

SMITH MICRO SOFTWARE INC

Form 10-K

February 25, 2011

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-K**

**þ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2010**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission File Number 0-26536  
SMITH MICRO SOFTWARE, INC.  
(Exact name of registrant as specified in its charter)**

**Delaware**  
(State or other jurisdiction of incorporation or  
organization)

**33-0029027**  
(I.R.S. Employer Identification Number)

**51 Columbia, Aliso Viejo, CA**  
(Address of principal executive offices)  
Registrant's telephone number, including area code: **(949) 362-5800**

**92656**  
(Zip Code)

**Common Stock, \$.001 par value**  
(Title of each class)

**The NASDAQ Stock Market LLC**  
**(NASDAQ Global Market)**  
(Name of each exchange on which registered)

**Securities registered pursuant to Section 12(b) of the Act: Common Stock, \$.001 par value**  
**Securities registered pursuant to Section 12(g) of the Act: None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES  NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 YES  NO

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K .

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

Large accelerated filer <input type="radio"/>	Accelerated filer <input type="checkbox"/>	Non-accelerated filer <input type="radio"/> (Do not check if a smaller reporting company)	Smaller reporting company <input type="radio"/>
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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES  NO

As of June 30, 2010, the last business day of the registrant's most recently completed second quarter, the aggregate market value of the common stock of the registrant held by non-affiliates was \$289,135,326 based upon the closing sale price of such stock as reported on the Nasdaq Global Market on that date. For purposes of such calculation, only executive officers, board members, and beneficial owners of more than 10% of the registrant's outstanding common stock are deemed to be affiliates.

As of February 18, 2011, there were 34,971,796 shares of common stock outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's Proxy Statement for the 2011 Annual Meeting of Stockholders to be filed under the Securities Exchange Act of 1934 are incorporated by reference in Part III of this report.

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**SPECIAL NOTE REGARDING FORWARD LOOKING STATEMENTS**

*In this document, the terms Smith Micro, Company, we, us, and our refer to Smith Micro Software, Inc. and, where appropriate, its subsidiaries.*

*This report contains forward-looking statements regarding Smith Micro which include, but are not limited to, statements concerning projected revenues, expenses, gross profit and income, the competitive factors affecting our business, market acceptance of products, customer concentration, the success and timing of new product introductions and the protection of our intellectual property. These forward-looking statements are based on our current expectations, estimates and projections about our industry, management's beliefs, and certain assumptions made by us. Words such as anticipates, expects, intends, plans, predicts, potential, believes, seeks, estimates, should, may, will and variations of these words or similar expressions are intended to identify forward-looking statements. Forward-looking statements also include the assumptions underlying or relating to any of the foregoing statements. These statements are not guarantees of future performance and are subject to risks, uncertainties and assumptions that are difficult to predict. Therefore, our actual results could differ materially and adversely from those expressed or implied in any forward-looking statements as a result of various factors. Such factors include, but are not limited to, the following:*

*the continued economic slowdown and uncertainty and its effects on capital expenditures by our customers and their end users;*

*our ability to predict consumer needs, introduce new products, gain broad market acceptance for such products and ramp up manufacturing in a timely manner;*

*changes in demand for our products from our customers and their end-users;*

*the intensity of the competition and our ability to successfully compete;*

*the pace at which the market for new products develop;*

*the response of competitors, many of whom are bigger and better financed than us;*

*our ability to successfully execute our business plan and control costs and expenses;*

*our ability to protect our intellectual property and our ability to not infringe on the rights of others; and*

*those additional factors which are listed under the section 1A. Risk Factors beginning on page 11 of this report.*

*The forward-looking statements contained in this report are made on the basis of the views and assumptions of management regarding future events and business performance as of the date this report is filed with the Securities and Exchange Commission (the SEC). We do not undertake any obligation to update these statements to reflect events or circumstances occurring after the date this report is filed.*

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**PART I**

**Item 1. BUSINESS**

**General**

Smith Micro Software, Inc. designs, develops and markets software products and services primarily for the mobile computing and communications industries. The Company is focused on developing connectivity, communications, and content management solutions for a converging world of wireless and wired networks. The Company's portfolio of wireless software products and services includes a wide range of software solutions including our QuickLink® family of products. We provide mobile voice and data connectivity across 3G, 4G and Wi-Fi networks. Our mobile communications portfolio includes solutions for Push-To-Talk, Visual Voicemail, mobile device management and video. We also offer user-friendly solutions for the management of mobile content, contacts and calendar data. Our patented compression technologies are utilized within various Smith Micro products including our line of Personal Computer ( PC ) and Smartphone compression products and our managed file-transfer solution. We sell our products and services to many of the world's leading mobile network operators, original equipment manufacturers ( OEM ), device manufacturers and enterprise businesses, as well as directly to consumers. The proliferation of broadband mobile wireless technologies is providing new opportunities for our products and services on a global basis. When these broadband wireless technologies EVDO, UMTS/HSPA, Wi-Fi, LTE and WiMAX are combined with new devices such as mobile phones, Personal Computers, Smartphones, Netbooks, and tablets and emerging Machine-to-Machine ( M2M ) devices, opportunities emerge for new communications software products. Our core technologies are designed to address these emerging mobile connectivity and convergence opportunities. Our innovative line of productivity and graphics products are distributed through a variety of consumer channels worldwide, our online stores, and third-party wholesalers, retailers and value-added resellers. We offer products that operate on Windows, Mac, UNIX, Linux, iOS, Android, Windows Mobile, Symbian and Java platforms. The underlying design concept common to all of our products is our ability to improve the customer's experience. This philosophy is based on the combination of solid engineering and exceptional design that reinforces our brand's competitive differentiation. We have over 25 years of experience in design, creation and custom engineering services for software products.

We continue to invest significantly in our leading-edge technologies. Our research and development investments for the years ending December 31, 2010, 2009 and 2008 were \$42.8 million, \$36.5 million and \$30.8 million, respectively. Our research and development expenses consist primarily of personnel costs required to conduct our software development efforts.

We were incorporated in California in November 1983, and we reincorporated in Delaware in June 1995. Our principal executive offices are located at 51 Columbia, Aliso Viejo, California 92656. Our telephone number is (949) 362-5800. Our website address is [www.smithmicro.com](http://www.smithmicro.com). We make our SEC filings available on the Investor Relations page of our website. Information contained on our website is not part of this Annual Report on Form 10-K.

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### **Business Segments**

Our operations are organized into two business segments: Wireless and Productivity & Graphics. We do not separately allocate operating expenses, nor do we allocate specific assets to these groups. Therefore, segment information reported includes only revenues and cost of revenues. See Note 6 of Notes to Consolidated Financial Statements for financial information related to our business segments.

#### **Wireless**

The Wireless Group's primary focus is to develop mobile connectivity, mobile information management and mobile security solutions. QuickLink® Mobile, the group's leading product, provides mobile users the ability to easily connect a notebook or other wireless device to wireless wide area networks ( WWANs ) and wireless local area networks ( WLANs ) or Wi-Fi hotspots. Many of the world's largest mobile operators and service providers including AT&T, Bell Canada, Bouygues, Clear, Comcast, Orange, Sprint, Time Warner, T-Mobile USA, Verizon Wireless, Vodafone and others rely on QuickLink® Mobile technology to help their subscribers easily connect to their wireless networks every day. One of the reasons more mobile operators rely on our connection management solution for their subscribers is our patented technology to seamlessly switch a wireless device between WWANs and WLANs. We provide services to leading device manufacturers such as HTC, Motorola and Nokia.

In addition to marketing products to wireless carriers and device manufacturers, the Wireless Group also delivers wireless mobility solutions designed to address security and mobility needs of enterprises rapidly becoming more reliant on remote access to many types of wireless networks. In addition to addressing the need for robust security, the QuickLink® Mobility suite allows persistent connectivity for the user operating on WWANs, corporate Local Area Networks ( LAN s ) and Wi-Fi networks. The applications support most IP services and interoperate with approximately 200 carriers worldwide, as well as hundreds of the popular broadband mobile devices and embedded WWAN PC notebooks.

As a result of network and device proliferation, there is an emerging need for smarter connectivity. Our latest solutions to emerge utilize our unique blend of Smith Micro DNA spanning connectivity, communications and content management that can be combined in virtually limitless combinations to create unique, strategic customer solutions. Smith Micro continues to introduce solutions for mobile device communications. These include synchronization, back-up and restore of critical user data, push-to-talk software and visual voicemail services. This portfolio serves wireless carriers and device manufacturers with mobile handset software, as well as hosted software-as-a-service solutions. These products are designed to work across a broad spectrum of handset operating systems and platforms, including a rich array of feature phones and today's most popular Smartphones.

Wireless carriers and mobile device manufacturers incorporate our products into their branded product and service offerings, selling directly to their market segments. Our technologies are utilized in many major wireless networks to facilitate data communications via mobile devices, media solutions and device management. Our primary products for connection management are QuickLink® Mobile and QuickLink® Mobility. For managing the media on mobile devices, we have QuickLink® Media. Our Device Management Suite provides intelligent, automated mobile device provisioning and configuration. Rounding out our wireless portfolio, we also offer Push-To-Talk, Visual Voicemail, and mobile video solutions.

#### **Productivity & Graphics**

The Productivity & Graphics Group focuses on developing a variety of software for the consumer, prosumer, and professional markets. Our solutions span compression, graphics and utilities. This group



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also republishes and markets third party software titles that complement our existing line of products. All of these products are available through direct sales on the Smith Micro websites (smithmicro.com, mysmithmicro.com and contentparadise.com), on partner websites, direct through customer service order desks, on-line resellers and through traditional retail outlets.

The lead product line in this area is StuffIt®, driven by its patented and patent-pending image compression, with a focus on our innovative lossless JPEG compression technology. StuffIt® provides superior lossless compression, encryption and archiving. We have enhanced this industry-leading product's feature set with new, online file transfer capabilities.

In addition to compression technology, the Company is focused on growing its line of graphic titles, in particular Poser®, Anime Studio and Manga Studio .

**Industry Background**

Smith Micro offers products in the following technology and communications related markets:

*Wireless and mobility* In order to capitalize on the emerging adoption trends for mobile Internet services and connectivity to global networks, mobile operators and service providers are introducing a wide array of data services and new mobile devices. Traditional mobile phone devices, Smartphones, laptops, tablet devices, Netbooks and other wirelessly connected devices are being deployed at escalating rates. Wireless data access service plans for these multimedia-enabled devices are being adopted at such a fast pace that global infrastructure for wireless networks is rapidly being updated to support higher speeds and greater capacity. The burgeoning demand for pervasive connectivity is driven by a need to access information anytime and from anywhere. In addition to this trend, there is an evolving and changing pattern of media being consumed on-demand from multiple different device types, including handheld terminals. Creating software that can enable capabilities to meet this demand for wireless access via 3G, 4G and Wi-Fi, in a way that enhances the user's enjoyment of their online experience, represents the primary opportunity and area of focus for Smith Micro.

Smith Micro offers a variety of products that fit into our primary area of focus which enables connectivity to networks, devices, information and data. Providing software that connects devices in a simple and secure way to wireless networks using our QuickLink® Mobile family of products for mobile operators continues to expand. Wireless carriers are facing increased complexity in trying to serve customers' connectivity needs as they move from 3G networks to beginning to support new higher speed technologies such as HSPA+, LTE and WiMAX network protocols which enable new capacity and higher speeds for the wireless subscribers. The increase in the amount of data traffic on the carrier networks is being fueled by new subscriber growth and higher bandwidth applications, such as video services. These developments, along with mobile devices that combine multiple radio chip-sets including Wi-Fi, 3G and 4G, are creating an increased interest in software that can support intelligent connectivity and service continuity across these differing network technologies. The QuickLink® Mobile family of connectivity software has been designed to help mobile operators meet the challenges of serving their subscriber base in this evolving and increasingly complex world of broadband wireless access.

These rapid changes in wireless technology including higher speed networks, improved intelligent connected devices and increasing demands for access to digital content and critical information, is fueling the evolution of a new *connected digital lifestyle*. Software that simplifies the complexity associated with serving this digital lifestyle and managing access to data from many sources, from any network type and via multiple devices is in demand for both the service providers and their end-user customers. As wireless carriers continue to seek new ways to offer premium services that allow their subscribers to better access the information, data and communications services that are becoming so vital to the way they lead their lives, Smith Micro's portfolio of connectivity software, content delivery, device management and messaging solutions are addressing this demand.

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*Productivity and graphic software* Smith Micro also offers a secondary line of software that centers on serving the growing demand for improved graphic related products for 2D and 3D design. The Company's products include Poser®, a 3D figure design and animation program, Manga Studio , the number one selling Manga software worldwide and Anime Studio , a complete solution for creating 2D movies, cartoons, anime or cut-out animations and is ideal for animators of any caliber. Many of the animations that people create with Anime Studio can be seen on social networking websites and YouTube. In addition to the graphics products, the growing prevalence and complexity of personal computers and mobile device operating systems require increasingly sophisticated diagnostic and utility software solutions to improve the consumer's overall computing and mobile experience. Consumers demand products that can enhance PC performance, protect against spam, spyware, and computer hacking and remove malicious code. Businesses rely on cross-platform solutions that can quickly identify and repair a broad range of computer-related problems. The Company's software solution for Windows and Mac platforms performs diagnostics, maximizes performance and helps to protect consumer's online identity.

**Products and Services**

Our primary products consist of the following:

<b>Product Groups</b>	<b>Products</b>	<b>Description</b>
Wireless	QuickLink® Mobile	Centralized connection management application to control, customize and automate wireless connections of all types.
	QuickLink® Mobility	A mobile VPN and connection management solution delivering network session persistence.
	QuickLink® Media	Media and content management solution to synchronize and manage access to digital content from mobile devices, personal computers and the Cloud.
	SendStuffNow	Secure Cloud-based large file delivery solution.
	Device Management Suite	Provides intelligent, automated mobile device provisioning and configuration.
	Push-To-Talk	A data service that uses a mobile Internet connection to send and receive walkie-talkie style calls.
	Visual Voicemail	Voicemail is delivered directly to your mobile phone and stored in a visual inbox and also includes voicemail translation to text.
	Vidio	Video content delivery and optimization system for streaming to personal computers, tablets and mobile devices.
Productivity & Graphics	StuffIt Deluxe®	Patented, lossless compression solution for documents and media.
	CheckIt® Diagnostics & CheckIt® Netbook Suite	A diagnosis and troubleshooting solution for many hardware and system problems.
	Poser®	A solution for creating 3D character art and animations.
	Anime Studio	An animation tool for professionals and digital artists.
	Manga Studio	A solution for creating manga and comic art.

**Marketing and Sales Strategy**

Our primary focus is on developing the next mobile software experience through our Smith Micro DNA mobile platform for wireless operators and enterprises. Because of our broad product offerings, we are able to capitalize on technology synergies across our portfolio and quickly bring to market solutions that resonate with our target customers.

We continue to develop innovative, enabling technology and infrastructure products that facilitate the usage of wireless data and other premium mobile services, thereby providing our customers with additional revenue opportunities and differentiated services that encourage customer loyalty.



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A core strategy is our ability to enable our wireless carrier and device manufacturer customers to introduce new products to their markets that generate revenue more quickly. Our industry knowledge and our research are used to help determine the next market opportunities for our customers in the mobile market.

Our sales strategy is as follows:

*Leverage Carrier and OEM Relationships.* We continue to capitalize on our strong relationships with the world's leading wireless carriers and mobile device manufacturers. For example, our carrier customers serve as a valuable distribution channel, providing access to millions of end-users and also providing market feedback for future product offerings.

*Focus on Multiple High-Growth Markets.* We continue to focus on wireless connectivity, communications and content management. Within these markets, we see ongoing enhancement of networks and services by wireless carriers and an increasing availability of rich media and application-oriented Smartphones. This represents a remarkable alignment between our product portfolio and market opportunity.

*Expand our Customer Base.* In addition to introducing new products to new customers, we intend to grow our domestic and international business through cross-selling our portfolio of products to our current customer base.

*Selectively Pursue Acquisitions of Complementary Products and Services.* In line with the Company's strategy, we will continue to pursue selected acquisition opportunities in an effort to expand our product and technological abilities, enter complementary markets and extend our geographic reach. In the past, we have used acquisitions to enhance our technology features and customer base, and to extend our product offerings into new markets.

Smith Micro is expanding its ability to serve wireless carriers, OEMs and enterprise customers in Europe and Asia through international sales and support offices based in Sweden, the United Kingdom, Australia and Hong Kong. Our three largest customers are in the Wireless segment and each exceeded 10% of revenues for fiscal year 2010. Verizon Wireless, Sprint and AT&T accounted for 66.3% of our revenues in fiscal 2010. In 2009, our four largest customers (Verizon Wireless, Dell, Sprint and AT&T) accounted for 65.7% of our revenues. In 2008, our three largest customers (Verizon Wireless, AT&T and Sprint) accounted for 48.1% of our revenues. Our major customers could reduce their orders of our products in favor of a competitor's product or for any other reason. The loss of any of our major customers or decisions by a significant customer to substantially reduce purchases could have a material adverse effect on our business.

Sales to Verizon Wireless and their affiliates amounted to 40.1%, 32.8%, and 32.0% of the Company's revenues for fiscal years 2010, 2009 and 2008, respectively. We have a master software and license distribution agreement with Verizon Wireless whereas Smith Micro grants them non-exclusive licenses to reproduce and have produced, market, and distribute the software, in object form only, to distributors, re-sellers, OEM customers of Verizon Wireless and end users. The license term for end users continues in perpetuity unless otherwise stated in subsequent amendments. The master agreement commenced in December 2000 and has been consistently extended through subsequent amendments. They can cancel the agreement at any time. Products and services sold to Verizon include per unit license fees for connectivity and security and VZAccess manager software, engineering design and development fees, customization and adaptation fees and website hosting. The master agreement and subsequent amendments are detailed in Exhibit 10.4 in this document.

### **Integration Initiatives**

Smith Micro is committed to the integration of recent acquisitions for engineering, sales and marketing within the Company. The Company continues to drive greater productivity, flexibility and cost savings by integrating its own business processes and functions, thereby eliminating redundancies.

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**Customer Service and Technical Support**

We provide technical support and customer service through our online knowledge base, via email and by telephone. OEM customers generally provide their own primary customer support functions and rely on us for support to their own technical support personnel.

**Product Development**

The software industry, particularly the wireless market, is characterized by rapid and frequent changes in technology and user needs. We work closely with industry groups and customers, both current and potential, to help us anticipate changes in technology and determine future customer needs. Software functionality depends upon the capabilities of the hardware. Accordingly, we maintain engineering relationships with various hardware manufacturers and we develop our software in tandem with their product development. Our engineering relationships with manufacturers, as well as with our major customers, are central to our product development efforts. We remain focused on the development and expansion of our technology, particularly in the wireless space. Research and development expenditures amounted to \$42.8 million, \$36.5 million, and \$30.8 million for the years ended December 31, 2010, 2009 and 2008, respectively.

**Manufacturing**

Although we primarily deliver our software via electronic downloads, we do deliver our software in several other forms. We offer a package or kit that may include CD-ROM(s), a cable and certain other documentation or marketing material. We also permit selected OEM customers to duplicate our products on their own CD-ROM s, USB devices, or embedded devices, and pay a royalty based on usage. Some OEM business requires that we provide a CD, which includes a soft copy of a user guide. Finally, we grant licenses to certain OEM customers that enable those customers to preload a copy of our software onto a personal computer. With the enterprise sales program, we offer site licenses under which a corporate user is allowed to distribute copies of the software to users within their corporate sites. Our product development group produces a product master for each product that is then duplicated and packaged into products by the manufacturing organization. All product components are purchased by our personnel in our Aliso Viejo, California facility. Our manufacturing is subcontracted to outside vendors and includes the replication of CD-ROM s and the printing of documentation materials. Assembly of the final package is completed by our Aliso Viejo, California facility.

**Competition**

The markets in which we operate are highly competitive and subject to rapid changes in technology. Rapidly changing technology combined with relatively low barriers to entry in the mobile software market is constantly creating new opportunities, and we expect new competitors to enter the market. We also believe that competition from established and emerging software companies will continue to intensify as the emerging mobile, wireless and Internet markets evolve. We compete with other software vendors for the attention of customers as well as in our efforts to acquire technology and qualified personnel.

We believe that the principal competitive factors affecting the mobile software market include product features, usability, quality, price, customer service and effective sales and marketing efforts. Although we believe that our products currently compete favorably with respect to these factors, there can be no assurance that we can maintain our competitive position against current and potential competitors. We believe that the market for our software products has been and will continue to be characterized by significant price competition. A material reduction in the price of our products could negatively affect our profitability.

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Many existing and potential OEM customers have technological capabilities to develop products that compete directly with our products. These customers may discontinue the purchase of our products. Our future performance is substantially dependent upon the extent to which existing OEM customers elect to purchase communications software from us rather than design and develop their own software. Because our customers are not contractually obligated to purchase any of our products, they may cease to rely, or fail to expand their reliance on us as a source for communications software in the future.

**Proprietary Rights and Licenses**

Our success and ability to compete is dependent upon our software code base, our programming methodologies and other intellectual properties. To protect our proprietary technology, we rely on a combination of trade secrets, nondisclosure agreements, patents, copyright and trademark law that may afford only limited protection. As of December 31, 2010, we owned 42 issued U.S. patents and have 52 U.S. patent applications that are currently pending. These patents are intended to provide generalized protection of our intellectual property technology base and we will continue to apply for various patents and trademarks in the future as we deem necessary to protect our intellectual property technology base.

We seek to avoid unauthorized use and disclosure of our proprietary intellectual property by requiring employees and consultants with access to our proprietary information to execute confidentiality agreements with us and by restricting access to our source code. The deterrent steps that we have taken to protect our proprietary technology may not be adequate to deter misappropriation of our proprietary information or prevent the successful assertion of any adverse claim against us relating to software or intellectual property utilized by us. In addition, we may not be able to detect unauthorized use of our intellectual property rights or take effective steps to enforce those rights.

In selling our products, we primarily rely on shrink wrap licenses that are not signed by licensees and may be unenforceable under the laws of certain jurisdictions. In addition, the laws of some foreign countries do not protect our proprietary rights to as great an extent as do the laws of the United States. Accordingly, the means we use currently to protect our proprietary rights and intellectual property rights may not be adequate. Moreover, our competitors may independently develop competitive technology similar to ours. We also license technology on a non-exclusive basis from several companies for inclusion in our products and anticipate that we will continue to do so in the future. If we are unable to continue to license these technologies or to license other necessary technologies for inclusion in our products, or such third party technologies become subject to claims directed to or against the third party technologies used by us, or if we experience substantial increases in royalty payments under these third party licenses, our business could be materially and adversely affected.

**Employees**

As of December 31, 2010, we had a total of 549 employees within the following departments: 370 in engineering, 115 in sales and marketing, 41 in management and administration, 13 in customer support and 10 in manufacturing. We utilize temporary labor to assist during peak periods of manufacturing volume. We believe that our future success will depend in large part upon our continuing ability to attract and retain highly skilled managerial, sales, marketing, customer support, research and development personnel and consulting staff. Like other software companies, we face intense competition for such personnel, and we have at times experienced and continue to experience difficulty in recruiting qualified personnel. There can be no assurance that we will be successful in attracting, assimilating and retaining other qualified personnel in the future. We are not subject to any collective bargaining agreement and we believe that our relationships with our employees are good.

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**Item 1A. RISK FACTORS**

Our future operating results are highly uncertain. Before deciding to invest in our common stock or to maintain or increase your investment, you should carefully consider the risks described below, in addition to the other information contained in this report and in our other filings with the SEC, including our reports on Forms 10-K, 10-Q and 8-K. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also affect our business operations. If any of these risks actually occur, that could seriously harm our business, financial condition or results of operations. In that event, the market price for our common stock could decline and you may lose all or part of your investment.

***Our operating results may be adversely impacted by the continued worldwide economic slowdown and uncertainties in the marketplace.***

Since the second half of 2008, economic conditions worldwide and in the United States have experienced a general deterioration, resulting in slower economic activity and a highly uncertain recovery, decreased consumer confidence and retail spending, reduced corporate profits and capital spending, and generally adverse business conditions. These conditions make it difficult for our wireless carrier and OEM customers and their end users to accurately forecast and plan future business activities and capital expenditures, which could cause them to slow spending on our products and services. Furthermore, during challenging economic times our customers may face issues gaining timely access to sufficient credit, which could result in an impairment of their ability to make timely payments to us. We cannot predict the timing, strength or duration of the current economic slowdown or the emerging economic recovery, or to what extent they will continue to affect us. If the economy, consumer spending or the markets in which we operate do not continue at their present levels or deteriorate, we may need to record charges related to restructuring costs and the impairment of goodwill and other long-lived assets, and our business, financial condition and results of operations will likely be materially and adversely affected.

***Our quarterly revenues and operating results are difficult to predict and could fall below analyst or investor expectations, which could cause the price of our common stock to fall.***

Our quarterly revenues and operating results have fluctuated significantly in the past and may continue to vary from quarter to quarter due to a number of factors, many of which are not within our control. If our operating results do not meet the expectations of securities analysts or investors, our stock price may decline. Fluctuations in our operating results may be due to a number of factors, including the following:

the gain or loss of a key customer;

the size and timing of orders from and shipments to our major customers;

the size and timing of any return product requests for our products;

our ability to maintain or increase gross margins;

variations in our sales channels or the mix of our product sales;

our ability to anticipate market needs and to identify, develop, complete, introduce, market and produce new products and technologies in a timely manner to address those needs;

the availability and pricing of competing products and technologies and the resulting effect on sales and pricing of our products;

acquisitions;

the effect of new and emerging technologies;

the timing of acceptance of new mobile services by users of our customers' services;

deferrals of orders by our customers in anticipation of new products, applications, product enhancements or operating systems; and



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general economic and market conditions.

We have difficulty predicting the volume and timing of orders. In any given quarter, our sales have involved, and we expect will continue to involve, large financial commitments from a relatively small number of customers. As a result, the cancellation or deferral of even a small number of orders would reduce our revenues, which would adversely affect our quarterly financial performance. Also, we have often booked a large amount of our sales in the last month of the quarter and often in the last week of that month. Accordingly, delays in the closing of sales near the end of a quarter could cause quarterly revenues to fall substantially short of anticipated levels. Significant sales may also occur earlier than expected, which could cause operating results for later quarters to compare unfavorably with operating results from earlier quarters.

A large portion of our operating expenses, including rent, depreciation and amortization is fixed and difficult to reduce or change. Accordingly, if our total revenue does not meet our expectations, we may not be able to adjust our expenses quickly enough to compensate for the shortfall in revenue. In that event, our business, financial condition and results of operations would be materially and adversely affected.

Due to all of the foregoing factors, and the other risks discussed in this report, you should not rely on quarter-to-quarter comparisons of our operating results as an indication of future performance.

***Our total revenues currently depend on a small number of products and customers, so our operating results are vulnerable to unexpected shifts in demand.***

A substantial majority of our total revenue is derived from sales of our wireless connectivity and security software products. Although our strategy is to continue to introduce new products, these efforts may not reduce the extent to which our total revenues are dependent on a small number of products in these market sectors. Rapid shifts in the markets for these products and consumer habits, changes in demand by end-users and changes in underlying technology present both opportunities and risks for our business. Factors which could affect our business include the rate of adoption of the 4G networking standard by wireless carriers and handset manufacturers, and changes in consumer demand for PC networking due to the adoption of Smartphones and tablet computing. If our products fail to remain current with and useful to new and emerging markets, our business, financial condition and results of operations would be materially and adversely affected.

We also derive a significant portion of our revenues from a few vertical markets, such as wireless carriers and handset manufacturers. In order to sustain and grow our business, we must continue to sell our software products into these vertical markets. Shifts in the dynamics of these vertical markets, such as new product introductions by our competitors, could seriously harm our results of operations, financial condition and prospects. To increase our sales outside our core vertical markets, for example to large enterprises, requires us to devote time and resources to hire and train sales employees familiar with those industries. Even if we are successful in hiring and training sales teams, customers in other vertical markets may not need or sufficiently value our current products or new product introductions.

In addition, because we sell primarily to large carriers and OEMs, there are a limited number of actual and potential customers for our products, resulting in customer concentration for sales of our products and services. For the year ended December 31, 2010, one customer, Verizon Wireless, comprised 40.1% of our total revenues. Two other customers (Sprint and AT&T) individually comprised of at least 10% of our total revenues. Because of our customer concentration, our largest customers may have significant pricing power over us. Furthermore, a substantial decrease in sales to any of our largest customers could materially affect our revenues and profitability. Additionally, these customers are not the end-users of our products. If any of these customers' efforts to market their products which incorporate our software are unsuccessful in the marketplace, our revenues and profitability could be adversely affected.

***Competition within our target markets is intense and includes numerous established competitors and new entrants, which could negatively affect our revenues and results of operations.***

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We operate in markets that are extremely competitive and subject to rapid changes in technology. A number of established software companies, such as Microsoft Corporation, Google Inc. and Apple Inc. pose a significant competitive threat to us because their handset operating systems may include some capabilities now provided by certain of our OEM and retail software products. If handset manufacturers and carriers are satisfied relying on the capabilities of systems using Windows, Android or iPhone OS, or other hardware or operating systems, sales of our products are likely to decline. In addition, because there are low barriers to entry into the software markets in which we participate and may participate in the future, we expect significant competition from both established and emerging software companies in the future, both domestic and international. In fact, our growth opportunities in new product markets could be limited to the extent established and emerging software companies enter or have entered those markets. Furthermore, our existing and potential OEM customers may acquire or develop products that compete directly with our products.

Many of our other current and prospective competitors have significantly greater financial, marketing, service, support, technical and other resources than we do. As a result, they may be able to adapt more quickly than we to new or emerging technologies and changes in customer requirements or to devote greater resources to the promotion and sale of their products. Announcements of competing products by competitors could result in the cancellation of orders by customers in anticipation of the introduction of such new products. In addition, some of our competitors currently make complementary products that are sold separately. Such competitors could decide to enhance their competitive position by bundling their products to attract customers seeking integrated, cost-effective software applications. Some competitors have a retail emphasis and offer OEM products with a reduced set of features. The opportunity for retail upgrade sales may induce these and other competitors to make OEM products available at their own cost or even at a loss. We also expect competition to increase as a result of software industry consolidations, which may lead to the creation of additional large and well-financed competitors. Increased competition is likely to result in price reductions, fewer customer orders, reduced margins and loss of market share. ***Acquisitions of companies or technologies may disrupt our business and divert management attention and cause our current operations to suffer.***

We have historically made targeted acquisitions of smaller companies with important technology and expect to continue to do so in the future. As part of any acquisition, we will be required to assimilate the operations, products and personnel of the acquired businesses and train, retain and motivate key personnel from the acquired businesses. We may not be able to maintain uniform standards, controls, procedures and policies if we fail in these efforts. Similarly, acquisitions may cause disruptions in our operations and divert management's attention from our company's day-to-day operations, which could impair our relationships with our current employees, customers and strategic partners. Acquisitions may also subject us to liabilities and risks that are not known or identifiable at the time of the acquisition.

We may also have to incur debt or issue equity securities in order to finance future acquisitions. Our financial condition could be harmed to the extent we incur substantial debt or use significant amounts of our cash resources in acquisitions. The issuance of equity securities for any acquisition could be substantially dilutive to our existing stockholders. In addition, we expect our profitability could be adversely affected because of acquisition-related accounting costs, write offs, amortization expenses, and charges related to acquired intangible assets. In consummating acquisitions, we are also subject to risks of entering geographic and business markets in which we have had limited or no prior experience. If we are unable to fully integrate acquired businesses, products or technologies within existing operations, we may not receive the intended benefits of acquisitions.

***We are entering new, emerging markets in which we have limited experience; if these markets do not develop or we are unable to otherwise succeed in them, our revenues will suffer and the price of our common stock will likely decline.***

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Our recent and planned product introductions to support new higher speed networking and 4G technologies such as HSPA+, LTE and WiMAX network protocols have allowed us to enter new markets. A viable market for these products may not develop or be sustainable, and we may face intense competition in these markets. In addition, our success in these markets depends on our carrier customers' ability to successfully introduce new mobile services enabled by our products and our ability to broaden our carrier customer base, which we believe will be difficult and time-consuming. If the expected benefits from entering new markets do not materialize our revenues will suffer and the price of our common stock would likely decline. In addition, to the extent we enter new markets through acquisitions of companies or technologies, our financial condition could be harmed or our stockholders could suffer dilution without a corresponding benefit to our company if we do not realize expected benefits of entering such new markets.

***If the adoption of and investments in new technologies and services grows more slowly than anticipated in our product planning and development, our operating results, financial condition and prospects may be negatively affected.***

If the adoption of and investments in new networking and 4G technologies and services does not grow or grows more slowly than anticipated, we will not obtain the anticipated returns from our planning and development investments. For example, our Device Management Suite of products allows our customers to update mobile devices from a home office and incorporates technology that provides a mechanism to allow for efficient firmware updates for mobile devices. In addition, we have introduced new high-speed networking and 4G products, but the pace of the market introduction of such technologies is uncertain. Future sales and any future profits from these and related products are substantially dependent upon the acceptance and use of these new technologies, and on the continued adoption and use of mobile data services by end-users.

Many of our customers and other communications service providers have made and continue to make major investments in next generation networks that are intended to support more complex applications. If communications service providers delay their deployment of networks or fail to deploy such networks successfully, demand for our products could decline, which would adversely affect our revenues. Also, to the extent we devote substantial resources and incur significant expenses to enable our products to be interoperable with new networks that have failed or have been delayed or not deployed, our operating results, financial condition and prospects may be negatively affected.

***Our growth depends in part on our customers' ability and willingness to promote services and attract and retain new customers or achieve other goals outside of our control.***

We sell our products for use on handheld devices primarily through our carrier customers. Losing the support of these customers may limit our ability to compete in existing and potential markets and could negatively affect our revenues. In addition, the success of these customers and their ability and willingness to market services supported by our products are critical to our future success. Our ability to generate revenues from sales of our software is also constrained by our carrier customers' ability to attract and retain customers. We have no input into or influence upon their marketing efforts and sales and customer retention activities. If our carrier customers, particularly our largest customer, Verizon Wireless, fail to maintain or grow demand for their services, revenues or revenue growth from our products designed for use on mobile devices will decline and our results of operations will suffer.

***Our operating income may continue to change due to shifts in our sales mix and increased spending on our research and development and infrastructure.***

Our operating income can change quarter to quarter and year to year due to a change in our sales mix and the timing of our continued investments in research and development and infrastructure. Operating income as a percentage of revenues has ranged from 2.8% in 2008 to 10.4% in 2009 to 14.1% in 2010. We continue to invest in research and development which is the lifeline of our technology portfolio. In addition we continue to invest in our infrastructure with facility expansions in Aliso Viejo, California and a

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new engineering design and data center in Pittsburgh, Pennsylvania. The timing of these additional expenses can vary significantly quarter to quarter and even from year to year.

***Our products may contain undetected software defects, which could negatively affect our revenues.***

Our software products are complex and may contain undetected defects. In the past, we have discovered software defects in certain of our products and have experienced delayed or lost revenues during the period it took to correct these problems. Although we and our OEM customers test our products, it is possible that errors may be found or occur in our new or existing products after we have commenced commercial shipment of those products. Defects, whether actual or perceived, could result in adverse publicity, loss of revenues, product returns, a delay in market acceptance of our products, loss of competitive position or claims against us by customers. Any such problems could be costly to remedy and could cause interruptions, delays, or cessation of our product sales, which could cause us to lose existing or prospective customers and could negatively affect our results of operations. In addition, some of our software contains open source components that are licensed under the GNU General Public License and similar open source licenses. These components may contain undetected defects or incompatibilities, may cause us to lose control over the development of portions of our software code, and may expose us to claims of infringement if these components are, or incorporate, infringing materials, the licenses are not enforceable or are modified to become incompatible with other open source licenses, or exposure to misappropriation claims if these components include unauthorized materials from a third party.

***Technology and customer needs change rapidly in our market, which could render our products obsolete and negatively affect our business, financial condition and results of operations.***

Our success depends on our ability to anticipate and adapt to changes in technology and industry standards. We will also need to continue to develop and introduce new and enhanced products to meet our target markets' changing demands, keep up with evolving industry standards, including changes in the Microsoft and Google operating systems with which our products are designed to be compatible, and to promote those products successfully. The communications and utilities software markets in which we operate are characterized by rapid technological change, changing customer needs, frequent new product introductions, evolving industry standards and short product life cycles. Any of these factors could render our existing products obsolete and unmarketable. In addition, new products and product enhancements can require long development and testing periods as a result of the complexities inherent in today's computing environments and the performance demanded by customers and called for by evolving wireless networking technologies. If our target markets do not develop as we anticipate, our products do not gain widespread acceptance in these markets, or we are unable to develop new versions of our software products that can operate on future wireless networks and PC and mobile device operating systems and interoperate with other popular applications, our business, financial condition and results of operations could be materially and adversely affected.

***Regulations affecting our customers and us and future regulations, to which they or we may become subject to, may harm our business.***

Certain of our customers in the communications industry are subject to regulation by the Federal Communications Commission, which could have an indirect effect on our business. In addition, the United States telecommunications industry has been subject to continuing deregulation since 1984. We cannot predict when, or upon what terms and conditions, further regulation or deregulation might occur or the effect regulation or deregulation may have on demand for our products from customers in the communications industry. Demand for our products may be indirectly affected by regulations imposed upon potential users of those products, which may increase our costs and expenses.

***We may be unable to adequately protect our intellectual property and other proprietary rights, which could negatively impact our revenues.***

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Our success is dependent upon our software code base, our programming methodologies and other intellectual properties and proprietary rights. In order to protect our proprietary technology, we rely on a combination of trade secrets, nondisclosure agreements, patents, and copyright and trademark law. We currently own U.S. trademark registrations for certain of our trademarks and U.S. patents for certain of our technologies. However, these measures afford us only limited protection. Furthermore, we rely primarily on shrink wrap licenses that are not signed by the end user and, therefore, may be unenforceable under the laws of certain jurisdictions. Accordingly, it is possible that third parties may copy or otherwise obtain our rights without our authorization. It is also possible that third parties may independently develop technologies similar to ours. It may be difficult for us to detect unauthorized use of our intellectual property and proprietary rights.

We may be subject to claims of intellectual property infringement as the number of trademarks, patents, copyrights and other intellectual property rights asserted by companies in our industry grows and the coverage of these patents and other rights and the functionality of software products increasingly overlap. From time to time, we have received communications from third parties asserting that our trade name or features, content, or trademarks of certain of our products infringe upon intellectual property rights held by such third parties. We have also received correspondence from third parties separately asserting that our products may infringe on certain patents held by each of the parties. Although we are not aware that any of our products infringe on the proprietary rights of others, third parties may claim infringement by us with respect to our current or future products. Additionally, our customer agreements require that we indemnify our customers for infringement claims made by third parties involving our intellectual property embedded in their products. Infringement claims, whether with or without merit, could result in time-consuming and costly litigation, divert the attention of our management, cause product shipment delays or require us to enter into royalty or licensing agreements with third parties. If we are required to enter into royalty or licensing agreements, they may not be on terms that are acceptable to us. Unfavorable royalty or licensing agreements could seriously impair our ability to market our products.

***If we are unable to retain key personnel, the loss of their services could materially and adversely affect our business, financial condition and results of operations.***

Our future performance depends in significant part upon the continued service of our senior management and other key technical and consulting personnel. We do not have employment agreements with our key employees that govern the length of their service. The loss of the services of our key employees would materially and adversely affect our business, financial condition and results of operations. Our future success also depends on our ability to continue to attract, retain and motivate qualified personnel, particularly highly skilled engineers involved in the ongoing research and development required to develop and enhance our products. Competition for these employees remains high and employee retention is a common problem in our industry. Our inability to attract and retain the highly trained technical personnel that are essential to our product development, marketing, service and support teams may limit the rate at which we can generate revenue, develop new products or product enhancements and generally would have an adverse effect on our business, financial condition and results of operations.

***If we fail to continue to establish and maintain strategic relationships with mobile device manufacturers, market acceptance of our products and our profitability, may suffer.***

Most of our strategic relationships with mobile device manufacturers are not subject to written contract, but rather are in the form of informal working relationships. We believe these relationships are valuable to our success. In particular, these relationships provide us with insights into product development and emerging technologies, which allows us to keep abreast of, or anticipate, market trends and helps us serve our current and prospective customers. Because these relationships are not typically governed by written agreements, there is no obligation for many of our partners to continue working with us. If we are unable to maintain our existing strategic relationships with mobile device manufacturers or if we fail to enter into additional strategic relationships or the parties with whom we have strategic relationships favor one of our competitors, our ability to provide products that meet our current and prospective customers' needs could

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be compromised and our reputation and future revenue prospects could suffer. For example, if our software does not function well with a popular mobile device because we have not maintained a relationship with its manufacturer, carriers seeking to provide that device to their respective customers could choose a competitor's software over ours or develop their own. Even if we succeed in establishing these relationships, they may not result in additional customers or revenues.

***We may raise additional capital through the issuance of additional equity or convertible debt securities or by borrowing money, in order to meet our capital needs. Additional funds may not be available on terms acceptable to us to allow us to meet our capital needs.***

We believe that the cash, cash equivalents and short-term investments on hand and the cash we expect to generate from operations will be sufficient to meet our capital needs for at least the next twelve months. However, it is possible that we may need or choose to obtain additional financing to fund our activities in the future. We could raise these funds by selling more stock to the public or to selected investors, or by borrowing money. We may not be able to obtain additional funds on favorable terms, or at all. If adequate funds are not available, we may be required to curtail our operations or other business activities significantly or to obtain funds through arrangements with strategic partners or others that may require us to relinquish rights to certain technologies or potential markets. We have on file with the SEC a shelf Form S-3 to sell from time to time up to 4,000,000 shares of our common stock in one or more offerings in amounts, at prices and on the terms that we will determine at the time of offering. In addition, we have on file with the SEC a shelf Form S-4 to sell from time to time up to 1,000,000 shares of our common stock in connection with our future acquisitions of other businesses, assets or securities. If we raise additional funds by issuing additional equity or convertible debt securities (whether in a public offering or private placement), the ownership percentages of existing stockholders would be reduced. In addition, the equity or debt securities that we issue may have rights, preferences or privileges senior to those of the holders of our common stock. We currently have no established line of credit or other business borrowing facility in place.

It is possible that our future capital requirements may vary materially from those now planned. The amount of capital that we will need in the future will depend on many factors, including:

the market acceptance of our products;

the levels of promotion and advertising that will be required to launch our products and achieve and maintain a competitive position in the marketplace;

our business, product, capital expenditure and research and development plans and product and technology roadmaps;

the levels of inventory and accounts receivable that we maintain;

capital improvements to new and existing facilities;

technological advances;

our competitors' response to our products; and

our relationships with suppliers and customers.

In addition, we may raise additional capital to accommodate planned growth, hiring, infrastructure and facility needs or to consummate acquisitions of other businesses, products or technologies.

***Our business, financial condition and operating results could be adversely affected as a result of legal, business and economic risks specific to international operations.***

In recent years, our revenues derived from sales to customers outside the U.S. have not been material. Our revenues derived from such sales can vary from quarter to quarter and from year to year. We also frequently ship products to our domestic customers' international manufacturing divisions and



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subcontractors. In the future, we may expand these international business activities. International operations are subject to many inherent risks, including:

general political, social and economic instability;

trade restrictions;

the imposition of governmental controls;

exposure to different legal standards, particularly with respect to intellectual property;

burdens of complying with a variety of foreign laws;

import and export license requirements and restrictions of the United States and any other country in which we operate;

unexpected changes in regulatory requirements;

foreign technical standards;

changes in tariffs;

difficulties in staffing and managing international operations;

difficulties in securing and servicing international customers;

difficulties in collecting receivables from foreign entities;

fluctuations in currency exchange rates and any imposition of currency exchange controls; and

potentially adverse tax consequences.

These conditions may increase our cost of doing business. Moreover, as our customers are adversely affected by these conditions, our business with them may be disrupted and our res