

Starent Networks, Corp.  
Form 10-Q  
May 08, 2009  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended March 31, 2009

or

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

For the transition period from            to

Commission File Number: 001-33511

**STARENT NETWORKS, CORP.**

(Exact name of registrant as specified in its charter)

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

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

**30 International Place**  
**Tewksbury, MA 01876**

(Address of principal executive offices) (zip code)

**(978) 851-1100**

(Registrant's telephone number, including area code)

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

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

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

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

As of May 4, 2009, there were 70,819,715 shares of the registrant's \$0.001 par value per share common stock outstanding.

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**STARENT NETWORKS, CORP.**  
**QUARTERLY REPORT ON FORM 10-Q**  
**FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2009**

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**Table of Contents****PART I. FINANCIAL INFORMATION****ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****STARENT NETWORKS, CORP.****CONDENSED CONSOLIDATED BALANCE SHEETS****(unaudited and in thousands, except share and per share data)**

	March 31, 2009	December 31, 2008
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 387,204	\$ 369,351
Accounts receivable	58,712	53,689
Inventories	48,696	48,734
Deferred tax assets, net	8,729	3,449
Prepaid expenses and other current assets	4,583	4,709
Total current assets	507,924	479,932
Property and equipment, net	32,040	29,632
Deferred tax assets, net	11,350	9,699
Other assets	8,061	8,011
Restricted cash	810	943
Total assets	\$ 560,185	\$ 528,217
<b>Liabilities and stockholders' equity</b>		
Current liabilities:		
Accounts payable	\$ 4,264	\$ 9,042
Accrued expenses and other current liabilities	10,532	8,164
Accrued payroll and related expenses	10,049	15,195
Accrued income taxes	15,420	1,945
Current portion of deferred revenue	151,734	141,726
Total current liabilities	191,999	176,072
Deferred revenue, net of current portion	9,153	10,959
Other long-term liabilities	2,878	2,985
Commitments and contingencies (Note 7)		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 5,000,000 shares authorized and no shares outstanding		
Common stock, \$0.001 par value; 250,000,000 shares authorized; 70,274,758 and 69,867,985 shares issued and outstanding at March 31, 2009 and December 31, 2008, respectively	70	70
Additional paid-in capital	376,831	371,655
Accumulated deficit	(20,746)	(33,524)
Total stockholders' equity	356,155	338,201

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Total liabilities and stockholders' equity	\$ 560,185	\$ 528,217
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The accompanying notes are an integral part of these condensed consolidated financial statements.

**Table of Contents****STARENT NETWORKS, CORP.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(unaudited and in thousands, except per share data)**

	<b>Three Months Ended March 31,</b>	
	<b>2009</b>	<b>2008</b>
<b>Revenues:</b>		
Product	\$ 63,130	\$ 48,887
Service	10,071	7,340
 Total revenues	 73,201	 56,227
<b>Cost of revenues:</b>		
Product	9,768	9,048
Service	4,546	3,910
 Total cost of revenues	 14,314	 12,958
 Gross profit	 58,887	 43,269
<b>Operating expenses:</b>		
Research and development	14,037	12,343
Sales and marketing	16,468	18,851
General and administrative	6,685	5,156
 Total operating expenses	 37,190	 36,350
 Income from operations	 21,697	 6,919
Interest income	466	2,285
Foreign currency exchange gain (loss)	(949)	900
Other income (expense), net	(37)	
 Income before income tax expense	 21,177	 10,104
Income tax expense	(8,399)	(450)
 Net income	 \$ 12,778	 \$ 9,654
 Net income per common share (Note 3):		
Basic	\$ 0.18	\$ 0.14
 Diluted	 \$ 0.17	 \$ 0.13
 Weighted-average shares outstanding used in computing net income per common share (Note 3):		
Basic	70,090	68,769

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Diluted	74,592	74,274
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The accompanying notes are an integral part of these condensed consolidated financial statements.

**Table of Contents****STARENT NETWORKS, CORP.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(unaudited and in thousands)

	<b>Three Months Ended March 31,</b>	
	<b>2009</b>	<b>2008</b>
<b>Cash flows from operating activities:</b>		
Net income	\$ 12,778	\$ 9,654
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	3,805	2,353
Share-based compensation	3,992	3,370
Loss on disposal of property and equipment	26	
Benefit from deferred income taxes, net	(6,930)	
Changes in operating assets and liabilities:		
Accounts receivable	(5,029)	(25,337)
Inventories	40	(3,784)
Prepaid expenses and other current assets	170	753
Other assets	(49)	(98)
Accounts payable	(4,761)	(154)
Accrued expenses and other liabilities	(2,190)	(4,439)
Accrued income taxes	13,359	(141)
Deferred revenue	8,046	74,805
Net cash provided by operating activities	23,257	56,982
<b>Cash flows from investing activities:</b>		
Purchases of property and equipment	(6,261)	(6,641)
Proceeds from maturities of short-term investments		7,106
Change in restricted cash	125	(45)
Net cash provided by (used in) investing activities	(6,136)	420
<b>Cash flows from financing activities:</b>		
Proceeds from exercises of stock options	1,120	1,223
Additional expenses from public offerings		(87)
Net cash provided by financing activities	1,120	1,136
Effect of exchange rate changes on cash and cash equivalents	(388)	431
Net increase in cash and cash equivalents	17,853	58,969
Cash and cash equivalents, beginning of period	369,351	223,987
Cash and cash equivalents, end of period	\$ 387,204	\$ 282,956



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

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**STARENT NETWORKS, CORP.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**1. Overview**

***Business Description***

Starent Networks, Corp. ( Starent or the Company ) was incorporated in Delaware on August 11, 2000 and is a leading provider of infrastructure hardware and software products and services that enable mobile operators to deliver multimedia services to their subscribers. The Company's products and services integrate multiple network functions and services needed for the delivery of advanced multimedia services, such as video, Internet access, voice-over-IP, e-mail, mobile TV, photo sharing and gaming.

***Basis of Presentation***

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

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

***Significant Estimates and Assumptions***

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosures of contingent assets and liabilities. Management evaluates these estimates and assumptions on an ongoing basis. Significant estimates and assumptions relied upon by management in preparing these financial statements include revenue recognition, allowances for doubtful accounts, net realizable value of inventories, expensing and capitalization of research and development costs for software, the determination of fair value of share-based compensation and the recoverability of the Company's net deferred tax assets.

Although the Company regularly assesses these estimates, actual results could differ materially from these estimates. Changes in estimates are recorded in the period in which they become known. The Company bases its estimates on historical experience and various other assumptions that it believes to be reasonable under the circumstances. Actual results could differ from management's estimates if past experience or other assumptions do not turn out to be substantially accurate.

***Reclassification***

Certain prior year amounts related to the classification of foreign currency gains or losses in the condensed consolidated statements of cash flows have been reclassified to conform to the current year presentation. These reclassifications had no impact on previously reported results of operations.

***Concentrations of Risk and Off-Balance-Sheet Risk***

The Company has no significant off-balance-sheet risk such as foreign exchange contracts, option contracts or other foreign hedging arrangements. Financial instruments that potentially subject the Company to concentrations of credit risk are principally cash equivalents, accounts receivable and inventories. The Company's cash equivalents are principally maintained with one commercial bank.

The Company had one customer for the three months ended March 31, 2009 that accounted for 75% of revenues. The Company had two customers for the three months ended March 31, 2008 that each accounted for more than 10% of revenues and in the aggregate accounted for

91% of revenues.

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At March 31, 2009, the Company had two customers that accounted for 60% of accounts receivable. At December 31, 2008, the Company had two customers that accounted for 76% of accounts receivable.

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

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

**2. Share-Based Compensation**

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

The fair value of options granted for the three months ended March 31, 2009 and 2008 was estimated at the date of grant using the following assumptions:

	Three Months Ended March 31,	
	2009	2008
Risk-free interest rates	2.14%	3.01%
Expected dividend yield	0%	0%
Expected life	6.25 years	6.25 years
Expected volatility	58%	56%

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

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

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2009</b>	<b>2008</b>
Share-based compensation included in:		
Cost of revenues	\$ 348	\$ 313
<b>Total share-based compensation included in cost of revenues</b>	<b>348</b>	<b>313</b>
Research and development	1,400	1,304
Sales and marketing	1,245	927
General and administrative	999	826
<b>Total share-based compensation included in operating expenses</b>	<b>3,644</b>	<b>3,057</b>
<b>Total share-based compensation</b>	<b>\$ 3,992</b>	