

LEAP WIRELESS INTERNATIONAL INC

Form 10-Q/A

April 20, 2006

**Table of Contents**

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**FORM 10-Q/A  
(Amendment No. 1)**

(Mark One)

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

**For the quarterly period ended June 30, 2005**

**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 0-29752**

**Leap Wireless International, Inc.  
(Exact name of registrant as specified in its charter)**

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

**33-0811062  
(I.R.S. Employer  
Identification No.)**

**10307 Pacific Center Court, San Diego, CA  
(Address of principal executive offices)**

**92121  
(Zip Code)**

**(858) 882-6000  
(Registrant's telephone number, including area code)**

**Not applicable  
(Former name, former address and former fiscal year, if changed since last reported)**

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 ninety days. Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

The number of shares of registrant's common stock outstanding on April 17, 2006 was 61,212,528.

---

**Table of Contents**

**EXPLANATORY NOTE**

The previously issued unaudited condensed consolidated financial statements of Leap Wireless International, Inc. have been amended and restated to correct errors: (i) in the calculation of the tax bases of certain wireless licenses and deferred taxes associated with tax deductible goodwill, (ii) in the accounting for the release of the valuation allowance on deferred tax assets recorded in fresh-start reporting, and (iii) based on the determination that the netting of deferred tax assets associated with wireless licenses against deferred tax liabilities associated with wireless licenses was not appropriate, as well as the resulting error in the calculation of the valuation allowance on the license-related deferred tax assets. These errors arose in connection with our implementation of fresh-start reporting on July 31, 2004. See Note 3 to our condensed consolidated financial statements included in Part I Item 1 of this report for additional information.

We have amended and restated in its entirety each item of the quarterly report on Form 10-Q for the quarter ended June 30, 2005 (the Original Form 10-Q ), filed with the Securities and Exchange Commission on August 12, 2005 (the Original Filing Date ), that required a change to reflect the restatement. These items include Part I: Item 1. Financial Statements; Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations; and Item 4. Controls and Procedures. We have supplemented Item 6 of Part II to include current certifications of our Chief Executive Officer and Chief Financial Officer pursuant to Sections 302 and 906 of the Sarbanes-Oxley Act of 2002, filed as Exhibits 31.1, 31.2 and 32 to this amendment.

This amendment contains only the sections and exhibits to the Original Form 10-Q that are being amended and restated, and those unaffected parts or exhibits are not included herein. This amendment continues to speak as of the Original Filing Date, and the Company has not updated the disclosure contained herein to reflect events that have occurred since the Original Filing Date. Accordingly, this amendment should be read in conjunction with the Company's other filings made with the Securities and Exchange Commission subsequent to the filing of the Original Form 10-Q, including the amendments to those filings, if any.

---

**LEAP WIRELESS INTERNATIONAL, INC.**

**QUARTERLY REPORT ON FORM 10-Q/A  
For the Quarter Ended June 30, 2005**

**TABLE OF CONTENTS**

	<b>Page</b>
<b><u>PART I FINANCIAL INFORMATION</u></b>	
<u>Item 1.</u> <u>Financial Statements</u>	1
<u>Item 2.</u> <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	17
<u>Item 4.</u> <u>Controls and Procedures</u>	36
<b><u>PART II OTHER INFORMATION</u></b>	
<u>Item 6.</u> <u>Exhibits</u>	40
<u>EXHIBIT 31.1</u>	
<u>EXHIBIT 31.2</u>	
<u>EXHIBIT 32</u>	

---

**Table of Contents**

**PART I**  
**FINANCIAL INFORMATION**

**Item 1. Financial Statements.**

**LEAP WIRELESS INTERNATIONAL, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(In thousands)**

	<b>Successor Company</b>	
	<b>June 30,</b>	<b>December 31,</b>
	<b>2005</b>	<b>2004</b>
	<b>(Unaudited)</b>	<b>(As Restated)</b>
	<b>(As</b>	
	<b>Restated)</b>	<b>(See Note 3)</b>
	<b>(See Note 3)</b>	
<b>Assets</b>		
Cash and cash equivalents	\$ 82,396	\$ 141,141
Short-term investments	75,258	113,083
Restricted cash, cash equivalents and short-term investments	25,737	31,427
Inventories	30,081	25,816
Other current assets	30,065	37,531
Total current assets	243,537	348,998
Property and equipment, net	534,458	575,486
Wireless licenses	766,187	652,653
Assets held for sale (Note 7)	87,961	
Goodwill	449,438	457,637
Other intangible assets, net	132,245	151,461
Deposits for wireless licenses (Note 7)	68,221	24,750
Other assets	13,416	9,902
Total assets	\$ 2,295,463	\$ 2,220,887
<b>Liabilities and Stockholders Equity</b>		
Accounts payable and accrued liabilities	\$ 79,571	\$ 91,093
Current maturities of long-term debt (Note 5)	5,000	40,373
Other current liabilities	64,791	71,770
Total current liabilities	149,362	203,236
Long-term debt (Note 5)	492,500	371,355
Other long-term liabilities	167,628	176,240
Total liabilities	809,490	750,831

Minority interest	1,000	
Commitments and contingencies (Notes 2, 5 and 8)		
Stockholders' equity:		
Preferred stock - authorized 10,000,000 shares; \$.0001 par value, no shares issued and outstanding		
Common stock - authorized 160,000,000 shares; \$.0001 par value, 60,806,423 and 60,000,000 shares issued and outstanding at June 30, 2005 and December 31, 2004, respectively	6	6
Additional paid-in capital	1,507,751	1,478,392
Unearned stock-based compensation	(22,229)	
Retained earnings (accumulated deficit)	228	(8,391)
Accumulated other comprehensive income (loss)	(783)	49
Total stockholders' equity	1,484,973	1,470,056
Total liabilities and stockholders' equity	\$ 2,295,463	\$ 2,220,887

See accompanying notes to condensed consolidated financial statements.

Table of Contents**LEAP WIRELESS INTERNATIONAL, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND  
COMPREHENSIVE INCOME (LOSS)****(UNAUDITED)****(In thousands, except per share data)**

	<b>Successor Company</b>	<b>Predecessor Company</b>	<b>Successor Company</b>	<b>Predecessor Company</b>
	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2005</b>	<b>2004</b>	<b>2005</b>	<b>2004</b>
	<b>(As Restated)</b>		<b>(As Restated)</b>	
	<b>(See Note 3)</b>		<b>(See Note 3)</b>	
Revenues:				
Service revenues	\$ 189,704	\$ 172,025	\$ 375,685	\$ 341,076
Equipment revenues	37,125	33,676	79,514	71,447
Total revenues	226,829	205,701	455,199	412,523
Operating expenses:				
Cost of service (exclusive of items shown separately below)	(49,608)	(47,827)	(99,805)	(95,827)
Cost of equipment	(42,799)	(40,635)	(91,977)	(84,390)
Selling and marketing	(24,810)	(21,939)	(47,805)	(45,192)
General and administrative	(42,423)	(33,922)	(78,458)	(72,532)
Depreciation and amortization	(47,281)	(76,386)	(95,385)	(151,847)
Impairment of indefinite-lived intangible assets	(11,354)		(11,354)	
Total operating expenses	(218,275)	(220,709)	(424,784)	(449,788)
Operating income (loss)	8,554	(15,008)	30,415	(37,265)
Interest income	1,176		3,079	
Interest expense (contractual interest expense was \$67.2 million and \$133.6 million for the three and six months ended June 30, 2004, respectively)	(7,566)	(1,908)	(16,689)	(3,731)
Other income (expense), net	(39)	(615)	(1,325)	(596)
Income (loss) before reorganization items and income taxes	2,125	(17,531)	15,480	(41,592)
Reorganization items, net		1,313		(712)
Income (loss) before income taxes	2,125	(16,218)	15,480	(42,304)
Income taxes	(1,022)	(1,927)	(6,861)	(3,871)



Edgar Filing: LEAP WIRELESS INTERNATIONAL INC - Form 10-Q/A

Net income (loss)	1,103	(18,145)	8,619	(46,175)
Other comprehensive income (loss):				
Unrealized holding gains (losses) on investments, net	8	(204)	(38)	61
Unrealized loss on derivative instrument	(794)		(794)	
Comprehensive income (loss)	\$ 317	\$ (18,349)	\$ 7,787	\$ (46,114)
Net income (loss) per share:				
Basic	\$ 0.02	\$ (0.31)	\$ 0.14	\$ (.79)
Diluted	\$ 0.02	\$ (0.31)	\$ 0.14	\$ (.79)
Shares used in per share calculations:				
Basic	60,030	58,622	60,015	58,621
Diluted	60,242	58,622	60,234	58,621

See accompanying notes to condensed consolidated financial statements.

**Table of Contents****LEAP WIRELESS INTERNATIONAL, INC.**

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**  
**(In thousands)**

	<b>Successor Company Six Months Ended June 30, 2005</b>	<b>Predecessor Company Six Months Ended June 30, 2004</b>
Operating activities:		
Net cash provided by operating activities	\$ 108,536	\$ 89,935
Investing activities:		
Purchase of property and equipment	(45,498)	(30,418)
Purchase of and deposits for wireless licenses	(239,168)	
Purchase of investments	(103,057)	(70,769)
Sale and maturity of investments	142,296	51,793
Restricted cash, cash equivalents and short-term investments, net	326	13,970
Net cash used in investing activities	(245,101)	(35,424)
Financing activities:		
Proceeds from long-term debt	500,000	
Repayment of long-term debt	(415,229)	
Payment of debt issuance costs	(6,951)	
Net cash provided by financing activities	77,820	
Net increase (decrease) in cash and cash equivalents	(58,745)	54,511
Cash and cash equivalents at beginning of period	141,141	84,070
Cash and cash equivalents at end of period	\$ 82,396	\$ 138,581
Supplementary disclosure of cash flow information:		
Cash paid for interest	\$ 35,072	\$
Cash paid for income taxes	\$ 228	\$ 76
Supplementary disclosure of non-cash investing and financing activities:		
Issuance of restricted stock awards under stock compensation plan	\$ 22,489	\$

See accompanying notes to condensed consolidated financial statements.

**Table of Contents**

**LEAP WIRELESS INTERNATIONAL, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**Note 1. The Company and Nature of Business**

Leap Wireless International, Inc. ( Leap ), a Delaware corporation, together with its wholly owned subsidiaries, is a wireless communications carrier that offers digital wireless service in the United States of America under the brand Cricket®. Leap conducts operations through its subsidiaries and has no independent operations or sources of operating revenue other than through dividends, if any, from its operating subsidiaries. Cricket service is operated by Leap's wholly owned subsidiary, Cricket Communications, Inc. ( Cricket ). Leap, Cricket and their subsidiaries are collectively referred to herein as the Company. As of June 30, 2005, the Company provided wireless service in 20 states covering a total potential customer base of 26.8 million. As of August 11, 2005, the Company owned wireless licenses covering a total potential customer base of 60.2 million.

In November 2004, the Company acquired a 75% non-controlling membership interest in Alaska Native Broadband 1, LLC ( ANB 1 ) for the purpose of participating in the Federal Communication Commission's ( FCC's ) Auction #58 (Note 7) through ANB 1's wholly owned subsidiary, Alaska Native Broadband 1 License, LLC ( ANB 1 License ). The Company consolidates its investment in ANB 1.

**Note 2. Reorganization and Fresh-Start Reporting**

On April 13, 2003 (the Petition Date ), Leap, Cricket and substantially all of their subsidiaries filed voluntary petitions for relief under Chapter 11 of the United States Bankruptcy Code ( Chapter 11 ) in the United States Bankruptcy Court for the Southern District of California (the Bankruptcy Court ). On October 22, 2003, the Bankruptcy Court confirmed the Fifth Amended Joint Plan of Reorganization (the Plan of Reorganization ) of Leap, Cricket and their debtor subsidiaries. All material conditions to the effectiveness of the Plan of Reorganization were resolved on August 5, 2004, and on August 16, 2004 (the Effective Date ), the Plan of Reorganization became effective and the Company emerged from Chapter 11 bankruptcy. On that date, a new Board of Directors of Leap was appointed, Leap's previously existing stock, options and warrants were cancelled, and Leap issued 60 million shares of new Leap common stock for distribution to two classes of creditors. The Plan of Reorganization implemented a comprehensive financial reorganization that significantly reduced the Company's outstanding indebtedness. On the Effective Date of the Plan of Reorganization, the Company's long-term debt was reduced from a book value of more than \$2.4 billion to debt with an estimated fair value of \$412.8 million, consisting of new Cricket 13% senior secured pay-in-kind notes due 2011 with a face value of \$350 million and an estimated fair value of \$372.8 million, issued on the Effective Date, and approximately \$40 million of remaining indebtedness to the FCC (net of the repayment of \$45 million of principal and accrued interest to the FCC on the Effective Date). A summary of the material actions that occurred during the bankruptcy process and as of the Effective Date of the Plan of Reorganization is included in the Company's Annual Report on Form 10-K for the year ended December 31, 2004 as originally filed with the Securities and Exchange Commission ( SEC ) on May 16, 2005 and subsequently restated as of and for the five months ended December 31, 2004 in the Company's Annual Report on Form 10-K for the year ended December 31, 2005 filed with the SEC on March 27, 2006.

As of the Petition Date and through the adoption of fresh-start reporting on July 31, 2004, the Company implemented American Institute of Certified Public Accountants' Statement of Position ( SOP ) 90-7, Financial Reporting by Entities in Reorganization under the Bankruptcy Code. In accordance with SOP 90-7, the Company separately reported certain expenses, realized gains and losses and provisions for losses related to the Chapter 11 filings as reorganization items. In addition, commencing as of the Petition Date and continuing while in bankruptcy, the Company ceased accruing interest and amortizing debt discounts and debt issuance costs for its pre-petition debt that was subject to compromise,

which included debt with a book value totaling approximately \$2.4 billion as of the Petition Date.

The Company adopted the fresh-start reporting provisions of SOP 90-7 as of July 31, 2004. Under fresh-start reporting, a new entity is deemed to be created for financial reporting purposes. Therefore, as used in these condensed consolidated financial statements, the Company is referred to as the Predecessor Company for periods on or prior to July 31, 2004 and is referred to as the Successor Company for periods after July 31, 2004, after

## **Table of Contents**

giving effect to the implementation of fresh-start reporting. The financial statements of the Successor Company are not comparable in many respects to the financial statements of the Predecessor Company because of the effects of the consummation of the Plan of Reorganization as well as the adjustments for fresh-start reporting.

Under SOP 90-7, reorganization value represents the fair value of the entity before considering liabilities and approximates the amount a willing buyer would pay for the assets of the entity immediately after the reorganization. In implementing fresh-start reporting, the Company allocated its reorganization value to the fair value of its assets in conformity with procedures specified by Statement of Financial Accounting Standards ( SFAS ) No. 141, Business Combinations, and stated its liabilities, other than deferred taxes, at the present value of amounts expected to be paid. The amount remaining after allocation of the reorganization value to the fair value of the Company's identified tangible and intangible assets is reflected as goodwill, which is subject to periodic evaluation for impairment. In addition, under fresh-start reporting, the Company's accumulated deficit was eliminated and new equity was issued according to the Plan of Reorganization. The determination of reorganization value and the adjustments to the Predecessor Company's consolidated balance sheet at July 31, 2004 resulting from the application of fresh-start reporting are summarized in the Company's Annual Report on Form 10-K for the year ended December 31, 2004, as originally filed, and subsequently restated as of and for the five months ended December 31, 2004 in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

The fair values of goodwill and intangible assets reported in the Successor Company's consolidated balance sheet were estimated based upon the Company's estimates of future cash flows and other factors including discount rates. If these estimates or the assumptions underlying these estimates change in the future, the Company may be required to record impairment charges. In addition, a permanent and sustained decline in the market value of the Company's outstanding common stock could also result in the requirement to recognize impairment charges in future periods.

### **Note 3. Basis of Presentation and Significant Accounting Policies**

#### ***Interim Financial Statements***

The accompanying interim condensed consolidated financial statements have been prepared by the Company without audit, in accordance with the instructions to Form 10-Q and, therefore, do not include all information and footnotes required by accounting principles generally accepted in the United States of America for a complete set of financial statements. These condensed consolidated financial statements and notes thereto should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005. In the opinion of management, the unaudited financial information for the interim periods presented reflects all adjustments necessary for a fair statement of the results for the periods presented, with such adjustments consisting only of normal recurring adjustments. Operating results for interim periods are not necessarily indicative of operating results for an entire fiscal year.

#### ***Principles of Consolidation***

The condensed consolidated financial statements include the accounts of Leap and its wholly owned subsidiaries as well as the accounts of ANB 1 and its wholly owned subsidiary ANB 1 License. The Company consolidates its interest in ANB 1 in accordance with FASB Interpretation No. 46-R, Consolidation of Variable Interest Entities, because the Company will absorb a majority of ANB 1's expected losses. The Company records 100% of the losses of ANB 1 to the extent of its investment in and loans to ANB 1 and ANB 1 License, since the Company expects to be a primary financing source for ANB 1 License. All significant intercompany accounts and transactions have been eliminated in the condensed consolidated financial statements.

#### ***Restatement of Previously Reported Unaudited Interim Consolidated Financial Information***

The Company has restated its consolidated financial information for the three and six months ended June 30, 2005. The determination to restate the interim financial information was made by the Company's Audit Committee

**Table of Contents**

upon the recommendation of management as a result of the identification of the following errors related to the accounting for deferred income taxes:

The tax bases of several wireless licenses were inaccurately compiled by the Company during its adoption of fresh-start reporting as of July 31, 2004, which had the effect in the aggregate of understating wireless license deferred tax liabilities and overstating wireless license deferred tax assets. In addition, the misstatement of the tax bases of operating licenses with deferred tax liabilities had the net effect of overstating deferred income tax expense in the periods subsequent to July 31, 2004.

The Company incorrectly accounted for tax-deductible goodwill upon the adoption of fresh-start reporting as of July 31, 2004, which had the effect of understating deferred tax liabilities and understating deferred income tax expense in the periods subsequent to July 31, 2004.

In connection with the adoption of fresh-start reporting as of July 31, 2004, the Company adopted the practice of netting deferred tax assets associated with wireless licenses against deferred tax liabilities associated with wireless licenses and, as a result, did not record valuation allowances on its wireless license deferred tax assets. However, because the Company's wireless licenses have indefinite useful lives, the deferred tax liabilities related to the licenses will not reverse until some indefinite future period when a license is either sold or written down due to impairment. As a result, the wireless license deferred tax liabilities may not be used to support the realization of the wireless license deferred tax assets and, thus, may not be used to offset the wireless license deferred tax assets. Accordingly, the Company has now determined that the netting of deferred tax assets associated with wireless licenses against deferred tax liabilities associated with wireless licenses was not appropriate. Instead, valuation allowances should have been recorded on the wireless license deferred tax assets.

The Company incorrectly accounted for the release of valuation allowances on deferred tax assets recorded in fresh-start reporting. The Company previously concluded that there had been no release of fresh-start valuation allowances during the three and six months ended June 30, 2005. However, the reversal of deferred tax assets recorded in fresh-start reporting resulted in a release of the related fresh-start valuation allowances. As restated, the release of fresh-start valuation allowances is recorded as a reduction of goodwill and resulted in deferred income tax expense for the three and six months ended June 30, 2005.

The following tables present the effects of the restatements on the Company's previously issued consolidated financial statements and interim consolidated financial information (in thousands, except per share data):

	<b>As of December 31, 2004</b>		
	<b>Previously Reported</b>	<b>Adjustment</b>	<b>As Restated</b>
<b>Consolidated Balance Sheet Data:</b>			
Other current assets	\$ 35,144	\$ 2,387	\$ 37,531
Goodwill	\$ 329,619	\$ 128,018	\$ 457,637
Other current liabilities	\$ 71,965	\$ (195)	\$ 71,770
Other long-term liabilities	\$ 45,846	\$ 130,394	\$ 176,240
Accumulated deficit	\$ (8,629)	\$ 238	\$ (8,391)
Accumulated other comprehensive income	\$ 81	\$ (32)	\$ 49





**Table of Contents**

	<b>As of and for the Three Months Ended June 30, 2005</b>		
	<b>Previously Reported (Unaudited)</b>	<b>Adjustment (Unaudited)</b>	<b>As Restated (Unaudited)</b>
<b>Consolidated Balance Sheet Data:</b>			
Other current assets	\$ 27,678	\$ 2,387	\$ 30,065
Goodwill	\$ 329,619	\$ 119,819	\$ 449,438
Other current liabilities	\$ 65,272	\$ (481)	\$ 64,791
Other long-term liabilities	\$ 39,128	\$ 128,500	\$ 167,628
Retained earnings	\$ 6,546	\$ (6,318)	\$ 228
Accumulated other comprehensive loss	\$ (1,288)	\$ 505	\$ (783)
<b>Consolidated Statement of Operations Data:</b>			
Income tax expense (benefit)	\$ (404)	\$ 1,426	\$ 1,022
Net income	\$ 2,529	\$ (1,426)	\$ 1,103
Comprehensive income	\$ 1,235	\$ (918)	\$ 317
Basic and diluted net income per share	\$ 0.04	\$ (0.02)	\$ 0.02

	<b>For the Six Months Ended June 30, 2005</b>		
	<b>Previously Reported (Unaudited)</b>	<b>Adjustment (Unaudited)</b>	<b>As Restated (Unaudited)</b>
<b>Consolidated Statement of Operations Data:</b>			
Income tax expense	\$ 305	\$ 6,556	\$ 6,861
Net income	\$ 15,175	\$ (6,556)	\$ 8,619
Comprehensive income	\$ 13,887	\$ (6,100)	\$ 7,787
Basic and diluted net income per share	\$ 0.25	\$ (0.11)	\$ 0.14

**Reorganization Items**

Reorganization items represent amounts incurred by the Predecessor Company as a direct result of the Chapter 11 filings and are presented separately in the Predecessor Company's condensed consolidated statements of operations. For the three and six months ended June 30, 2004, reorganization items consisted primarily of professional fees for legal, financial advisory and valuation services directly associated with the Company's Chapter 11 filings and reorganization process, partially offset by income from the settlement of certain pre-petition liabilities and interest income earned while the Company was in bankruptcy.

**Restricted Cash, Cash Equivalents and Short-Term Investments**

Restricted cash, cash equivalents and short-term investments include funds set aside or pledged to satisfy remaining administrative claims and priority claims against Leap and Cricket following their emergence from bankruptcy, and cash restricted for other purposes.

**Revenues and Cost of Revenues**

Cricket's business revenues arise from the sale of wireless services, handsets and accessories. Wireless services are generally provided on a month-to-month basis. Amounts received in advance for wireless services from customers who pay in advance are initially recorded as deferred revenues and are recognized as service revenue as services are rendered. Service revenues for customers who pay in arrears are recognized only after the service has been rendered and payment has been received. This is because the Company does not require any of its customers to sign long-term service commitments or submit to a credit check, and therefore some of its customers may be more likely to terminate service for inability to pay than the customers of other wireless providers. The Company also charges customers for service plan changes, activation fees and other service fees. Revenues from service plan

## **Table of Contents**

change fees are deferred and recorded to revenue over the estimated customer relationship period, and other service fees are recognized when received. Activation fees are allocated to the other elements of the multiple element arrangement (including service and equipment) on a relative fair value basis. Because the fair values of the Company's handsets are higher than the total consideration received for the handsets and activation fees combined, the Company allocates the activation fees entirely to equipment revenues and recognizes the activation fees when received. Activation fees included in equipment revenues during the three months ended June 30, 2005 and 2004 totaled \$4.3 million and \$4.4 million, respectively. Activation fees included in equipment revenues during the six months ended June 30, 2005 and 2004 totaled \$8.9 million and \$10.2 million, respectively. Direct costs associated with customer activations are expensed as incurred. Cost of service generally includes direct costs and related overhead, excluding depreciation and amortization, of operating the Company's networks.

Equipment revenues arise from the sale of handsets and accessories, and activation fees as described above. Revenues and related costs from the sale of handsets are recognized when service is activated by customers. Revenues and related costs from the sale of accessories are recognized at the point of sale. The costs of handsets and accessories sold are recorded in cost of equipment. Amounts due from third-party dealers and distributors for handsets are recorded as deferred revenue upon shipment of the handsets by the Company to such dealers and distributors and are recognized as equipment revenues when service is activated by customers. Handsets sold by third-party dealers and distributors are recorded as inventory until they are sold to and activated by customers. Sales incentives offered without charge to customers and volume-based incentives paid to the Company's third-party dealers and distributors are recognized as a reduction of revenue and as a liability when the related service or equipment revenue is recognized. Customers have limited rights to return handsets and accessories based on time and/or usage. Returns of handsets and accessories have historically been insignificant.

### ***Property and Equipment***

Property and equipment are initially recorded at cost. Additions and improvements, including interest and certain labor costs incurred during the construction period, are capitalized, while expenditures that do not enhance the asset or extend its useful life are charged to operating expenses as incurred. Depreciation is applied using the straight-line method over the estimated useful lives of the assets once the assets are placed in service.

Upon emergence from Chapter 11 and adoption of fresh-start reporting, the Company re-assessed the carrying values and useful lives of its property and equipment. As a result of this re-assessment, which included a review of the Company's historical usage of and expected future service from existing property and equipment, and a review of industry averages for similar property and equipment, the Company changed the depreciable lives for certain network equipment assets. These network equipment assets that were previously depreciated over periods ranging from two to five years are now depreciated over periods ranging from three to fifteen years. As a result of this change, depreciation expense was reduced and net income increased by approximately \$29.7 million, or \$0.49 per diluted share, for the three months ended June 30, 2005 and by approximately \$60.5 million, or \$1.00 per diluted share, for the six months ended June 30, 2005, compared to what they would have been if the useful lives had not been revised. The estimated useful lives for the Company's other property and equipment, which have remained unchanged, are three to five years for computer hardware and software, and three to seven years for furniture, fixtures and retail and office equipment. Property and equipment to be disposed of by sale is not depreciated, and is carried at the lower of carrying value or fair value less costs to sell.

The Company's network construction expenditures are recorded as construction-in-progress until the network or assets are placed in service, at which time the assets are transferred to the appropriate property and equipment category. As a component of construction-in-progress, the Company capitalizes interest and salaries and related costs of engineering and technical operations employees, to the extent time and expense are contributed to the construction effort, during the construction period.

At June 30, 2005, equipment with a net book value in the amount of \$15.2 million was classified in assets held for sale (see Note 7). At December 31, 2004, there was no equipment to be disposed of by sale.

**Table of Contents**

***Impairment of Long-Lived Assets***

In accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, the Company assesses potential impairments to its long-lived assets, including property and equipment and certain intangible assets, when there is evidence that events or changes in circumstances indicate that the carrying value may not be recoverable. An impairment loss may be required to be recognized when the undiscounted cash flows expected to be generated by a long-lived asset (or group of such assets) is less than its carrying value. Any required impairment loss would be measured as the amount by which the asset's carrying value exceeds its fair value and would be recorded as a reduction in the carrying value of the related asset and charged to results of operations.

***Wireless Licenses***

Wireless licenses are initially recorded at cost. The Company has determined that its wireless licenses meet the definition of indefinite-lived intangible assets under SFAS No. 142, Goodwill and Other Intangible Assets. Wireless licenses to be disposed of by sale are carried at the lower of carrying value or fair value less costs to sell. At June 30, 2005, wireless licenses with a carrying value of \$70.8 million were classified in assets held for sale (see Note 7). At December 31, 2004, wireless licenses to be disposed of by sale were not significant. In connection with the adoption of fresh-start reporting, the Company increased the carrying value of its wireless licenses to their estimated fair market values.

***Goodwill and Other Intangible Assets***

Goodwill represents the excess of reorganization value over the fair value of identified tangible and intangible assets recorded in connection with fresh-start reporting. Other intangible assets were recorded upon adoption of fresh-start reporting and consist of customer relationships and trademarks, which are being amortized on a straight-line basis over their estimated useful lives of four and fourteen years, respectively. At June 30, 2005, intangible assets with a carrying value of \$1.9 million were classified in assets held for sale (see Note 7). At December 31, 2004, there were no intangible assets to be disposed of by sale.

***Impairment of Indefinite-lived Intangible Assets***

In accordance with SFAS No. 142, the Company assesses potential impairments to its indefinite-lived intangible assets, consisting of goodwill and wireless licenses, annually and when there is evidence that events or changes in circumstances indicate that an impairment condition may exist. The Successor Company conducts its annual test for impairment during the third quarter of each year. An impairment loss is recognized when the fair value of the asset is less than its carrying value, and would be measured as the amount by which the asset's carrying value exceeds its fair value. Any required impairment loss would be recorded as a reduction in the carrying value of the related asset and charged to results of operations. During the three and six months ended June 30, 2005, the Company recorded impairment charges of \$11.4 million to reduce the carrying value of certain non-operating wireless licenses to their estimated fair values (see Note 7).

***Basic and Diluted Net Income (Loss) Per Share***

Basic earnings per share is calculated by dividing net income (loss) by the weighted average number of common shares outstanding during the reporting period. Diluted earnings per share reflect the potential dilutive effect of additional common shares that are issuable upon exercise of outstanding stock options, restricted stock awards, deferred stock units and warrants calculated using the treasury stock method.



**Table of Contents**

A reconciliation of weighted average shares outstanding used in calculating basic and diluted net income (loss) per share for the three and six months ended June 30, 2005 and 2004 is as follows (unaudited) (in thousands):

	<b>Successor Company Three Months Ended June 30, 2005</b>	<b>Predecessor Company Three Months Ended June 30, 2004</b>	<b>Successor Company Six Months Ended June 30, 2005</b>	<b>Predecessor Company Six Months Ended June 30, 2004</b>
Weighted average shares outstanding basic earnings per share	60,030	58,622	60,015	58,621
Effect of dilutive securities:				
Restricted stock awards	1			
Warrants to MCG	211		219	
Adjusted weighted average shares outstanding diluted earnings per share	60,242	58,622	60,234	58,621

The number of shares not included in the computation of diluted net income (loss) per share because their effect would have been antidilutive totaled 0.9 million and 0.8 million for the three and six months ended June 30, 2005, respectively, and 11.8 million for both the three and six months ended June 30, 2004.

***Stock-based Compensation***

The Company measures compensation expense for its employee and director stock-based compensation plans using the intrinsic value method. All outstanding stock options of the Predecessor Company were cancelled upon emergence from bankruptcy in accordance with the Plan of Reorganization. The Board of Directors of the Company adopted the Leap Wireless International, Inc. 2004 Stock Option, Restricted Stock and Deferred Stock Unit Plan (the 2004 Plan) on December 30, 2004. A total of 4,800,000 shares of Leap common stock are reserved for issuance under the 2004 Plan. During the three months ended June 30, 2005, the Company granted a total of 566,463 non-qualified stock options, 806,423 shares of restricted common stock and 246,484 deferred stock units to directors, executive officers and other employees of the Company. During the three months ended March 31, 2005, the Company granted a total of 839,658 non-qualified stock options to directors, executive officers and other employees of the Company. There were no stock options, restricted stock shares or deferred stock units issued during the three or six months ended June 30, 2004.

The non-qualified stock options were granted with an exercise price equal to the market price of the common stock on the date of grant. The restricted shares of common stock were granted with an exercise price of \$0.0001 per share, and the weighted average grant date market price of the restricted common stock was \$27.89 per share. The stock options and restricted common stock vest in full three or five years from the grant date with no interim time-based vesting, but with provisions for annual accelerated performance-based vesting of a portion of the awards if the Company achieves specified performance conditions. The deferred stock units were immediately vested upon grant and allow the holders to purchase common stock at an exercise price of \$0.0001 per share in a 30-day period commencing on the earlier of August 15, 2005, the date immediately prior to a change in control (as defined in the 2004 Plan), or the date the holder's employment is terminated. The weighted average grant date market price of the deferred stock units was \$27.87 per share.

The Company recorded \$7.1 million in stock-based compensation expense for the three and six months ended June 30, 2005 resulting from the grant of the restricted common stock and deferred stock units. The total intrinsic value of the deferred stock units of \$6.9 million was recorded as stock-based compensation expense during the three and six months ended June 30, 2005 because the deferred stock units were immediately vested upon grant. The total intrinsic value of the restricted stock awards as of the measurement date of \$22.5 million was recorded as unearned compensation, which is included in stockholder's equity in the unaudited condensed consolidated balance sheet as of June 30, 2005. The unearned compensation is amortized on a straight-line basis over the maximum vesting period of the awards of either three or five years. For the three and six months ended June 30, 2005, \$0.2 million was recorded in stock-based compensation expense for the amortization of the unearned compensation.



**Table of Contents**

The following table shows the amount of stock-based compensation expense included in operating expenses (allocated to the appropriate line item based on employee classification) in the condensed consolidated statements of operations for the three and six months ended June 30, 2005:

	<b>Three and Six Months Ended June 30, 2005</b>
Stock-based compensation expense included in:	
Cost of service	\$ 797
Selling and marketing expenses	693
General and administrative expenses	5,639
<b>Total stock-based compensation expense</b>	<b>\$ 7,129</b>

The following table shows the effects on net income (loss) and net income (loss) per share if the Company had applied the fair value provisions of SFAS No. 123, Accounting for Stock-Based Compensation in measuring compensation expense for its stock-based compensation plans (unaudited) (in thousands, except per share data):

	<b>Successor Company Three Months Ended June 30, 2005 (As Restated)</b>	<b>Predecessor Company Three Months Ended June 30, 2004</b>	<b>Successor Company Six Months Ended June 30, 2005 (As Restated)</b>	<b>Predecessor Company Six Months Ended June 30, 2004</b>
As reported net income (loss)	\$ 1,103	\$ (18,145)	\$ 8,619	\$ (46,175)
Add back stock-based compensation (benefit) expense included in net income (loss)	7,129	(202)	7,129	(856)
Less net pro forma compensation (expense) benefit	(8,514)	(1,803)	(10,040)	4,874
<b>Pro forma net income (loss)</b>	<b>\$ (282)</b>	<b>\$ (20,150)</b>	<b>\$ 5,708</b>	<b>\$ (42,157)</b>
Basic net income (loss) per share:				
As reported	\$ 0.02	\$ (0.31)	\$ 0.14	\$ (0.79)
Pro forma	\$ (0.00)	\$ (0.34)	\$ 0.10	\$ (0.72)
Diluted net income (loss) per share:				
As reported	\$ 0.02	\$ (0.31)	\$ 0.14	\$ (0.79)
Pro forma	\$ (0.00)	\$ (0.34)	\$ 0.09	\$ (0.72)

Edgar Filing: LEAP WIRELESS INTERNATIONAL INC - Form 10-Q/A

The weighted average grant date fair value per share of the stock options granted during the three and six months ended June 30, 2005 was \$20.04 and \$19.25, respectively, which was estimated using the Black-Scholes option pricing model and the following weighted average assumptions:

	<b>Three Months Ended June 30, 2005</b>	<b>Six Months Ended June 30, 2005</b>
Risk free interest rate	3.65%	3.54%
Expected dividend yield		
Expected volatility	87%	87%
Expected life (in years)	5.8	5.5

***Reclassifications***

Certain prior period amounts have been reclassified to conform to the current period presentation.

**Table of Contents****Note 4. Supplementary Balance Sheet Information (in thousands):**

	<b>Successor Company</b>	
	<b>June 30, 2005</b>	<b>December 31, 2004</b>
	<b>(Unaudited)</b>	<b>(As Restated)</b>
	<b>(As Restated)</b>	
Property and equipment, net:		
Network equipment	\$ 612,442	\$ 599,598
Computer equipment and other	30,022	26,285
Construction-in-progress	28,705	10,517
	671,169	636,400
Accumulated depreciation	(136,711)	(60,914)
	\$ 534,458	\$ 575,486
Accounts payable and accrued liabilities:		
Trade accounts payable	\$ 20,797	\$ 35,184
Accrued payroll and related benefits	13,573	13,579
Other accrued liabilities	45,201	42,330
	\$ 79,571	\$ 91,093
Other current liabilities:		
Accrued taxes	\$ 38,245	\$ 49,665
Deferred revenue	21,323	18,145
Accrued interest		1,025
Other	5,223	2,935
	\$ 64,791	\$ 71,770
Other long-term liabilities:		
Deferred tax liabilities	\$ 143,781	\$ 145,673
Other	23,847	30,567
	\$ 167,628	\$ 176,240

**Note 5. Debt*****Credit Agreement***

On January 10, 2005, Cricket entered into a senior secured credit agreement (the *Credit Agreement*) with a syndicate of lenders and Bank of America, N.A. (as administrative agent and letter of credit issuer).

The new facilities under the Credit Agreement consist of a six-year \$500 million term loan, which was fully drawn at closing, and an undrawn five-year \$110 million revolving credit facility. Under the Credit Agreement, the term loan bears interest at the London Interbank Offered Rate (LIBOR) plus 2.5 percent, with interest periods of one, two, three or six months, or bank base rate plus 1.5 percent, as selected by Cricket. Outstanding borrowings under the term loan must be repaid in 20 quarterly payments of \$1.25 million each, commencing March 31, 2005, followed by four quarterly payments of \$118.75 million each, commencing March 31, 2010. The maturity date for outstanding borrowings under the revolving credit facility is January 10, 2010. The commitment of the lenders under the revolving credit facility may be reduced in the event mandatory prepayments are required under the Credit Agreement and by one-twelfth of the original aggregate revolving credit commitment on January 1, 2008 and by one-sixth of the original aggregate revolving credit commitment on January 1, 2009 (each such amount to be net of all prior reductions) based on certain leverage ratios and other tests. The commitment fee on the revolving credit facility is payable quarterly at a rate of 1.0 percent per annum when the utilization of the facility (as specified in the Credit Agreement) is less than 50 percent and at 0.75 percent per annum when the utilization exceeds 50 percent.

**Table of Contents**

Borrowings under the revolving credit facility would currently accrue interest at LIBOR plus 2.5 percent, with interest periods of one, two, three or six months, or bank base rate plus 1.5 percent, as selected by Cricket, with the rate subject to adjustment based on the Company's leverage ratio. The new credit facilities are guaranteed by Leap and all of its direct and indirect domestic subsidiaries (other than Cricket, which is the primary obligor, ANB 1 and ANB 1 License) and are secured by all present and future personal property and owned real property of Leap, Cricket and such direct and indirect domestic subsidiaries.

A portion of the proceeds from the term loan borrowing was used to redeem Cricket's 13% senior secured pay-in-kind notes, to pay approximately \$43 million of call premium and accrued interest on such notes, to repay approximately \$41 million in principal amount of debt and accrued interest owed to the FCC, and to pay transaction fees and expenses. The remaining proceeds from the term loan borrowing of approximately \$60 million are being used for general corporate purposes.

Under the Credit Agreement, the Company is subject to certain limitations, including limitations on its ability to: incur additional debt or sell assets, with restrictions on the use of proceeds; make certain investments and acquisitions; grant liens; and pay dividends and make certain other restricted payments. In addition, the Company will be required to pay down the facilities under certain circumstances if it issues debt or equity, sells assets or property, receives certain extraordinary receipts or generates excess cash flow (as defined in the Credit Agreement). The Company is also subject to financial covenants which include a minimum interest coverage ratio, a maximum total leverage ratio, a maximum senior secured leverage ratio and a minimum fixed charge coverage ratio.

Affiliates of Highland Capital Management, L.P. (a beneficial shareholder of Leap and an affiliate of James D. Dondero, a director of Leap) participated in the syndication of the Company's new Credit Agreement in the following initial amounts: \$100 million of the \$500 million term loan and \$30 million of the \$110 million revolving credit facility.

At June 30, 2005, the effective interest rate on the \$500 million term loan was 6.4%, including the effect of interest rate swaps, and the outstanding indebtedness was \$497.5 million. The terms of the Credit Agreement require the Company to enter into interest rate hedging agreements in an amount equal to at least 50% of its outstanding indebtedness. In accordance with this requirement, in April 2005 the Company entered into interest rate swap agreements with respect to \$250 million of its debt. These swap agreements effectively fix the interest rate on \$250 million of the outstanding indebtedness at 6.7% through June 2007. The \$1.3 million fair value of the swap agreements at June 30, 2005 was recorded as a liability in the condensed consolidated balance sheet.

On July 22, 2005, the Company amended the Credit Agreement to increase the six-year \$500 million term loan by \$100 million. The interest and related terms are substantially the same as the original term loan agreement. Outstanding borrowings under the incremental term loan must be repaid in 18 quarterly payments of approximately \$278,000 each, commencing September 30, 2005, followed by four quarterly payments of \$23.75 million each, commencing March 31, 2010. The Company also amended the terms of the facility to accommodate the planned expansion of the Company's business including: increasing certain leverage ratios and permitting the Company to invest up to \$325 million in ANB 1 and ANB 1 License and up to \$60 million in other joint ventures. The amendments also increased the amount of permitted purchase money security interests and capitalized leases and also allow the Company to provide limited guarantees for the benefit of ANB 1 License and other joint ventures.

Affiliates of Highland Capital Management, L.P. (a beneficial shareholder of Leap and an affiliate of James D. Dondero, a director of Leap) participated in the syndication of the additional term facility in the amount of \$9 million.

In July 2005, the Company entered into another interest rate swap agreement with respect to a further \$105 million of its outstanding indebtedness. This swap agreement effectively fixes the interest rate on \$105 million of the outstanding

indebtedness at 6.8% through June 2009.

***Senior Secured Pay-in-Kind Notes Issued Under Plan of Reorganization***

On the Effective Date of the Plan of Reorganization, Cricket issued new 13% senior secured pay-in-kind notes due 2011 with a face value of \$350 million and an estimated fair value of \$372.8 million. As of December 31, 2004, the carrying value of the notes was \$371.4 million. A portion of the proceeds from the term loan facility under the

**Table of Contents**

new Credit Agreement was used to redeem these notes. Upon repayment of these notes, the Company recorded a loss from debt extinguishment of approximately \$1.7 million which was included in other income (expense) in the condensed consolidated statement of operations for the six months ended June 30, 2005.

***US Government Financing***

The balance in current maturities of long-term debt at December 31, 2004 consisted entirely of debt obligations to the FCC incurred as part of the purchase price for wireless licenses. At July 31, 2004, the remaining principal of the FCC debt was revalued in connection with the Company's adoption of fresh-start reporting. The carrying value of this debt at December 31, 2004 was \$40.4 million. The balance was repaid in full in January 2005 with a portion of the term loan borrowing as noted above. Upon repayment of this debt, the Company recorded a gain from debt extinguishment of approximately \$0.4 million which was included in other income (expense) in the condensed consolidated statement of operations for the six months ended June 30, 2005.

**Note 6. Income Taxes**

The Company estimates income taxes in each of the jurisdictions in which it operates. This process involves estimating the actual current tax liability together with assessing temporary differences resulting from differing treatments of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities. Deferred tax assets are also established for the expected future tax benefits to be derived from tax loss and tax credit carryforwards. The Company must then assess the likelihood that its deferred tax assets will be recovered from future taxable income. To the extent that the Company believes that recovery is not likely, it must establish a valuation allowance. Significant management judgment is required in determining the provision for income taxes, deferred tax assets and liabilities and any valuation allowance recorded against net deferred tax assets. The Company has recorded a full valuation allowance on its net deferred tax asset balances for all periods presented because of uncertainties related to utilization of the deferred tax assets. At such time as it is determined that it is more likely than not that the deferred tax assets are realizable, the valuation allowance will be reduced. The provision for income taxes during interim quarterly reporting periods is based on the Company's estimate of the annual effective tax rate for the full fiscal year. Pursuant to SOP 90-7, future decreases in the valuation allowance established in fresh-start accounting are accounted for as a reduction in goodwill.

**Note 7. Significant Acquisitions and Dispositions**

In February 2005, Cricket's wholly-owned subsidiary, Cricket Licensee (Reaction), Inc., was named the winning bidder in the FCC's Auction #58 for four wireless licenses for \$166.9 million. Cricket Licensee (Reaction), Inc. purchased these licenses in the second quarter of fiscal 2005.

In February 2005, ANB 1 License was named the winning bidder in Auction #58 for nine wireless licenses for \$68.2 million. The transfers of the wireless licenses to ANB 1 License are subject to FCC approval. Although the Company expects that such approvals will be issued in the normal course, there can be no assurance that the FCC will grant such approvals. During the six months ended June 30, 2005, Cricket made loans under its senior secured credit facility with ANB 1 License in the aggregate principal amount of \$56.3 million. ANB 1 License paid these borrowed funds, together with \$4.0 million of equity contributions, to the FCC to increase its total FCC payments to \$68.2 million, which is classified as deposits for wireless licenses at June 30, 2005.

In March 2005, subsidiaries of Leap signed an agreement to sell 23 wireless licenses and substantially all of the Company's operating assets in its Michigan markets for \$102.5 million. The Company has not launched commercial operations in most of the markets covered by the licenses to be sold. As described in Note 3, the long-lived assets included in this transaction, including wireless licenses with a carrying value of \$70.8 million, property and equipment

with a net book value of \$15.2 million and intangible assets with a net book value of \$1.9 million, have been classified in assets held for sale in the condensed consolidated balance sheet as of June 30, 2005. On June 22, 2005, the FCC granted its approval of the transaction. The transaction was completed on August 2, 2005, resulting in an estimated gain of approximately \$14.5 million.

On June 24, 2005, Cricket completed its purchase of a wireless license to provide service in Fresno, California and related assets for approximately \$27.6 million. The Company launched service in Fresno on August 2, 2005.



## **Table of Contents**

In July 2005, the Company agreed in principle to sell non-operating wireless spectrum licenses covering 0.9 million potential customers for a sales price of approximately \$10.0 million. The Company expects to enter into a definitive agreement for this sale in the near future, subject to FCC approval of the transfer of the licenses. During the three and six months ended June 30, 2005, the Company recorded impairment charges of \$11.4 million to adjust the carrying values of these licenses to their estimated fair values, which were based on the agreed upon sales prices.

### **Note 8. Commitments and Contingencies**

In connection with the Chapter 11 proceedings, the Bankruptcy Court established deadlines by which the holders of pre-emergence claims against the Company were required to file proofs of claim. The final deadline for such claims, relating to claims that arose during the course of the bankruptcy, was October 15, 2004, 60 days after the Effective Date of the Plan of Reorganization. Parties who were required to, but who failed to, file proofs of claim before the applicable deadlines are barred from asserting such claims against the Company in the future. Generally, the Company's obligations have been discharged with respect to general unsecured claims for pre-petition obligations, although the holders of allowed general unsecured pre-petition claims against Leap have (and holders of pending general unsecured claims against Leap may have) a pro rata beneficial interest in the assets of the Leap Creditor Trust. The Company reviewed the remaining claims filed against it (consisting primarily of claims for pre-petition taxes and for obligations incurred by the Company during the course of the Chapter 11 proceedings) and filed further objections by the Bankruptcy Court deadline of January 17, 2005. The Company does not believe that the resolution of the outstanding claims filed against it in bankruptcy will have a material adverse effect on the Company's consolidated financial statements.

Foreign governmental authorities have asserted or are likely to assert tax claims of approximately \$9.1 million (including interest and based on recent currency exchange rates) against Leap with respect to periods prior to the bankruptcy, although the Company believes that the true value of these asserted or potential claims is lower. The Bankruptcy Court has established new claims bar dates for these governmental entities; by such dates, such entities must file a formal claim with the Bankruptcy Court for amounts owed by Leap for periods prior to April 13, 2003 or such claims will be barred. The Company does not believe that the resolution of these issues will have a material adverse effect on its consolidated financial statements.

On December 31, 2002, several members of American Wireless Group, LLC, referred to as AWG, filed a lawsuit against various officers and directors of Leap in the Circuit Court of the First Judicial District of Hinds County, Mississippi, referred to herein as the Whittington Lawsuit. Leap purchased certain FCC wireless licenses from AWG and paid for those licenses with shares of Leap stock. The complaint alleges that Leap failed to disclose to AWG material facts regarding a dispute between Leap and a third party relating to that party's claim that it was entitled to an increase in the purchase price for certain wireless licenses it sold to Leap. In their complaint, plaintiffs seek rescission and/or damages according to proof at trial of not less than the aggregate amount paid for the Leap stock (alleged in the complaint to have a value of approximately \$57.8 million in June 2001 at the closing of the license sale transaction), plus interest, punitive or exemplary damages in the amount of not less than three times compensatory damages, and costs and expenses. Leap is not a defendant in the Whittington Lawsuit. Plaintiffs contend that the named defendants are the controlling group that was responsible for Leap's alleged failure to disclose the material facts regarding the third party dispute and the risk that the shares held by the plaintiffs might be diluted if the third party was successful in an arbitration proceeding. Defendants filed a motion to compel arbitration or in the alternative, dismiss the Whittington Lawsuit, noting that plaintiffs as members of AWG agreed to arbitrate disputes pursuant to the license purchase agreement, that they failed to plead facts that show that they are entitled to relief, that Leap made adequate disclosure of the relevant facts regarding the third party dispute, and that any failure to disclose such information did not cause any damage to the plaintiffs.

In a related action to the action described above, on June 6, 2003, AWG filed a lawsuit in the Circuit Court of the First Judicial District of Hinds County, Mississippi, referred to herein as the AWG Lawsuit, against the same individual defendants named in the Whittington Lawsuit. The complaint generally sets forth the same claims made by the plaintiffs in the Whittington Lawsuit. Leap is not a defendant in the AWG Lawsuit. In its complaint, plaintiff seeks rescission and/or damages according to proof at trial of not less than the aggregate amount paid for the Leap stock (alleged in the complaint to have a value of approximately \$57.8 million in June 2001 at the closing of the license sale transaction), plus interest, punitive or exemplary damages in the amount of not less than three times

**Table of Contents**

compensatory damages, and costs and expenses. Defendants filed a motion to compel arbitration or in the alternative, dismiss the AWG Lawsuit, making arguments similar to those made in their motion to dismiss the Whittington Lawsuit.

Although Leap is not a defendant in either the Whittington or AWG Lawsuits, several of the defendants have indemnification agreements with the Company. Leap's D&O insurers have not filed a reservation of rights letter and have been paying defense costs. Management believes that the liability, if any, from the AWG and Whittington Lawsuits and the related indemnity claims of the defendants against Leap is neither probable nor reasonably estimable; therefore, no accrual has been made in the Company's condensed consolidated financial statements as of June 30, 2005 related to these contingencies.

A third party with a large patent portfolio has contacted the Company and suggested that the Company needs to obtain a license under a number of patents in connection with the Company's current business operations. The Company understands that the third party has initiated similar discussions with other telecommunications carriers. The Company does not currently expect that the resolution of this matter will have a material adverse effect on the Company's consolidated financial statements.

The Company is involved in certain other claims arising in the course of business, seeking monetary damages and other relief. The amount of the liability, if any, from such claims cannot currently be reasonably estimated; therefore, no accruals have been made in the Company's condensed consolidated financial statements as of June 30, 2005 for such claims. In the opinion of the Company's management, the ultimate liability for such claims will not have a material adverse effect on the Company's consolidated financial statements.

The Company has entered into non-cancelable operating lease agreements to lease its facilities, certain equipment and sites for towers, equipment and antennas required for the operation of its wireless networks. These leases typically include renewal options and escalation clauses. In general, site leases have five year initial terms with four five year renewal options. The following table summarizes the approximate future minimum rentals under non-cancelable operating leases, including renewals that are reasonably assured, in effect at June 30, 2005 (in thousands):

**Year Ended December 31:**

Remainder of 2005	\$ 27,363
2006	36,916
2007	21,900
2008	19,405
2009	16,978
Thereafter	85,543
Total	\$ 208,105

**Table of Contents**

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

*As used in this report, the terms we, our, ours and us refer to Leap Wireless International, Inc., a Delaware corporation, and its subsidiaries, unless the context suggests otherwise. Leap refers to Leap Wireless International, Inc., and Cricket refers to Cricket Communications, Inc. Unless otherwise specified, information relating to population and potential customers, or POPs, is based on 2005 population estimates provided by Claritas Inc.*

The following information should be read in conjunction with the unaudited condensed consolidated financial statements and notes thereto included in Item 1 of this Quarterly Report and the audited consolidated financial statements and notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K for the year ended December 31, 2005 filed with the Securities and Exchange Commission on March 27, 2006.

Except for the historical information contained herein, this document contains forward-looking statements reflecting management's current forecast of certain aspects of our future. These forward-looking statements are subject to a number of risks, uncertainties and assumptions that could cause actual results to differ materially from those anticipated or implied in our forward-looking statements. Such risks, uncertainties and assumptions include, among other things:

- our ability to attract and retain customers in an extremely competitive marketplace;
- changes in economic conditions that could adversely affect the market for wireless services;
- the impact of competitors' initiatives;
- our ability to successfully implement product offerings and execute market expansion plans;
- our ability to comply with the covenants in our senior secured credit facilities;
- our ability to attract, motivate and retain an experienced workforce;
- failure of network systems to perform according to expectations;
- failure of the Federal Communications Commission, or the FCC, to approve the transfers to Alaska Native Broadband 1 License, LLC, or ANB 1 License, of the wireless licenses for which it was the winning bidder in the FCC's Auction #58;
- global political unrest, including the threat or occurrence of war or acts of terrorism; and
- other factors detailed in the section entitled "Risk Factors" included in this report.

All forward-looking statements in this report should be considered in the context of these risk factors. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. In light of these risks and uncertainties, the forward-looking events and circumstances discussed in this report may not occur and actual results could differ materially from those anticipated or implied in the forward-looking statements. Accordingly, readers of this report are cautioned not to place undue reliance on the

forward-looking statements.

## **Overview**

*Restatement of Previously Reported Unaudited Interim Consolidated Financial Information.* The accompanying Management's Discussion and Analysis of Financial Condition and Results of Operations gives effect to certain restatement adjustments made to the previously reported consolidated financial information of the Successor Company for the three and six months ended June 30, 2005. See Note 3 to the condensed consolidated financial statements included in Part I Item 1 of this report.

*Our Business.* We conduct our business primarily through Cricket. Cricket provides mobile wireless services targeted to meet the needs of customers who are under-served by traditional communications companies. Our Cricket service is a simple and affordable wireless alternative to traditional landline service. Our basic Cricket service offers customers virtually unlimited anytime minutes within the Cricket calling area over a high-quality, all-

**Table of Contents**

digital CDMA network. Our revenues come from the sale of wireless services, handsets and accessories to customers. Our liquidity and capital resources come primarily from our existing cash, cash equivalents and short-term investments, cash generated from operations, and cash available from borrowings under our revolving credit facility. In addition, in August 2005, we completed the sale of our Michigan markets and 23 wireless licenses for \$102.5 million.

At June 30, 2005, we operated in 20 states and had approximately 1,618,000 customers and the total potential customer base covered by our networks in our operating markets was approximately 26.8 million. As of August 11, 2005, we owned wireless licenses covering a total potential customer base of 60.2 million.

In February 2005, a wholly-owned subsidiary of Cricket was named the winning bidder in the FCC's Auction #58 for four wireless licenses covering approximately 11.1 million potential customers. We acquired these licenses in May 2005. We currently expect to launch commercial operations in the markets covered by these licenses and have commenced build-out activities. In addition, in February 2005, a subsidiary of Alaska Native Broadband 1, LLC, an entity in which we own a 75% non-controlling interest and which is referred to in this report as ANB 1, was the winning bidder in Auction #58 for nine wireless licenses covering approximately 10.1 million potential customers. The transfers of the wireless licenses to ANB 1's subsidiary are subject to FCC approval. Although we expect that such approvals will be issued in the normal course, there can be no assurance that the FCC will grant such approvals. In July 2005, we increased the term loan portion of our senior secured credit facility by \$100 million to increase our liquidity and help assure we have sufficient funds for the build-out and initial operation of our new licenses and to finance the build-out and initial operation of the licenses ANB 1 expects to acquire through its subsidiary. For a further discussion of our arrangements with Alaska Native Broadband, see Item 1. Business Arrangements with Alaska Native Broadband in our Annual Report on Form 10-K for the year ended December 31, 2004 as originally filed with the Securities and Exchange Commission on May 16, 2005.

*Voluntary Reorganization Under Chapter 11.* On April 13, 2003, Leap, Cricket and substantially all of their subsidiaries filed voluntary petitions for relief under Chapter 11 in the U.S. Bankruptcy Court for the Southern District of California. On August 5, 2004, all material conditions to the effectiveness of the Plan of Reorganization were resolved and, on August 16, 2004, the Plan of Reorganization became effective and the Company emerged from Chapter 11 bankruptcy. On that date, a new Board of Directors of Leap was appointed, our previously existing stock, options and warrants were cancelled, and Leap issued 60 million shares of new Leap common stock for distribution to two classes of creditors.

Our Plan of Reorganization implemented a comprehensive financial reorganization that significantly reduced our outstanding indebtedness. When the Plan of Reorganization became effective on August 16, 2004, our long-term debt was reduced from a book value of more than \$2.4 billion to debt with an estimated fair value of \$412.8 million, consisting of new Cricket 13% senior secured pay-in-kind notes due 2011 with a face value of \$350 million and an estimated fair value of \$372.8 million and approximately \$40 million of remaining indebtedness to the FCC. On January 10, 2005, we entered into new senior secured credit facilities and used a portion of the proceeds from the \$500 million term loan included as a part of such facilities to redeem Cricket's 13% senior secured pay-in-kind notes and to repay the remaining indebtedness to the FCC. The new facilities consist of a six-year \$500 million term loan and a five-year \$110 million revolving credit facility and were amended in July 2005 to increase the term loan by \$100 million.

*Fresh-Start Reporting.* In connection with our emergence from Chapter 11, we adopted the fresh-start reporting provisions of Statement of Position 90-7, Financial Reporting by Entities in Reorganization under the Bankruptcy Code, or SOP 90-7, as of July 31, 2004. Under SOP 90-7, reorganization value represents the fair value of the entity before considering liabilities and approximates the amount a willing buyer would pay for the assets of the entity immediately after the reorganization. In implementing fresh-start reporting, we allocated our reorganization value to

the fair value of our assets in conformity with procedures specified by SFAS No. 141, Business Combinations, and stated our liabilities, other than deferred taxes, at the present value of amounts expected to be paid. The amount remaining after allocation of the reorganization value to the fair value of our identified tangible and intangible assets is reflected as goodwill, which is subject to periodic evaluation for impairment. In addition, under fresh-start reporting, our accumulated deficit was eliminated and new equity was issued according to the Plan of Reorganization. See further discussion of fresh-start reporting in our Annual Report on Form 10-K for the year

**Table of Contents**

ended December 31, 2004, as originally filed, and in our Annual Report on Form 10-K for the year ended December 31, 2005.

This overview is intended to be only a summary of significant matters concerning our results of operations and financial condition. It should be read in conjunction with the management discussion below and all of the business and financial information contained in this report, including the condensed consolidated financial statements in Item 1 of this Quarterly Report, as well as our Annual Report on Form 10-K for the year ended December 31, 2005.

**Results of Operations**

As a result of our emergence from Chapter 11 bankruptcy and the application of fresh-start reporting, we are deemed to be a new entity for financial reporting purposes. In this report, the Company is referred to as the Predecessor Company for periods on or prior to July 31, 2004, and is referred to as the Successor Company for periods after July 31, 2004, after giving effect to the implementation of fresh-start reporting. The financial statements of the Successor Company are not comparable in many respects to the financial statements of the Predecessor Company because of the effects of the consummation of the Plan of Reorganization as well as the adjustments for fresh-start reporting.

**Financial Performance**

The following table presents the consolidated statement of operations data for the periods indicated (in thousands). This data has been derived from interim condensed consolidated financial statements that have been restated for the three and six months ended June 30, 2005 to reflect adjustments that are further discussed in Note 3 of the condensed consolidated financial statements included in Part 1 Item 1 of this report.

	<b>Successor Company</b>	<b>Predecessor Company</b>	<b>Successor Company</b>	<b>Predecessor Company</b>
	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2005</b>	<b>2004</b>	<b>2005</b>	<b>2004</b>
	<b>(As Restated)</b>		<b>(As Restated)</b>	
Revenues:				
Service revenues	\$ 189,704	\$ 172,025	\$ 375,685	\$ 341,076
Equipment revenues	37,125	33,676	79,514	71,447
Total revenues	226,829	205,701	455,199	412,523
Operating expenses:				
Cost of service (exclusive of items shown separately below)	(49,608)	(47,827)	(99,805)	(95,827)
Cost of equipment	(42,799)	(40,635)	(91,977)	(84,390)
Selling and marketing	(24,810)	(21,939)	(47,805)	(45,192)
General and administrative	(42,423)	(33,922)	(78,458)	(72,532)
Depreciation and amortization	(47,281)	(76,386)	(95,385)	(151,847)
Impairment of indefinite-lived intangible assets	(11,354)		(11,354)	



Edgar Filing: LEAP WIRELESS INTERNATIONAL INC - Form 10-Q/A

Total operating expenses	(218,275)	(220,709)	(424,784)	(449,788)
Operating income (loss)	8,554	(15,008)	30,415	(37,265)
Interest income	1,176		3,079	
Interest expense	(7,566)	(1,908)	(16,689)	(3,731)
Other income (expense), net	(39)	(615)	(1,325)	(596)
Income (loss) before reorganization items and income taxes	2,125	(17,531)	15,480	(41,592)
Reorganization items, net		1,313		(712)
Income (loss) before income taxes	2,125	(16,218)	15,480	(42,304)
Income taxes	(1,022)	(1,927)	(6,861)	(3,871)
Net income (loss)	\$ 1,103	\$ (18,145)	\$ 8,619	\$ (46,175)

**Table of Contents*****Three and Six Months Ended June 30, 2005 Compared to the Three and Six Months Ended June 30, 2004***

At June 30, 2005, we had approximately 1,618,000 customers compared to approximately 1,547,000 customers at June 30, 2004. Gross customer additions during the three months ended June 30, 2005 and 2004 were approximately 191,000 and 180,000, respectively, and net customer additions during these periods were approximately 3,000 and 9,000, respectively. Gross customer additions during the six months ended June 30, 2005 and 2004 were approximately 393,000 and 387,000, respectively, and net customer additions during these periods were approximately 48,000 and 75,000, respectively. The weighted average number of customers during the three months ended June 30, 2005 and 2004 was approximately 1,612,000 and 1,538,000, respectively. The weighted average number of customers during the six months ended June 30, 2005 and 2004 was approximately 1,600,000 and 1,518,000, respectively. At June 30, 2005, the total potential customer base covered by our networks in our operating markets was approximately 26.8 million.

During the three and six months ended June 30, 2005, service revenues increased \$17.7 million, or 10%, and \$34.6 million, or 10%, respectively, compared to the corresponding periods of the prior year. Higher average customers contributed \$8.2 million and \$18.4 million, respectively, to the increases for the three- and six-month periods. The remaining increase was attributable to higher average revenues per customer during the three and six months ended June 30, 2005, compared with the same periods of the prior year. The increasing average revenue per customer primarily reflects increasing customer acceptance of higher-value, higher-priced service offerings, and the reduced utilization of service-based mail-in rebate promotions in 2005.

During the three and six months ended June 30, 2005, equipment revenues increased \$3.4 million, or 10%, and \$8.1 million, or 11%, respectively, compared to the corresponding periods of the prior year. For the three months ended June 30, 2005, an increase in handset sales of 2% increased equipment revenue by \$0.5 million over the corresponding period in 2004, and the remaining \$2.9 million increase was driven by higher net revenues per handset sold, including accessory sales and reductions in dealer compensation costs. For the six months ended June 30, 2005, an increase in handset sales of 4% increased equipment revenue by \$2.2 million over the corresponding period in 2004, and the remaining \$5.9 million increase was driven by a \$7.2 million increase in net revenues per handset sold, including accessory sales and reductions in dealer compensation costs, offset by a \$1.3 million reduction in activation fees.

During the three and six months ended June 30, 2005, cost of service increased \$1.8 million, or 4%, and \$4.0 million, or 4%, respectively, compared to the corresponding periods of the prior year. The increase in cost of service for the three months ended June 30, 2005 was primarily attributable to an increase of \$2.7 million in variable costs associated with additional product usage and continued customer adoption of new value-added products, an increase of \$0.8 million in network-related costs, and stock-based compensation expense of \$0.8 million. These increases were offset by reductions of \$1.2 million in software maintenance and \$1.3 million in other labor-related costs. For the six months ended June 30, 2005, the increase in cost of service was primarily attributable to increases of \$6.2 million in additional product usage, an increase of \$1.4 million in network-related costs, and stock-based compensation expense of \$0.8 million, offset by reductions of \$1.4 million in software maintenance and \$3.3 million in other labor-related expenses. During 2005, we expect the variable costs associated with usage and value-added features to continue to increase as our customer base grows and the adoption of add-on products accelerates. Additionally, we expect that the launch of the Fresno market, which occurred on August 2, 2005, will increase fixed network infrastructure costs.

Cost of equipment for the three and six months ended June 30, 2005 increased by \$2.2 million, or 5%, and \$7.6 million, or 9%, respectively, compared to the corresponding periods of the prior year. The increase in cost of equipment for the three months ended June 30, 2005 consisted of \$1.0 million associated with slight increases in both handsets sold and the cost per handset and \$1.2 million associated with higher reverse logistics costs. For the six

months ended June 30, 2005, the increase in cost of equipment consisted of \$4.2 million associated with higher-cost handsets, \$2.8 million associated with higher handset sales volumes, and \$0.6 million associated with higher reverse logistics costs.

During the three and six months ended June 30, 2005, selling and marketing expenses increased by \$2.9 million, or 13%, and \$2.6 million, or 6%, respectively, compared to the corresponding periods of the prior year. For the three months ended June 30, 2005, the increase consisted of \$1.2 million in media and advertising

**Table of Contents**

costs, \$0.7 million in stock-based compensation expense and \$0.9 million in other labor-related costs. For the six months ended June 30, 2005, the increase consisted of \$1.7 million of media and advertising costs, \$0.7 million in stock-based compensation expense and \$0.3 million in other labor-related and other costs.

During the three and six months ended June 30, 2005, general and administrative expenses increased \$8.5 million, or 25%, and \$5.9 million, or 8%, respectively, compared to the corresponding periods of the prior year. For the three months ended June 30, 2005, the increase was primarily due to increases of \$3.2 million in legal and other professional services, \$5.6 million in stock-based compensation expense and an increase of \$0.8 million in other labor-related costs. These increases were partially offset by reductions in customer care and billing costs of \$1.1 million. For the six months ended June 30, 2005, the increase was primarily due to increases of \$4.6 million in legal and other professional services, \$5.6 million in stock-based compensation expense and an increase of \$0.3 million in other labor-related costs. These increases were partially offset by reductions in customer care and billing costs of \$4.6 million.

During the three and six months ended June 30, 2005, we recorded stock-based compensation expense of \$7.1 million in connection with the grant of restricted common shares and deferred stock units exercisable for common stock to directors, executive officers and other employees. The total intrinsic value of the deferred stock units of \$6.9 million was recorded as stock-based compensation expense during the three and six months ended June 30, 2005 because the deferred stock units were immediately vested upon grant. The total intrinsic value of the restricted stock awards as of the measurement date of \$22.5 million was recorded as unearned compensation as of June 30, 2005. The unearned compensation is amortized on a straight-line basis over the maximum vesting period of the awards of either three or five years. For the three and six months ended June 30, 2005, \$0.2 million was recorded in stock-based compensation expense for the amortization of the unearned compensation. The amount of stock-based compensation expense expected for the remainder of fiscal year 2005 is approximately \$4-5 million.

During the three and six months ended June 30, 2005, depreciation and amortization expense decreased \$29.1 million, or 38%, and \$56.5 million, or 37%, respectively, compared to the corresponding periods of the prior year. The decreases in depreciation expense were primarily due to the revision of the estimated useful lives of network equipment and the reduction in the carrying value of property and equipment as a result of fresh-start reporting at July 31, 2004. As a result of this change, depreciation expense was reduced by approximately \$30.4 million and \$61.2 million for the three and six months ended June 30, 2005, respectively, compared to what it would have been if the useful lives had not been revised. In addition, depreciation and amortization expense for the three and six months ended June 30, 2005 included amortization expense of \$8.6 million and \$17.3 million, respectively, related to identifiable intangible assets recorded upon the adoption of fresh-start reporting. As a result of our build-out and initial operation of our planned new markets, we expect a significant increase in depreciation and amortization expense in the future. In addition, we will record accelerated depreciation charges in the future related to the planned decommissioning or replacement of network assets as we upgrade our equipment and optimize our network.

During the three and six months ended June 30, 2005, we recorded impairment charges of \$11.4 million in connection with an agreement in principle to sell non-operating wireless spectrum licenses. We adjusted the carrying values of those licenses to their estimated fair values, which were based on the agreed upon sales prices.

During the three and six months ended June 30, 2005, interest expense increased \$5.7 million, or 297%, and \$13.0 million, or 347%, respectively, compared to the corresponding periods of the prior year. The increases in interest expense resulted from the application of SOP 90-7 during the three and six months ended June 30, 2004, which required that, commencing on April 13, 2003 (the date of the filing of the Company's bankruptcy petition, or the Petition Date), we cease to accrue interest and amortize debt discounts and debt issuance costs on pre-petition liabilities that were subject to compromise, which comprised substantially all of our debt. Upon our emergence from bankruptcy, we began accruing interest on the newly issued 13% senior secured pay-in-kind notes. The pay-in-kind

notes were repaid in January 2005 and replaced with a \$500 million term loan. At June 30, 2005, the effective interest rate on the \$500 million term loan was 6.4%, including the effect of interest rate swaps. The terms of the Credit Agreement require us to enter into interest rate hedging agreements in an amount equal to at least 50% of our outstanding indebtedness. In accordance with this requirement, in April 2005 we entered into interest rate swap agreements with respect to \$250 million of our debt. These swap agreements effectively fix the interest rate on

## **Table of Contents**

\$250 million of the outstanding indebtedness at 6.7% through June 2007. We capitalize interest costs associated with our wireless licenses and property and equipment during the build-out of a new market. The amount of such capitalized interest depends on the particular markets being built out, the carrying values of the licenses and property and equipment involved in those markets and the duration of the build out. We expect capitalized interest to be significant during the build out of our planned new markets.

During the three and six months ended June 30, 2005, there were no reorganization items. Reorganization items for the three and six months ended June 30, 2004 represented amounts incurred by the Predecessor Company as a direct result of the Chapter 11 filings and consisted primarily of professional fees for legal, financial advisory and valuation services directly associated with the Company's Chapter 11 filings and reorganization process, partially offset by income from the settlement of pre-petition liabilities and interest income earned while the Company was in bankruptcy.

During the three months ended June 30, 2005, we recorded income tax expense of \$1.0 million compared to income tax expense of \$1.9 million for the three months ended June 30, 2004. During the six months ended June 30, 2005, we recorded income tax expense of \$6.9 million compared to income tax expense of \$3.9 million for the six months ended June 30, 2004. Income tax expense for the three and six months ended June 30, 2004 consisted primarily of the tax effect of the amortization, for income tax purposes, of wireless licenses related to deferred tax liabilities. During the three and six months ended June 30, 2005, we recorded income tax expense at an effective tax rate of 48.1% and 44.3%, respectively. Despite the fact that we have recorded a full valuation allowance on our deferred tax assets, we recognized income tax expense for the three and six months ended June 30, 2005 because the release of valuation allowance associated with the reversal of deferred tax assets recorded in fresh-start reporting is recorded as a reduction of goodwill rather than as a reduction of income tax expense. The effective tax rate for the three and six months ended June 30, 2005 was higher than the statutory tax rate due primarily to permanent items not deductible for tax purposes. We expect to incur tax losses for 2005 due to, among other things, tax deductions associated with the repayment of the 13% senior secured pay-in-kind notes. Therefore, we expect to pay only minimal cash taxes for 2005.

## ***Performance Measures***

In managing our business and assessing our financial performance, management supplements the information provided by financial statement measures with several customer-focused performance metrics that are widely used in the telecommunications industry. These metrics include average revenue per user per month (ARPU), which measures service revenue per customer; cost per gross customer addition (CPGA), which measures the average cost of acquiring a new customer; cash costs per user per month (CCU), which measures the non-selling cash cost of operating our business on a per customer basis; and churn, which measures turnover in our customer base. CPGA and CCU are non-GAAP financial measures. A non-GAAP financial measure, within the meaning of Item 10 of Regulation S-K promulgated by the Securities and Exchange Commission, is a numerical measure of a company's financial performance or cash flows that (a) excludes amounts, or is subject to adjustments that have the effect of excluding amounts, that are included in the most directly comparable measure calculated and presented in accordance with generally accepted accounting principles in the consolidated balance sheet, consolidated statement of operations or consolidated statement of cash flows; or (b) includes amounts, or is subject to adjustments that have the effect of including amounts, that are excluded from the most directly comparable measure so calculated and presented. See *Reconciliation of Non-GAAP Financial Measures* below for a reconciliation of CPGA and CCU to the most directly comparable GAAP financial measures.

ARPU is an industry metric that measures service revenue divided by the weighted average number of customers, divided by the number of months during the period being measured. Management uses ARPU to identify average revenue per customer, to track changes in average customer revenues over time, to help evaluate how changes in our business, including changes in our service offerings and fees, affect average revenue per customer, and to forecast

future service revenue. In addition, ARPU provides management with a useful measure to compare our subscriber revenue to that of other wireless communications providers. We believe investors use ARPU primarily as a tool to track changes in our average revenue per customer and to compare our per customer service revenues to those of other wireless communications providers.

**Table of Contents**

CPGA is an industry metric that represents selling and marketing costs, excluding applicable stock-based compensation expense, and the gain or loss on sale of handsets (generally defined as cost of equipment less equipment revenue), excluding costs unrelated to initial customer acquisition, divided by the total number of gross new customer additions during the period being measured. Costs unrelated to initial customer acquisition include the revenues and costs associated with the sale of handsets to existing customers as well as costs associated with handset replacements and repairs (other than warranty costs which are the responsibility of the handset manufacturers). We deduct customers who do not pay their first monthly bill from our gross customer additions, which tends to increase CPGA because we incur the costs associated with this customer without receiving the benefit of a gross customer addition. Management uses CPGA to measure the efficiency of our customer acquisition efforts, to track changes in our average cost of acquiring new subscribers over time, and to help evaluate how changes in our sales and distribution strategies affect the cost-efficiency of our customer acquisition efforts. In addition, CPGA provides management with a useful measure to compare our per customer acquisition costs with those of other wireless communications providers. We believe investors use CPGA primarily as a tool to track changes in our average cost of acquiring new customers and to compare our per customer acquisition costs to those of other wireless communications providers.

CCU is an industry metric that measures cost of service and general and administrative costs, excluding applicable stock-based compensation expenses, gain or loss on sale of handsets to existing customers and costs associated with handset replacements and repairs (other than warranty costs which are the responsibility of the handset manufacturers), divided by the weighted average number of customers, divided by the number of months during the period being measured. CCU does not include any depreciation and amortization expense. Management uses CCU as a tool to evaluate the non-selling cash expenses associated with ongoing business operations on a per customer basis, to track changes in these non-selling cash costs over time, and to help evaluate how changes in our business operations affect non-selling cash costs per customer. In addition, CCU provides management with a useful measure to compare our non-selling cash costs per customer with those of other wireless communications providers. We believe investors use CCU primarily as a tool to track changes in our non-selling cash costs over time and to compare our non-selling cash costs to those of other wireless communications providers.

Churn, an industry metric that measures customer turnover, is calculated as the net number of customers that disconnect from our service divided by the weighted average number of customers divided by the number of months during the period being measured. As noted above, customers who do not pay their first monthly bill are deducted from our gross customer additions; as a result, these customers are not included in churn. Management uses churn to measure our retention of customers, to measure changes in customer retention over time, and to help evaluate how changes in our business affect customer retention. In addition, churn provides management with a useful measure to compare our customer turnover activity to that of other wireless communications providers. We believe investors use churn primarily as a tool to track changes in our customer retention over time and to compare our customer retention to that of other wireless communications providers.

The following table shows metric information for the three months ended June 30, 2005 and 2004:

	<b>Successor Company Three Months Ended June 30, 2005</b>	<b>Predecessor Company Three Months Ended June 30, 2004</b>
ARPU	\$ 39.24	\$ 37.28
CPGA	\$ 138	\$ 141
CCU	\$ 18.43	\$ 18.47



Churn	3.9%	3.7%
-------	------	------

***Reconciliation of Non-GAAP Financial Measures***

We utilize certain financial measures, as described above, that are calculated based on industry conventions and are not calculated based on GAAP. Certain of these financial measures are considered non-GAAP financial measures within the meaning of Item 10 of Regulation S-K promulgated by the SEC.

**Table of Contents**

CPGA The following table reconciles total costs used in the calculation of CPGA to selling and marketing expense, which we consider to be the most directly comparable GAAP financial measure to CPGA (in thousands, except gross customer additions and CPGA):

	<b>Successor Company Three Months Ended June 30, 2005</b>	<b>Predecessor Company Three Months Ended June 30, 2004</b>
Selling and marketing expense	\$ 24,810	\$ 21,939
Less stock-based compensation expense included in selling and marketing expense	(693)	
Plus cost of equipment	42,799	40,635
Less equipment revenue	(37,125)	(33,676)
Less net loss on equipment transactions unrelated to initial customer acquisition	(3,484)	(3,453)
Total costs used in the calculation of CPGA	\$ 26,307	\$ 25,445
Gross customer additions	191,288	180,128
CPGA	\$ 138	\$ 141

CCU The following table reconciles total costs used in the calculation of CCU to cost of service, which we consider to be the most directly comparable GAAP financial measure to CCU (in thousands, except weighted-average number of customers and CCU):

	<b>Successor Company Three Months Ended June 30, 2005</b>	<b>Predecessor Company Three Months Ended June 30, 2004</b>
Cost of service	\$ 49,608	\$ 47,827
Plus general and administrative expense	42,423	33,922
Less stock-based compensation expense included in cost of service and general and administrative expense	(6,436)	
Plus net loss on equipment transactions unrelated to initial customer acquisition	3,484	3,453
Total costs used in the calculation of CCU	\$ 89,079	\$ 85,202
Weighted-average number of customers	1,611,524	1,537,957
CCU	\$ 18.43	\$ 18.47

**Liquidity and Capital Resources**

Our principal sources of liquidity are our existing cash, cash equivalents and short-term investments, cash generated from operations, and cash available from borrowings under our \$110 million revolving credit facility (which was undrawn at June 30, 2005). From time to time, we may also generate additional liquidity through the sale of assets that are not required for the ongoing operation of our business. We may also generate liquidity from offerings of debt and/or equity in the capital markets. At June 30, 2005, we had a total of \$157.7 million in unrestricted cash, cash equivalents and short-term investments. As of June 30, 2005, we also had restricted cash, cash equivalents and short-term investments of \$25.7 million that included funds set aside or pledged to satisfy remaining administrative claims and priority claims against Leap and Cricket, and cash restricted for other purposes. Subsequent to June 30, 2005, we amended our credit agreement to increase the term loan by \$100 million and we completed the sale of our Michigan markets and 23 wireless licenses for \$102.5 million. We believe that our existing cash and investments, including the cash obtained from the incremental term loan and the sale of assets, and anticipated cash flows from operations will be sufficient to meet our operating and capital requirements through at least the next 12 months.

## **Table of Contents**

Cash provided by operating activities was \$108.5 million during the six months ended June 30, 2005 compared to \$89.9 million during the six months ended June 30, 2004. The increase was primarily attributable to higher net income (net of depreciation and amortization expense and non-cash stock-based compensation expense) in the six months ended June 30, 2005, partially offset by the timing of payments on accounts payable and interest payments on Cricket's 13% senior secured pay-in-kind notes and FCC debt.

Cash used in investing activities was \$245.1 million during the six months ended June 30, 2005 compared to \$35.4 million during the six months ended June 30, 2004. This increase was due primarily to payments by subsidiaries of Cricket and ANB 1 of the purchase price of and deposits for wireless licenses totaling \$239.2 million, an increase in the purchase of property and equipment of \$15.1 million, and a net decrease in restricted investment activity of \$13.6 million, partially offset by a net increase in the sale of investments of \$58.2 million.

Cash provided by financing activities during the six months ended June 30, 2005 was \$77.8 million, which consisted of borrowings under our new term loan of \$500.0 million, less amounts which were used to repay the FCC debt of \$40.0 million, to repay the pay-in-kind notes of \$372.7 million, to make two quarterly payments under the term loan totaling \$2.5 million and to pay debt issuance costs of \$7.0 million.

### ***New Credit Agreement***

On January 10, 2005, we entered into a new senior secured Credit Agreement with a syndicate of lenders and Bank of America, N.A. (as administrative agent and letter of credit issuer).

The facilities under the new Credit Agreement consist of a six-year \$500 million term loan, which was fully drawn at closing, and an undrawn five-year \$110 million revolving credit facility. Under the Credit Agreement, the term loan bears interest at LIBOR plus 2.5 percent, with interest periods of one, two, three or six months, or bank base rate plus 1.5 percent, as selected by Cricket. Outstanding borrowings under the term loan must be repaid in 20 quarterly payments of \$1.25 million each, commencing March 31, 2005, followed by four quarterly payments of \$118.75 million each, commencing March 31, 2010. The maturity date for outstanding borrowings under the revolving credit facility is January 10, 2010. The commitment of the lenders under the \$110 million revolving credit facility may be reduced in the event mandatory prepayments are required under the Credit Agreement and by one-twelfth of the original aggregate revolving credit commitment on January 1, 2008 and by one-sixth of the original aggregate revolving credit commitment on January 1, 2009 (each such amount to be net of all prior reductions) based on certain leverage ratios and other tests. The commitment fee on the revolving credit facility is payable quarterly at a rate of 1.0 percent per annum when the utilization of the facility (as specified in the Credit Agreement) is less than 50 percent and at 0.75 percent per annum when the utilization exceeds 50 percent. Borrowings under the revolving credit facility will accrue interest at LIBOR plus 2.5 percent, with interest periods of one, two, three or six months, or bank base rate plus 1.5 percent, as selected by Cricket, with the rate subject to adjustment based on our leverage ratio. The new credit facilities are guaranteed by Leap and all of its direct and indirect domestic subsidiaries (other than Cricket, which is the primary obligor, ANB 1 and ANB 1 License) and are secured by all present and future personal property and owned real property of Leap, Cricket and such direct and indirect domestic subsidiaries.

A portion of the proceeds from the term loan borrowing was used to redeem Cricket's \$350 million 13% senior secured pay-in-kind notes, to pay approximately \$43 million of call premium and accrued interest on such notes, to repay approximately \$41 million in principal amount of debt and accrued interest owed to the FCC, and to pay transaction fees and expenses. The remaining proceeds from the term loan borrowing of approximately \$60 million are being used for general corporate purposes.

Under the Credit Agreement, we are subject to certain limitations, including limitations on our ability: (1) to incur additional debt or sell assets, with restrictions on the use of proceeds; (2) to make certain investments and

acquisitions; (3) to grant liens; and (4) to pay dividends and make certain other restricted payments. In addition, we will be required to pay down the facilities under certain circumstances if we issue debt or equity, sell assets or property, receive certain extraordinary receipts or generate excess cash flow (as defined in the Credit Agreement). We are also required to maintain compliance with financial covenants which include a minimum interest coverage ratio, a maximum total leverage ratio, a maximum senior secured leverage ratio and a minimum fixed charge coverage ratio.

## **Table of Contents**

Affiliates of Highland Capital Management, L.P. (a beneficial shareholder of Leap and an affiliate of James D. Dondero, a director of Leap) participated in the syndication of the Company's new Credit Agreement in the following initial amounts: \$100 million of the \$500 million term loan and \$30 million of the \$110 million revolving credit facility.

At June 30, 2005, the effective interest rate on the \$500 million term loan was 6.4%, including the effect of interest rate swaps, and the outstanding indebtedness was \$497.5 million. The terms of the Credit Agreement require us to enter into interest rate hedging agreements in an amount equal to at least 50% of our outstanding indebtedness. In accordance with this requirement, in April 2005 we entered into interest rate swap agreements with respect to \$250 million of our debt. These swap agreements effectively fix the interest rate on \$250 million of the outstanding indebtedness at 6.7% through June 2007. The \$1.3 million fair value of the swap agreements at June 30, 2005 was recorded as a liability in the condensed consolidated balance sheet.

On July 22, 2005, we amended our credit agreement to increase the term loan by \$100 million. The interest and related terms are substantially the same as the original term loan agreement. Outstanding borrowings under the incremental term loan must be repaid in 18 quarterly payments of approximately \$278,000 each, commencing September 30, 2005, followed by four quarterly payments of \$23.75 million each, commencing March 31, 2010. We also amended the terms of the facility to accommodate the planned expansion of our business including: increasing certain leverage ratios and permitting us to invest up to \$325 million in ANB 1 and ANB 1 License and up to \$60 million in other joint ventures. The amendments also increased the amount of permitted purchase money security interests and capitalized leases and also allow us to provide limited guarantees for the benefit of ANB 1 License and other joint ventures.

Affiliates of Highland Capital Management, L.P. (a beneficial shareholder of Leap and an affiliate of James D. Dondero, a director of Leap) participated in the syndication of the additional term facility in the amount of \$9 million.

In July 2005, we entered into another interest rate swap agreement with respect to a further \$105 million of our outstanding indebtedness. This swap agreement effectively fixes the interest rate on \$105 million of the outstanding indebtedness at 6.8% through June 2009.

## ***Capital Expenditures and Other Asset Acquisitions and Dispositions***

### ***2005 Capital Expenditures***

During the six months ended June 30, 2005, we incurred approximately \$45.5 million in capital expenditures. We currently expect to incur between \$175 million and \$230 million in capital expenditures, excluding capitalized interest, for the year ending December 31, 2005. These capital expenditures are primarily for maintenance and improvement of our existing wireless networks, for the build-out and launch of the Fresno, California market and the related expansion and network change-out of the Company's existing Visalia and Modesto/Merced markets, and costs associated with the initial development of markets covered by licenses acquired as a result of Auction #58 and costs to be incurred by ANB 1 in connection with the initial development of licenses ANB 1 expects to acquire as a result of its participation in Auction #58. We expect to finance the remaining capital expenditures for 2005 with our existing cash, cash equivalents and short-term investments including the cash obtained from the incremental term loan and the sale of assets, as well as cash generated from operations.

### ***Auction #58 Properties and Build-Out***

In February 2005, our wholly-owned subsidiary, Cricket Licensee (Reauction), Inc., was named the winning bidder in the FCC's Auction #58 for four wireless licenses covering approximately 11.1 million potential customers. Cricket

Licensee (Reauction), Inc. purchased these licenses in the second quarter of fiscal 2005.

ANB 1's wholly-owned subsidiary, Alaska Native Broadband 1 License, LLC, or ANB 1 License, was named the winning bidder in Auction #58 for nine wireless licenses covering approximately 10.1 million potential customers. The transfers of the wireless licenses to ANB 1 License are subject to FCC approval. Although we expect that such approvals will be made in the normal course, there can be no assurance that the FCC will grant such approvals. During the six months ended June 30, 2005, we made loans under our senior secured credit facility with

**Table of Contents**

ANB 1 License in the aggregate amount of \$56.3 million. ANB 1 License paid these borrowed funds, together with \$4.0 million of equity contributions, to the FCC to increase its total FCC payments to \$68.2 million, which is classified as deposits for wireless licenses at June 30, 2005. Under our senior secured credit facility with ANB 1 License, as amended, we have committed to loan ANB 1 License up to \$24.8 million in additional funds to finance its initial build-out costs and working capital requirements. However, ANB 1 License will need to obtain additional capital from Cricket or another third party to build out and launch its networks. Under Cricket's Credit Agreement, we are permitted to invest up to an aggregate of \$325 million in loans to and equity investments in ANB 1 and ANB 1 License.

We currently expect to launch commercial operations in the markets covered by the licenses we have acquired as a result of Auction #58 and we have commenced build out activities. Pursuant to a management services agreement, we are also providing services to ANB 1 License with respect to planning for the build-out and launch of the licenses it expects to acquire in connection with Auction #58. See Item 1. Business-Arrangements with Alaska Native Broadband in our Annual Report on Form 10-K for the year ended December 31, 2004, as originally filed, for further discussion of our arrangements with Alaska Native Broadband.

We currently anticipate that the networks for our Auction #58 licenses and the networks for ANB 1 License's expected Auction #58 licenses will cover an aggregate of 14 million to 17 million potential customers. Given this anticipated network coverage, we currently expect that the aggregate costs we will incur to build-out our new markets and that ANB 1 License will incur to build out its expected markets, and to upgrade new and existing markets to EVDO technology, to the extent appropriate, will cost approximately \$475 million or less. These capital expenditures are expected to be incurred primarily in 2005 and 2006 (the portion expected for 2005 is reflected in the discussion of 2005 Capital Expenditures set forth above). We expect that we will have sufficient liquidity to finance these capital expenditures from the various sources of liquidity available to us, including our existing cash, cash equivalents and short-term investments, cash generated from operations, cash obtained from borrowings under our revolving credit facility and, as appropriate, cash proceeds from capital markets transactions.

*Other Acquisitions and Dispositions*

In March 2005, subsidiaries of Leap signed an agreement to sell 23 wireless licenses and substantially all of the operating assets in our Michigan markets for \$102.5 million. We have not launched commercial operations in most of the markets covered by the licenses to be sold. On June 22, 2005, the FCC granted its approval of the transaction. This transaction was completed on August 2, 2005, resulting in an estimated gain of approximately \$14.5 million.

On June 24, 2005, Cricket completed its purchase of a wireless license to provide service in Fresno, California and related assets for approximately \$27.6 million. We launched service in Fresno on August 2, 2005.

In July 2005, we agreed in principle to sell non-operating wireless spectrum licenses covering 0.9 million potential customers for a sales price of approximately \$10.0 million. We expect to enter into a definitive agreement for this sale in the near future, subject to FCC approval of the transfer of the licenses. During the three and six months ended June 30, 2005, we recorded impairment charges of \$11.4 million to adjust the carrying values of these licenses to their estimated fair values, which were based on the agreed upon sales prices.



**Table of Contents*****Certain Contractual Obligations and Commitments***

The table below summarizes information as of June 30, 2005 regarding certain future minimum contractual obligations and commitments for Leap and Cricket for the next five years and thereafter (in thousands):

	<b>Total</b>	<b>Remainder of 2005</b>	<b>Year Ended December 31,</b>				<b>Thereafter</b>
			<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	
Long-term debt(1)	\$ 497,500	\$ 2,500	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000	\$ 475,000
Origination fees for ANB 1 investment	5,450	750	4,700				
Contractual interest(2)	156,129	16,201	32,178	31,003	29,828	29,107	17,812
Operating leases	208,105	27,363	36,916	21,900	19,405	16,978	85,543
<b>Total</b>	<b>\$ 867,184</b>	<b>\$ 46,814</b>	<b>\$ 78,794</b>	<b>\$ 57,903</b>	<b>\$ 54,233</b>	<b>\$ 51,085</b>	<b>\$ 578,355</b>

(1) Amounts shown for Cricket's term loan under the new credit facilities executed on January 10, 2005 include principal only. Interest on this term loan, calculated at the current interest rate, is stated separately.

(2) Contractual interest is based on the current interest rates in effect at June 30, 2005 for debt outstanding as of that date.

The table above does not include the following contractual obligations relating to ANB 1, a company which we consolidate under FASB Interpretation No. 46-R: (1) Cricket's obligation to loan to ANB 1 License up to \$24.8 million, as amended in June 2005, to finance its initial build-out costs and working capital requirements, of which approximately \$0.1 million was drawn at June 30, 2005, and (2) Cricket's obligation to pay \$2.0 million to ANB 1 if ANB 1 exercises its right to sell its membership interest in ANB 1 to Cricket following the initial build-out of ANB 1 License's wireless licenses. The table above also does not include the additional \$100 million term loan executed in July 2005 or the related interest.

***Off-Balance Sheet Arrangements***

We had no material off-balance sheet arrangements at June 30, 2005.

**Table of Contents**

**RISK FACTORS**

**Risks Related to Our Business and Industry**

**We Have Experienced Net Losses And We May Not Be Profitable In The Future**

We experienced losses of \$8.4 million and \$49.3 million (excluding reorganization items, net) for the five months ended December 31, 2004 and the seven months ended July 31, 2004, respectively. In addition, we experienced net losses of \$597.4 million for the year ended December 31, 2003, \$664.8 million for the year ended December 31, 2002, \$483.3 million for the year ended December 31, 2001 and \$0.2 million for the year ended December 31, 2000. We may not generate profits in the future on a consistent basis or at all. If we fail to achieve consistent profitability, that failure could have a negative effect on our financial condition and on the value of the common stock of Leap.

**We May Not Be Successful In Increasing Our Customer Base Which Would Force Us To Change Our Business Plans And Financial Outlook And Would Likely Negatively Affect The Price Of Our Stock**

Our growth on a quarter by quarter basis has varied substantially in the recent past. In the first quarter of 2003, we gained approximately 1,000 net customers but we lost approximately 54,000 net customers in the second quarter of 2003. Net customers increased by approximately 18,000 in the third quarter of 2003, but decreased by approximately 4,000 during the fourth quarter of 2003. During the first and second quarters of 2004, we experienced a net increase of approximately 65,700 customers and 9,000 customers, respectively, but lost approximately 8,000 net customers in the third quarter of 2004. During the fourth quarter of 2004 and the first quarter of 2005, we gained approximately 30,000 net customers and approximately 45,000 net customers, respectively. In the second quarter of 2005, we gained approximately 3,000 net customers. We believe that this uneven growth over the last several quarters generally reflects seasonal trends in customer activity, promotional activity, the competition in the wireless telecommunications market, our attenuated spending on capital investments and advertising while we were in bankruptcy, and varying national economic conditions. Our current business plans assume that we will increase our customer base over time, providing us with increased economies of scale. If we are unable to attract and retain a growing customer base, we would be forced to change our current business plans and financial outlook and there would likely be a material negative affect on the price of our common stock.

**If We Experience High Rates Of Customer Turnover or Credit Card, Subscription or Dealer Fraud, Our Ability To Become Profitable Will Decrease**

Customer turnover, frequently referred to as "churn," is an important business metric in the telecommunications industry because it can have significant financial effects. Because we do not require customers to sign long-term commitments or pass a credit check, our service is available to a broader customer base than many other wireless providers and, as a result, some of our customers may be more likely to terminate service due to an inability to pay than the average industry customer. In addition, our rate of customer turnover may be affected by other factors, including the size of our calling areas, handset issues, customer care concerns, number portability and other competitive factors. Our strategies to address customer turnover may not be successful. A high rate of customer turnover would reduce revenues and increase the total marketing expenditures required to attract the minimum number of replacement customers required to sustain our business plan, which, in turn, could have a material adverse effect on our business, financial condition and results of operations.

Our operating costs can also increase substantially as a result of customer credit card and subscription fraud and dealer fraud. We have implemented a number of strategies and processes to detect and prevent efforts to defraud us, and we believe that our efforts have substantially reduced the types of fraud we have identified. However, if our strategies are not successful in detecting and controlling fraud in the future, it would have a material adverse impact on our financial

condition and results of operations.

**We Face Increasing Competition Which Could Have A Material Adverse Effect On Demand For The Cricket Service**

In general, the telecommunications industry is very competitive. Some competitors have announced rate plans substantially similar to the Cricket service plan (and have also introduced products that consumers perceive to be

## **Table of Contents**

similar to Cricket's service plan) in markets in which we offer wireless service. In addition, the competitive pressures of the wireless telecommunications market have caused other carriers to offer service plans with large bundles of minutes of use at low prices which are competing with the predictable and virtually unlimited Cricket calling plans. Some competitors also offer prepaid wireless plans that are being advertised heavily to demographic segments that are strongly represented in Cricket's customer base. These competitive offerings could adversely affect our ability to maintain our pricing and market penetration. Our competitors may attract more customers because of their stronger market presence and geographic reach. Potential customers may perceive the Cricket service to be less appealing than other wireless plans, which offer more features and options.

We compete as a mobile alternative to landline service providers in the telecommunications industry. Wireline carriers have begun to advertise aggressively in the face of increasing competition from wireless carriers, cable operators and other competitors. Wireline carriers are also offering unlimited national calling plans and bundled offerings that include wireless and data services. We may not be successful in our efforts to persuade potential customers to adopt our wireless service in addition to, or in replacement of, their current landline service.

Many competitors have substantially greater financial and other resources than we have, and we may not be able to compete successfully. Because of their size and bargaining power, our larger competitors may be able to purchase equipment, supplies and services at lower prices than we can. As consolidation in the industry creates even larger competitors, any purchasing advantages our competitors have may increase.

### **We Have Identified Material Weaknesses In Our Internal Control Over Financial Reporting, And Our Business And Stock Price May Be Adversely Affected If We Do Not Remediate All Of These Material Weaknesses, Or If We Have Other Material Weaknesses In Our Internal Control Over Financial Reporting**

In connection with their evaluation of our disclosure controls and procedures, our CEO and CFO concluded that certain material weaknesses in our internal control over financial reporting existed: (i) as of December 31, 2004, March 31, 2005 and June 30, 2005 with respect to turnover and staffing levels in our accounting, financial reporting and tax departments (arising in part in connection with the Company's now completed bankruptcy proceedings) and the preparation of our income tax provision, and (ii) as of December 31, 2004 and March 31, 2005 with respect to the application of lease-related accounting principles, fresh-start reporting oversight, and account reconciliation procedures. We believe we have adequately remediated the material weaknesses associated with lease accounting, fresh-start reporting oversight and account reconciliation procedures. For a description of the material weaknesses and the steps we are undertaking to remediate them, see Item 4. Controls and Procedures contained in Part I of this report. The existence of one or more material weaknesses could result in errors in our financial statements, and substantial costs and resources may be required to rectify any internal control deficiencies. If we cannot produce reliable financial reports, investors could lose confidence in our reported financial information, the market price of our stock could decline significantly, we may be unable to obtain additional financing to operate and expand our business, and our business and financial condition could be harmed.

### **Our Internal Control Over Financial Reporting Was Not Effective as of December 31, 2005, and Our Business May Be Adversely Affected if We Are Not Able to Implement Effective Control Over Financial Reporting**

Section 404 of the Sarbanes-Oxley Act of 2002 requires companies to do a comprehensive evaluation of their internal control over financial reporting. To comply with this statute, we are required to document and test our internal control over financial reporting; our management is required to assess and issue a report concerning our internal control over financial reporting; and our independent auditors are required to attest to and report on management's assessment. Reporting on our compliance with Section 404 of the Sarbanes-Oxley Act was first required in connection with the filing of our Annual Report on Form 10-K for the fiscal year ended December 31, 2005. We conducted a rigorous review of our internal control over financial reporting in order to become compliant with the requirements of

Section 404. The standards that must be met for management to assess our internal control over financial reporting are new and require significant documentation and testing. Our assessment identified the need for remediation of our internal control over financial reporting. Our internal control over financial reporting has been subject to certain material weaknesses in the past and is currently subject to material weaknesses related to

## **Table of Contents**

staffing levels and preparation of our income tax provision as described in Item 4. Controls and Procedures in Part I of this report. Our management concluded and our independent registered public accounting firm has attested and reported that our internal control over financial reporting was not effective as of December 31, 2005. If we are unable to implement effective control over financial reporting, investors could lose confidence in our reported financial information, we may be unable to obtain additional financing to operate and expand our business, and our business and financial condition could be harmed.

### **Our Primary Business Strategy May Not Succeed In The Long Term**

A major element of our business strategy is to offer consumers a service that allows them to make virtually unlimited calls within their Cricket service area and receive unlimited calls from any area for a flat monthly rate without entering into a long-term service commitment or passing a credit check. This strategy may not prove to be successful in the long term. From time to time, we also evaluate our service offerings and the demands of our target customers and may modify, change or adjust our service offerings or offer new services. We cannot assure you that these service offerings will be successful or prove to be profitable.

### **Our Indebtedness Could Adversely Affect Our Financial Health, And If We Fail To Maintain Compliance With The Covenants Under Our Senior Secured Credit Facilities, Any Such Failure Could Materially Adversely Affect Our Liquidity And Financial Condition**

As of July 31, 2005, we had approximately \$598 million of outstanding indebtedness and, to the extent we raise additional capital in the future, we expect to obtain much of such capital through debt financing. This existing indebtedness bears interest at a variable rate, but we have entered into interest rate swap agreements with respect to \$250 million of our debt as of June 30, 2005 and an additional \$105 million of our debt in July 2005, which mitigates the interest rate volatility. Our present and future debt financing could have important consequences. For example, it could:

- Increase our vulnerability to general adverse economic and industry conditions;

- Require us to dedicate a substantial portion of our cash flows from operations to payments on our indebtedness, thereby reducing the availability of our cash flows to fund working capital, capital expenditures, acquisitions and other general corporate purposes;

- Limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate; and

- Reduce the value of stockholders' investments in Leap because debt holders have priority regarding our assets in the event of a bankruptcy or liquidation.

In addition, the Credit Agreement governing our senior secured credit facilities contains restrictive covenants that limit our ability to engage in activities that may be in our long-term best interest. The Credit Agreement also contains various affirmative and negative covenants, including covenants that require us to maintain compliance with certain financial leverage and coverage ratios. Our failure to comply with any of these covenants could result in an event of default that, if not cured or waived, could result in the acceleration of all of our debt. Any such acceleration would have a material adverse affect on our liquidity and financial condition and on the value of the common stock of Leap. Our failure to timely file our Annual Report on Form 10-K for the year ended December 31, 2004 and our Quarterly Report on Form 10-Q for the period ended March 31, 2005 constituted defaults under the Credit Agreement. Although we were able to obtain a limited waiver of these defaults, we cannot assure you that we will be able to obtain a waiver in the future should a default occur.

**We Expect To Be Able To Incur Substantially More Debt; This Could Increase The Risks Associated With Our Leverage**

The covenants in our Credit Agreement allow us to incur substantial additional indebtedness in the future. If we incur additional indebtedness, the risks associated with our leverage could increase substantially.

**Table of Contents**

**The Wireless Industry Is Experiencing Rapid Technological Change, And We May Lose Customers If We Fail To Keep Up With These Changes**

The wireless communications industry is experiencing significant technological change, as evidenced by the ongoing improvements in the capacity and quality of digital technology, the development and commercial acceptance of wireless data services, shorter development cycles for new products and enhancements and changes in end-user requirements and preferences. The cost of implementing future technological innovations may be prohibitive to us, and we may lose customers if we fail to keep up with these changes.

**The Loss Of Key Personnel And Difficulty Attracting And Retaining Qualified Personnel Could Harm Our Business**

We believe our success depends heavily on the contributions of our employees and on maintaining our experienced workforce. We do not, however, generally provide employment contracts to our employees and the uncertainties associated with our bankruptcy and our emergence from bankruptcy have caused many employees to consider or pursue alternative employment. Since we announced reorganization discussions and filed for Chapter 11, we have experienced higher than normal employee turnover, including turnover of individuals at the chief executive officer, president and chief operating officer, senior vice president, vice president and other management levels. The loss of key individuals, and particularly the cumulative effect of such losses, may have a material adverse impact on our ability to effectively manage and operate our business.

**Risks Associated With Wireless Handsets Could Pose Product Liability, Health And Safety Risks That Could Adversely Affect Our Business**

We do not manufacture handsets or other equipment sold by us and generally rely on our suppliers to provide us with safe equipment. Our suppliers are required by applicable law to manufacture their handsets to meet certain governmentally imposed safety criteria. However, even if the handsets we sell meet the regulatory safety criteria, we could be held liable with the equipment manufacturers and suppliers for products we sell if they are later found to have design or manufacturing defects. We generally have indemnification agreements with the manufacturers who supply us with handsets to protect us from direct losses associated with product liability, but we cannot guarantee that we will be fully protected against all losses associated with a product that is found to be defective.

Media reports have suggested that the use of wireless handsets may be linked to various health concerns, including cancer, and may interfere with various electronic medical devices, including hearing aids and pacemakers. Certain class action lawsuits have been filed in the industry claiming damages for alleged health problems arising from the use of wireless handsets. In addition, interest groups have requested that the FCC investigate claims that wireless technologies pose health concerns and cause interference with airbags, hearing aids and other medical devices. The media has also reported incidents of handset battery malfunction, including reports of batteries that have overheated. Malfunctions have caused at least one major handset manufacturer to recall certain batteries used in its handsets, including batteries in a handset sold by Cricket and other wireless providers.

Concerns over radio frequency emissions and defective products may discourage the use of wireless handsets, which could decrease demand for our services. In addition, if one or more Cricket customers were harmed by a defective product provided to us by the manufacturer and subsequently sold in connection with our services, our ability to add and maintain customers for Cricket service could be materially adversely affected by negative public reactions.

There also are some safety risks associated with the use of wireless handsets while driving. Concerns over these safety risks and the effect of any legislation that has been and may be adopted in response to these risks could limit our ability to sell our wireless service.



**We Rely Heavily On Third Parties To Provide Specialized Services; A Failure By Such Parties To Provide The Agreed Services Could Materially Adversely Affect Our Business, Results Of Operations And Financial Condition**

We depend heavily on suppliers and contractors with specialized expertise in order for us to efficiently operate our business. In the past, our suppliers, contractors and third-party retailers have not always performed at the levels

## **Table of Contents**

we expect or at the levels required by their contracts. If key suppliers, contractors or third-party retailers fail to comply with their contracts, fail to meet our performance expectations or refuse to supply us in the future, our business could be severely disrupted. Generally, there are multiple sources for the types of products we purchase. However, some suppliers, including software suppliers, are the exclusive sources of their specific products. Because of the costs and time lags that can be associated with transitioning from one supplier to another, our business could be substantially disrupted if we were required to replace the products or services of one or more major, specialized suppliers with products or services from another source, especially if the replacement became necessary on short notice. Any such disruption could have a material adverse affect on our business, results of operations and financial condition.

### **We May Be Subject To Claims Of Infringement Regarding Telecommunications Technologies That Are Protected By Patents And Other Intellectual Property Rights**

Telecommunications technologies are protected by a wide array of patents and other intellectual property rights. As a result, third parties may assert infringement claims against us from time to time based on our general business operations or the specific operation of our wireless networks. We generally have indemnification agreements with the manufacturers and suppliers who provide us with the equipment and technology that we use in our business to protect us against possible infringement claims, but we cannot guarantee that we will be fully protected against all losses associated with an infringement claim. Whether or not an infringement claim was valid or successful, it could adversely affect our business by diverting management attention, involving us in costly and time-consuming litigation, requiring us to enter into royalty or licensing agreements (which may not be available on acceptable terms, or at all), or requiring us to redesign our business operations or systems to avoid claims of infringement.

A third party with a large patent portfolio has contacted us and suggested that we need to obtain a license under a number of its patents in connection with our current business operations. We understand that the third party has initiated similar discussions with other telecommunications carriers. We have begun to evaluate the third party's position but have not yet reached a conclusion as to the validity of its position. If we cannot reach a mutually agreeable resolution with the third party, we may be forced to enter into a licensing or royalty agreement with the third party. We do not currently expect that such an agreement would materially adversely affect our business, but we cannot provide assurance to our investors about the effect of any such license.

### **Regulation By Government Agencies May Increase Our Costs Of Providing Service Or Require Us To Change Our Services**

Our operations are subject to varying degrees of regulation by the FCC, the Federal Trade Commission, the Federal Aviation Administration, the Environmental Protection Agency, the Occupational Safety and Health Administration and state and local regulatory agencies and legislative bodies. Adverse decisions or regulations of these regulatory bodies could negatively impact our operations and costs of doing business. State regulatory agencies are increasingly focused on the quality of service and support that wireless carriers provide to their customers and several agencies have proposed or enacted new and potentially burdensome regulations in this area. Governmental regulations and orders can significantly increase our costs and affect our competitive position compared to other telecommunications providers. We are unable to predict the scope, pace or financial impact of regulations and other policy changes that could be adopted by the various governmental entities that oversee portions of our business.

### **If Call Volume Under Our Cricket Flat Price Plans Exceeds Our Expectations, Our Costs Of Providing Service Could Increase, Which Could Have A Material Adverse Effect On Our Competitive Position**

Cricket customers currently use their handsets approximately 1,500 minutes per month, and some markets are experiencing substantially higher call volumes. We own less spectrum in many of our markets than our competitors, but we design our networks to accommodate our expected high call volume, and we consistently assess and

implement technological improvements to increase the efficiency of our wireless spectrum. However, if future wireless use by Cricket customers exceeds the capacity of our networks, service quality may suffer. We may be forced to raise the price of Cricket service to reduce volume or otherwise limit the number of new customers, or incur substantial capital expenditures to improve network capacity.

## **Table of Contents**

We offer service plans that bundle certain features, long distance and virtually unlimited local service for a fixed monthly fee to more effectively compete with other telecommunications providers. If customers exceed expected usage, we could face capacity problems and our costs of providing the services could increase. Further, long distance rates and the charges for interconnecting telephone call traffic between carriers can be affected by governmental regulatory actions (and in some cases are subject to regulatory control) and, as a result, could increase with limited warning. If we are unable to cost-effectively provide our products and services to customers, our competitive position and business prospects could be materially adversely affected.

### **Future Declines In The Fair Value Of Our Wireless Licenses Could Result In Future Impairment Charges**

During the three months ended June 30, 2003, we recorded an impairment charge of \$171.1 million to reduce the carrying value of our wireless licenses to their estimated fair value. However, as a result of our adoption of fresh-start reporting under SOP 90-7, we increased the carrying value of our wireless licenses to \$652.6 million at July 31, 2004, the fair value estimated by management based in part on information provided by an independent valuation consultant. During the three months ended June 30, 2005, we recorded an impairment charge of \$11.4 million.

The market values of wireless licenses have varied dramatically over the last several years, and may vary significantly in the future. In particular, valuation swings could occur if:

consolidation in the wireless industry allowed or required carriers to sell significant portions of their wireless spectrum holdings;

a sudden large sale of spectrum by one or more wireless providers occurs; or

market prices decline as a result of the bidding activity in recently concluded or upcoming FCC auctions.

In addition, the price of wireless licenses could decline as a result of the FCC's pursuit of policies designed to increase the number of wireless licenses available in each of our markets. If the market value of wireless licenses were to decline significantly in the future, the value of our wireless licenses could be subject to non-cash impairment charges in the future. A significant impairment loss could have a material adverse effect on our operating income and on the carrying value of our wireless licenses on our balance sheet.

### **Declines In Our Operating Performance Could Ultimately Result In An Impairment Of Our Indefinite-Lived Assets, Including Goodwill, Or Our Long-Lived Assets, Including Property and Equipment**

We assess potential impairments to our long-lived assets, including property and equipment and certain intangible assets, when there is evidence that events or changes in circumstances indicate that the carrying value may not be recoverable. We assess potential impairments to indefinite-lived intangible assets, including goodwill and wireless licenses, annually and when there is evidence that events or changes in circumstances indicate that an impairment condition may exist. If we do not achieve our planned operating results, this may ultimately result in a non-cash impairment charge related to our long-lived and/or our indefinite-lived intangible assets. A significant impairment loss could have a material adverse effect on our operating results and on the carrying value of our goodwill or wireless licenses and/or our long-lived assets on our balance sheet.

### **Because Our Consolidated Financial Statements Reflect Fresh-Start Reporting Adjustments Made Upon Our Emergence From Bankruptcy, Financial Information In Our Current And Future Financial Statements Will Not Be Comparable To Our Financial Information From Periods Prior To Our Emergence From Bankruptcy**

As a result of adopting fresh-start reporting on July 31, 2004, the carrying values of our wireless licenses and our property and equipment, and the related depreciation and amortization expense, among other things, changed considerably from that reflected in our historical consolidated financial statements. Thus, our current and future balance sheets and results of operations will not be comparable in many respects to our balance sheets and consolidated statements of operations data for periods prior to our adoption of fresh-start reporting. You are not able to compare information reflecting our post-emergence balance sheet data, results of operations and changes in financial condition to information for periods prior to our emergence from bankruptcy, without making adjustments for fresh-start reporting.

**Table of Contents**

**Risks Related to Ownership of Our Common Stock**

**Our Stock Price May Be Volatile, And You May Lose All Or Some Of Your Investment**

The trading prices of the securities of telecommunications companies have been highly volatile. Accordingly, the trading price of our common stock is likely to be subject to wide fluctuations. Factors affecting the trading price of our common stock may include, among other things:

variations in our operating results;

announcements of technological innovations, new services or service enhancements, strategic alliances or significant agreements by us or by our competitors;

recruitment or departure of key personnel;

changes in the estimates of our operating results or changes in recommendations by any securities analysts that elect to follow our common stock; and

market conditions in our industry and the economy as a whole.

**The 17,198,252 Shares Of Our Common Stock Registered For Resale By Our Shelf Registration Statement on Form S-1 May Adversely Affect The Market Price Of Our Common Stock**

As of August 9, 2005, 60,876,871 shares of our common stock were issued and outstanding. Our resale shelf Registration Statement on Form S-1, which we expect to be declared effective in the near future, registered for resale 17,198,252 shares, or approximately 28.3%, of our outstanding common stock. We are unable to predict the potential effect that sales into the market of any material portion of such shares may have on the then prevailing market price of our common stock. We also have registered all shares of common stock that we may issue under our stock option, restricted stock and deferred stock unit plan. When we issue shares under the stock plan, they can be freely sold in the public market. If any of these holders cause a large number of securities to be sold in the public market, the sales could reduce the trading price of our common stock. These sales also could impede our ability to raise future capital.

**Our Directors and Affiliated Entities Have Substantial Influence Over Our Affairs**

Our directors and entities affiliated with them beneficially own in the aggregate approximately 28.5% of our common stock as of August 1, 2005. These stockholders have the ability to exert substantial influence over all matters requiring approval by our stockholders. These stockholders will be able to influence the election and removal of directors and any merger, consolidation or sale of all or substantially all of our assets and other matters. This concentration of ownership could have the effect of delaying, deferring or preventing a change in control or impeding a merger or consolidation, takeover or other business combination.

**Provisions In Our Amended And Restated Certificate Of Incorporation And Bylaws Or Delaware Law Might Discourage, Delay Or Prevent A Change In Control Of Our Company Or Changes In Our Management And Therefore Depress The Trading Price Of Our Common Stock**

Our amended and restated certificate of incorporation and bylaws contain provisions that could depress the trading price of our common stock by acting to discourage, delay or prevent a change in control of our company or changes in our management that the stockholders of Leap may deem advantageous. These provisions:

require super-majority voting to amend some provisions in our amended and restated certificate of incorporation and bylaws;

authorize the issuance of blank check preferred stock that our board of directors could issue to increase the number of outstanding shares to discourage a takeover attempt;

prohibit stockholder action by written consent, and require that all stockholder actions be taken at a meeting of our stockholders;

provide that the board of directors is expressly authorized to make, alter or repeal our bylaws; and

**Table of Contents**

establish advance notice requirements for nominations for elections to our board or for proposing matters that can be acted upon by stockholders at stockholder meetings.

Additionally, we are subject to Section 203 of the Delaware General Corporation Law, which generally prohibits a Delaware corporation from engaging in any of a broad range of business combinations with any interested stockholder for a period of three years following the date on which the stockholder became an interested stockholder and which may discourage, delay or prevent a change in control of our company.

**Item 4. Controls and Procedures.**

**(a) Evaluation of Disclosure Controls and Procedures**

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified by the SEC and that such information is accumulated and communicated to management, including its chief executive officer ( CEO ) and chief financial officer ( CFO ), as appropriate, to allow for timely decisions regarding required disclosure. Management, with participation by the Company's CEO and CFO, has designed the Company's disclosure controls and procedures to provide reasonable assurance of achieving the desired objectives. As required by SEC Rule 13a-15(b), in connection with filing this Amendment No. 1 on Form 10-Q/A, management again conducted an evaluation, with the participation of the Company's CEO and CFO, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of June 30, 2005, the end of the period covered by this report. Based upon that evaluation, the Company's CEO and CFO concluded that certain control deficiencies, each of which constituted a material weakness, as discussed below, existed in the Company's internal control over financial reporting as of June 30, 2005. As a result of the material weaknesses, the Company's CEO and CFO concluded that the Company's disclosure controls and procedures were not effective at the reasonable assurance level as of June 30, 2005.

The Company's CEO and CFO previously concluded that certain control deficiencies, each of which constituted a material weakness, as discussed below, existed in the Company's internal control over financial reporting as of December 31, 2004 and March 31, 2005. As a result of the material weaknesses, the Company's CEO and CFO concluded that the Company's disclosure controls and procedures were not effective at the reasonable assurance level as of December 31, 2004 and March 31, 2005.

The Company has performed additional analyses and procedures in order to conclude that its audited consolidated financial statements for the years ended December 31, 2005 and 2004, included in its Annual Report on Form 10-K for the year ended December 31, 2005, as well as its unaudited interim condensed consolidated financial statements included in this Quarterly Report on Form 10-Q/A and the Quarterly Report on Form 10-Q/A for the first quarter of fiscal 2005, were presented in accordance with accounting principles generally accepted in the United States of America for such financial statements. Accordingly, management believes that despite these material weaknesses, the Company's audited consolidated financial statements for the years ended December 31, 2005 and 2004, included in its Annual Report on Form 10-K for the year ended December 31, 2005, as well as its unaudited interim financial statements included in this Quarterly Report on Form 10-Q/A and the Quarterly Report on Form 10-Q/A for the first quarter ended March 31, 2005, reflect all adjustments necessary to state fairly the financial information set forth therein.

The material weaknesses and the steps the Company has taken to remediate the material weaknesses are described more fully as follows:



*Insufficient Staffing in the Accounting, Financial Reporting and Tax Functions.* As of June 30, 2005, March 31, 2005 and December 31, 2004, the Company did not maintain a sufficient complement of personnel with the appropriate skills, training and Company-specific experience to identify and address the application of generally accepted accounting principles in complex or non-routine transactions. Specifically, the Company has experienced staff turnover, and as a result, has experienced a lack of knowledge transfer to new employees within its accounting, financial reporting and tax functions. In addition, the Company does not have a full-time director of its tax function. Additionally, this control deficiency could result in a misstatement of accounts and disclosures that would result in a material misstatement to the Company's interim or annual consolidated financial statements that would not be

**Table of Contents**

prevented or detected. Accordingly, management has determined that this control deficiency constitutes a material weakness.

The Company believes that its insufficient complement of personnel and high turnover resulted, in large part, from (1) the significantly increased workload placed on its accounting and financial reporting staff during the Company's bankruptcy and the months after the Company's emergence from bankruptcy during which it was implementing fresh-start reporting, and (2) the departure of some staff members during the Company's bankruptcy and in the first several months after its emergence due to concerns about the Company's prospects.

The Company has taken the following actions to remediate the material weakness related to insufficient staffing in its accounting, financial reporting and tax functions:

The Company hired a new vice president, chief accounting officer in May 2005. This individual is a certified public accountant with over 19 years of experience as an accounting professional, including over 14 years of Big Four public accounting experience. He possesses a strong background in technical accounting and the application of generally accepted accounting principles.

The Company has hired a number of key accounting personnel since February 2005 that are appropriately qualified and experienced to identify and apply technical accounting literature, including several new directors and managers.

Based on the new leadership and management in the accounting department and on its identification of certain of the historical errors in the Company's accounting for income taxes, the Company believes that it has made substantial progress in addressing this material weakness as of December 31, 2005. However, this material weakness was not remediated as of such date. The Company expects that this material weakness will be fully remediated once it has filled the remaining key open management positions, including a full-time tax department leader, with qualified personnel and those personnel have had sufficient time in their positions.

This material weakness contributed to the following four control deficiencies, each of which is individually considered to be a material weakness.

*Errors in the Accounting for Income Taxes.* As of June 30, 2005, March 31, 2005 and December 31, 2004, the Company did not maintain effective controls over its accounting for income taxes. Specifically, the Company did not have adequate controls designed and in place to ensure the completeness and accuracy of the deferred income tax provision and the related deferred tax assets and liabilities and the related goodwill in conformity with generally accepted accounting principles. This control deficiency resulted in the restatement of the Company's consolidated financial statements for the five months ended December 31, 2004 and the consolidated financial statements for the two months ended September 30, 2004 and the quarters ended March 31, 2005, June 30, 2005 and September 30, 2005. Additionally, this control deficiency could result in a misstatement of accounts and disclosures that would result in a material misstatement to the Company's interim or annual consolidated financial statements that would not be prevented or detected. Accordingly, management has determined that this control deficiency constitutes a material weakness.

The Company has taken the following actions to remediate the material weakness related to its accounting for income taxes:

The Company has initiated a search for a qualified full-time tax department leader and continues to make this a priority. The Company has been actively recruiting for this position for several months, but has experienced difficulty in finding qualified applicants. Nevertheless, the Company is striving to fill the position as soon as

possible.

As part of its 2005 annual income tax provision, the Company improved its internal control over income tax accounting to establish detailed procedures for the preparation and review of the income tax provision, including review by the Company's chief accounting officer.

The Company used experienced qualified consultants to assist management in interpreting and applying income tax accounting literature and preparing the Company's 2005 annual income tax provision, and will continue to use such consultants in the future to obtain access to as much income tax accounting expertise as

**Table of Contents**

it needs. The Company recognizes, however, that a full-time tax department leader with appropriate tax accounting expertise is important for the Company to maintain effective internal controls on an ongoing basis.

As a result of the remediation initiatives described above, the Company identified certain of the errors that gave rise to the restatements of the consolidated financial statements for deferred income taxes.

The Company expects that the material weakness related to its accounting for income taxes will be remediated once it has hired a full-time leader of the tax department, that person has had sufficient time in his or her position, and the Company demonstrates continued accurate and timely preparation of its income tax provisions.

*Errors in the Application of Lease-Related Accounting Principles.* In the first few months of 2005, the Company identified errors in assumptions that resulted in the incorrect accounting for rent expense and remediation obligations associated with its leases for periods ending on or before December 31, 2004. Additionally, this control deficiency could result in a misstatement of accounts and disclosures that would result in a material misstatement to the Company's interim or annual consolidated financial statements that would not be prevented or detected. Accordingly, management has determined that this control deficiency constitutes a material weakness.

The Company took the following actions between February 2005 and the filing of the Company's Annual Report on Form 10-K for the year ended December 31, 2004 in May 2005 to remediate this material weakness:

reviewed the terms of over 2,500 cell-site, switch and other leases and re-assessed lease term assumptions to assure proper accounting for the rent expense and asset retirement obligations with respect to these leases;

corrected the errors identified in its condensed consolidated interim financial statements for the one and seven month periods ended July 31, 2004 and the two month period ended September 30, 2004;

changed its internal control over financial reporting to identify the procedures to follow for appropriate lease accounting; and

educated accounting department personnel regarding correct lease accounting procedures.

The Company used its revised controls over lease accounting in connection with the preparation of the unaudited interim condensed consolidated financial statements for the first and second quarters of fiscal 2005. Based upon its implementation and application of the revised controls, the Company believes that it has adequately remediated this material weakness as of June 30, 2005.

*Fresh-Start Reporting Adjustments.* In preparing for its 2004 annual audit, the Company identified several errors resulting from inadequate oversight of the fresh-start reporting adjustments recorded as of July 31, 2004 in connection with the Company's emergence from bankruptcy. The Company believes these errors occurred as a result of the substantial additional workload on its accounting staff in connection with fresh-start reporting and the insufficient staffing levels and the associated lack of knowledge transfer to new employees within these functions as described above. The Company determined that as of July 31, 2004 it overstated deferred rent and certain vendor obligations which should have been eliminated as a result of the emergence from bankruptcy and the implementation of fresh-start reporting. Additionally, this control deficiency could result in a misstatement of accounts and disclosures that would result in a material misstatement to the Company's interim or annual consolidated financial statements that would not be prevented or detected. Accordingly, management has determined that this control deficiency constitutes a material weakness.

The Company took the following actions between February 2005 and the filing of the Company's Annual Report on Form 10-K for the year ended December 31, 2004 in May 2005 with respect to its fresh-start reporting to remediate this material weakness:

reviewed the fresh-start reporting adjustments made in connection with the Company's emergence from bankruptcy; and

corrected the errors identified in its unaudited interim condensed consolidated financial statements for the one and seven month periods ended July 31, 2004.

**Table of Contents**

In addition to the aforementioned steps, the Company implemented new procedures for the review of its remaining obligations arising from fresh-start reporting, including review of the account analyses for all significant accruals related to fresh-start reporting by the Company's chief accounting officer and controller. As of the end of the second quarter of fiscal 2005, the remaining material obligations relate to taxes owed to various taxing jurisdictions as of the Company's emergence from bankruptcy. Based on these review procedures, the Company believes that the remaining accruals for these liabilities are appropriate and that the Company has adequately remediated this material weakness as of June 30, 2005.

*Inadequate Account Reconciliation Procedures.* In preparing for its 2004 annual audit, the Company identified errors that resulted from inadequate reconciliation of deferred revenue that should have been recognized as service revenue. In addition, with the implementation of fresh-start reporting, the Company's investments were re-valued at fair market value but the Company did not have the reconciliation procedures in place to separately track the gains and losses on such investments subsequent to the implementation of fresh-start reporting. Additionally, this control deficiency could result in a misstatement of accounts and disclosures that would result in a material misstatement to the Company's interim or annual consolidated financial statements that would not be prevented or detected. Accordingly, management has determined that this control deficiency constitutes a material weakness.

The Company took the following actions between February 2005 and the filing of the Company's Annual Report on Form 10-K for the year ended December 31, 2004 in May 2005 to address this material weakness:

established and communicated additional procedures for the analysis, review and approval of account reconciliations;

instituted procedures requiring supervisory personnel to review and approve all account reconciliations; and

corrected the related errors identified in its condensed consolidated interim financial statements for the one and seven month periods ended July 31, 2004 and the two month period ended September 30, 2004.

Since May 2005 and through the filing of the Company's Quarterly Report on Form 10-Q/A for the second quarter of fiscal 2005, the Company has closely followed its new procedures, and believes that all financial statement accounts have been properly reconciled on a timely basis and that the reconciliations have been reviewed and approved by appropriate managers and/or directors. In addition, the Company has implemented procedures under which the chief accounting officer and controller monitors this process and confirms that all account reconciliations have been completed and reviewed by accounting management in a timely manner. These controls have been fully documented and evaluated for design effectiveness as part of the Company's Sarbanes-Oxley Section 404 internal control assessment. As a result of these improved control activities, the Company believes that it has adequately remediated this material weakness as of June 30, 2005.

**(b) Changes in Internal Control Over Financial Reporting**

Apart from the changes to the Company's internal control over financial reporting described above with respect to the application of lease-related accounting principles, fresh-start reporting adjustments and account reconciliation procedures, there were no other changes in the Company's internal control over financial reporting during the Company's fiscal quarter ended June 30, 2005 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**Table of Contents****PART II  
OTHER INFORMATION****Item 6. Exhibits.***Index to Exhibits:*

<b>Exhibit Number</b>	<b>Description of Exhibit</b>
4.2.1(1)	Amendment No. 1 to Registration Rights Agreement dated as of June 7, 2005 by and among Leap Wireless International, Inc., MHR Institutional Partners II LP, MHR Institutional Partners IIA LP and Highland Capital Management, L.P.
10.1(2)#	Form of Restricted Stock Award Grant Notice and Restricted Stock Award Agreement (February 2008 Vesting).
10.2(2)#	First Amendment to Amended and Restated Executive Employment Agreement, effective as of June 17, 2005, between the Company and S. Douglas Hutcheson.
10.3(2)#	Form of Restricted Stock Award Grant Notice and Restricted Stock Award Agreement (Five-Year Vesting).
10.4(3)#	Form of Deferred Stock Unit Award Grant Notice and Deferred Stock Unity Award Agreement.
10.5(2)#	Form of Stock Option Grant Notice and Non-Qualified Stock Option Agreement (February 2008 Vesting).
10.6(2)#	Form of Stock Option Grant Notice and Non-Qualified Stock Option Agreement (Five-Year Vesting).
10.7.1(4)#	Form of Restricted Stock Award Grant Notice and Restricted Stock Award Agreement, dated as of July 8, 2005, between the Company and David B. Davis.
10.7.2(4)#	Form of Restricted Stock Award Grant Notice and Restricted Stock Award Agreement, dated as of July 8, 2005, between the Company and Robert J. Irving, Jr.
10.7.3(4)#	Form of Restricted Stock Award Grant Notice and Restricted Stock Award Agreement, dated as of July 8, 2005, between the Company and Leonard C. Stephens.
10.7.4(4)#	Agreement, dated as of July 8, 2005, between the Company and Harvey P. White.
10.11.2(1)	Amendment No. 2, dated June 24, 2005, to the Credit Agreement, dated as of December 22, 2004, among Cricket Communications, Inc., Alaska Native Broadband 1 License, LLC and Alaska Native Broadband 1, LLC.
10.14.4(5)	Letter from Cricket Communications, Inc. to the Lenders under the Credit Agreement, dated as of January 10, 2005, among the Company, Bank of America, N.A., Goldman Sachs Credit Partners L.P., Credit Suisse First Boston and the other lenders party thereto, dated April 12, 2005.
10.14.5(6)	Amendment No. 1 to the Credit Agreement among Cricket Communications, Inc., Leap Wireless International, Inc., the lenders party to the Credit Agreement and Bank of American, N.A., as agent, dated as of July 22, 2005.
10.14.6(6)	Amendment No. 2 to the Credit Agreement among Cricket Communications, Inc., Leap Wireless International, Inc., the lenders party to the Credit Agreement and Bank of American, N.A., as agent, dated as of July 22, 2005.
31.1*	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32\*\* Certifications of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

\* Filed herewith.

\*\* These certifications are being furnished solely to accompany this quarterly report pursuant to 18 U.S.C. § 1350, and are not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and are not to be incorporated by reference into any filing of Leap Wireless International, Inc., whether made before or after the date hereof, regardless of any general incorporation language in such filing.



**Table of Contents**

Portions of this exhibit (indicated by asterisks) have been omitted pursuant to a request for confidential treatment pursuant to Rule 24b-2 under the Securities Exchange Act of 1934.

# Management contract or compensatory plan or arrangement in which one or more executive officers or directors participates.

- (1) Filed as an exhibit to Leap's Registration Statement on Form S-1 (File No. 333-126246), as filed with the SEC on June 30, 2005, and incorporated herein by reference.
- (2) Filed as an exhibit to Leap's Current Report on Form 8-K, dated June 17, 2005, as filed with the SEC on June 23, 2005, and incorporated herein by reference.
- (3) Filed as an exhibit to Leap's Current Report on Form 8-K, dated January 5, 2005, as filed with the SEC on January 11, 2005, and incorporated herein by reference.
- (4) Filed as an exhibit to Leap's Current Report on Form 8-K, dated July 8, 2005, as filed with the SEC on July 14, 2005, and incorporated herein by reference.
- (5) Filed as an exhibit to Leap's Current Report on Form 8-K, dated April 12, 2005, as filed with the SEC on April 13, 2005, and incorporated herein by reference.
- (6) Filed as an exhibit to Leap's Current Report on Form 8-K, dated July 22, 2005, as filed with the SEC on July 2, 2005, and incorporated herein by reference.

**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this Amendment No. 1 to Quarterly Report on Form 10-Q/A to be signed on its behalf by the undersigned thereunto duly authorized.

LEAP WIRELESS INTERNATIONAL, INC.

Date: April 19, 2006

By: /s/ S. Douglas Hutcheson  
S. Douglas Hutcheson  
Chief Executive Officer and President  
(Principal Executive Officer)

Date: April 19, 2006

By: /s/ Dean M. Luvisa  
Dean M. Luvisa  
Vice President, Finance and  
Acting Chief Financial Officer  
(Principal Financial Officer)