Retail Distribution Capabilities
- Continue to Improve the Customer Experience
- Expand into New Geographic Markets

**Our Investors**

Simultaneously with the completion of this offering, all outstanding shares of all series of our convertible preferred stock will automatically convert into shares of common stock. Upon completion of this offering, after giving effect to the conversion of our preferred stock into shares of common stock but not giving effect to the conversion or exercise of other securities convertible into or exercisable for common stock, affiliates of 3i Group plc, Bain Capital, LLC, Institutional Venture Partners, Meritech Capital Partners and New Enterprise Associates collectively will own 70,287,914 shares of common stock, or 45% of our common stock. Jeffrey A. Citron, our principal stockholder, founder, Chairman and Chief Strategist, will own 48,427,617 shares of common stock, or 31% of our common stock. These financial sponsors and Mr. Citron had collectively invested an aggregate of $450.5 million in our company as of March 31, 2006.

**E-911 Initiative**

The U.S. Federal Communications Commission, or FCC, required us to provide enhanced emergency dialing capabilities, or E-911, to all of our U.S. customers by November 28, 2005. We are not currently in compliance with the FCC's order, although approximately 75% of our U.S. subscriber lines were E-911 compliant as of April 1, 2006. Additional progress is being made on a daily basis and we expect to provide E-911 capabilities to nearly all of our remaining subscriber lines within the year. We have requested a waiver from the FCC to provide us with the additional time needed to complete the roll-out. It is possible the FCC will deny our request and subject us to fines or penalties or order us to stop accepting new customers in certain areas until we have rolled out E-911 capability in those areas.

**Risk Factors**

An investment in our common stock involves a high degree of risk. The following risks, as well as the other risks discussed in "Risk Factors," should be carefully considered before participating in this offering:

- our history of net operating losses and our need for cash to finance our growth;
- the competition we face, including from companies with greater financial resources;
- our dependence on our customers' existing broadband connections, which gives us less control over call quality than traditional telephone networks;
- differences between our service and traditional telephone services, including our 911 service;
- uncertainties relating to regulation of VoIP services;
- system disruptions or flaws in our technology;
- our ability to manage our rapid growth; and
- the risk that VoIP does not gain broader acceptance.

**Corporate Information**

We were incorporated in Delaware in May 2000 and changed our name to Vonage Holdings Corp. in February 2001. Our principal executive offices are located at 23 Main Street, Holmdel, NJ 07733. Our telephone number is (732) 528-2600. Our websites are http://www.vonage.com, http://www.vonage.ca and http://www.vonage.co.uk. **Information contained on our websites or that can be accessed through our websites is not part of this prospectus, and investors should not rely on any such information in making the decision whether to purchase our common stock.**

**The Offering**

| | |
|---|---|
| Common stock offered by us | 31,250,000 shares |
| Common stock outstanding after the offering | 155,732,440 shares |
| Over-allotment option | 4,687,500 shares |
| Use of proceeds | We estimate that the net proceeds from our sale of 31,250,000 shares of our common stock in this offering will be approximately $493.7 million. We intend to use these net proceeds to fund the expansion of our business, including funding marketing expenses and operating losses. |
| Dividend policy | We do not intend to pay any cash dividends on our common stock. |
| Directed share programs | We intend to reserve a portion of our common stock offered in this prospectus for sale to certain of our customers and other persons related to us. See "Underwriting Directed Share Programs" for more information. |
| Risk factors | Investing in our common stock involves a high degree of risk. See "Risk Factors" beginning on page 8 to read about risk factors you should consider before buying shares of our common stock. |
| Proposed symbol | VG |

The number of shares of common stock outstanding after this offering excludes:

16,904,494 shares of common stock issuable upon exercise of currently outstanding options as of March 31, 2006 with exercise prices ranging from $0.70 to $35.00 and having a weighted average exercise price of $7.89 per share;

3,085,715 shares of common stock issuable upon exercise of currently outstanding warrants with exercise prices ranging from $0.70 to $1.40 per share and having a weighted average exercise price of $1.28 per share;

shares of common stock reserved for future grants under our stock option plans which will be determined under a formula set forth in our 2006 Incentive Plan, and will equal approximately 17.65% of the number of shares that are issued and outstanding from time to time. As of March 31, 2006, assuming the conversion of the outstanding shares of preferred stock and sale of the shares in this offering, there would be approximately 27,486,776 shares reserved for grant; and

shares of common stock issuable upon conversion of our convertible notes, which totaled 17,826,424 shares as of March 31, 2006, based on a conversion price of $14.22 per share. Additional shares will be issuable upon conversion if we elect to pay interest on these notes in kind by increasing the principal outstanding under the notes. See "Description of Convertible Notes."

Except as otherwise indicated, all information in this prospectus assumes no exercise of the underwriters' over-allotment option and reflects the conversion of all outstanding shares of our preferred stock into a total of 123,069,420 shares of common stock upon the closing of this offering and reflects a 1 for 2.8 reverse stock split, which took effect on May 18, 2006.

**Summary Consolidated Financial Data**

The following table sets forth our summary consolidated financial data. The statement of operations data for the years ended December 31, 2003, 2004 and 2005 and the balance sheet data as of December 31, 2004 and 2005 are derived from our audited consolidated financial statements and related notes included in the back of this prospectus. The balance sheet data as of December 31, 2003 is derived from our audited consolidated financial statements and related notes not included in this prospectus. The statement of operations data for the three months ended March 31, 2005 and 2006 and the balance sheet data as of March 31, 2006 are derived from our unaudited consolidated financial statements included in the back of this prospectus. In the opinion of management, the unaudited consolidated financial statements have been prepared on the same basis as our audited consolidated financial statements and include all adjustments, consisting of only normal recurring adjustments, necessary for a fair presentation of the information set forth therein. The results for any interim period are not necessarily indicative of the results that may be expected for a full year.

The results included below and elsewhere in this prospectus are not necessarily indicative of our future performance. You should read this information together with "Capitalization," "Selected Historical Financial Data," "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and the related notes included elsewhere in this prospectus.

| | For the Years Ended December 31, | | | For the Three Months Ended March 31, | |
|---|---|---|---|---|---|
| | 2003 | 2004 | 2005 | 2005 | 2006 |
| | (dollars in thousands) | | | | |
| | | | | | (Restated(14)) |
| **Statement of Operations Data:** | | | | | |
| Operating Revenues: | | | | | |
| Telephony services | $ 16,905 | $ 75,864 | $ 258,165 | $ 38,583 | $ 111,658 |
| Customer equipment and shipping | 1,817 | 3,844 | 11,031 | 2,127 | 7,225 |
| | 18,722 | 79,708 | 269,196 | 40,710 | 118,883 |
| Operating Expenses: | | | | | |
| Direct cost of telephony services (excluding depreciation and amortization of $1,388, $2,519, $6,671, $954 and $2,552) | 8,556 | 23,209 | 84,050 | 12,108 | 37,584 |
| Direct cost of goods sold | 4,867 | 18,878 | 40,441 | 11,588 | 17,580 |
| Selling, general and administrative | 19,174 | 49,186 | 154,716 | 20,553 | 52,875 |
| Marketing(1) | 11,819 | 56,075 | 243,404 | 55,436 | 88,288 |
| Depreciation and amortization | 2,367 | 3,907 | 11,122 | 1,610 | 4,959 |
| | 46,783 | 151,255 | 533,733 | 101,295 | 201,286 |
| Loss from operations | (28,061) | (71,547) | (264,537) | (60,585) | (82,403) |
| Net loss | $ (29,974) | $ (69,921) | $ (261,334) | $ (60,002) | $ (85,160) |
| **Statement of Cash Flow Data:** | | | | | |
| Net cash used in operating activities | $ (16,583) | $ (38,600) | $ (189,765) | $ (23,493) | $ (74,559) |
| Net cash provided by (used in) investing activities | (4,933) | (73,707) | (154,638) | 7,896 | 21,770 |
| Net cash provided by financing activities | 34,226 | 141,094 | 434,006 | 148 | 1,851 |

| | December 31, | | | March 31, | Pro forma March 31, |
|---|---|---|---|---|---|
| | 2003 | 2004 | 2005 | 2006 | 2006(13) |
| | (dollars in thousands) | | | (Restated(14)) | (Restated(14)) |
| **Balance Sheet Data (at period end):** | | | | | |
| Cash, cash equivalents and marketable securities | $ 14,245 | $ 105,768 | $ 266,379 | $ 175,461 | $ 175,461 |
| Property and equipment, net | 9,325 | 16,290 | 103,638 | 118,947 | 118,947 |
| Total assets | 28,311 | 136,493 | 446,882 | 378,197 | 378,197 |
| Convertible notes(2) | | | 247,958 | 253,352 | 253,352 |
| Capital lease obligations | 5 | | 22,431 | 24,907 | 24,907 |
| Total liabilities | 14,038 | 51,045 | 426,940 | 438,790 | 438,790 |
| Total redeemable preferred stock | 51,409 | 192,521 | 388,427 | 388,439 | |
| Total stockholders' deficit | (37,136) | (107,073) | (368,485) | (449,032) | (60,593) |

| | For the Years Ended December 31, | | | For the Three Months Ended March 31, | |
|---|---|---|---|---|---|
| | 2003 | 2004 | 2005 | 2005 | 2006 |
| **Operating and Other Data (unaudited):** | | | | | |
| Gross subscriber line additions(3) | 91,522 | 364,214 | 1,099,641 | 280,123 | 421,890 |
| Net subscriber line additions(4) | 77,936 | 304,849 | 878,472 | 249,333 | 328,279 |
| Subscriber lines(5)(6) | 85,717 | 390,566 | 1,269,038 | 639,899 | 1,597,317 |
| Average monthly customer churn(7) | 2.48% | 1.82% | 2.05% | 1.70% | 2.11% |
| Average monthly revenue per line(8) | $ 33.37 | $ 27.89 | $ 27.03 | $ 26.34 | $ 27.65 |
| Average monthly telephony services revenue per line(9) | $ 30.13 | $ 26.55 | $ 25.93 | $ 24.96 | $ 25.97 |
| Average monthly direct cost of telephony services per line(10) | $ 15.25 | $ 8.12 | $ 8.44 | $ 7.83 | $ 8.74 |
| Marketing cost per gross subscriber line addition(11) | $ 129.14 | $ 153.96 | $ 221.35 | $ 197.90 | $ 209.27 |
| Employees(5)(12) | 189 | 648 | 1,355 | 1,045 | 1,416 |

(1) Marketing expense consists of costs of advertising, which includes online, television, print and radio advertising and direct mail, promotions, sponsorships and inbound and outbound telemarketing; creative and production costs; the costs to serve and track our online advertising; certain amounts we pay to retailers for newspaper insert advertising, product placement and activation commissions; and the cost associated with our customer referral program. Marketing expense does not include the cost of certain customer acquisition activities, such as rebates and promotions, which are accounted for as an offset to revenues, or customer equipment subsidies, which are accounted for as direct cost of goods sold.

(2) As of March 31, 2006, we had convertible notes with a principal amount of $253.6 million before unamortized discount of $0.2 million.

(3) Gross subscriber line additions for a particular period are calculated by taking the net subscriber line additions during that period and adding to that the number of subscriber lines that terminated during that period. This number does not include subscriber lines both added and terminated during the period, where termination occurred within the first 30 days after activation. The number does include, however, subscriber lines added during the period that are terminated within 30 days of activation but after the end of the period.

(4) Net subscriber line additions for a particular period reflect the number of subscriber lines at the end of the period less the number of subscriber lines at the beginning of the period.

(5) At end of period.

6

(6)
Subscriber lines include, as of a particular date, all subscriber lines from which a customer can make an outbound telephone call on that date. Our subscriber lines include fax lines, SoftPhones and WiFi phones but do not include our virtual phone numbers or toll free numbers, which only allow inbound telephone calls to customers.

(7)
Average monthly customer churn for a particular period is calculated by dividing the number of customers that terminated during that period by the simple average number of customers during the period and dividing the result by the number of months in the period. The simple average number of customers during the period is the number of customers on the first day of the period, plus the number of customers on the last day of the period, divided by two. Terminations, as used in the calculation of churn statistics, do not include customers terminated during the period if termination occurred within the first 30 days after activation. We monitor churn on a daily basis and use it as an indicator of the level of customer satisfaction. Other companies may calculate churn differently, and their churn data may not be directly comparable to ours. Average monthly customer churn is calculated using the number of customers, not subscriber lines. The number of customers is lower than the number of subscriber lines because some customers have more than one subscriber line.

(8)
Average monthly revenue per line for a particular period is calculated by dividing our total revenue for that period by the simple average number of subscriber lines for the period and dividing the result by the number of months in the period. The simple average number of subscriber lines for the period is the number of subscriber lines on the first day of the period, plus the number of subscriber lines on the last day of the period, divided by two.

(9)
Average monthly telephony services revenue per line for a particular period is calculated by dividing our total telephony services revenue for that period by the simple average number of subscriber lines for the period and dividing the result by the number of months in the period.

(10)
Average monthly direct cost of telephony services per line for a particular period is calculated by dividing our direct cost of telephony services for that period by the simple average number of subscriber lines for the period and dividing the result by the number of months in the period.

(11)
Marketing cost per gross subscriber line addition is calculated by dividing our marketing expense for a particular period by the number of gross subscriber line additions during the period.

(12)
Represents the number of personnel that are on our payroll and excludes temporary or outsourced labor.

(13)
Assumes all redeemable preferred stock was converted on January 1, 2006 into common stock with the exception of the Series A-2 preferred stock warrant which has been reclassified to additional paid-in capital on the balance sheet.

(14)
In December 2005 and January 2006, we issued approximately $249,900 of convertible notes, and an additional $3,600 as the payment of interest in kind in March 2006. Originally, we believed that the convertible notes contained an embedded derivative and accordingly accounted for the embedded derivative by bifurcating the embedded derivative from the convertible notes at the date of issuance and subsequently remeasuring the fair value of the embedded derivative at December 31, 2005 and March 31, 2006. In May 2006, upon further review, we concluded that the convertible notes do not contain an embedded derivative. See "Note 1 to our consolidated financial statements." "Restated" amounts in the Statements of Operations Data reflect the removal of the income attributable to the change in fair value of derivatives embedded within the convertible notes of $13,392 and a reduction to interest expense related to the convertible notes of $1,029. "Restated" amounts in the Balance Sheet Data reflect the removal of the fair value of derivatives embedded within the convertible notes of $8,800 and the removal of the unamortized discount related to embedded derivatives which increased the outstanding amount of the convertible notes by $21,161. The convertible notes also decreased by $212 for the beneficial conversion feature. The impact to the December 31, 2005 consolidated financial statements for these changes was not considered material and accordingly only reclassifications were required.

## RISK FACTORS

*Investing in our common stock involves a high degree of risk. Before you invest in our common stock, you should understand and carefully consider the risks below, as well as all of the other information contained in this prospectus and our financial statements and the related notes included elsewhere in this prospectus. Any of these risks could materially adversely affect our business, financial condition and results of operations and the trading price of our common stock, and you may lose all or part of your investment.*

### Risks Related to Our Business

***We have incurred increasing quarterly losses since our inception, and we expect to continue to incur losses in the future.***

We have incurred losses since our inception, and we expect to continue to incur losses in the future. For the period from our inception through March 31, 2006, our accumulated deficit was $467.4 million. Our quarterly net losses generally have increased each quarter from our inception through the quarter ended March 31, 2006, for which our net loss was $85.2 million. Initially, our net losses were driven principally by start-up costs and the costs of developing our technology. More recently, our net losses have been driven principally by marketing expense, which was $88.3 million for the three months ended March 31, 2006. In order to grow our revenue and customer base, we have chosen to increase our marketing expenditures significantly. We are pursuing growth, rather than profitability, in the near term to capitalize on the current expansion of the broadband and VoIP markets and enhance the future value of our company. This strategy, however, may not be successful, and we may never achieve profitability. In the past, we projected that we would generate net income during future periods, but then generated a net loss. For example, in 2003, we projected that we would generate net income in the first quarter of 2005. However, we generated a net loss of $60.0 million during that quarter, in large part due to our decision to increase our marketing expense. We intend to continue to increase our marketing expense, and we may continue to generate net losses for the foreseeable future. In addition, we will always be required to incur some marketing expense in order to replace customers who terminate our service, or "churn." Further, marketing expense is not the only factor that may contribute to our net losses. For example, interest expense on our convertible notes of at least $12.7 million annually will contribute to our net losses. As a result, even if we significantly reduce our marketing expense, we may continue to incur net losses.

***If we are unable to compete successfully, we could lose market share and revenue.***

The telecommunications industry is highly competitive. We face intense competition from traditional telephone companies, wireless companies, cable companies and alternative voice communication providers. Our principal competitors are the traditional telephone service providers, namely AT&T, Inc. (formerly SBC Communications Inc.), BellSouth Corp., Citizens Communications Corp., Qwest Communications International Inc. and Verizon Communications, Inc., which provide telephone service based on the public switched telephone network. Some of these traditional providers also have added or are planning to add VoIP services to their existing telephone and broadband offerings. We also face, or expect to face, competition from cable companies, such as Cablevision Systems Corp., Charter Communications, Inc., Comcast Corporation, Cox Communications, Inc. and Time Warner Cable (a division of Time Warner Inc.), which have added or are planning to add VoIP services to their existing cable television, voice and broadband offerings. Further, wireless providers, including Cingular Wireless LLC, Sprint Nextel Corporation, T-Mobile USA Inc. and Verizon Wireless, offer services that some customers may prefer over wireline service. In the future, as wireless companies offer more minutes at lower prices, their services may become more attractive to customers as a replacement for wireline service. Some of these providers may be developing a dual mode phone that will be able to use VoIP where broadband access is available and cellular phone service elsewhere, which will pose additional competition to our offerings.

Most traditional wireline and wireless telephone service providers and cable companies are substantially larger and better capitalized than we are and have the advantage of a large existing customer base. Because most of our target customers are already purchasing communications services from one or more of these providers, our success is dependent upon our ability to attract target customers away from their existing providers. Until recently, our target market has been composed largely of early adopters, or people who tend to seek out new technologies and services. Attracting customers away from their existing providers will become more difficult as the early adopter market becomes saturated and mainstream customers make up more of our target market. These competitors could focus their substantial financial resources to develop competing technology that may be more attractive to potential customers than what we offer. Our competitors' financial resources may allow them to offer services at prices below cost or even for free in order to maintain and gain market share or otherwise improve their competitive positions. Our competitors also could use their greater financial resources to offer VoIP services with more attractive service packages that include on-site installation and more robust customer service. In addition, because of the other services our competitors provide, they may choose to offer VoIP services as part of a bundle that includes other products, such as video, high speed Internet access and wireless telephone service, which we do not offer. This bundle may enable our competitors to offer VoIP service at prices with which we may not be able to compete or to offer functionality that integrates VoIP service with their other offerings, both of which may be more desirable to consumers. Any of these competitive factors could make it more difficult for us to attract and retain customers, cause us to lower our prices in order to compete and reduce our market share and revenues.

We also compete against established alternative voice communication providers, such as Skype (a service of eBay Inc.), and face competition from other large, well-capitalized Internet companies, such as America Online, Inc., Google Inc., Microsoft Corporation and Yahoo! Inc., which have recently launched or plan to launch VoIP-enabled instant messaging services. In addition, we compete with independent VoIP service providers. Some of these service providers may choose to sacrifice revenue in order to gain market share and have offered their services at lower prices or for free. In order to compete with such service providers, we may have to significantly reduce our prices, which would delay or prevent our profitability. See "Business Competition."

***Decreasing telecommunications prices may cause us to lower our prices to remain competitive, which could delay or prevent our future profitability.***

Currently, our prices are lower than those of many of our competitors for comparable services. However, domestic and international telecommunications prices have decreased significantly over the last few years, and we anticipate that prices will continue to decrease. Users who select our service offerings to take advantage of our prices may switch to another service provider as the difference between prices diminishes or disappears, and we may be unable to use our price as a distinguishing feature to attract new customers in the future. Such competition or continued price decreases may require us to lower our prices to remain competitive, may result in reduced revenue, a loss of customers or a decrease in our subscriber line growth and may delay or prevent our future profitability.

***If VoIP technology fails to gain acceptance among mainstream consumers, our ability to grow our business will be limited.***

The market for VoIP services has only recently begun to develop and is rapidly evolving. We currently generate all of our revenue from the sale of VoIP services and related products to residential and small office or home office customers. Revenue generated from sales to residential customers will continue to account for most of our revenue for the foreseeable future. We believe that a significant portion of our revenue currently comes from consumers who are early adopters of VoIP technology. However, in order for our business to continue to grow and to become profitable, VoIP technology must gain acceptance among mainstream consumers, who tend to be less technically knowledgeable and more resistant to new technology or unfamiliar services. Because potential VoIP customers need to connect additional hardware at their location and take other technical steps not required for the use of traditional telephone service, mainstream consumers may be reluctant to use our service. If mainstream consumers choose not to adopt our technology, our ability to grow our business will be limited.

***Certain aspects of our service are not the same as traditional telephone service, which may limit the acceptance of our services by mainstream consumers and our potential for growth.***

Certain aspects of our service are not the same as traditional telephone service. Our continued growth is dependent on the adoption of our services by mainstream customers, so these differences are becoming increasingly important. For example:

- Both our new E-911 and emergency calling services are different, in significant respects, from the 911 service associated with traditional wireline and wireless telephone providers and, in certain cases, with other VoIP providers.

- Our customers may experience lower call quality than they are used to from traditional wireline telephone companies, including static, echoes and delays in transmissions.

- Our customers may experience higher dropped-call rates than they are used to from traditional wireline telephone companies.

- Customers who obtain new phone numbers from us do not appear in the phone book and their phone numbers are not available through directory assistance services offered by traditional telephone companies.

- Our customers cannot accept collect calls.

- In the event of a power loss or Internet access interruption experienced by a customer, our service is interrupted. Unlike some of our competitors, we have not installed batteries at customer premises to provide emergency power for our customers' equipment if they lose power, although we do have backup power systems for our network equipment and service platform.

If customers do not accept the differences between our service and traditional telephone service, they may choose to remain with their current telephone service provider or may choose to return to service provided by traditional telephone companies.

***Our emergency and new E-911 calling services are different from those offered by traditional wireline telephone companies and may expose us to significant liability.***

Both our emergency calling service and our new E-911 calling service are different, in significant respects, from the emergency calling services offered by traditional wireline telephone companies. In each case, those differences may cause significant delays, or even failures, in callers' receipt of the emergency assistance they need.

Traditional wireline telephone companies route emergency calls over a dedicated infrastructure directly to an emergency services dispatcher at the public safety answering point, or PSAP, in the caller's area. Generally, the dispatcher automatically receives the caller's phone number and actual location information. While our new E-911 service being deployed in the United States is designed to route calls in a fashion similar to traditional wireline services, our new E-911 capabilities are not yet available in all locations. In addition, the only location information that our E-911 service can transmit to a dispatcher at a PSAP is the information that our customers have registered with us. A customer's registered location may be different from the customer's actual location at the time of the call because customers can use their Vonage-enabled devices to make calls almost anywhere a broadband connection is available.

We are currently deploying E-911 service that is comparable to the emergency calling services provided to customers of traditional wireline telephone companies in the same area. For those customers located in an E-911 area, emergency calls are routed, subject to the limitations discussed

below, directly to an emergency services dispatcher at the PSAP in the area of the customer's registered location. The dispatcher will have automatic access to the customer's telephone number and registered location information. However, if a customer places an emergency call using the customer's Vonage-enabled device in a location different from the one registered with us, the emergency call will be routed to a PSAP in the customer's registered location, not the customer's actual location at the time of the call. Every time a customer moves his or her Vonage-enabled device to a new location, the customer's registered location information must be updated and verified. Until that takes place, the customer will have to verbally advise the emergency dispatcher of his or her actual location at the time of the call and wait for the call to be transferred, if possible, to the appropriate local emergency response center before emergency assistance can be dispatched.

In some cases, even under our new 911 service, emergency calls may be routed to a PSAP in the area of the customer's registered location, but such PSAP will not be capable of receiving our transmission of the caller's registered location information and, in some cases, the caller's phone number. Where the emergency call center is unable to process the information, the caller is provided a service that is similar to the basic 911 services offered to some wireline telephone customers. In these instances, the emergency caller may be required to verbally advise the operator of their location at the time of the call and, in some cases, a call back number so that the call can be handled or forwarded to an appropriate emergency dispatcher.

The emergency calls of customers located in areas where we are currently unable to provide either E-911 or the basic 911 described above are either routed directly to the PSAP in the area of the customer's location or supported by a national call center that is run by a third-party provider and operates 24 hours a day, seven days a week. In these cases, a caller must provide the operator with his or her physical location and call back number. If a customer reaches the call center, the operator will coordinate connecting the caller to the appropriate PSAP or emergency services provider. Our E-911 service does not support the calls of our WiFi phone and SoftPhone users. The emergency calls of our WiFi phone and SoftPhone users are supported by the national call center.

If one of our customers experiences a broadband or power outage, or if a network failure were to occur, the customer will not be able to reach an emergency services provider.

Delays our customers encounter when making emergency services calls and any inability of the answering point to automatically recognize the caller's location or telephone number can have devastating consequences. Customers have attempted, and may in the future attempt, to hold us responsible for any loss, damage, personal injury or death suffered as a result. Some traditional phone companies also may be unable to provide the precise location or the caller's telephone number when their customers place emergency calls. However, traditional phone companies are covered by legislation exempting them from liability for failures of emergency calling services and we are not. This liability could be significant. In addition, we have lost, and may in the future lose, existing and prospective customers because of the limitations inherent in our emergency calling services. Any of these factors could cause us to lose revenues, incur greater expenses or cause our reputation or financial results to suffer.

***Flaws in our technology and systems could cause delays or interruptions of service, damage our reputation, cause us to lose customers and limit our growth.***

Although we have designed our service network to reduce the possibility of disruptions or other outages, our service may be disrupted by problems with our technology and systems, such as malfunctions in our software or other facilities and overloading of our network. Our customers have experienced interruptions in the past and may experience interruptions in the future as a result of these types of problems. Interruptions have in the past and may in the future cause us to lose customers and offer substantial customer credits, which could adversely affect our revenue and profitability. For example, during 2005 our service was significantly impaired on two separate occasions. In March 2005, a problem during a software upgrade to our call processing system caused most of our customers to experience intermittent service for several hours. In August 2005, one of our third-party carriers experienced an outage of approximately 90 seconds, which caused a failure in some of our gateways. As a result, during a period of several hours, approximately two out of three outbound calls from our customers to the public switched telephone network experienced an "all circuits busy" condition. We have since had other outages that affected smaller groups of customers at various times. In addition, because our systems and our customers' ability to use our services are Internet-dependent, our services may be subject to "hacker attacks" from the Internet, which could have a significant impact on our systems and services. If service interruptions adversely affect the perceived reliability of our service, we may have difficulty attracting and retaining customers and our brand reputation and growth may suffer.

***Our ability to provide our service is dependent upon third-party facilities and equipment, the failure of which could cause delays or interruptions of our service, damage our reputation, cause us to lose customers and limit our growth.***

Our success depends on our ability to provide quality and reliable service, which is in part dependent upon the proper functioning of facilities and equipment owned and operated by third parties and is, therefore, beyond our control. Unlike traditional wireline telephone service or wireless service, our service requires our customers to have an operative broadband Internet connection and an electrical power supply, which are provided by the customer's Internet service provider and electric utility company, respectively, and not by us. The quality of some broadband Internet connections may be too poor for customers to use our services properly. In addition, if there is any interruption to a customer's broadband Internet service or electrical power supply, that customer will be unable to make or receive calls, including emergency calls, using our service. We also outsource several of our network functions to third-party providers. For example, we outsource the maintenance of our regional data connection points, which are the facilities at which our network interconnects with the public switched telephone network. If our third-party service providers fail to maintain these facilities properly, or fail to respond quickly to problems, our customers may experience service interruptions. Our customers have experienced such interruptions in the past and will experience interruptions in the future. In addition, our new E-911 service is currently dependent upon several third-party providers. Interruptions in service from these vendors could cause failures in our customers' access to E-911 services. Interruptions in our service caused by third-party facilities have in the past caused and may in the future cause us to lose customers, or cause us to offer substantial customer credits, which could adversely affect our revenue and profitability. If interruptions adversely affect the perceived reliability of our service, we may have difficulty attracting new customers and our brand, reputation and growth will be negatively impacted.

***We may not be able to maintain adequate customer care during periods of growth or in connection with our addition of new and complex Vonage-enabled devices, which could adversely affect our ability to grow and cause our financial results to be negatively impacted.***

Good customer care is important to acquiring and retaining customers. At some points in the past, we have not been able to expand our customer care operations quickly enough to meet the needs of our greatly increased customer base, and the quality of our customer care has suffered. For example, in the first quarter of 2005, our customers experienced longer than acceptable hold times when they called us for assistance. In the first quarter of 2006, our average monthly customer churn rate increased to 2.11% from 1.90% in the prior quarter. We believe this increase was due to our rapid growth and inability to hire enough qualified customer care employees which led to less than satisfactory customer care during the quarter, which we are working to address. In the future, as we broaden our Vonage-enabled device offerings and our customers build increasingly complex home networking environments, we will face additional challenges in training our customer care staff. We face a high turnover rate among our customer care employees. We continue to hire and train customer care representatives at a rapid rate in order to meet the needs of our growing customer base. If we are unable to hire, train and retain sufficient personnel to provide adequate customer care, we may experience slower growth, increased costs and higher churn levels, which would cause our financial results to be negatively impacted.

***If we are unable to improve our process for local number portability provisioning, our growth may be negatively impacted.***

We support local number portability for our customers, which allows our customers to retain their existing telephone numbers when subscribing to our services. Transferring numbers is a manual process that in the past could have taken us 20 business days or longer, although we have taken steps to automate this process to reduce the delay. A new Vonage customer must maintain both Vonage service and the customer's existing telephone service during the transferring process. By comparison, transferring wireless telephone numbers among wireless service providers generally takes several hours, and transferring wireline telephone numbers among traditional wireline service providers generally takes a few days. The additional delay that we experience is due to our reliance on the telephone company from which the customer is transferring and to the lack of full automation in our process. Further, because we are not a regulated telecommunications provider, we must rely on the telephone companies, over whom we have no control, to transfer numbers. We also rely on two third parties who have contractual obligations to us to facilitate the transfer of customers' telephone numbers. Local number portability is considered an important feature by many potential customers, and if we fail to reduce related delays, we may experience increased difficulty in acquiring new customers.

***A higher rate of customer terminations would negatively impact our business by reducing our revenue or requiring us to spend more money to grow our customer base.***

Our rate of customer terminations, or average monthly customer churn, was 2.11% for the three months ended March 31, 2006. During those three months, approximately 77,000 of our customers terminated. Our churn rate could increase in the future if customers are not satisfied with our service. Other factors, including increased competition from other providers, also influence our churn rate.

Because of churn, we have to acquire new customers on an ongoing basis just to maintain our existing level of customers and revenues. As a result, marketing expense is an ongoing requirement of our business. If our churn rate increases, we will have to acquire even more new customers in order to maintain our existing revenues. We incur significant costs to acquire new customers, and those costs are an important factor in determining our net losses and achieving future profitability. Therefore, if we are unsuccessful in retaining customers or are required to spend significant amounts to acquire new customers beyond those budgeted, our revenue could decrease and our net losses could increase.

***We may require significant capital to pursue our growth strategy, but we may not be able to obtain additional financing on favorable terms or at all.***

We intend to continue spending substantial amounts on marketing and product development in order to grow our business. We may need to obtain additional financing to pursue this business strategy, to respond to new competitive pressures or to respond to opportunities to acquire complementary businesses or technologies. Our significant losses to date may prevent us from obtaining additional funds on favorable terms or at all. For the three months ended March 31, 2006, we recorded a net loss of $85.2 million. Because of these losses and our limited tangible assets, we do not fit traditional credit lending criteria, which, in particular, could make it difficult for us to obtain loans or to access the capital markets. For example, we discussed a revolving credit facility with commercial banks in the summer of 2005. As a result of those discussions, we believe most commercial lenders will require us to very significantly reduce our loss from operations before they will lend us money. In addition, the terms of our outstanding convertible notes provide for additional shares to be issued upon conversion if we sell shares of our common stock after our initial public offering at a price that is less than the average trading price of our common stock over the 10-day period prior to any such sale, which might further limit our access to the capital markets. A failure to obtain additional financing could adversely affect our ability to grow and maintain our business.

***As a result of being a public company, we will incur increased costs that may place a strain on our resources or divert our management's attention from other business concerns.***

As a public company, we will incur additional legal, accounting and other expenses that we do not incur as a private company. The Exchange Act will require us to file annual, quarterly and current reports with respect to our business and financial condition, which will require us to incur legal and accounting expenses. The Sarbanes-Oxley Act will require us to maintain effective disclosure controls and procedures and internal controls for financial reporting. In order to maintain and improve the effectiveness of our disclosure controls and procedures and internal control over financial reporting, significant resources and management oversight will be required. We expect the corporate governance rules and regulations of the SEC and the New York Stock Exchange will increase our legal and financial compliance costs and make some activities more time consuming and costly. These requirements may place a strain on our systems and resources and may divert our management's attention from other business concerns, which could have a material adverse effect on our business, financial condition and results of operations. In addition, we are hiring and will continue to hire additional legal, accounting and financial staff with appropriate public company experience and technical accounting knowledge, which will increase our operating expenses in future periods.

We also 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 substantially higher costs to obtain the same or similar coverage. As a result, it may be more difficult for us to attract and retain qualified persons to serve on our board of directors or as executive officers.

***Our rapid growth has placed substantial demands on our management and operations. If we fail to hire and train additional personnel or improve our controls and procedures to respond to this growth, our business, operating results and financial position could be harmed.***

Our business and operations have expanded rapidly since our inception in May 2000. For example, during the 12 months ended December 31, 2005, the number of our employees more than doubled, growing from 648 to 1,355, and we experienced high turnover among our customer care employees. To support our expanded customer base effectively and meet our growth objectives for the future, we must continue to successfully hire, train, motivate and retain our employees. We expect that significant further expansion will be necessary. In addition, in order to manage our expanded operations, we will need to continue to improve our management, operational and financial controls and our reporting systems and procedures. All of these measures will require significant expenditures and will demand the attention of management. If we are not able to hire, train and retain the necessary personnel, or if these operational and reporting improvements are not implemented successfully, we may have to make significant additional expenditures and further draw management attention away from running our business to address these issues. The quality of our services could suffer, which could negatively affect our brand, operating results and financial position.

***Because much of our potential success and value lies in our use of internally developed systems and software, if we fail to protect them, it could negatively affect us.***

Our ability to compete effectively is dependent in large part upon the maintenance and protection of systems and software that we have developed internally. While we have several pending patent applications, we cannot patent much of the technology that is important to our business. In addition, our pending patent applications may not be successful. To date, we have relied on copyright, trademark and trade secret laws, as well as confidentiality procedures and licensing arrangements, to establish and protect our rights to this technology. We typically enter into confidentiality or license agreements with our employees, consultants, customers and vendors in an effort to control access to and distribution of technology, software, documentation and other information. Despite these precautions, it may be possible for a third party to copy or otherwise obtain and use this technology without authorization. Policing unauthorized use of this technology is difficult. The steps we take may not prevent misappropriation of the technology we rely on. In addition, effective protection may be unavailable or limited in some jurisdictions outside the United States, Canada and the United Kingdom. Litigation may be necessary in the future to enforce or protect our rights or to determine the validity and scope of the rights of others. That litigation could cause us to incur substantial costs and divert resources away from our daily business, which in turn could materially adversely affect our business.

***We may be subject to damaging and disruptive intellectual property litigation.***

We have been named as a defendant in three suits currently pending that relate to alleged patent infringement. See "Business Legal Proceedings Patent Litigation." In addition, we have been subject to other infringement claims in the past and may be subject to infringement claims in the future. We may be unaware of filed patent applications and issued patents that could relate to our products and services. Intellectual property litigation could:

- be time-consuming and expensive;
- divert attention and resources away from our daily business;
- impede or prevent delivery of our products and services; and
- require us to pay significant royalties, licensing fees and damages.

Parties making claims of infringement may be able to obtain injunctive or other equitable relief that could effectively block our ability to provide our services and could cause us to pay substantial damages. In the event of a successful claim of infringement, we may need to obtain one or more licenses from third parties, which may not be available at a reasonable cost, if at all. The defense of any lawsuit could result in time-consuming and expensive litigation, regardless of the merits of such claims, and could also result in damages, license fees, royalty payments and restrictions on our ability to provide our services, any of which could harm our business.

***Our service requires an operative broadband connection, and if the adoption of broadband does not progress as expected, the market for our services will not grow and we may not be able to grow our business and increase our revenue.***

Use of our service requires that the user be a subscriber to an existing broadband Internet service, most typically provided through a cable or digital subscriber line, or DSL, connection. Although the number of broadband subscribers worldwide has grown significantly over the last five years, this service has not yet been adopted by a majority of consumers. If the adoption of broadband services does not continue to grow, the market for our services may not grow. As a result, we may not be able to increase our revenue and become profitable.

***Future disruptive new technologies could have a negative effect on our businesses.***

VoIP technology, which our business is based upon, did not exist and was not commercially viable until relatively recently. VoIP technology is having a disruptive effect on traditional telephone companies, whose businesses are based on other technologies. We also are subject to the risk of future disruptive technologies. If new technologies develop that are able to deliver competing voice services at lower prices, better or more conveniently, it could have a material adverse effect on us.

***We are dependent on a small number of individuals, and if we lose key personnel upon whom we are dependent, our business will be adversely affected.***

Many of the key responsibilities of our business have been assigned to a relatively small number of individuals. Our future success depends to a considerable degree on the vision, skills, experience and effort of our senior management, including Jeffrey Citron, our founder, Chairman and Chief Strategist, John Rego, our Chief Financial Officer, and Louis Mamakos, our Chief Technology Officer. In addition, we recently added Michael Snyder as our new Chief Executive Officer. We may add additional senior personnel in the future.

If we lose the services of any of our key employees, or if members of our management team do not work well together, it would have an adverse effect on our business. In particular, Mr. Citron has been the driving force in the development of our business to date, and he will continue to be in charge of our overall strategy and be closely involved with our technology and other aspects of our business. However, Mr. Citron could decide to resign as our Chairman and Chief Strategist, which could have a material adverse effect on us.

***The past background of our founder, Chairman and Chief Strategist, Jeffrey A. Citron, may adversely affect our ability to enter into business relationships and may have other adverse effects on our business.***

Prior to joining Vonage, Mr. Citron was associated with Datek Securities Corporation and Datek Online Holdings Corp., including as an employee of, and consultant for, Datek Securities and, later, as one of the principal executive officers and largest stockholders of Datek Online. Datek Online, which was formed in early 1998 following a reorganization of the Datek business, was a large online brokerage firm. Datek Securities was a registered broker-dealer that engaged in a number of businesses, including proprietary trading and order execution services. During a portion of the time Mr. Citron was associated with Datek Securities, the SEC alleged that Datek Securities, Mr. Citron and other individuals participated in an extensive fraudulent scheme involving improper use of the Nasdaq Stock Market's Small Order Execution System, or SOES. Datek Securities (through its successor iCapital Markets LLC), Mr. Citron and other individuals entered into settlements with the SEC in 2002 and 2003, which resulted in extensive fines, bans from future association with securities brokers or dealers and enjoinments against future violations of certain U.S. securities laws. The NASD previously had imposed disciplinary action against Datek Securities, Mr. Citron and other individuals in connection with alleged violations of the rules and regulations regarding the SOES. These and other matters are discussed under "Information Concerning our Founder, Chairman and Chief Strategist."

There is a risk that some third parties will not do business with us, that some prospective investors will not purchase our securities or that some customers may be wary of signing up for service with us as a result of allegations against Mr. Citron and his past SEC and NASD settlements. We believe that some financial institutions and accounting firms have declined to enter into business relationships with us in the past, at least in part because of these matters. Other institutions and potential business associates may not be able to do business with us because of internal policies that restrict associations with individuals who have entered into SEC and NASD settlements. While we believe that these matters have not had a material impact on our business, they may have a greater impact on us when we become a public company, including by adversely affecting our ability to enter into commercial relationships with third parties that we need to effectively and competitively grow our business. Further, should Mr. Citron in the future be accused of, or be shown to have engaged in, additional improper or illegal activities, the impact of those accusations or the potential penalties from such activities could be exacerbated because of the matters discussed above. If any of these risks were to be realized, there could be a material adverse effect on our business or the market price of our common stock.

**Risks Related to Regulation**

Set forth below are certain material risks related to regulation. For additional information about these and other regulatory risks we face, see "Regulation" in this prospectus.

***Regulation of VoIP services is developing and therefore uncertain, and future legislative, regulatory or judicial actions could adversely impact our business and expose us to liability.***

Our business has developed in an environment largely free from government regulation. However, the United States and other countries have begun to assert regulatory authority over VoIP and are continuing to evaluate how VoIP will be regulated in the future. Both the application of existing rules to us and our competitors and the effects of future regulatory developments are uncertain.

Future legislative, judicial or other regulatory actions could have a negative effect on our business. If we become subject to the rules and regulations applicable to telecommunications providers in individual states, we may incur significant litigation and compliance costs, and we may have to restructure our service offerings, exit certain markets or raise the price of our services, any of which could cause our services to be less attractive to customers. In addition, future regulatory developments could increase our cost of doing business and limit our growth.

Our international operations are also subject to regulatory risks, including the risk that regulations in some jurisdictions will prohibit us from providing our services cost-effectively or at all, which could limit our growth. Currently, there are several countries where regulations prohibit us from offering service. In addition, because customers can use our services almost anywhere that a broadband Internet connection is available, including countries where providing VoIP services is illegal, the governments of those countries may attempt to assert jurisdiction over us, which could expose us to significant liability and regulation.

***The success of our business relies on customers' continued and unimpeded access to broadband service. Providers of broadband services may be able to block our services or charge their customers more for also using our services, which could adversely affect our revenue and growth.***

Our customers must have broadband access to the Internet in order to use our service. Some providers of broadband access may take measures that affect their customers' ability to use our service, such as degrading the quality of the data packets we transmit over their lines, giving those packets low priority, giving other packets higher priority than ours, blocking our packets entirely or attempting to charge their customers more for also using our services.

It is not clear whether suppliers of broadband Internet access have a legal obligation to allow their customers to access and use our service without interference. As a result of recent decisions by the U.S. Supreme Court and the FCC, providers of broadband services are subject to relatively light regulation by the FCC. Consequently, federal and state regulators might not prohibit broadband providers from limiting their customers' access to VoIP or otherwise discriminating against VoIP providers. Interference with our service or higher charges for also using our service could cause us to lose existing customers, impair our ability to attract new customers and harm our revenue and growth. See "Regulation Access to Networks."

These problems could also arise in international markets. For example, a Canadian cable provider recently began offering an optional Cdn$10 per month "quality of service premium" to customers who use third-party VoIP services over its facilities. However, customers who purchase VoIP services directly from this cable provider are not required to pay this additional fee.

***If we fail to comply with new FCC regulations requiring us to provide E-911 emergency calling services, we may be subject to fines or penalties, which could include disconnection of our service for certain customers or prohibitions on marketing of our services and accepting new customers in certain areas.***

The FCC released an order on June 3, 2005 requiring us to notify our customers of any differences between our emergency calling services and those available through traditional telephone providers and obtain affirmative acknowledgments from our customers of those notifications. The rules also required us to offer by November 28, 2005 enhanced emergency calling services, or E-911, to all of our customers located in areas where E-911 service is available from their traditional wireline telephone company. E-911 service allows emergency calls from our customers to be routed directly to an emergency dispatcher in a customer's registered location and gives the dispatcher automatic access to the customer's telephone number and registered location information.

We have notified our customers of the differences between our emergency calling services and those available through traditional telephony providers and have received affirmative acknowledgement from substantially all of our customers. We also have taken steps to comply with the FCC's order by the November 28, 2005 deadline, but we are not currently in full compliance and do not expect to be in full compliance in the short term unless we are granted a waiver of the requirements by the FCC. As of April 1, 2006, we were not providing E-911 service to approximately 25% of our U.S. subscriber lines.

The consequences of failure to comply fully with the FCC's order currently are unclear. On November 7, 2005, the FCC's Enforcement Bureau issued a public notice stating that it would not require disconnection of existing customers to whom E-911 service cannot be provided by November 28, 2005, but it also stated that it expected VoIP providers to stop marketing and accepting new subscribers in areas where they cannot provide E-911 service after November 28, 2005. It is not clear whether the FCC will enforce this restriction or how it would do so. On November 28, 2005, we filed a petition for extension of time and limited waiver of certain of the enhanced emergency service requirements, including the limitations on marketing and accepting new customers. We are continuing to market our services and accept new customers in areas in which we do not provide E-911 service. The FCC has not acted on our petition, and we cannot predict whether the FCC will grant our petition or provide other relief. Should we be unable to obtain an extension of time to implement the requirements of the order, we may be subject to enforcement action by the FCC that could include monetary forfeitures, cease and desist orders and other penalties. We also may be required to stop serving customers to whom we cannot provide the E-911 service required by the FCC's rules and to stop marketing our services and accepting new customers in areas in which we cannot provide the E-911 service. Any of these actions could significantly harm our business. See "Business  Network Operations" and "Regulation  VoIP E-911 Matters" for further information on the FCC's E-911 requirements, our existing systems and our measures for compliance.

***Sales taxes and 911-related fees will increase our customers' cost of using our services and could result in penalties being imposed on us.***

There are numerous fees and taxes assessed on traditional telephone services that we believe have not been applicable to us and that we have not paid in the past. Previously, we only collected and remitted sales taxes for customers with a billing address in New Jersey, where our corporate operations are conducted. However, as a result of sales tax initiatives in certain states and sales tax agreements we have entered into with three other states, we began collecting and remitting sales taxes in 21 additional states effective May 1, 2006. We also believe it is likely that we eventually will be required to collect and remit sales taxes in virtually all U.S. states that charge sales taxes. This will have the effect of decreasing any price advantage we may have.

Some states have taken the position that we should have collected and remitted sales taxes in the past and have sought to collect those past sales taxes from us and impose fines, penalties or interest charges on us. We established a reserve of $11.9 million, as of March 31, 2006, for these matters. If our ultimate liability exceeds that amount, it could have a material adverse effect on us.

We began charging customers an Emergency 911 Cost Recovery fee of $0.99 per month, effective March 7, 2006. This fee is designed to cover some of our costs associated with complying with E-911 regulation and our national 911 emergency call center. State and local governments may also assess fees to pay for emergency services in a customer's community. We expect to begin collecting these 911-related fees and remitting them to the appropriate authorities later this year. We expect this fee for most of our customers to be between approximately $0.50 to $1.50 per month, and as high as $3.00 for a limited number of our customers, depending on their location. This will also have the effect of decreasing any price advantage we may have.

***We may be required to contribute to the Universal Service Fund, increasing our cost of providing services. If we collect those contributions from our customers, the cost advantage we offer customers would be reduced.***

FCC regulations require providers of interstate telecommunications services, but not providers of information services, to contribute to the federal Universal Service Fund, or USF. Currently, we are not subject to direct contribution to the USF, although we do contribute indirectly to the USF through our purchase of telecommunications services from our suppliers. The FCC is considering a number of proposals that could alter the way that the USF is assessed. For instance, the FCC is considering an assessment based on the use of telephone numbers, in which case we would be required to contribute directly to the Universal Service Fund. In addition, the FCC may increase the contribution obligations of our suppliers, which would result in an increase in the surcharges those suppliers charge to us. We intend to collect from our customers any additional USF contributions we are required, directly or indirectly, to make. Many of our competitors are required to contribute directly to the USF and already collect those USF contributions from their customers.

***Once we become a public company, we will need to comply with Section 404 of the Sarbanes-Oxley Act of 2002, and if we fail to achieve and maintain adequate internal controls over financial reporting, our business, results of operations and financial condition could be materially adversely affected.***

As a public company, our systems of internal controls over financial reporting will be required to comply with the standards adopted by the Public Company Accounting Oversight Board. We are presently evaluating our internal controls for compliance. During the course of our evaluation, we may identify areas requiring improvement and may be required to design enhanced processes and controls to address issues identified through this review. This could result in significant delays and cost to us and require us to divert substantial resources, including management time, from other activities. We have commenced a review of our existing internal control structure and plan to hire additional personnel. Although our review is not complete, we have taken steps to improve our internal control structure by hiring dedicated, internal Sarbanes-Oxley Act compliance personnel to analyze and improve our internal controls, to be supplemented periodically with outside consultants as needed. However, we cannot be certain regarding when we will be able to successfully complete the procedures, certification and attestation requirements of Section 404 of the Sarbanes-Oxley Act of 2002. If we fail to achieve and maintain the adequacy of our internal controls, we may not be able to conclude that we have effective internal controls over financial reporting in accordance with the Sarbanes-Oxley Act. Moreover, effective internal controls are necessary for us to produce reliable financial reports and are important to help prevent fraud. As a result, our failure to satisfy the requirements of Section 404 on a timely basis could result in the loss of investor confidence in the reliability of our financial statements, which in turn could harm the market value of our common stock. Any failure to maintain effective internal controls also could impair our ability to manage our business and harm our financial results.

**Risks Related to this Offering**

***There is no existing market for our common stock, and we do not know if one will develop that will provide you with adequate liquidity. You may not be able to resell our common stock at or above the initial public offering price.***

Currently there is no public market for our common stock. We cannot predict the extent to which investor interest in us will lead to the development of a trading market or otherwise or how liquid that market might become. The initial public offering price for the shares will be determined by negotiations between us and the representatives of the underwriters and may not be indicative of prices that will prevail in the open market following this offering. You may not be able to resell our common stock at or above the initial public offering price.

***As a new investor, you will experience immediate and substantial dilution.***

The price you will pay in this offering for each share of our common stock will exceed the per share value attributed from our tangible assets less our total liabilities. Therefore, if we distributed our tangible assets to our stockholders following this offering, you would receive less value per share of common stock than you paid in this offering. Assuming an initial public offering price of $17.00 per share (the midpoint of the range set forth on the cover page of this prospectus) the net tangible book value adjusted for the net proceeds of this offering at March 31, 2006 was approximately $433.1 million, or approximately $2.78 per share. Pro forma net tangible book value per share represents the amount of our total consolidated tangible assets less our total consolidated liabilities, divided by the total number of shares of common stock outstanding. Accordingly, if you purchase shares of our common stock in this offering you will suffer immediate dilution of $14.22 per share in pro forma net tangible book value. 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 our capital stock and the losses we have incurred. You may suffer additional dilution to the extent outstanding warrants to purchase shares of our common stock are exercised. For more information, see "Dilution."

***Our stock price may decline due to sales of shares by our other stockholders.***

Sales of substantial amounts of our common stock, or the perception that these sales may occur, may adversely affect the price of our common stock and impede our ability to raise capital through the issuance of equity securities in the future. There will be 155,732,440 shares of our common stock outstanding immediately after this offering. All shares sold in this offering will be freely transferable without restriction or further registration under the Securities Act, subject to restrictions that may be applicable to our "affiliates," as that term is defined in Rule 144 under the Securities Act, and subject to the 180-day lock-up restrictions described in the "Underwriting" section of this prospectus. We expect a substantial portion of the shares sold in this offering, including through our proposed directed share programs, to be held by retail investors. In addition, immediately after this offering we expect that our existing investors will hold 124,482,440 shares of our common stock and convertible notes that are convertible into 17,826,424 shares of our common stock. Further, as of March 31, 2006, warrants exercisable for 3,085,715 shares of our common stock and stock options to purchase 16,904,494 shares of our common stock were outstanding. Of these shares of common stock, 124,482,440 shares may be sold into the public market after this offering pursuant to Rule 144 under the Securities Act, subject to volume limitations and other restrictions that may be applicable to some holders pursuant to that rule and subject to the 180-day lock-up restrictions applicable to holders of those shares. Substantially all of the shares held by our existing stockholders, as well as shares issuable upon conversion of our convertible notes, are subject to registration rights, and we believe these rights will be exercised. You should expect a significant number of these shares to be sold, which may decrease the price of shares of our common stock. Shares issuable upon exercise of our options also may be sold in the market in the future, subject to any restrictions on resale following underwritten offerings contained in our option agreements. We expect that many of these shares will be sold when these lock-ups expire. See "Shares Eligible for Future Sale."

In connection with this offering, we and our executive officers, directors, substantially all our stockholders and all of the holders of our convertible notes have entered into 180-day lock-up agreements with the underwriters of this offering. These lock-up agreements prohibit us and our executive officers, directors and such stockholders and holders of our convertible notes from selling or otherwise disposing of shares of common stock, except in limited circumstances. The terms of the lock-up agreements can be waived, at any time, by Citigroup Global Markets Inc., Deutsche Bank Securities Inc., and UBS Securities LLC, at their discretion, without prior notice or announcement, to allow us or our executive officers, directors, stockholders and holders of our convertible notes to sell shares of our common stock. If the terms of the lock-up agreements are waived, shares of our common stock will be available for sale in the public market sooner, which could reduce the price of our common stock. See "Shares Eligible for Future Sale  Lock-up Agreements."

***Jeffrey A. Citron, our founder, Chairman, Chief Strategist and principal stockholder, will continue to exert significant influence over us.***

After completion of this offering, Mr. Citron will beneficially own approximately 33% of our outstanding common stock, including outstanding securities convertible into or exercisable for common stock held by Mr. Citron. As a result, Mr. Citron will be able to exert significant influence over all matters presented to our stockholders for approval, including election and removal of our directors and change of control transactions. In addition, as our Chairman and Chief Strategist, Mr. Citron has and will continue to have significant influence over our strategy, technology and other matters. Mr. Citron's interests may not always coincide with the interests of other holders of our common stock.

***The market price of our common stock may be volatile, which could cause the value of your investment to decline.***

Securities markets experience significant price and volume fluctuations. This market volatility, as well as general economic conditions, could cause the market price of our common stock to fluctuate substantially. Many factors that are beyond our control may significantly affect the market price of our shares. These factors include:

- price and volume fluctuations in the stock markets generally;
- changes in our earnings or variations in operating results;
- any shortfall in revenue or increase in losses from levels expected by securities analysts;
- changes in regulatory policies or tax law;
- operating performance of companies comparable to us; and
- general economic trends and other external factors.

Such factors may cause the market price of our common stock to decrease significantly. You may be unable to sell your shares of common stock at or above the initial public offering price.

***Our certificate of incorporation, bylaws and convertible notes contain provisions that could delay or discourage a takeover attempt, which could prevent the completion of a transaction in which our stockholders could receive a substantial premium over the then-current market price for their shares.***

Upon completion of this offering, certain provisions of our restated certificate of incorporation and our amended and restated bylaws may make it more difficult for, or have the effect of discouraging, a third party from acquiring control of us or changing our board of directors and management. See

"Description of Capital Stock Anti-Takeover Effects of Various Provisions of Delaware Law and Our Restated Certificate of Incorporation and Amended and Restated Bylaws." These provisions:

- permit our board of directors to issue additional shares of common stock and preferred stock and to establish the number of shares, series designation, voting powers (if any), preferences, other special rights, qualifications, limitations or restrictions of any series of preferred stock;
- limit the ability of stockholders to amend our restated certificate of incorporation and bylaws, including supermajority requirements;
- allow only our board of directors, Chairman of the board of directors, Chief Strategist or Chief Executive Officer to call special meetings of our stockholders;
- eliminate the ability of stockholders to act by written consent;
- require advance notice for stockholder proposals and director nominations;
- limit the removal of directors and the filling of director vacancies; and
- establish a classified board of directors with staggered three-year terms.

In addition, our convertible notes provide that, upon a change of control, holders may require us to redeem all or a portion of their convertible notes at a price equal to the principal amount of notes to be redeemed, plus any accrued and unpaid interest and potentially a premium.

Such provisions could have the effect of depriving stockholders of an opportunity to sell their shares at a premium over prevailing market prices. Any delay or prevention of, or significant payments required to be made upon, a change of control transaction or changes in our board of directors or management could deter potential acquirors or prevent the completion of a transaction in which our stockholders could receive a substantial premium over the then-current market price for their shares.

**SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS**

This prospectus contains "forward-looking statements," which include information relating to future events, future financial performance, strategies, expectations, competitive environment and regulation. Words such as "may," "should," "could," "would," "predicts," "potential," "continue," "expects," "anticipates," "future," "intends," "plans," "believes," "estimates," and similar expressions, as well as statements in future tense, identify forward-looking statements. These forward-looking statements include, without limitation, statements regarding:

- projections, predictions, expectations, estimates or forecasts as to broadband Internet access, VoIP adoption, our business, financial and operating results and future economic performance;
- proposed new product and service offerings;
- expectations that regulatory developments or other matters will not have a material adverse effect on our consolidated financial position, results of operations or liquidity; and
- our management's goals and objectives and other similar expressions concerning matters that are not historical facts.

Forward-looking statements should not be read as a guarantee of future performance or results and will probably not be accurate indications of when such performance or results will be achieved. Forward-looking statements are based on information we have when those statements are made or our management's good faith belief as of that time with respect to future events, and are subject to risks and uncertainties that could cause actual performance or results to differ materially from those expressed in or suggested by the forward-looking statements. Important factors that could cause such differences include, but are not limited to:

- our history of operating losses;
- the highly competitive nature of our industry;
- decreasing telecommunications prices to consumers;
- the acceptance of VoIP technology by mainstream consumers;
- the differences between our calling service, including our emergency calling service, compared to incumbent telephony providers;
- system disruptions, power outages and failures of the third-party facilities and equipment we utilize and flaws in our technology;
- our ability to maintain adequate customer care and manage increases in our churn rate;
- our ability to improve local number portability provisioning;
- our ability to sustain the growth rates we have enjoyed so far;
- the costs associated with being a public company and our ability to comply with the internal control and reporting obligations of public companies;

- our ability to manage our rapid growth, train additional personnel and improve our controls and procedures;
- intellectual property litigation initiated against us and our ability to protect our internally developed systems and software;
- the growth of broadband Internet access;
- our ability to retain key personnel;
- increasing regulation of our services and the imposition of federal, state and municipal sales and use taxes, fees or surcharges on our services;
- our ability to comply with the FCC's new regulations regarding E-911 services; and
- the assessment of the Universal Service Fund on our services.

Forward-looking statements speak only as of the date the statements are made. You should not put undue reliance on any forward-looking statements. We assume no obligation to update forward-looking statements to reflect actual results, changes in assumptions or changes in other factors affecting forward-looking information, except to the extent required by applicable securities laws.

## USE OF PROCEEDS

We expect that the net proceeds from our sale of 31,250,000 shares of common stock in this offering will be approximately $493.7 million, based on an estimated initial public offering price of $17.00 per share (the midpoint of the range set forth on the cover page of this prospectus), after deducting the underwriting discounts and commissions and estimated offering expenses payable by us. A $1.00 change in the initial public offering price per share would change the expected net proceeds by approximately $29.4 million.

The primary purposes of the offering are to fund the expansion of our business, including funding marketing expenses and operating losses, and to create a public market for our common stock. In addition, we could use a portion of the proceeds of this offering to pursue acquisitions or to make strategic investments. Our management will have broad discretion in the allocation of the net proceeds of this offering. The amounts actually expended and the timing of such expenditures will depend on a number of factors, including our realization of the different elements of our growth strategy and the amount of cash generated by our operations. Pending their use to fund our expansion, the proceeds of the offering will be invested in short-term, interest-bearing securities.

We have requested that, pursuant to our Directed Share Programs, the underwriters reserve up to 13.5% and 1.5% of the common stock offered in this prospectus for sale to certain of our customers and other persons related to us, respectively, at the initial public offering price. See "Underwriting  Directed Share Programs" for more information. In connection with the Directed Share Programs, we have agreed to indemnify the underwriters against certain liabilities, including those that may be caused by the failure of Directed Share Program participants to pay for and accept delivery of the common stock which had been allocated to them or were subject to a properly confirmed agreement to purchase. As a result, our expected net proceeds could be reduced if Directed Share Program participants fail to pay for and accept delivery of the common stock which had been allocated to them or were subject to a properly confirmed agreement to purchase and, as a result, we must indemnify the underwriters for such failure.

## DIVIDEND POLICY

In the past, we have not declared or paid cash dividends on our common stock, and we do not intend to pay any cash dividends on our common stock. Rather, we intend to retain future earnings (if any) to fund the operation and expansion of our business and for general corporate purposes. Subject to legal and contractual limits, our board of directors will make any decision as to whether to pay dividends in the future.

**CAPITALIZATION**

The following table sets forth our cash, cash equivalents and marketable securities and capitalization as of March 31, 2006 on an actual basis and on a pro forma as adjusted basis, after giving effect to:

- the conversion of all outstanding shares of our preferred stock into shares of our common stock upon consummation of this offering; and

- our receipt of the net proceeds from our sale of common stock in this offering.

For purposes of the as adjusted column of the capitalization table below, we have assumed the net proceeds from the offering will be $495.8 million after deducting underwriting discounts and commissions and estimated offering expenses payable by us, but excluding $2.2 million of offering expenses that have already been paid. A $1.0 million change in the gross proceeds from this offering would change each of the cash, cash equivalents and marketable securities, total stockholders' equity (deficit) and total capitalization line items by approximately $0.94 million.

You should read the information in this table in conjunction with "Use of Proceeds," "Dividend Policy," "Selected Historical Financial Information," and "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and the related notes included elsewhere in this prospectus.

| | As of March 31, 2006 | |
|---|---|---|
| | **Actual** | **Pro forma as adjusted** |
| | **(Restated (10))** | **(Restated (10))** |
| | **(in thousands, except par value)** | |
| Cash, cash equivalents and marketable securities | $ 175,461 | $ 671,289 |
| Total debt: | | |
| Convertible notes(1) | $ 253,352 | $ 253,352 |
| Capital lease obligations (current and long-term) | 24,907 | 24,907 |
| Total debt | 278,259 | 278,259 |
| Redeemable Preferred Stock: | | |
| Series E Redeemable Convertible Preferred Stock(2) | 195,736 | |
| Series D Redeemable Convertible Preferred Stock(3) | 102,722 | |
| Series C Redeemable Convertible Preferred Stock(4) | 38,090 | |
| Series B Redeemable Convertible Preferred Stock(5) | 14,489 | |
| Series A-2 Redeemable Convertible Preferred Stock(6) | 20,292 | |
| Series A-2 Convertible Redeemable Preferred Stock Warrant to purchase 321 shares, actual; converts into a warrant to purchase shares of common stock, pro forma as adjusted | 1,557 | |
| Series A Redeemable Convertible Preferred Stock(7) | 15,968 | |
| Stock subscriptions receivable | (415) | |
| Total Redeemable Preferred Stock | 388,439 | |

| | As of March 31, 2006 | |
|---|---|---|
| | Actual | Pro forma as adjusted |
| | (Restated (10)) | (Restated (10)) |
| | (in thousands, except par value) | |
| Stockholders' equity: | | |
| Common stock, par value $0.001 per share; 596,950 shares authorized and 1,652 shares issued and 1,414 shares outstanding, actual; 596,950 shares authorized and 155,971 and 155,733 shares issued and outstanding, pro forma as adjusted(8) | 2 | 156 |
| Additional paid in capital(9) | 17,149 | 901,677 |
| Stock subscriptions receivable | (37) | (452) |
| Accumulated deficit | (467,444) | (467,444) |
| Treasury stock | (619) | (619) |
| Accumulated other comprehensive loss | (236) | (236) |
| Total stockholders' equity (deficit) | (451,185) | 433,082 |
| Total capitalization | $ 215,513 | $ 711,341 |

(1) Represents principal amount of $253,564 less unamortized discount of $212.

(2) Par value $0.001 per share, 9,435 shares authorized and 9,429 shares issued and outstanding, actual; no shares authorized, issued or outstanding, pro forma as adjusted.

(3) Par value $0.001 per share, 8,729 shares authorized and 8,729 shares issued and outstanding, actual; no shares authorized, issued or outstanding, pro forma as adjusted.

(4) Par value $0.001 per share, 8,000 shares authorized and 8,000 shares issued and outstanding, actual; no shares authorized, issued or outstanding, pro forma as adjusted.

(5) Par value $0.001 per share, 3,750 shares authorized and 3,750 shares issued and outstanding, actual; no shares authorized, issued or outstanding, pro forma as adjusted.

(6) Par value $0.001 per share, 6,067 shares authorized and 5,167 shares issued and outstanding, actual; no shares authorized, issued or outstanding, pro forma as adjusted.

(7) Par value $0.001 per share, 8,000 shares authorized and 8,000 shares issued and outstanding, actual; no shares authorized, issued or outstanding, pro forma as adjusted.

(8) The number of shares of common stock outstanding after this offering excludes:

16,904 shares of common stock issuable upon exercise of currently outstanding options with exercise prices ranging from $0.70 to $35.00 and having a weighted average exercise price of $7.89 per share;

3,086 shares of common stock issuable upon exercise of currently outstanding warrants with exercise prices ranging from $0.70 to $1.40 per share and having a weighted average exercise price of $1.28 per share;

shares of common stock reserved for future grants under our stock option plans which will be determined under a formula set forth in our 2006 Incentive Plan, and will equal approximately 17.65% of the number of shares that are issued and outstanding from time to time. As of March 31, 2006, assuming the conversion of the outstanding shares of preferred stock and sale of the shares in this offering, there would be approximately 27,487 shares reserved for grant; and

17,826 shares of common stock issuable upon conversion of our convertible notes, based on a conversion price of $14.22 per share. Additional shares will be issuable upon conversion if we elect to pay interest on these notes in kind by increasing the principal outstanding under the notes. See "Description of Convertible Notes."

(9)
March 31, 2006 actual excludes $2,153 of expenses related to the offering which are included in other assets on the balance sheet.

(10)
In December 2005 and January 2006, we issued approximately $249,900 of convertible notes, and an additional $3,600 as the payment of interest in kind in March 2006. Originally, we believed that the convertible notes contained an embedded derivative and accordingly accounted for the embedded derivative by bifurcating the embedded derivative from the convertible notes at the date of issuance and subsequently remeasuring the fair value of the embedded derivative at December 31, 2005 and March 31, 2006. In May 2006, upon further review, we concluded that the convertible notes do not contain an embedded derivative. See "Note 1 to our consolidated financial statements." "Restated" amounts reflect the removal of the fair value of derivatives embedded within the convertible notes of $8,800 and the removal of the unamortized discount related to embedded derivatives which increased the outstanding amount of the convertible notes by $21,161. The convertible notes also decreased by $212 for the beneficial conversion feature.

## DILUTION

If you invest in our common stock, your interest will be diluted to the extent of the difference between the initial public offering price per share of our common stock and the net tangible book value per share of our common stock immediately after the completion of this offering.

Dilution results from the fact that the per share offering price of the common stock is substantially in excess of the book value per share attributable to the existing stockholders for the presently outstanding stock. Our net tangible book value at March 31, 2006 was $(451.2) million, or $(319.30) per share of common stock. Assuming the conversion of our preferred stock into common stock and that the 31,250,000 shares of our common stock offered by us under this prospectus are sold at an initial public offering price of $17.00 per share (the midpoint of the range set forth on the cover page of this prospectus), after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us, our pro forma net tangible book value as of March 31, 2006, would have been approximately $433.1 million, or $2.78 per share. This represents an immediate increase in pro forma net tangible book value of $3.28 per share to existing stockholders and an immediate dilution of $14.22 per share to new investors purchasing shares of common stock in this offering.

The following table illustrates this substantial and immediate per share dilution to new investors:

| | | |
|---|---|---|
| Assumed initial public offering price per share | | $ 17.00 |
| Net tangible book value per share as of March 31, 2006 | $ (319.30) | |
| Increase attributable to conversion of preferred stock | 318.80 | |
| Pro forma net tangible book value per share as of March 31, 2006 | (0.50) | |
| Increase in net tangible book value per share attributable to new investors purchasing shares in this offering | 3.28 | |
| Pro forma as adjusted net tangible book value per share after this offering | | 2.78 |
| Dilution of pro forma net tangible book value per share to new investors | | $ 14.22 |

The following table summarizes, as of March 31, 2006, on a pro forma basis after giving effect to this offering, the total number of shares of common stock purchased from us, the total consideration paid to us, assuming an initial public offering price of $17.00 per share (before deducting the estimated underwriting discounts and commissions and offering expenses payable by us in this offering), and the average price per share paid by existing stockholders and by new investors purchasing shares in this offering:

| | Shares Purchased | | Total Consideration | | |
|---|---|---|---|---|---|
| | **Number** | **Percent** | **Amount** | **Percent** | **Average Price Per Share** |
| Existing stockholders | 124,482,440 | 79.9% | $ 409,701,924 | 43.5% | $ 3.29 |
| New investors | 31,250,000 | 20.1 | 531,250,000 | 56.5 | 17.00 |
| Total | 155,732,440 | 100% | $ 940,951,924 | 100% | |

If the underwriters exercise their over-allotment option in full, the pro forma net tangible book value per share of common stock would be approximately $3.17 and the dilution in pro forma net tangible book value per share of common stock to new investors would be $13.83.

A $1.00 change in the assumed public offering price of $17.00 per share of our common stock would change our pro forma net tangible book value after giving effect to the offering by $29.4 million, the pro forma net tangible book value per share of our common stock after giving effect to this offering by $0.19 and the dilution in pro forma net tangible book value per share of our common stock to new investors in this offering by $0.81, assuming no change to the number of shares of common stock offered by us as set forth on the cover page of this prospectus, and after deducting underwriting discounts and commission and other expenses of the offering. The pro forma information discussed above is illustrative only. Our net tangible book value following the completion of the offering is subject to adjustment based on the actual offering price of our common stock and other terms of this offering determined at pricing.

The discussion and tables above exclude the following:

16,904,494 shares of common stock issuable upon the exercise of options outstanding as of March 31, 2006, at a weighted average exercise price of $7.89 per share;

17,826,424 shares of common stock issuable upon conversion of our convertible notes as of March 31, 2006, based on a conversion price of $14.22 per share; and

3,085,715 shares of common stock issuable upon exercise of currently outstanding warrants with exercise prices ranging from $0.70 to $1.40 per share. If these warrants are exercised, you will experience additional dilution of $0.03 per share.

## SELECTED HISTORICAL FINANCIAL DATA

The following table sets forth our selected historical financial information. The statement of operations and cash flow data for the years ended December 31, 2003, 2004 and 2005 and the balance sheet data as of December 31, 2004 and 2005 are derived from our audited consolidated financial statements and related notes included in the back of this prospectus. The statement of operations and cash flow data for the years ended December 31, 2001 and 2002 and the balance sheet data as of December 31, 2001, 2002 and 2003 are derived from our audited consolidated financial statements and related notes not included in this prospectus. The statement of operations and cash flow data for the three months ended March 31, 2005 and 2006 and the balance sheet data as of March 31, 2006 are derived from our unaudited consolidated financial statements included in the back of this prospectus. In the opinion of management, the unaudited consolidated financial statements have been prepared on the same basis as our audited consolidated financial statements and include all adjustments, consisting of only normal recurring adjustments, necessary for a fair presentation of the information set forth therein. The results for any interim period are not necessarily indicative of the results that may be expected for a full year.

The results included below and elsewhere in this prospectus are not necessarily indicative of our future performance. You should read this information together with "Capitalization," "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and the related notes included elsewhere in this prospectus.

| | For the Years Ended December 31, | | | | | For the Three Months Ended March 31, | |
|---|---|---|---|---|---|---|---|
| | 2001(1) | 2002 | 2003 | 2004 | 2005 | 2005 | 2006 |
| | (in thousands, except per share amounts) | | | | | | (Restated(5)) |
| **Statement of Operations Data:** | | | | | | | |
| Operating Revenues: | | | | | | | |
| Telephony services | $ | $ 797 | $ 16,905 | $ 75,864 | $ 258,165 | $ 38,583 | $ 111,658 |
| Customer equipment and shipping | | 174 | 1,817 | 3,844 | 11,031 | 2,127 | 7,225 |
| | | 971 | 18,722 | 79,708 | 269,196 | 40,710 | 118,883 |
| Operating Expenses: | | | | | | | |
| Direct cost of telephony services(2) | | 1,599 | 8,556 | 23,209 | 84,050 | 12,108 | 37,584 |
| Direct cost of goods sold | | 855 | 4,867 | 18,878 | 40,441 | 11,588 | 17,580 |
| Selling, general and administrative | 6,846 | 7,846 | 19,174 | 49,186 | 154,716 | 20,553 | 52,875 |
| Marketing | 50 | 1,983 | 11,819 | 56,075 | 243,404 | 55,436 | 88,288 |
| Depreciation and amortization | 550 | 1,114 | 2,367 | 3,907 | 11,122 | 1,610 | 4,959 |
| | 7,446 | 13,397 | 46,783 | 151,255 | 533,733 | 101,295 | 201,286 |
| Loss from operations | (7,446) | (12,426) | (28,061) | (71,547) | (264,537) | (60,585) | (82,403) |
| Net loss | $ (7,217) | $ (12,742) | $ (29,974) | $ (69,921) | $ (261,334) | $ (60,002) | $ (85,160) |
| Net loss per common share calculation: | | | | | | | |
| Net loss | $ (7,217) | $ (12,742) | $ (29,974) | $ (69,921) | $ (261,334) | $ $(60,002) | $ (85,160) |
| Imputed dividend on preferred shares | | | | | (605) | | |

| | For the Years Ended December 31, | | | | | For the Three Months Ended March 31, | |
|---|---|---|---|---|---|---|---|
| Net loss attributable to common stockholders | $ (7,217) | $ (12,742) | $ (29,974) | $ (69,921) | $ (261,939) | $ (60,002) | $ (85,160) |
| Net loss per common share: | | | | | | | |
| Basic and diluted | $ (5.68) | $ (8.96) | $ (21.14) | $ (51.41) | $ (189.67) | $ (43.83) | $ (60.40) |
| Weighted-average common shares outstanding: | | | | | | | |
| Basic and diluted | 1,271 | 1,422 | 1,418 | 1,360 | 1,381 | 1,369 | 1,410 |

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| For the Years Ended December 31, | | | | | For the Three Months Ended March 31, |
|---|---|---|---|---|---|
| **2001(1)** | **2002** | **2003** | **2004** | **2005** | **2005** |