

LIGHTBRIDGE INC
Form 10-K/A
February 17, 2006

Table of Contents

SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
Form 10-K/A
(Amendment No. 1)
FOR ANNUAL AND TRANSITION REPORTS PURSUANT TO
SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

(Mark One)

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

For the fiscal year ended December 31, 2004

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: 000-21319

Lightbridge, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware

(State or Other Jurisdiction of Incorporation or Organization)

04-3065140

(I.R.S. Employer Identification No.)

30 Corporate Drive
Burlington, Massachusetts

(Address of Principal Executive Offices)

01803

(Zip Code)

(781) 359-4000

(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act:

common stock, \$.01 par value per share

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes No

The aggregate market value of the voting common stock held by nonaffiliates of the registrant as of June 30, 2004 was \$146,254,634 based on a total of 26,116,899 shares held by nonaffiliates and on a closing price of \$5.60 as reported on The Nasdaq Stock Market (National Market System).

The number of shares of common stock outstanding as of March 11, 2005 was 26,585,455.

DOCUMENTS INCORPORATED BY REFERENCE

The registrant intends to file a definitive proxy statement pursuant to Regulation 14A with regard to its 2005 annual meeting of stockholders or special meeting in lieu thereof on or before April 30, 2005. Certain portions of such proxy statement are incorporated by reference in Part III of this Form 10-K/A.

Table of Contents

EXPLANATORY NOTE
RESTATEMENT OF CONSOLIDATED FINANCIAL STATEMENTS

This Amendment No. 1 on Form 10-K/A, which amends and restates items identified below with respect to our Form 10-K for the fiscal year ended December 31, 2004, filed with the Securities and Exchange Commission (the SEC) on March 17, 2005 (the Original Filing), is being filed to reflect the restatement of our financial statements for the fiscal year ended December 31, 2004. In separate filings, we will restate our financial statements for the quarterly periods ended March 31, 2005, June 30, 2005 and September 30, 2005. The first three quarterly periods of fiscal 2005 are referred to herein as the 2005 Quarters.

During the fiscal 2005 year end close process, we determined that, historically, the deferred income tax liability for the book and income tax basis difference in goodwill and trademarks as a result of our acquisition of Authorize.Net Corporation in 2004 was incorrectly offset against the deferred income tax assets in considering the size of the valuation allowance that was required. In accordance with Statement of Financial Accounting Standards No. 142,

Goodwill and Other Intangible Assets , the deferred tax liability that arises as our goodwill and trademarks are amortized for tax purposes must be considered as a liability related to an asset with an indefinite life. Accordingly, the deferred tax liability was not available as a source of future taxable income to offset the future deductions or benefits embedded in the deferred tax assets created by other deductible temporary timing differences. Accordingly, the increase in the tax valuation allowance should have been recorded (exclusive of the deferred tax liability for non-amortizing goodwill and trademarks) in the year ended December 31, 2004 and the 2005 Quarters. Therefore we have recorded additional deferred tax expense of \$1.3 million to increase our deferred tax liability as of December 31, 2004. See Note 2, Restatement of Financial Statements in the Notes to Consolidated Financial Statements for further details. The additional deferred tax expense in the 2005 Quarters will be set forth in detail in amendments to the related Quarterly Reports to be filed on Form 10-Q/A as soon as possible.

This Form 10-K/A only amends and restates certain information in Items 6, 7, 8, and 9A of Part II and Item 15 of Part IV of the Original Filing, in each case solely as a result of and to reflect the restatement. In addition, Item 15 of Part IV of the Original Filing has been amended to include an updated consent of our independent registered public accounting firm and certifications executed as of the date of this Form 10-K/A from our Chief Executive Officer and Chief Financial Officer as required by Sections 302 and 906 of the Sarbanes-Oxley Act of 2002. The consent of our independent registered public accounting firm and the certifications of the Chief Executive Officer and Chief Financial Officer are attached to this Form 10-K/A as exhibits 23.1, 31.1, 31.2 and 32.

Except for the foregoing amended and restated information, this Form 10-K/A continues to describe conditions as of the date of the Original Filing, and the disclosures contained herein have not been updated to reflect events, results or developments that have occurred after the Original Filing, or to modify or update those disclosures affected by subsequent events. Among other things, forward looking statements made in the Original Filing have not been revised to reflect events, results or developments that have occurred or facts that have become known to us after the date of the Original Filing (other than the restatement), and such forward looking statements should be read in their historical context.

TABLE OF CONTENTS

| | Page |
|---|-------------|
| <u>PART II</u> | |
| <u>Item 6.</u> <u>Selected Financial Data</u> | 4 |
| <u>Item 7.</u> <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 5 |
| <u>Item 8.</u> <u>Financial Statements and Supplementary Data</u> | 34 |
| <u>Item 9A.</u> <u>Controls and Procedures</u> | 34 |
| <u>PART IV</u> | |
| <u>Item 15.</u> <u>Exhibits and Financial Statement Schedules</u> | 38 |
| <u>Signatures</u> | 43 |
| <u>Ex-23.1 Consent of Deloitte & Touche LLP</u> | |
| <u>Ex-31.1 Sect. 302 Certification of the C.E.O.</u> | |
| <u>Ex-31.2 Sect. 302 Certification of the C.F.O.</u> | |
| <u>Ex-32.1 Sect. 906 Certification of the C.E.O. & C.F.O.</u> | |

THIS ANNUAL REPORT ON FORM 10-K/A CONTAINS FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF SECTION 27A OF THE SECURITIES ACT OF 1933 AND SECTION 21E OF THE SECURITIES EXCHANGE ACT OF 1934. ANY STATEMENTS CONTAINED HEREIN THAT ARE NOT STATEMENTS OF HISTORICAL FACT MAY BE DEEMED TO BE FORWARD-LOOKING STATEMENTS. WITHOUT LIMITING THE FOREGOING, THE WORDS BELIEVES, ANTICIPATES, PLANS, EXPECTS AND SIMILAR EXPRESSIONS ARE INTENDED TO IDENTIFY FORWARD-LOOKING STATEMENTS. THE FORWARD-LOOKING STATEMENTS INVOLVE KNOWN AND UNKNOWN RISKS, UNCERTAINTIES AND OTHER FACTORS, INCLUDING THE FACTORS SET FORTH BELOW IN ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS RISK FACTORS, THAT MAY CAUSE THE ACTUAL RESULTS, PERFORMANCE AND ACHIEVEMENTS OF LIGHTBRIDGE, INC. TO DIFFER MATERIALLY FROM THOSE INDICATED BY THE FORWARD-LOOKING STATEMENTS. LIGHTBRIDGE, INC. UNDERTAKES NO OBLIGATION TO UPDATE ANY FORWARD-LOOKING STATEMENTS IT MAKES.

Table of Contents**PART II****Item 6. Selected Financial Data**

The following selected financial data have been derived from the Company's audited historical consolidated financial statements, certain of which are included elsewhere in this Annual Report on Form 10-K/A. The following selected financial data should be read in conjunction with the Company's consolidated financial statements and related notes and Management's Discussion and Analysis of Financial Condition and Results of Operations appearing elsewhere in this Annual Report on Form 10-K/A.

The following selected financial data includes the results of operations, from the date of acquisition, of Authorize.Net Corporation, which the Company acquired on March 31, 2004. See Note 1 to the Company's consolidated financial statements for further information concerning this acquisition.

| | 2004 | Years Ended Dec. 31, | | | |
|--|---|-----------------------------|-------------|-------------|-------------|
| | Restated | 2003 | 2002 | 2001 | 2000 |
| | (1) | | | | |
| | (In thousands, except per share amounts) | | | | |
| Statement of Operations Data: | | | | | |
| Revenues | \$ 133,055 | \$ 119,978 | \$ 133,438 | \$ 176,616 | \$ 186,644 |
| Cost of revenues | 67,890 | 61,949 | 65,943 | 80,811 | 81,732 |
| Gross profit | 65,165 | 58,029 | 67,495 | 95,805 | 104,912 |
| Operating expenses: | | | | | |
| Engineering and development costs | 29,000 | 28,426 | 29,269 | 32,259 | 29,256 |
| Sales and marketing | 22,541 | 14,239 | 13,270 | 20,460 | 22,159 |
| General and administrative | 15,987 | 14,143 | 18,170 | 19,517 | 17,955 |
| Restructuring costs | 4,346 | 5,079 | 3,616 | 4,000 | |
| Impairment of goodwill and other intangible assets | 2,263 | | | | |
| Purchased in-process research and development | 679 | | 1,618 | | |
| Gain on sale of Fraud Centurion assets | (2,673) | | | | |
| Amortization of goodwill and acquired workforce | | | | | 502 |
| Merger related costs | | | | 5,999 | |
| Total operating expenses | 72,143 | 61,887 | 65,943 | 82,235 | 69,872 |
| Income (loss) from operations | (6,978) | (3,858) | 1,552 | 13,570 | 35,040 |
| Interest income | 1,185 | 1,778 | 2,439 | 4,233 | 5,446 |
| Equity in loss of partnership investment | | (471) | (464) | | |
| Income (loss) before income taxes | (5,793) | (2,551) | 3,527 | 17,803 | 40,486 |
| | 9,612 | (1,102) | (103) | 3,848 | 9,974 |

Provision for (benefit from) income
taxes

| | | | | | |
|-----------------------------------|-------------|------------|----------|-----------|-----------|
| Net income (loss) | \$ (15,405) | \$ (1,449) | \$ 3,630 | \$ 13,955 | \$ 30,512 |
| Basic earnings (loss) per share | \$ (0.58) | \$ (0.05) | \$ 0.13 | \$ 0.50 | \$ 1.12 |
| Diluted earnings (loss) per share | \$ (0.58) | \$ (0.05) | \$ 0.13 | \$ 0.48 | \$ 1.04 |

Table of Contents

| | 2004 Restated (1) | 2003 | December 31, 2002 | 2001 | 2000 |
|---|-------------------------|------------|----------------------|------------|------------|
| | (In thousands) | | | | |
| Balance Sheet Data: | | | | | |
| Cash, cash equivalents and short-term investments | \$ 51,625 | \$ 133,488 | \$ 133,470 | \$ 118,570 | \$ 98,743 |
| Working capital | \$ 42,997 | \$ 137,684 | \$ 136,501 | \$ 127,129 | \$ 109,672 |
| Total assets | \$ 170,486 | \$ 177,836 | \$ 180,672 | \$ 188,882 | \$ 187,680 |
| Long-term obligations, less current portion | \$ 149 | \$ 33 | \$ 259 | \$ 667 | \$ 963 |
| Stockholders' equity | \$ 135,667 | \$ 154,503 | \$ 159,641 | \$ 161,522 | \$ 144,986 |

(1) The financial statements as of December 31, 2004 and for the fiscal year ended December 31, 2004, have been restated. During the fiscal 2005 year end close process, the Company determined that, historically, the deferred income tax liability for the book and income tax basis difference in goodwill and trademarks as a result of the Authorize.Net acquisition in 2004 was incorrectly offset against deferred income tax assets. As a result Company has recorded additional deferred tax expense of \$1.3 million to increase its deferred tax liability as of December 31, 2004. See Note 2, Restatement of Financial Statements in the Notes to Financial Statements for further details.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations
Restatement of Financial Statements

During the fiscal 2005 year end close process, we determined that, historically, the deferred income tax liability for the book and income tax basis difference in goodwill and trademarks as a result of the Authorize.Net acquisition in 2004 was incorrectly offset against deferred income tax assets in considering the size of the valuation allowance that was required. In accordance with Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets, the deferred tax liability that arises as our goodwill and trademarks are amortized for tax purposes must be considered as a liability related to an asset with an indefinite life. Accordingly, the deferred tax liability was not available as a source of future taxable income to offset the future deductions or benefits embedded in the deferred tax assets created by other deductible temporary timing differences; and the increase in the tax valuation allowance should have been recorded exclusive of the deferred tax liability for non-amortizing goodwill and trademarks in the year ended December 31, 2004. Therefore, we have recorded additional deferred tax expense of \$1.3 million to increase its deferred tax liability as of December 31, 2004.

We have restated our December 31, 2004 balance sheet and our fiscal 2004 statements of operations for the impact of this deferred tax liability. Its impact in the balance sheet, income statement, and deferred tax valuation allowance are as follows:

| | December 31, 2004 | |
|----------------------------|------------------------------|-------------|
| | As previously reported | As restated |
| BALANCE SHEET DATA: | | |
| Deferred tax liability | \$ | \$ 1,261 |
| Total liabilities | 33,558 | 34,819 |
| Accumulated deficit | (10,072) | (11,333) |

| | | |
|----------------------------|---------|---------|
| Total stockholders' equity | 136,928 | 135,667 |
|----------------------------|---------|---------|

STATEMENT OF OPERATIONS DATA:

| | | |
|-------------------------------------|-----------|-----------|
| Income tax expense | \$ 8,351 | \$ 9,612 |
| Net income (loss) | (14,144) | (15,405) |
| Net income (loss) per common share: | | |
| Basic and Diluted | \$ (0.53) | \$ (0.58) |

| | | |
|---|----------|----------|
| DEFERRED TAX VALUATION ALLOWANCE | (24,703) | (25,964) |
|---|----------|----------|

There was no impact on net cash provided by operating, financing, or investing activities on the statements of cash flows.

Table of Contents**Critical Accounting Policies and Estimates**

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of this Annual Report on Form 10-K/A requires us to make estimates and assumptions that affect the reported amount of assets and liabilities, disclosure of contingent assets and liabilities at the date of our financial statements, and the reported amounts of revenue and expenses during the reporting period. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily derived from other sources. There can be no assurance that actual amounts will not differ from those estimates.

We have identified the policies below as critical to our business operations and the understanding of our results of operations.

Revenue Recognition. Our revenue recognition policy is significant because revenue is a key component affecting our operations. In addition, revenue recognition determines the timing of certain expenses, such as commissions and bonuses. Certain judgments relating to the elements required for revenue recognition affect the application of our revenue policy. Revenue results are difficult to predict, and any shortfall in revenue, change in judgments concerning recognition of revenue, change in mix, amount of international sales or delay in recognizing revenue could cause operating results to vary significantly from quarter to quarter.

Allowance for Doubtful Accounts. We must also make estimates of the collectibility of our accounts receivable. An increase in the allowance for doubtful accounts is recorded when the prospect of collecting a specific account receivable becomes doubtful. We analyze accounts receivable and historical bad debts, customer creditworthiness, current domestic and international economic trends and changes in our customer payment terms when evaluating the adequacy of the allowance for doubtful accounts. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, or if our estimates of uncollectibility prove to be inaccurate, additional allowances would be required.

Income Taxes and Deferred Taxes. Our income tax policy records the estimated future tax effects of temporary differences between the tax bases of assets and liabilities and the amounts reported in the accompanying consolidated balance sheets, as well as operating loss and tax credit carryforwards. We assess the recoverability of any tax assets recorded on the balance sheet and provide any necessary valuation allowances as required. If we were to determine that it was more likely than not that we would be unable to realize all or part of our net deferred tax asset in the future, an adjustment to the valuation allowance against the deferred tax asset would be charged to operations in the period that such determination was made.

Restructuring Estimates. Restructuring-related liabilities include estimates for, among other things, anticipated disposition of lease obligations. Key variables in determining such estimates include anticipated commencement of sublease rentals, estimates of sublease rental payment amounts and tenant improvement costs and estimates for brokerage and other related costs. We periodically evaluate and, if necessary, adjust our estimates based on currently available information.

Goodwill and Acquired Intangible Assets. We recorded goodwill of \$1.7 million and \$57.6 million in connection with the acquisitions of Altawave, Inc. (Altawave) and Authorize.Net, respectively and we recorded other intangible assets of \$23.3 million in connection with the acquisition of Authorize.Net. We are required to test such goodwill for impairment on at least an annual basis. We have adopted January 1st and March 31st as the dates of the annual impairment tests for Altawave and Authorize.Net, respectively. Application of the goodwill impairment test requires judgment, including the identification of reporting units, assigning assets and liabilities to reporting units, assigning goodwill to reporting units, and determining the fair value of each reporting unit. Significant judgments required to estimate the fair value of reporting units include estimating future cash flows, determining appropriate discount rates and other assumptions. Changes in these estimates and assumptions could materially affect the determination of fair value for each reporting unit. We will assess the impairment of goodwill on an annual basis or more frequently if other indicators of impairment arise.

Table of Contents

Overview

We develop, market and support a suite of products and services for merchants that sell products and services online and communications providers, including payment processing, customer acquisition and qualification, risk management, prepaid billing, instant teleconferencing, and authentication services.

A majority of our revenues historically have been derived from clients located in the United States. Our revenues are derived from transaction services, consulting and maintenance services, software licensing and hardware.

Our transaction service revenues are derived primarily from the processing of applications for qualification of subscribers for telecommunications services, the activation of services for those subscribers and from the processing of payment transactions for merchants. We have expanded our telecommunications transactions offerings from credit evaluation services to include screening for subscriber fraud, evaluating carriers' existing accounts, interfacing with carrier and third-party systems and providing call center services. We also offer transaction services to screen and authenticate the identity of users engaged in online transactions. Our transaction-based solutions provide multiple, remote, systems access for workflow management, along with centrally managed client-specified business policies, and links to client and third-party systems. Transaction services are provided through contracts with carriers and others, which specify the services to be utilized and the markets to be served. Our clients are charged for these services on a per transaction basis. Pricing varies depending primarily on the volume and type of transactions, the number and type of other products and services selected for integration with the services and the term of the contract under which services are provided. The volume of transactions processed varies depending on seasonal and retail trends, the success of the carriers and others utilizing our services in attracting subscribers and the markets served by our clients. Transaction revenues are recognized in the period in which the services are performed.

Transaction services revenues related to payment processing are derived from our credit card processing and eCheck processing services, and other services (collectively, payment processing services) gateway fees and set-up fees. Payment processing services revenue is based on a fee per transaction and is recognized in the period in which the transaction occurs. Gateway fees are monthly subscription fees charged to our merchant customers for the use of our payment gateway. Gateway fees are recognized in the period in which the service is provided. Set-up fees represent one-time charges for initiating our payment processing services. Although these fees are generally paid to us at the commencement of the agreement, they are recognized ratably over the estimated average life of the merchant relationship, which is determined through a series of analyses of active and deactivated merchants. Commissions paid to outside sales partners are recorded in sales and marketing expense in our statements of operations.

We also offer instant voice conferencing transaction services through our GroupTalk offering. No significant revenues have been recognized from our GroupTalk offering to date and the Instant Conferencing business segment is not expected to generate significant revenues in 2005.

Our consulting revenues are derived principally from providing solution development and deployment services and business advisory consulting in the areas of customer acquisition and retention, authentication, prepay billing and risk management. The majority of consulting engagements are performed on a time and materials basis and revenues from these engagements are generally recognized as the services are performed. When we perform work under a fixed fee arrangement, revenues are generally recognized as services are performed. Revenues from software maintenance contracts are recognized ratably over the term of the maintenance agreement.

Our software licensing revenues consist of revenues attributable to the licensing of our CAS Application Modules and PrePay billing software. The PrePay billing system allows carriers to market and manage prepaid wireless services to customers. Prepay is licensed as a packaged software product and each product generally requires incidental customization or integration with other products and systems to varying degrees. Software licensing revenues are recognized when persuasive evidence of an arrangement exists, delivery of the product has been made, and a fixed fee and collectibility have been determined. Our hardware revenues historically have been derived in connection with sales of our PrePay and PhonePrint products. Revenue from hardware is recognized upon shipment, unless testing, integration or other services are required, in which case it is recognized upon commissioning and acceptance of the product. Revenue from hardware sold in conjunction with software is deferred until the software revenue is recognized.

In 2004, we determined that we would no longer actively market or sell our Retail Management System (RMS) product or our PhonePrint product. In October 2004, we completed the sale of certain assets related to our Fraud Centurion software product to Subex. As a result of these actions, we do not expect to recognize significant future revenues from these products.

Table of Contents

In 2003 and 2004, the rate of subscriber growth in the wireless telecommunications industry declined. We believe, based in part on reports of wireless telecommunications industry analysts, that the rate of subscriber growth will continue to slow in upcoming years. We also believe we may continue to experience changes in the combination of services acquired by clients and that competitive pricing pressures will continue to negatively affect transaction revenues in 2005. We do not expect significant growth in capital spending in the telecommunications industry in 2005. In order to add to our business, we are seeking to expand our reach in the e-commerce and payment processing business markets and to target industry sectors in the TDS business we do not currently serve.

On February 22, 2002, we acquired all of the assets and certain of the liabilities of Altawave in exchange for the payment of \$4.0 million in cash, plus up to an additional \$6.0 million contingent on the achievement of certain revenue goals in 2002 and 2003. No contingent payments were required to be made in connection with the Altawave acquisition. The technology acquired from Altawave included solutions to offer wireless carriers a service platform for the development and management of data content and applications (Mobile Data Manager). Certain of Altawave's technology was used to develop our GroupTalk product.

In December 2003, we entered into an agreement to lease approximately 80,000 square feet in a single building in Burlington, Massachusetts for our new principal administrative, sales, consulting, operations marketing and product development facility for our TDS business. The lease was executed and delivered in January 2004. In February 2004, we announced the planned expansion of our call center operations to Liverpool, Nova Scotia, Canada. Our Nova Scotia facility became operational in the second quarter of 2004.

On March 31, 2004, we acquired all of the outstanding stock of Authorize.Net from InfoSpace Inc., for \$81.6 million in cash and incurred approximately \$2.0 million in acquisition related transaction costs. Authorize.Net is a provider of payment solutions for online customer transactions. The Authorize.Net payment gateway provides credit card and electronic check solutions to companies that process orders for goods and services over the Internet. Authorize.Net connects small and medium sized businesses to large credit card processors and banking organizations, allowing those businesses to accept electronic payments.

On January 28, 2005, we closed our call center facility in Broomfield, Colorado. The Broomfield, Colorado call center facility had been supporting our TDS operating segment. The work being performed at the facility was transitioned to our other call center facilities. In conjunction with the closure, we expect to record a restructuring charge of approximately \$0.9 million in the first quarter of 2005, primarily relating to facility closing costs and employee severance and termination benefits.

We plan to close our Fremont, California facility, where our Instant Conferencing business is located, effective March 31, 2005. In connection with the closure, we expect to record a restructuring charge in the first quarter of 2005 of approximately \$0.3 million primarily relating to employee severance and termination benefits. We expect to continue to provide the services for GroupTalk, our Instant Conferencing product, under our agreement with AOL.

Operating Segments

As a result of our corporate reorganization efforts during 2004, we changed our previously reported operating segments effective in the fourth quarter of 2004. All prior period segment financial information has been restated to conform to the current presentation. Based upon the way financial information is provided to our chief operating decision maker, the Chief Executive Officer, for use in evaluating allocation of resources and assessing performance of the business, we now report our operations in four distinct operating segments: Payment Processing Services (Payment Processing), Telecom Decisioning Services (TDS), Intelligent Network Solutions (INS) and Instant Conferencing Services (Instant Conferencing).

The Payment Processing segment offers a transaction processing system, under the Authorize.Net® brand, that allows businesses to authorize, settle and manage credit card, electronic check and other electronic payment transactions online. The TDS segment provides customer qualification, risk assessment, fraud screening, consulting services and call center services to telecommunications and other companies. The INS segment provides wireless carriers with a real-time rating engine for voice, data and IN services for prepaid subscribers as well as postpaid charging functionality and telecom calling card services. The Instant Conferencing segment provides managed instant conferencing services through our GroupTalk™ product. In 2005, we made the decision to no longer actively market or sell our GroupTalk™ product. We expect to continue to provide the services for GroupTalk under our agreement

with AOL. Within these four segments, performance is measured based on revenue, gross profit and operating income (loss) realized from each segment. There are no transactions between segments.

We do not allocate certain corporate or centralized marketing and general and administrative expenses to our business unit segments, because these activities are managed separately from the business units. Also, we do not allocate restructuring expenses and other non-recurring gains or charges to our business unit segments because our Chief Executive Officer evaluates the segment results exclusive of these items. Asset information by operating segment is not reported to or reviewed by our Chief Executive Officer and therefore we have not disclosed asset information for each operating segment.

Table of Contents

The historical operating results associated with our RMS product, which we no longer actively market or sell, are included in our TDS segment. The historical operating results associated with our PhonePrint product, which we no longer actively market or sell, and our Fraud Centurion products, which we sold to Subex in 2004, are included in our INS segment. The historical operating results associated with our Mobile Data Manager product, which we no longer actively market or sell, are included in our Instant Conferencing segment.

Customer Concentration

During fiscal 2004, three of our clients each accounted for more than 10% of our total revenues. In 2003 and 2002, four of our clients each accounted for more than 10% of our total revenues. Revenues from these clients, as a percentage of total revenues, were as follows:

| | Years Ended Dec. 31, | | |
|----------|-----------------------------|-------------|-------------|
| | 2004 | 2003 | 2002 |
| Sprint | 21% | 28% | 30% |
| AT&T | 16 | 21 | 21 |
| Ericsson | * | 14 | 15 |
| Nextel | 11 | 12 | 11 |
| | | | |
| Total | 48% | 75% | 77% |

* Represents less than 10% of total revenues in 2004.

We expect that a significant portion of our revenues will continue to come from a relatively small number of telecommunications clients in 2005, although the companies that comprise our largest clients in any given quarter may vary. Customer concentration is likely to decline if our revenues from Payment Processing Services grow. Our revenues, margins and net income may fluctuate significantly from quarter to quarter based on the actions of a single significant client. A client may take actions that significantly affect us for reasons that we cannot necessarily anticipate or control, such as reasons related to the client's financial condition, changes in the client's business strategy or operations, the introduction of alternative competing products or services, acquisitions or as the result of the perceived quality or cost-effectiveness of our products or services. In November 2004, we announced that we expected that our future revenues from AT&T will decline significantly as a result of the acquisition of AT&T by Cingular Wireless LLC. As a result of the acquisition, AT&T's customer activations will transition from our system to Cingular's internal system and we do not expect that AT&T will be a significant customer in 2005. Our services agreements with Sprint and Nextel expire on December 31, 2006. On December 15, 2004, Sprint and Nextel announced that their respective Boards of Directors had approved a definitive agreement for a merger of the two companies. We are unable to predict the effect of the merger of Nextel and Sprint on our relationship with either customer including, without limitation, the timing or extent of any reductions in applications processed or other services provided under our contracts with those customers. It is possible that Sprint or Nextel could elect not to renew their agreements, to reduce the volume of products and services they purchase from the Company or to request significant changes to the pricing or other terms in any renewal agreement. Additionally, a significant portion of our revenues from our PrePay billing system is generated through distribution agreements with Ericsson and Nortel Networks. A loss of one or more of these major clients, a decrease in orders by one or more of these clients or a change in the combination of products and services they obtain from us would adversely affect our revenues, margins and net income.

Table of Contents**Results of Operations****Year Ended December 31, 2004 Compared with Year Ended December 31, 2003**

Revenues. Revenues and certain revenues comparisons for the years ended December 31, 2004 and 2003 were as follows:

| | Year Ended December 31, 2004 | Year Ended December 31, 2003 | \$ Difference | % Difference |
|-------------------------------------|---|---|--------------------------|-------------------------|
| | (Dollars in thousands) | | | |
| Transaction services | \$ 103,648 | \$ 80,552 | \$ 23,096 | 28.7% |
| Consulting and maintenance services | 19,898 | 28,666 | (8,768) | (30.6) |
| Software licensing and hardware | 9,509 | 10,760 | (1,251) | (11.6) |
| Total | \$ 133,055 | \$ 119,978 | \$ 13,077 | 10.9% |

The increase in transaction services revenues was due primarily to the acquisition of Authorize.Net on March 31, 2004, which contributed \$26.8 million of revenue for the period from April 1, 2004 to December 31, 2004. Authorize.Net's revenues for the period from April 1, 2004 to December 31, 2004 have increased 25% compared to the same period in 2003, as reported by Authorize.Net's former owner, InfoSpace, Inc. The increased revenues are the result of an increase in the number of merchant customers and increased volume of transactions processed. The increased revenue related to the acquisition of Authorize.Net was partially offset by a decline in transactions services revenues in our TDS segment. The decline in TDS transaction services revenues was a result of lower transaction fees charged to certain clients as a result of competitive pricing pressures and an unfavorable change in the mix of services provided despite a 4% increase in the volume of subscriber applications processed during 2004. TDS transaction services revenues in 2004 included approximately \$0.5 million related to a settlement received as a result of the WorldCom, Inc. bankruptcy proceedings, for services provided to WorldCom, Inc. in 2002. We did not recognize revenue at the time the services were performed due to concerns regarding the collectibility of our fees.

In the near term, we expect transaction services revenue from Authorize.Net to continue to increase. However, we expect transaction services revenue associated with our TDS segment to decline from the 2004 level as a result of Cingular Wireless LLC's acquisition of AT&T and its decision to process all credit applications through Cingular's internal system, and continued price pressures. We do not expect Cingular/ AT&T Wireless to contribute significant revenues in 2005. In 2004, \$16.9 million in transaction services revenue was associated with AT&T. We expect TDS transaction services revenues to continue to reflect the industry's rate of growth of new subscribers as well as the rate of switching among carriers by subscribers (subscriber churn). While we experienced growth in the number of applications processed in 2004 as compared to 2003, we believe that transaction revenues in future periods will continue to be impacted by changes in the demand for our transaction offerings, changes in the combination of services purchased by clients, carrier consolidation including the proposed merger of Sprint and Nextel, and competitive pricing pressures.

The decrease in consulting and maintenance services revenues of \$8.8 million for 2004 was principally due to a decline in consulting and maintenance revenues related to our decision to no longer actively market, sell or develop our RMS and PhonePrint products and the sale of our Fraud Centurion product. Consulting and maintenance services revenues associated with these products were \$4.3 million lower in 2004 than in the preceding year. Additionally, maintenance revenues related to our PrePay software product suite declined \$2.9 million in 2004 as compared with the prior year as a result of pricing pressures, but an increase in consulting revenues during the same period related to this product partially mitigated this impact. In our TDS segment, pricing pressures on maintenance services and a reduced level of consulting activity also contributed to the revenue decrease.

We expect consulting and maintenance services revenue associated with our PrePay software product suite in 2005 to continue at a similar level as 2004. However, we expect our total consulting and maintenance services revenue in 2005 to decrease in comparison with the 2004 level, as we do not expect significant future revenues from our RMS or Fraud Centurion products. These products contributed \$4.8 million in consulting and maintenance services revenues in 2004. In addition, we recorded \$3.7 million in consulting and maintenance revenues associated with AT&T in 2004, and we do not expect significant revenues from this customer in future periods.

The decline in software licensing and hardware revenues of \$1.3 million in 2004 as compared to 2003 was due to our decision to no longer actively market sell or develop our RMS and PhonePrint products, which contributed \$1.7 million less in revenue than in the previous year. In addition, while the total revenues associated with our PrePay product remained largely unchanged, revenue associated with new software licenses and subscriber growth license fees increased, and revenue associated with hardware sales decreased.

Table of Contents

We expect software licensing and hardware revenues in 2005 to be lower than those in 2004, as a result of the discontinued marketing of our RMS and PhonePrint products and the sale of our Fraud Centurion product. In 2004, we recorded software licensing and hardware revenue of \$1.8 million associated with these products. We expect the level of capital spending by carriers to continue to affect the sales of our PrePay product in future quarters. Our PrePay software clients' growth rates for net new subscribers continue to impact the level of our growth fee license revenue, and hardware revenues are largely a function of the number of PrePay software license sales and the number of subscribers each new system sold will support.

Cost of Revenues and Gross Profit. Cost of revenues consists primarily of personnel costs, costs of resold third party hardware, software and services, costs of maintaining systems and networks used in processing qualification and activation transactions (including depreciation and amortization of systems and networks) and amortization of capitalized software and acquired technology. Cost of revenues for Authorize.Net, included in transaction services cost of revenues, consists of expenses associated with the delivery, maintenance and support of Authorize.Net's products and services, including personnel costs, communication costs, such as high-bandwidth Internet access, server equipment depreciation, transactional processing fees, as well as customer care costs. In the future, cost of revenues may vary as a percentage of total revenues as a result of a number of factors, including changes in the volume of transactions processed, changes in the mix of transaction revenues between those from automated transaction processing and those from processing transactions through our TeleServices call centers, changes in pricing to certain clients and changes in the mix of total revenues among transaction services revenues, consulting and maintenance services revenues, and software licensing and hardware revenues.

Cost of revenues, gross profit and certain comparisons for the years ended December 31, 2004 and 2003 were as follows:

| | Year Ended December 31, 2004 | Year Ended December 31, 2003 | \$ Difference | % Difference |
|--|---|---|--------------------------|-------------------------|
| | (Dollars in thousands) | | | |
| Cost of revenues: | | | | |
| Transaction services | \$ 54,831 | \$ 45,667 | \$ 9,164 | 20.1% |
| Consulting and maintenance services | 9,930 | 12,741 | (2,811) | (22.1) |
| Software licensing and hardware | 3,129 | 3,541 | (412) | (11.6) |
| | | | | |
| Total cost of revenues | \$ 67,890 | \$ 61,949 | \$ 5,941 | 9.6% |
| | | | | |
| Gross profit: | | | | |
| Transaction services | \$ 48,817 | \$ 34,885 | \$ 13,932 | 39.9% |
| Transaction services % | 47.1% | 43.3% | | |
| Consulting and maintenance services \$ | \$ 9,968 | \$ 15,925 | \$ (5,957) | (37.4)% |
| Consulting and maintenance services % | 50.1% | 55.6% | | |
| Software licensing and hardware \$ | \$ 6,380 | \$ 7,219 | \$ (839) | (11.6)% |
| Software licensing and hardware % | 67.1% | 67.1% | | |
| | | | | |
| Total gross profit | \$ 65,165 | \$ 58,029 | \$ 7,136 | 12.3% |

| | | |
|----------------------|-------|-------|
| Total gross profit % | 49.0% | 48.4% |
|----------------------|-------|-------|

Transaction services cost of revenues increased by \$9.2 million in 2004 from 2003. Costs of revenues associated with our Authorize.Net business were included in our results beginning in the second quarter of 2004 because of the acquisition of Authorize.Net on March 31, 2004. This change accounted for \$7.2 million of the spending increase in 2004 from 2003. In our TDS business, spending increased in our call centers as a result of the addition of a significant new client in the second half of 2003. Generally, cost of revenue from automated transaction processing tends to be lower than costs of revenue from processing transactions through our TeleServices call centers. This increase was partially offset by reduced costs of maintaining systems and networks used in processing qualification and activation transactions. In addition, included in transaction cost of revenues for 2004 was a one-time benefit of approximately \$0.2 million realized by us as part of the settlement of the WorldCom, Inc. bankruptcy, related to the release from liability for certain telecommunications services which we received from WorldCom, Inc. Transaction services gross profit and gross profit percentage increased primarily as a result of the acquisition of Authorize.Net on March 31, 2004. Authorize.Net contributed \$19.6 million to the 2004 transaction services gross profit amount. This was partially offset by a decrease in the 2004 transaction services gross profit related to our TDS segment. Authorize.Net generates a higher gross profit percentage than our TDS segment, resulting in increased transaction services gross profit percentage in 2004 in comparison to 2003.

Table of Contents

Consulting and maintenance services cost of revenues decreased by \$2.8 million in 2004. This decrease was attributable to a reduction in headcount associated with the June 2003, January 2004 and September 2004 restructurings, reduced use of contract labor primarily for consulting related to our RMS product, and the sale of our Fraud Centurion product to Subex. Consulting and maintenance services gross profit and gross profit percentage decreased in 2004 due to lower revenues related to our RMS, Fraud Centurion and PhonePrint products, as well as competitive pricing pressures.

Software licensing and hardware cost of revenues decreased slightly by \$0.4 million in 2004 in comparison with 2003. This decrease was primarily attributable to the mix of software products licensed during 2004 as compared to the prior year. The 2004 software licensing and hardware cost of revenue is more reflective of average historical and expected future software licensing and hardware cost of revenues than the cost in 2003. Software licensing and hardware gross profit decreased in 2004 in absolute dollars as a result of lower revenues, but gross profit percentage remained consistent with 2003. The gross profit percentage earned can vary significantly based on discounts given on individual transactions and the mix of software and hardware revenues.

We expect that fluctuations in gross profit may occur in future periods primarily because of a change in the mix of revenue generated from our three revenue components, and also because of competitive pricing pressures.

Operating Expenses. Operating expenses and certain operating expense comparisons for the years ended December 31, 2004 and 2003 were as follows:

| | Year Ended December 31, 2004 | Year Ended December 31, 2003 | \$ Difference | % Difference |
|---|---|---|--------------------------|-------------------------|
| | (Dollars in thousands) | | | |
| Engineering and development | \$ 29,000 | \$ 28,426 | \$ 574 | 2.0% |
| Sales and marketing | 22,541 | 14,239 | 8,302 | 58.3 |
| General and administrative | 15,987 | 14,143 | 1,844 | 13.0 |
| Restructuring | 4,346 | 5,079 | (733) | (14.4) |
| Impairment of goodwill | 1,664 | | 1,664 | |
| Impairment of other intangible assets | 599 | | 599 | |
| Purchased in-process research and development | 679 | | 679 | |
| Gain on sale of Fraud Centurion assets | (2,673) | | (2,673) | |
| Total | \$ 72,143 | \$ 61,887 | \$ 10,256 | 16.6% |

Engineering and Development. Engineering and development expenses include software development costs, consisting primarily of personnel and outside technical service costs related to developing new products and services, enhancing existing products and services, and implementing and maintaining new and existing products and services. The \$0.6 million increase in engineering and development expenses for 2004 as compared with 2003 was primarily due to the addition of Authorize.Net, the expenses from which are included in our results beginning on April 1, 2004. Authorize.Net represented \$3.2 million of engineering and development expenses in the 2004 year's results. This increase was largely offset by cost savings associated with the June 2003, September 2004 and October 2004 restructurings, our decision to cease new development and enhancement of our RMS software product, and our sale of the Fraud Centurion product to Subex. Engineering and development expenses as a percentage of total revenues decreased for 2004 as a result of increased revenues.

We expect engineering and development expenses for the quarter ending March 31, 2005 to be slightly higher than in the previous quarter as a result of an increased level of funded development activity associated with our PrePay software product.

Sales and Marketing. Sales and marketing expenses consist primarily of salaries, commissions and travel expenses of direct sales and marketing personnel, as well as costs associated with advertising, trade shows and conferences. For Authorize.Net, sales and marketing expenses also include commissions paid to outside sales partners. The increase in sales and marketing expenses in 2004, in absolute dollars and as a percentage of revenue, was due to the addition of Authorize.Net and the related sales partner commissions included in sales and marketing expense. Authorize.Net represented \$10.1 million of sales and marketing expenses in the 2004 results. This increase was partially offset by reductions in marketing costs for the other portions of our business as a result of reduced marketing headcount and program spending as compared with 2003.

We expect that sales and marketing expenses in the first quarter of 2005 will remain consistent with the fourth quarter of 2004. In future quarters, we expect sales and marketing expenses to increase with growth in Authorize.Net's revenues as a result of sales partner commissions associated with these revenues.

Table of Contents

General and Administrative. General and administrative expenses consist principally of salaries of executive, finance, human resources and administrative personnel and fees for certain outside professional services. The increase in general and administrative costs in 2004 was primarily due to the inclusion of Authorize.Net expenditures beginning on April 1, 2004. Authorize.Net represented approximately \$2.6 million of general and administrative expenses in 2004. In addition, during 2004, we incurred approximately \$0.9 million in separation costs associated with the resignation our former President and Chief Executive Officer in August 2004. We also incurred increased general and administrative expense as a result of increased regulatory and compliance requirements. These increases were offset by a one-time benefit in 2004 of approximately \$1.0 million related to the release from liability of amounts that had been reserved for potential claims against us related to the WorldCom, Inc. bankruptcy proceedings, by savings associated with the January 2004 and September 2004 restructuring activity, and by reductions in program spending.

We expect general and administrative expenses in the quarter ending March 31, 2005 to continue to be greater than the corresponding quarter of 2004 primarily due to the inclusion of Authorize.Net's general and administrative expenses and increased regulatory and compliance costs.

Restructuring. A discussion of restructuring charges recorded during 2004 and 2003 is contained in the separate Restructurings section below.

Impairment of Intangible Assets. On January 1, 2005, we performed the annual impairment test for the goodwill balance of approximately \$1.7 million related to our acquisition of Altavave in 2002. We used the discounted cash flow methodology to determine the fair value of the reporting unit related to these intangible assets. The discounted cash flow methodology is based upon converting expected cash flows to present value. Our assumptions and methodology in determining the fair value of the reporting unit were reviewed by an independent appraiser. A comparison of the resulting fair value of the reporting unit to its carrying amount, including goodwill, indicated that the goodwill and remaining other intangible assets of approximately \$0.6 million were fully impaired. As a result, a goodwill impairment charge of approximately \$1.7 million and an other intangible asset impairment charge of approximately \$0.6 million were recorded in our Consolidated Statement of Operations in 2004.

Purchased In-Process Research and Development (IPR&D). In connection with the Authorize.Net acquisition, we recorded a \$0.7 million charge during the first quarter of 2004 for two IPR&D projects. The Authorize.Net technology includes payment gateway solutions that enable merchants to authorize, settle and manage electronic transactions via the Internet, at retail locations and on wireless devices. The research projects in process at the date of acquisition related to the development of the Card Present Solution (CPS) and the Fraud Tool (FT). Development on the FT project and the CPS project was started at the end of 2003 and the beginning of 2004, respectively. The complexity of the CPS technology lies in its fast, flexible and redundant characteristics. The complexity of the FT technology lies in its responsiveness to changing fraud dynamics and efficiency.

The value of the projects was determined by an independent appraiser using the income method. The discounted cash flow method was utilized to estimate the present value of the expected income that could be generated through revenues from the projects over their estimated useful lives through 2009. The percentage of completion for the projects was determined based on the amount of research and development expenses incurred through the date of acquisition as a percentage of estimated total research and development expenses to bring the projects to technological feasibility. At the acquisition date, we estimated that the CPS and the FT projects were approximately 15% and 80% complete, respectively, with fair values of approximately \$638,000 and \$41,000, respectively. The discount rate used for the fair value calculation was 30% for the CPS project and 22% for the FT project. At the date of acquisition, development of the technology involved risks to us including the remaining development effort required to achieve technological feasibility and uncertainty with respect to the market for the technology.

We completed the development of the FT in May 2004 having spent approximately \$129,000 on the project after the acquisition. Total cost to complete the CPS project after acquisition is estimated to be approximately \$650,000. The CPS project is expected to be completed by September 2005. If the development of the technology is not completed on schedule, the potential consequences to us may include increased development costs and increased competition from other companies that have competitive products in the market.

Gain on Sale of Fraud Centurion Assets. On October 1, 2004, we closed the sale of our Fraud Centurion products pursuant to an agreement with India-based Subex. We received net cash proceeds of \$2.4 million as a result of the sale. As part of this transaction, we sold equipment with a net book value of approximately \$0.2 million to Subex and assigned the customer maintenance contracts to Subex. The liabilities for deferred revenue related to these contracts as of the closing date totaled \$0.5 million. We recorded a gain of approximately \$2.7 million in the fourth quarter of 2004 related to this transaction.

Interest Income. Interest income consists of earnings on our cash and short-term investment balances. Interest income decreased to \$1.2 million in 2004 from \$1.8 million in 2003. This decrease was primarily due to a decline in our cash and short-term investments balance as a result of the payment of the purchase price for the acquisition of Authorize.Net.

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| | | | | |
|--------------------------|-----------|-----------|------------|---------|
| INS \$ | \$ 8,790 | \$ 11,630 | \$ (2,840) | (24.4)% |
| INS % | 50.1% | 55.5% | | |
| Instant Conferencing \$ | \$ (225) | \$ | \$ (225) | % |
| Instant Conferencing % | (58.9)% | % | | |
| | | | | |
| Total gross profit \$ | \$ 65,165 | \$ 58,029 | \$ 7,136 | 12.3% |
| | | | | |
| Total gross profit % | 49.0% | 48.4% | | |
| | | | | |
| Operating Income (Loss): | | | | |
| TDS | \$ 16,188 | \$ 22,025 | \$ (5,837) | (26.5)% |
| Payment Processing | 3,560 | | 3,560 | |
| INS | (4,014) | (2,541) | (1,473) | (58.0) |
| Instant Conferencing | (4,309) | (3,536) | (773) | (21.9) |

Table of Contents

| | Year Ended December 31, 2004 | Year Ended December 31, 2003 | \$ Difference | % Difference |
|--------------------------------|---|---|--------------------------|-------------------------|
| Total segment operating income | \$ 11,425 | \$ 15,948 | \$ (4,523) | (28.4)% |
| Reconciling items(1) | (18,403) | (19,806) | | |
| Total operating loss | \$ (6,978) | \$ (3,858) | | |

- (1) Reconciling items consist of certain corporate or centralized marketing and general and administrative expenses not allocated to our business unit segments, because these activities are managed separately from the business units. Also, we do not allocate restructuring expenses and other non-recurring gains or charges to our business unit segments because our Chief Executive Officer evaluates the segment results exclusive of these items.

Revenues by Operating Segment

TDS. The decline in TDS revenues was a result of lower transaction fees charged to certain clients as a result of competitive pricing pressures, a decrease in the level of consulting activity, and an unfavorable change in the mix of services provided despite a 4% increase in the volume of subscriber applications processed during 2004. TDS transaction services revenues for the quarter ended September 30, 2004 included approximately \$0.5 million related to a settlement received, as a result of the WorldCom, Inc. bankruptcy proceedings, for services provided to WorldCom, Inc. in 2002. We did not recognize revenue at the time the services were performed because of concerns regarding the collectibility of our fees.

Payment Processing. Lightbridge began recording Payment Processing revenues as of April 1, 2004 following the acquisition of Authorize.Net on March 31, 2004. Authorize.Net's revenues for the period from April 1, 2004 to December 31, 2004 have increased 25% compared to the same period in 2003, as reported by Authorize.Net's former owner, InfoSpace, Inc. The increased revenues are the result of an increase in the number of merchant customers and increased volume of transactions processed.

INS. Revenues decreased by \$3.4 million in 2004 as compared with 2003 as a result of the sale of our Fraud Centurion products pursuant to an agreement with India-based Subex on October 1, 2004 and as a result of pricing pressures on maintenance fees related to our PrePay products.

Instant Conferencing. In 2004, we recorded revenues of \$0.4 million related to a contract for our Mobile Data Manager product. No future revenues from the Mobile Data Manager product are expected. In 2004, we did not record any revenues from our GroupTalk product.

Gross Profit (Loss) by Operating Segment

TDS. The decline in TDS gross profit was a result of lower transaction fees charged to certain clients as a result of competitive pricing pressures, a decrease in the level of consulting activity, and an unfavorable change in the mix of services provided despite a 4% increase in the volume of subscriber applications processed during 2004, partially offset by spending reductions associated with reduced depreciation expense in our data center operations and with our September 2004 restructuring activities.

Payment Processing. Lightbridge began recording Payment Processing results as of April 1, 2004 following the acquisition of Authorize.Net on March 31, 2004. We expect gross profit generated by our Payment Processing Segment to represent a larger portion of our total gross profit in 2005 as compared with 2004.

INS. The reduction in INS gross profit is largely the result of pricing pressures on maintenance fees associated with our PrePay product line.

Instant Conferencing. The decline in Instant Conferencing gross profit reflects spending to support our relationship with AOL, which began using the product in the second quarter of 2004.

Operating Income (Loss) by Operating Segment.

TDS. The decline in TDS operating income reflects the impact of reduced revenues, partially offset by spending reductions resulting from our January 2004 and September 2004 restructuring activities. In addition, 2004 results include a one-time benefit of approximately \$1.0 million related to the release from liability of amounts that had been reserved for potential claims against us related to the WorldCom, Inc. bankruptcy proceedings.

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| | | | | |
|-------------------------------------|-----------|-----------|------------|--------|
| Cost of revenues: | | | | |
| Transaction services | \$ 45,667 | \$ 49,194 | \$ (3,527) | (7.2)% |
| Consulting and maintenance services | 12,741 | 13,663 | (922) | (6.7) |
| Software licensing and hardware | 3,541 | 3,086 | 455 | 14.7 |
| | | | | |
| Total cost of revenues | \$ 61,949 | \$ 65,943 | \$ (3,994) | (6.1)% |

Table of Contents

| | Year Ended December 31, 2003 | Year Ended December 31, 2002 | \$ Difference | % Difference |
|--|---|---|--------------------------|-------------------------|
| (Dollars in thousands) | | | | |
| Gross profit: | | | | |
| Transaction services \$ | \$ 34,885 | \$ 39,182 | \$ (4,297) | (11.0)% |
| Transaction services % | 43.3% | 44.3% | | |
| Consulting and maintenance services \$ | \$ 15,925 | \$ 18,828 | \$ (2,903) | (15.4)% |
| Consulting and maintenance services % | 55.6% | 57.9% | | |
| Software licensing and hardware \$ | \$ 7,219 | \$ 9,485 | \$ (2,266) | (23.9)% |
| Software licensing and hardware % | 67.1% | 75.5% | | |
| | | | | |
| Total gross profit \$ | \$ 58,029 | \$ 67,495 | \$ (9,466) | (14.0)% |
| | | | | |
| Total gross profit % | 48.4% | 50.6% | | |

Transaction services cost of revenues decreased in 2003 from the prior year principally because of lower transaction revenues as a result of a lower volume of transactions processed through our TeleServices call centers and a decrease in costs attributable to our staff reductions. Transaction services cost of revenues was also affected by a shift in the combination of services acquired by clients during the year ended December 31, 2003. The decrease in transaction services gross profit percentage was due to a change in the combination of services acquired by clients in the year ended December 31, 2003, as well as the level of our fixed costs which resulted in lower gross profit percentage as revenues declined. Certain of these fixed costs were eliminated or reduced as a result of our restructurings in 2002 and 2003.

Consulting and maintenance services cost of revenues decreased in 2003 from the prior year and gross profit percentage decreased slightly in 2003. The decrease in consulting and maintenance services cost of revenue was attributable to a decrease in consulting projects and revenue as well as a reduction in headcount associated with the June 2002 restructuring.

Software licensing and hardware cost of revenues increased in 2003 compared to 2002. The decrease in software licensing and hardware gross profit percentage was attributable to the type of software products licensed during 2003 and as a result of lower software licensing revenue levels.

Operating Expenses. Operating expenses and certain operating expense comparisons for the years ended December 31, 2003 and 2002 were as follows:

| | Year Ended December 31, 2003 | Year Ended December 31, 2002 | \$ Difference | % Difference |
|---|---|---|--------------------------|-------------------------|
| (Dollars in thousands) | | | | |
| Engineering and development | \$ 28,426 | \$ 29,269 | \$ (843) | (2.9)% |
| Sales and marketing | 14,239 | 13,270 | 969 | 7.3 |
| General and administrative | 14,143 | 18,170 | (4,027) | (22.2) |
| Restructuring | 5,079 | 3,616 | 1,463 | 40.5 |
| Purchased in-process research and development | | 1,618 | (1,618) | (100.0) |

| | | | | |
|-------|-----------|-----------|------------|--------|
| Total | \$ 61,887 | \$ 65,943 | \$ (4,056) | (6.2)% |
|-------|-----------|-----------|------------|--------|

Engineering and Development. The decrease in engineering and development expenses in 2003 was primarily due to cost savings associated with the June 2002 and 2003 restructurings. Development expenses as a percentage of total revenues increased in 2003 as a result of lower revenue levels.

Sales and Marketing. The increase in sales and marketing expenses in 2003 was primarily due to the expansion of our business development organization and costs associated with our strategic partnerships and key initiatives.

General and Administrative. The decrease in general and administrative costs in 2003 was primarily due to a decrease in headcount associated with the June 2002 and June 2003 restructurings and our efforts to limit spending.

Restructuring. A discussion of restructuring charges recorded during 2003 and 2002 is set forth in the separate Restructurings section below.

Table of Contents

In-Process Research and Development (IPR&D). In connection with the Altawave acquisition, we recorded a \$1.6 million charge during the first quarter of 2002 for several IPR&D projects. The technology acquired from Altawave includes solutions that offer wireless carriers and enterprises a service platform for the development and management of data content and applications. The complexity of the technology lies in its comprehensive, secure and scalable characteristics. The research projects in process at the date of acquisition related to the development of the Lightbridge Mobile Data Manager (MDM) suite of products consisting of MDM Server, MDM Administration, MDM Altalinks and MDM Provisioner, as well as the Consumer Group Applications (CGA). Development of the technology was started in 2000.

The value of the projects was determined by an independent appraiser using the income approach. The discounted cash flow method was utilized to estimate the present value of the expected income that could be generated through revenues from the projects over their estimated useful lives through 2009. The percentage of completion for the projects was determined based on the amount of research and development expenses incurred through the date of acquisition as a percentage of estimated total research and development expenses to bring the projects to technological feasibility. At the acquisition date, we estimated that the MDM suite and CGA were approximately 70% and 32% complete, respectively, with fair values of approximately \$1.0 million and \$0.6 million, respectively. The discount rate used for the fair value calculation was 37% for the MDM suite and 40% for CGA. At the date of acquisition, development of the technology involved risks to us including the remaining development effort required to achieve technological feasibility and uncertainty with respect to the market for the technology. We completed the development of the MDM suite in the quarter ended September 30, 2002 and the CGA project in the quarter ended September 30, 2003 having spent approximately \$150,000 and \$300,000, respectively, on the projects after the acquisition.

Interest Income. Interest income decreased by 27.1% to \$1.8 million in the year ended December 31, 2003 from \$2.4 million in the prior year. This decrease was primarily due to a decline in interest rates.

Equity in Loss of Partnership Investment. In June 2001, we committed to invest up to \$5.0 million in a limited partnership that invested in businesses within the wireless industry. We used the equity method of accounting for this limited partnership investment. For the year ended December 31, 2002, our proportionate share of the loss of the limited partnership was \$0.5 million. In July 2003, the partners agreed to dissolve the partnership. Accordingly, future commitments were eliminated, and the remaining \$0.5 million investment was written off in the quarter ended June 30, 2003.

Provision for (Benefit from) Income Taxes. Our effective tax rate was 43.2% and (2.9)% for the years ended December 31, 2003 and 2002, respectively. The 2003 tax provision reflects a benefit of \$1.1 million, which was based upon the annual effective tax rate of 33.0%, as well as a \$0.3 million tax benefit from prior years' research and development tax credits. As of December 31, 2003, we had approximately \$11.7 million in loss carryforwards, principally the result of various acquisitions, and \$8.3 million of other deferred tax assets, against which a valuation reserve of approximately \$12.1 million had been provided. Net deferred tax assets were approximately \$7.8 million at December 31, 2003. We recorded a net benefit from income taxes in 2003 due primarily to the net loss before income taxes and the impact of a refund of prior years' research and development tax credits.

Results by Operating Segment. Certain operating results and comparisons by operating segment for the years ended December 31, 2003 and 2002 are as follows:

| | Year Ended December 31, 2003 | Year Ended December 31, 2002 | \$ Difference | % Difference |
|----------------------|---|---|-------------------------------|-------------------------|
| | | | (Dollars in thousands) | |
| Revenues: | | | | |
| TDS | \$ 99,023 | \$ 107,121 | \$ (8,098) | (7.6)% |
| INS | 20,955 | 26,045 | (5,090) | (19.5) |
| Instant Conferencing | | 272 | (272) | (100.0) |

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| | | | | |
|-------------------------|------------|------------|-------------|----------|
| Total | \$ 119,978 | \$ 133,438 | \$ (13,460) | (10.1)% |
| Gross Profit (Loss): | | | | |
| TDS \$ | \$ 46,399 | \$ 51,251 | \$ (4,852) | (9.5)% |
| TDS % | 46.9% | 47.8% | | |
| INS \$ | \$ 11,630 | \$ 15,972 | \$ (4,342) | (27.2)% |
| INS % | 55.5% | 61.3% | | |
| Instant Conferencing \$ | \$ | \$ 272 | \$ (272) | (100.0)% |
| Instant Conferencing % | % | 100.0% | | |
| Total gross profit \$ | \$ 58,029 | \$ 67,495 | \$ (9,466) | (14.0)% |

Table of Contents

| | Year Ended December 31, 2003 | Year Ended December 31, 2002 | \$ Difference | % Difference |
|--------------------------------|---|---|--------------------------|-------------------------|
| | | (Dollars in thousands) | | |
| Total gross profit % | 48.4% | 50.6% | | |
| Operating Income (Loss): | | | | |
| TDS | \$ 22,025 | \$ 25,749 | \$ (3,724) | (14.5)% |
| INS | (2,541) | (1,986) | (555) | (27.9) |
| Instant Conferencing | (3,536) | (4,711) | 1,175 | 24.9 |
| Total segment operating income | \$ 15,948 | \$ 19,052 | \$ (4,056) | (6.2)% |
| Reconciling items(1) | (19,806) | (17,500) | | |
| Total operating income (loss) | \$ (3,858) | \$ 1,552 | | |

- (1) Reconciling items consist of certain corporate or centralized marketing and general and administrative expenses not allocated to our business unit segments, because these activities are managed separately from the business units. Also, we do not allocate restructuring expenses and other non-recurring gains or charges to our business unit segments because our Chief Executive Officer evaluates the segment results exclusive of these items.

Revenues by Operating Segment

TDS. The decrease in TDS revenues of \$8.1 million was due to slower subscriber growth experienced by our clients, resulting in a reduction in transaction volume, and to clients selecting fewer transaction products and services. Our TDS revenues also declined as a result of reduced call volume and a change in the combination of services provided by our TeleServices call centers. In addition, in the first quarter of 2002, TDS revenues include approximately \$2.7 million in revenues from services provided to WorldCom. In the second quarter of 2002, we provided approximately \$2.0 million of transaction services to WorldCom, and did not record any related revenue due to doubts about collectibility stemming from WorldCom's financial difficulties. No services were provided to WorldCom in 2003.

INS. INS segment revenues declined by \$5.1 million in 2003 as compared to 2002 because of fewer software and hardware sales that affected the integration, deployment, optimization and maintenance services associated with our software sales, as well as a decline in other consulting services. The lower software sales were primarily a result of reduced capital spending in the telecommunications industry in 2003.

Instant Conferencing. Our Instant Conferencing segment did not produce any revenues in 2003 as compared to \$272,000 of revenues in 2002. The 2002 revenues from this segment were related to sales of our Mobile Data Manager product, which we no longer actively market or sell.

Gross Profit (Loss) by Operating Segment

TDS. Gross profit for our TDS segment in 2003 decreased by \$4.9 million in comparison to 2002 as a result of reduced revenue for this segment. Gross profit as a percentage of segment revenues decreased slightly in 2003 as a result of a change in the combination of services acquired by clients in the year ended December 31, 2003, as well as the level of our fixed costs which resulted in lower gross profit margins as revenues declined.

INS. Gross profit for our INS segment decreased by \$4.3 million in 2003 as compared to 2002 as a result of lower revenues in this segment. Gross profit as a percentage of INS segment revenues decreased to 55.5% in 2003 from 61.3% in 2002 due to a lower percentage of segment revenues being generated from higher margin software sales than in 2002.

Instant Conferencing. Our Instant Conferencing segment gross profit declined in 2003 in comparison with 2002 as a result of the decline in revenues for this segment.

Operating Income (Loss) by Operating Segment

TDS. Operating income in our TDS segment decreased by \$3.7 million to \$22.0 million in 2003 from \$25.7 million in 2002. The decline in operating income was a result of decreased revenues, partially offset by reduced operating expenses resulting from our restructuring initiatives in 2003 and 2002 and our efforts to limit spending.

INS. Operating loss in our INS segment increased to \$(2.5) million in 2003 from \$(2.0) million in 2002 as a result of reduced revenues for this segment and lower gross margin percentages earned on those revenues. These effects were partially offset by lower operating expenses in our INS segment as a result of our restructuring initiatives in 2003 and 2002 and our efforts to limit spending.

Table of Contents

Instant Conferencing. Operating loss in our Instant Conferencing segment decreased to \$(3.5) million in 2003 from \$(4.7) million in 2002 due to reduced operating expenses resulting from our restructuring initiatives in 2003 and 2002.

Liquidity and Capital Resources

As of December 31, 2004, we had cash and cash equivalents, short-term investments and restricted cash of \$52.2 million, which included \$5.6 million of cash due to merchants related to our payment processing business. Our working capital decreased to \$43.0 million at December 31, 2004 from \$137.7 million at December 31, 2003 as a result of our acquisition of Authorize.Net in March 2004. We believe that our current cash balances will be sufficient to finance our operations and capital expenditures for the next twelve months. Thereafter, the adequacy of our cash balances will depend on a number of factors that are not readily foreseeable such as the impact of general market conditions on our operations, cash requirements associated with acquisitions, investments and capital expenditures, and the profitability of our operations.

Accounts receivable as of December 31, 2004 decreased by \$2.9 million from December 31, 2003 primarily due to reduced revenues in transactions, excluding Authorize.Net, consulting and service revenues. As a result, accounts receivable days outstanding for the year ended December 31, 2004 decreased to 52 days as compared to 60 days and 48 days for the years ended December 31, 2003 and 2002, respectively, due to faster collections from the Authorize.Net business.

For the year ended December 31, 2004, we generated cash flows from operating activities of \$12.1 million and used \$39.3 million and \$3.3 million in investing and financing activities, respectively. Included in cash flow from operations was \$3.3 million of cash received as tenant improvement allowance in 2004. Included in investing activities was \$77.5 million spent on the acquisition of Authorize.Net, net of assets acquired.

Our capital expenditures for the years ended December 31, 2004 and 2003 were \$14.8 million and \$4.9 million, respectively. The capital expenditures during these periods consisted primarily of the relocation of our headquarters in June 2004 and the expansion of our call center operations to Liverpool, Nova Scotia, Canada as well as purchases of fixed assets for our operations infrastructure, and computer equipment for development activities. We lease our facilities and certain equipment under non-cancelable operating lease agreements that expire at various dates through November 2011.

On October 4, 2001, we announced that our board of directors authorized the repurchase of up to 2 million shares of our common stock at an aggregate price of up to \$20 million. The shares may be purchased from time to time on or after October 8, 2001, depending on market conditions. On April 23, 2003, the board approved an expansion of the plan to authorize us to purchase up to 4 million shares of our common stock at an aggregate price of up to \$40 million through September 26, 2005. As of December 31, 2004, we had purchased approximately 2.5 million shares at a total cost of approximately \$17.9 million since the inception of its repurchase program. For the year ended December 31, 2004, we used \$3.8 million for the repurchase of our common stock under our stock repurchase program. We may continue to repurchase shares during 2005 based on prevailing market prices and other financial considerations, and subject to the requirements of the repurchase program and applicable laws.

On January 14, 2003, we had an outstanding letter of credit in the amount of \$1.0 million, which expired in May 2004. On January 7, 2004, we entered into another \$1.0 million letter of credit, which was scheduled to expire in January 2005. This letter of credit was renewed in the amount of \$1.6 million and extends through January 2006. In January 2005, we restricted \$1.6 million of cash as collateral for the renewed letter of credit.

On January 14, 2003, we entered into a foreign exchange agreement, effective April 2003, with a bank for the purchase of one currency in exchange for the sale of another currency. This agreement expired on January 24, 2005. There were no transactions under this agreement.

Our primary contractual obligations and commercial commitments are under our operating leases and letters of credit. Our future minimum payments due under operating leases, including facilities affected by restructurings and our new headquarters lease, and the amount of our commitment per period under annually renewable letters of credit required as security under the leases for our current and new headquarters are as follows:

| | |
|------------------|------------------|
| Less than | More than |
|------------------|------------------|

| | Total | 1 Year | 1-3 Years | 3-5 Years | 5 Years |
|-------------------|-------------------------------|---------------|------------------|------------------|----------------|
| | (Dollars in thousands) | | | | |
| Operating leases | \$20,065 | \$ 4,840 | \$ 6,833 | \$ 4,866 | \$3,526 |
| Letters of credit | \$ 1,600 | \$ 1,600 | \$ 1,600 | | |

20

Table of Contents

We provide certain warranties and related indemnities in our client contracts. These warranties may include warranties that the transactions processed on a client's behalf have been processed in accordance with the contract, that products delivered or services rendered meet designated specifications or service levels, and that certain applicable laws and regulations are complied with in the performance of services for or provision of products to a client. We maintain errors and omissions insurance that may provide coverage for certain warranty and indemnity claims. However, such insurance might cease to be available to us on commercially reasonable terms or at all.

We generally undertake to defend and indemnify the indemnified party for damages and expenses or settlement amounts arising from certain patent, copyright or other intellectual property infringement claims by any third party with respect to our products. Some agreements provide for indemnification for claims relating to property damage or personal injury resulting from the performance of services or provision of products by us, breaches of contract by us or the failure by us to comply with applicable laws in the performance of services or provision of products by us to its clients. Historically, our costs to defend lawsuits, or settle or pay claims relating to such indemnification provisions, have not been material. Accordingly, the estimated fair value of these indemnification provisions is not material.

Off-Balance Sheet Arrangements

We had no off-balance sheet arrangements other than operating lease obligations during the year ended December 31, 2004, and we were not a party to any material transactions involving related persons or entities (other than employment, separation and other compensation agreements with certain executives) during 2004. Future annual minimum rental lease payments are detailed in Note 9 of the Notes to Consolidated Financial Statements in Item 8 of this Annual Report on Form 10-K/A.

Restructurings

In December 2004, we announced a restructuring of our business in order to lower overall expenses to better align them with future revenue expectations. This action followed our announcement of an anticipated revenue reduction as a result of the acquisition of AT&T by Cingular Wireless LLC. This restructuring resulted in the termination of 38 employees in our corporate offices in Burlington, Massachusetts as follows: 16 in product and service delivery, 11 in engineering and development, 10 in sales and marketing and 1 in general and administrative. We recorded a restructuring charge of approximately \$1.4 million relating to employee severance and termination benefits during the three months ended December 31, 2004. Additionally, subsequent to our acquisition of Authorize.net we relocated its offices in Bellevue, Washington and the remaining rent paid on the vacated space of \$178,000 was included in the restructuring charge during the fourth quarter of 2004. We anticipate that all costs related to this restructuring will be paid by the end of 2005.

The following summarizes the changes to the December 2004 restructuring reserve since it was accrued:

| | Balance at December 31, 2003 | Accrued | Utilized | Balance at December 31, 2004 |
|---|---|-----------------|-----------------|---|
| | (In thousands) | | | |
| Employee severance and termination benefits | \$ | \$ 1,410 | \$ 46 | \$ 1,364 |
| Facility closing and related costs | | 178 | 178 | |
| Total | \$ | \$ 1,588 | \$ 224 | \$ 1,364 |

In October 2004, we announced a restructuring of our business in accordance with the sale of Fraud Centurion product suite to Subex. This action, a continuation of our emphasis on expense management, resulted in the termination of nine employees in our Broomfield, Colorado location as follows: two in product and service delivery and seven in engineering and development. We recorded a restructuring charge of approximately \$172,000 relating to employee severance and termination benefits during the three months ended December 31, 2004. We anticipate that

all costs related to this restructuring will be paid by the end of 2005.

The following summarizes the changes to the October 2004 restructuring reserve since it was accrued:

| | Balance at December 31, 2003 | Accrued | Utilized (In thousands) | Balance at December 31, 2004 |
|---|---|----------------|--|---|
| Employee severance and termination benefits | \$ | \$ 172 | \$ 147 | \$ 25 |

Table of Contents

In September 2004, we announced a restructuring of our business in order to lower overall expenses to better align them with future revenue expectations. This action, a continuation of our emphasis on expense management, resulted in the termination of 64 employees and 2 contractors in our corporate offices in Burlington, Massachusetts and our Broomfield, Colorado location as follows: 12 in product and service delivery, 16 in engineering and development, 25 in sales and marketing and 13 in general and administrative. We recorded a restructuring charge of approximately \$2.1 million relating to employee severance and termination benefits during the three months ended September 30, 2004. We anticipate that all costs related to this restructuring will be paid by the end of 2005.

The following summarizes the changes to the September 2004 restructuring reserve since it was accrued:

| | Balance at December 31, 2003 | Accrued | Utilized | Balance at December 31, 2004 |
|---|---|----------------|-----------------|---|
| | (In thousands) | | | |
| Employee severance and termination benefits | \$ | \$ 2,090 | \$ 1,255 | \$ 835 |

In January 2004, we announced a reorganization of our internal business operations. This action, a continuation of our emphasis on expense management, resulted in the termination of ten individuals in our corporate office in Burlington, Massachusetts. We recorded a restructuring charge of approximately \$0.5 million relating to employee severance and termination benefits during the three months ended March 31, 2004. We anticipate that all costs related to this restructuring will be paid by the end of 2005.

The following summarizes the changes to the January 2004 restructuring reserves since it was accrued:

| | Balance at December 31, 2003 | Accrued | Utilized | Balance at December 31, 2004 |
|---|---|----------------|-----------------|---|
| | (In thousands) | | | |
| Employee severance and termination benefits | \$ | \$ 488 | \$ 483 | \$ 5 |

In June 2003, we announced that we would be closing our Irvine, California facility and transferring certain employment positions to our Broomfield, Colorado facility and reducing our headcount by an estimated 70 employees as follows: 16 in product and service delivery, 30 in development, 13 in sales and marketing and 11 in general and administrative. In the quarter ended June 30, 2003, we recorded a restructuring charge of approximately \$0.7 million, consisting mainly of workforce reduction costs. In the quarter ended September 30, 2003, we recorded an additional restructuring charge associated with this action of approximately \$3.3 million, consisting of \$1.1 million for workforce reduction, \$1.7 million in future lease obligations for unused facilities and \$0.5 million for capital equipment write-offs. In the quarter ended December 31, 2003, we recorded an additional restructuring charge of \$0.1 million related to future lease obligations and employee severance benefits. The capital equipment write-offs and a majority of severance costs related to this restructuring were incurred by the end of 2003, and we anticipate that all other costs related to this restructuring, consisting principally of lease obligations on unused space, will be paid by the end of 2006.

The following summarizes the changes to the June 2003 restructuring reserves for the year ended December 31, 2004:

| Balance at | Balance at |
|-----------------------|-------------------|
|-----------------------|-------------------|

| | December 31, 2003 | Accrued | Utilized | December 31, 2004 |
|---|----------------------------------|-----------------------|-----------------|----------------------------------|
| | | (In thousands) | | |
| Employee severance and termination benefits | \$ 253 | \$ (93) | \$ 160 | \$ |
| Facility closing and related costs | 1,396 | 137 | 665 | 868 |
| Total | \$ 1,649 | \$ 44 | \$ 825 | \$ 868 |

Table of Contents

In March 2003, we announced that we would be streamlining our existing Broomfield, Colorado call center operations into our Lynn, Massachusetts facility and a smaller facility in Broomfield, Colorado by the end of May 2003. In the quarter ended March 31, 2003, we recorded a restructuring charge of approximately \$0.1 million for workforce reductions. In the quarter ended June 30, 2003, we recorded an additional restructuring charge associated with this action of approximately \$1.0 million, consisting of approximately \$0.6 million in future lease obligations for unused facilities and approximately \$0.4 million for capital equipment write-offs. The capital equipment write-offs and all of the severance costs related to this restructuring were incurred by the end of 2003, and we anticipate that all other costs relating to this restructuring, consisting principally of lease obligations on unused space, will be paid by the end of the first quarter of 2005.

The following summarizes the changes to the March 2003 restructuring reserves for the year ended December 31, 2004:

| | Balance at December 31, 2003 | Accrued | Utilized | Balance at December 31, 2004 |
|------------------------------------|---|----------------|-----------------|---|
| | (In thousands) | | | |
| Facility closing and related costs | \$ 363 | \$ (36) | \$ 324 | \$ 3 |

In June 2002, we announced that we were reducing our workforce by seven percent and consolidating our Waltham, Massachusetts call center operations into our Lynn, Massachusetts and Broomfield, Colorado facilities by the end of 2002. We recorded a restructuring charge of approximately \$3.6 million, consisting of \$1.6 million for workforce reductions, \$1.3 million for facilities reductions including lease obligations, utilities and security costs on unused space and \$0.7 million for capital equipment write-offs associated with these measures. The restructuring plan resulted in the termination of 65 personnel as follows: 25 in product and service delivery, 22 in development, 11 in sales and marketing and seven in general and administrative. The capital equipment write-offs and a majority of severance costs related to this restructuring were incurred by the end of 2002, and we anticipate that all other costs relating to this restructuring, consisting principally of lease obligations on unused space, will be paid by the end of 2005.

The following summarizes the changes to the June 2002 restructuring reserves for the year ended December 31, 2004:

| | Balance at December 31, 2003 | Accrued | Utilized | Balance at December 31, 2004 |
|------------------------------------|---|----------------|-----------------|---|
| | (In thousands) | | | |
| Facility closing and related costs | \$ 622 | \$ | \$ 339 | \$ 283 |

Inflation

Although certain of the Company's expenses increase with general inflation in the economy, inflation has not had a material impact on the Company's financial results to date.

Recent Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 123R, *Share-Based Payment* (SFAS No. 123R). This Statement is a revision of SFAS No. 123,

Accounting for Stock-Based Compensation, and supersedes Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, and its related implementation guidance. SFAS No. 123R focuses primarily on

accounting for transactions in which an entity obtains employee services in share-based payment transactions. The Statement requires entities to recognize stock compensation expense for awards of equity instruments to employees based on the grant-date fair value of those awards (with limited exceptions). SFAS No. 123R is effective for the first interim or annual reporting period that begins after June 15, 2005. The Company is evaluating the two methods of adoption allowed by SFAS No. 123R; the modified-prospective transition method and the modified-retrospective transition method.

Table of Contents

Risk Factors

If One or More of Our Major Clients Stops Using Our Products or Services or Changes the Combination of Products and Services It Uses, Our Operating Results Would Suffer Significantly.

Our revenues are concentrated among a few major clients. Our 10 largest clients accounted for approximately 72% of our total revenues in 2004, and we expect that most of our revenues will continue to come from a relatively small number of clients for the foreseeable future. Consequently, our revenues, margins and net income may fluctuate significantly from quarter to quarter based on the actions of a single significant client. A client may take actions that significantly affect us for reasons that we cannot necessarily anticipate or control, such as reasons related to the client's financial condition, changes in the client's business strategy or operations, the introduction of alternative competing products or services, acquisitions, or as the result of the perceived quality or cost-effectiveness of our products or services. Our services agreements with Sprint Spectrum L.P. (Sprint), and Nextel Operations, Inc. (Nextel) expire on December 31, 2006. Our services agreement with AT&T Wireless Services, Inc. AT&T expires on April 1, 2009, but is subject to earlier termination of the services agreement upon twelve months' notice and designated services upon notice. In February 2004, Cingular Wireless LLC (Cingular) announced an agreement to acquire AT&T and in October 2004, Cingular announced that it had completed its merger with AT&T. Cingular is not presently a client of Lightbridge. As a result of the acquisition of AT&T, we do not expect that client to generate significant revenue in 2005. On December 15, 2004, Sprint and Nextel announced that their respective Boards of Directors had approved a definitive agreement for a merger of the two companies. We are unable to predict the effect of the merger of Nextel and Sprint on our relationship with either client including without limitation the timing or extent of any reductions in applications processed or other services provided under our contracts with those clients. It is possible that Sprint and/or Nextel could elect not to renew their agreements, to reduce the volume of products and services they purchase from us or to request significant changes to the pricing or other terms in any renewal agreement. The loss of Sprint and/or Nextel or any of our other major clients would cause sales to fall below expectations and materially reduce our revenues, margins and net income and adversely affect our business.

Certain of Our Revenues Are Uncertain Because Our Clients May Reduce the Amounts of or Change the Combination of Our Products or Services They Purchase.

Most of our communications client contracts extend for terms of between one and three years. During the terms of these contracts, our communications clients typically may elect to purchase any of several different combinations of products and services. The revenue that we receive for processing a transaction for such a client may vary significantly depending on the particular products and services used to process the transaction. In particular, transactions handled through our TeleServices Group generally result in significantly higher revenue than transactions that are submitted and processed electronically, but also result in higher cost of revenues. Therefore, our revenues or margins from a particular client may decline if the client changes the combination of products and services it purchases from us.

To the extent our client contracts contain minimum purchase or payment requirements, these minimums are typically at levels significantly below actual or historical purchase or payment levels. Therefore, our current clients may not continue to utilize our products or services at levels similar to previous years or at all, and may not generate significant revenues in future periods. If any of our major clients significantly reduces or changes the combination of products or services it purchases from us for any reason, our business would be seriously damaged.

Our Revenues Are Concentrated in the Wireless Telecommunications Industry, Which Is Experiencing Declining Growth Rates, Consolidation and Increasing Pressure to Control Costs.

We currently derive a majority of our revenues from companies in the wireless telecommunications industry, and we expect that wireless telecommunications companies will continue to account for a majority of our revenues in 2005. In recent years, the growth rate of the domestic wireless industry has slowed. In addition, consolidation has affected the number of carriers to whom our products and services can be marketed and sold, and competition among wireless carriers has continued to increase, resulting in heightened efforts by carriers to control costs. Many of our carrier clients have sought, and may in the future seek, pricing concessions when they renew their services agreements with us or at other times, which could affect our revenues, margins and net income. In addition, certain of our carrier clients have sought bankruptcy protection in recent years, and we believe it is possible that additional clients may file

for bankruptcy protection if current industry conditions continue. Bankruptcy filings by our clients or former clients such as WorldCom, Inc. may prevent us from collecting some or all of the amounts owing to us at the time of filing, may require us to return some or all of any payments received by us within 90 days prior to a bankruptcy filing and may also result in the termination of our service agreements. As a result of the foregoing conditions, our success depends on a number of factors:

- our ability to maintain our profit margins on sales of products and services to companies in the wireless telecommunications industry;

- the financial condition of our clients and their continuing ability to pay us for services and products;

Table of Contents

our ability to develop and market new or enhanced products and services to new and existing clients;

continued growth of the domestic wireless telecommunications markets;

the number of carriers seeking to implement prepaid billing services; and

our ability to increase sales of our products and services internationally.

Our Future Revenues May Be Uncertain Because of Reliance on Third Parties for Marketing and Distribution.

Authorize.Net distributes its service offerings primarily through outside sales partners. In 2004, Authorize.Net's revenues were derived predominantly through relationships with distribution partners. In addition, the PrePay billing system is currently marketed primarily through distribution agreements with Ericsson and Nortel. Ericsson has been the source of substantially all of our revenue derived from the PrePay billing system in recent years. Our agreement with Ericsson may be terminated by either party on 180 days' notice to the other. We have also entered into a business alliance with VeriSign, Inc. (VeriSign) to assist us in penetrating the online transaction market.

We intend to continue to market and distribute our current and future products and services through existing and other relationships both in and outside of the United States. There are no minimum purchase obligations applicable to any existing distributor or other sales and marketing partners and we do not expect to have any guarantees of continuing orders. Failure by our existing and future distributors or other sales and marketing partners to generate significant revenues or our failure to establish additional distribution or sales and marketing alliances or changes in the industry that render third party distribution networks obsolete could have a material adverse effect on our business, operating results and financial condition.

In addition, distributors and other sales and marketing partners may become our competitors with respect to the products they distribute either by developing a competitive product themselves or by distributing a competitive offering. For example, resellers of Authorize.Net products and services are permitted to and generally do market and sell competing products and services; Ericsson or Nortel may evaluate and seek to distribute or acquire alternative vendors' prepaid products that compete with PrePay; and VeriSign may elect to market or acquire alternative fraud and identity verification products. Competition from existing and future distributors or other sales and marketing partners could significantly harm sales of our products.

We Have Made and May Continue to Make Acquisitions, Which Involve Risks.

We acquired Corsair Communications, Inc. in February of 2001, the assets of Altawave, Inc. in February of 2002 and Authorize.Net Corporation in March of 2004. We may also make additional acquisitions in the future if we identify companies, technologies or assets that appear to complement our business. Acquisitions involve risks that could cause the actual results of any acquisitions we make to differ from our expectations. For example:

We may experience difficulty in integrating and managing acquired businesses successfully and in realizing anticipated economic, operational and other benefits in a timely manner. The need to retain existing clients, employees, and sales and distribution channels of an acquired company and to integrate and manage differing corporate cultures can also present significant risks. If we are unable to successfully integrate and manage acquired businesses, we may incur substantial costs and delays or other operational, technical or financial problems.

Our acquisition of Authorize.Net significantly reduced our available cash and liquidity. In other future acquisitions, we may issue equity securities that could be dilutive to our shareholders or we may use our remaining cash, which may have an adverse effect on our liquidity. We also may incur additional debt and amortization expense related to intangible assets as a result of acquisitions. This additional debt and amortization expense, as well as the potential impairment of any purchased goodwill, may materially and adversely affect our business and operating results. We may also be required to make continuing investments in acquired products or technologies to bring them to market, which may negatively affect our cash flows and net income. In addition, we may assume contingent liabilities that may be difficult to estimate.

Acquisitions may divert management's attention from our existing business and may damage our relationships with our key clients and employees.

Table of Contents

The Success of Our Growth Strategy Is Dependent on Our Ability to Expand into New or Complementary Markets.

In order to achieve growth in our business, we are seeking to expand our business into new markets or markets that are complementary to our existing business. If we are not able to expand successfully into new markets, our financial results and future prospects may be harmed. Our ability to enter new markets depends on a number of factors, including:

growth in our targeted markets;

our ability to provide products and services to address the needs of those markets; and

competition in those markets.

If We Do Not Continue to Enhance Our Existing Products and Services, and Develop or Acquire New Ones, We Will Not Be Able to Compete Effectively.

The industries in which we do business or intend to do business have been changing rapidly as a result of increasing competition, technological advances, regulatory changes and evolving industry practices and standards, and we expect these changes will continue. Current and potential clients have also experienced significant changes as the result of consolidation among existing industry participants and economic conditions. In addition, the business practices and technical requirements of our clients are subject to changes that may require modifications to our products and services. In order to remain competitive and successfully address the evolving needs of our clients, we must commit a significant portion of our resources to:

identify and anticipate emerging technological and market trends affecting the markets in which we do business;

enhance our current products and services in order to increase their functionality, features and cost-effectiveness to clients that are seeking to control costs and to meet regulatory requirements;

develop or acquire new products and services that meet emerging client needs, such as products and services for the online market;

modify our products and services in response to changing business practices and technical requirements of our clients, as well as to new regulatory requirements;

integrate our current and future products with third-party products; and

create and maintain interfaces to changing client and third party systems.

We must achieve these goals in a timely and cost-effective manner and successfully market our new and enhanced products and services to clients. In the past, we have experienced errors or delays in developing new products and services and in modifying or enhancing existing products and services. If we are unable to expand or appropriately enhance or modify our products and services quickly and efficiently, our business and operating results will be adversely affected.

We and Our Clients Must Comply with Complex and Changing Laws and Regulations.

Government regulation influences our activities and the activities of our current and prospective clients, as well as our clients' expectations and needs in relation to our products and services. Businesses that handle consumers' funds, such as our Authorize.Net business, are subject to numerous regulations, including those related to banking, credit cards, electronic transactions and communication, escrow, fair credit reporting, privacy of financial records and others. State money transmitter regulations and federal anti-money laundering and money services business regulations can also apply under some circumstances. The application of many of these laws with regard to electronic commerce is currently unclear. In addition, it is possible that a number of laws and regulations may be applicable or may be adopted in the future with respect to conducting business over the Internet concerning matters such as taxes,

pricing, content and distribution. If applied to us, any of the foregoing rules and regulations could require us to change the way we do business in a way that increases costs or makes our business more complex. In addition, violation of some statutes may result in severe penalties or restrictions on our ability to engage in e-commerce, which could have a material adverse effect on our business.

Our clients also include telecommunications companies that, to the extent that they extend consumer credit, may be subject to federal and state regulations. In making credit evaluations of consumers, performing fraud screening or user authentication, our clients are subject to requirements of federal law, including the Equal Credit Opportunity Act (ECOA), the Fair Credit Reporting Act (FCRA) and the Gramm-Leach-Bliley Act (GLBA) and regulations thereunder, as well as state laws which impose a variety of additional requirements. Privacy legislation may also affect the nature and extent of the products or services that we can provide to clients as well as our ability to collect, monitor and disseminate information subject to privacy protection.

Table of Contents

Although most of the products and services we provide to the telecommunications industry, other than our ProFile service, are not directly subject to these requirements, we must take these extensive and evolving requirements into account in order to meet our clients' needs. In some cases, consumer credit laws require our clients to notify consumers of credit decisions made in connection with their applications for telecommunications services, and we have contracted with some of our clients, including Sprint, AT&T, Nextel, Western Wireless Corporation and Dobson Communications, Inc., to provide such notices on their behalf. Our software has in the past contained, and could in the future contain, undetected errors affecting compliance by our clients with one or more of these legal requirements. Failure to properly implement these requirements in our products and services in a timely, cost-effective and accurate manner could result in liability, either directly or as indemnitor of our clients, damage to our reputation and relationships with clients and a loss of business.

Consumer protection laws in the areas of privacy, credit and financial transactions have been evolving rapidly at the state, federal and international levels. As the electronic transmission, processing and storage of financial information regarding consumers continues to grow and develop, it is likely that more stringent consumer protection laws may impose additional burdens on companies involved in such transactions. Uncertainty and new laws and regulations, as well as the application of existing laws to e-commerce, could limit our ability to operate in our markets, expose us to compliance costs and substantial liability and result in costly and time consuming litigation.

Furthermore, the growth and development of the market for e-commerce may prompt more stringent consumer protection laws that may impose additional regulatory burdens on those companies, such as Lightbridge, that provide services to online business. The adoption of additional laws or regulations may decrease the growth of the Internet or other online services, which could, in turn, decrease the demand for our products and services and increase our cost of doing business.

The Securities and Exchange Commission and the National Association of Securities Dealers, Inc. have also enacted regulations affecting our corporate governance, securities disclosure and compliance practices. We expect these regulations to increase our compliance costs and to make some of our activities more time-consuming. If we fail to comply with any of these regulations, we could be subject to legal actions by regulatory authorities or private parties.

On-Demand Voice Conferencing Services May Become Subject to Traditional Telecommunications Carrier Regulation by Federal and State Authorities, Which Would Increase the Cost of Providing Our Services, Require Us to Suspend Services to Existing Clients, and May Subject Us to Penalties.

The Federal Communications Commission (FCC) and state public service commissions may require us to submit to traditional telecommunications carrier regulations for our GroupTalk on-demand, voice conferencing service under the Communications Act of 1934, as amended, and various state laws or regulations as provider of telecommunications services. If the FCC or any state public service commission seeks to enforce any of these laws or regulations against us, we could be prohibited from providing the voice aspect of our voice conferencing service until we have obtained various federal and state licenses and filed tariffs. We believe we would be able to obtain those licenses, although in some states, doing so could significantly delay our ability to provide services. We also could be required to comply with other aspects of federal and state laws and regulations. Subjecting our voice conferencing service to these laws and regulations would increase our operating costs, may require us to suspend service to existing clients, could require restructuring of those services to charge separately for the voice and other components, and would involve on-going reporting and other compliance obligations. We also might be subject to fines or forfeitures and civil or criminal penalties for non-compliance.

We Need to Continue to Improve or Implement our Procedures and Controls.

Requirements adopted by the Securities and Exchange Commission in response to the passage of the Sarbanes-Oxley Act of 2002 require annual review and evaluation of our internal control systems, and attestation of these systems by our registered independent public accounting firm. As permitted by the rules and regulations of the Securities and Exchange Commission, management determined that the internal control over financial reporting of Authorize.Net would be excluded from the final 2004 internal control assessment. We need to periodically review our internal control procedures, enhance them as may be necessary and consider the adequacy of the documentation of such procedures. There can be no assurance that we will be able to maintain compliance with all of the new

requirements. Any improvements in our internal control systems or in documentation of such internal control systems and the internal control assessment of Authorize.Net could be costly to prepare or implement, divert attention of management or finance staff, and may cause our operating expenses to increase over the ensuing year.

Table of Contents

Changes to Credit Card Association Rules or Practices Could Adversely Impact Our Authorize.Net Business.

Our Authorize.Net credit card payment gateway does not directly access the Visa and MasterCard credit card associations. As a result, we must rely on banks and their service providers to process our transactions. We must comply with the operating rules of the credit card associations. The associations' member banks set these rules, and the associations interpret the rules. Some of those member banks compete with Authorize.Net. Visa, MasterCard, American Express or Discover could adopt new operating rules or interpretations of existing rules which we might find difficult or even impossible to comply with, resulting in our inability to give customers the option of using credit cards to fund their payments. If we were unable to provide a gateway for credit card transactions, our Authorize.Net business would be materially and adversely affected.

We Could Be Subject to Liability as a Result of Security Breaches, Service Interruptions by Cyber Terrorists or Fraudulent or Illegal Use of Our Services.

Because some of our activities involve the storage and transmission of confidential personal or proprietary information, such as credit card numbers and social security numbers, and because we are a link in the chain of e-commerce, security breaches, service interruptions and fraud schemes could damage our reputation and expose us to a risk of loss or litigation and possible monetary damages. Cyber terrorists have periodically interrupted, and may continue to interrupt, our payment gateway services in attempts to extort payments from us or disrupt commerce. Our payment gateway services may be susceptible to credit card and other payment fraud schemes, including unauthorized use of credit cards or bank accounts, identity theft or merchant fraud. We expect that technically sophisticated criminals will continue to attempt to circumvent our anti-fraud systems. If such fraud schemes become widespread or otherwise cause merchants to lose confidence in our services in particular, or in Internet systems generally, our business could suffer.

In addition, the large volume of payments that we handle for our clients makes us vulnerable to third party or employee fraud or other internal security breaches. Further, we may be required to expend significant capital and other resources to protect against security breaches and fraud to address any problems they may cause.

Our payment system may also be susceptible to potentially illegal or improper uses. These uses may include illegal online gambling, fraudulent sales of goods or services, illicit sales of prescription medications or controlled substances, software and other intellectual property piracy, money laundering, bank fraud, child pornography trafficking, prohibited sales of alcoholic beverages and tobacco products and online securities fraud. Despite measures we have taken to detect and lessen the risk of this kind of conduct, we cannot ensure that these measures will succeed. In addition, regulations under the USA Patriot Act of 2001 may require us to revise the procedures we use to comply with the various anti-money laundering and financial services laws. Our business could suffer if clients use our system for illegal or improper purposes or if the costs of complying with regulatory requirements increase significantly.

We have expended, and may be required to continue to expend, significant capital resources to protect against security breaches, service interruptions and fraud schemes. Our security measures may not prevent security breaches, service interruptions and fraud schemes and the failure to do so may disrupt our business, damage our reputation and expose us to risk of loss or litigation and possible monetary damages.

The Demand for Our Payment Processing Products and Services Could Be Negatively Affected by a Reduced Growth of e-Commerce or Delays in the Development of the Internet Infrastructure.

Sales of goods and services over the Internet do not currently represent a significant portion of overall sales of goods and services. We depend on the growing use and acceptance of the Internet as an effective medium of commerce by merchants and customers in the United States and as a means to grow our business. We cannot be certain that acceptance and use of the Internet will continue to develop or that a sufficiently broad base of merchants and consumers will adopt, and continue to use, the Internet as a medium of commerce.

It is also possible that the number of Internet users, or the use of Internet resources by existing users, will continue to grow, and may overwhelm the existing Internet infrastructure. Delays in the development or adoption of new standards and protocols required to handle increased levels of Internet activity could also have a detrimental effect on the Internet and correspondingly on our business. These factors would adversely affect usage of the Internet, and lower demand for our products and services.

Table of Contents

Our Reliance on Suppliers and Vendors Could Adversely Affect Our Ability to Provide Our Services and Products to Our Clients on a Timely and Cost-Efficient Basis.

We rely to a substantial extent on third parties to provide some of our equipment, software, data, systems and services. In some circumstances, we rely on a single supplier or limited group of suppliers. For example, our Authorize.Net business requires the services of third-party payment processors. If any of these processors cease to allow us to access their processing platforms, our ability to process credit card payments would be severely impacted. In addition, we depend on our Originating Depository Financial Institution (ODFI) partner to process Automated Clearing House transactions, and our ability to process these transactions would be severely impacted if we were to lose our ODFI partner for any reason.

Our reliance on outside vendors and service providers also subjects us to other risks, including a potential inability to obtain an adequate supply of required components and reduced control over quality, pricing and timing of delivery of components. For example, in order to provide our credit verification service, we need access to third-party credit information databases provided to us by outside vendors. Similarly, delivery of our activation services often requires the availability and performance of billing systems which are also supplied by outside vendors. If for any reason we were unable to access these databases or billing systems, our ability to process credit verification transactions could be impaired.

In addition, our business is materially dependent on services provided by various telecommunications providers. A significant interruption in telecommunications services could seriously harm our business.

From time to time, we must also rely upon third parties to develop and introduce components and products to enable us, in turn, to develop new products and product enhancements on a timely and cost-effective basis. In particular, we must rely on the development efforts of third-party wireless infrastructure providers in order to allow our PrePay product to integrate with both existing and future generations of the infrastructure equipment. We may not be able to obtain access, in a timely manner, to third-party products and development services necessary to enable us to develop and introduce new and enhanced products. We may not be able to obtain third-party products and development services on commercially reasonable terms and we may not be able to replace third-party products in the event such products become unavailable, obsolete or incompatible with future versions of our products.

Our Business May Be Harmed by Errors in Our Software.

The software that we develop and license to clients, and that we also use in providing our transaction processing and call center services, is extremely complex and contains hundreds of thousands of lines of computer code. Large, complex software systems such as ours are susceptible to errors. The difficulty of preventing and detecting errors in our software is compounded by the fact that we maintain multiple versions of our systems to meet the differing requirements of our major clients, and must implement frequent modifications to these systems in response to these clients' evolving business policies and technical requirements. Our software design, development and testing processes are not always adequate to detect errors in our software prior to its release or commercial use. As a result, we have from time to time discovered, and may likely in the future discover, errors in software that we have put into commercial use for our clients, including some of our largest clients. Because of the complexity of our systems and the large volume of transactions they process on a daily basis, we sometimes have not detected software errors until after they have affected a significant number of transactions. Software errors can have the effect of causing clients that utilize our products and services to fail to comply with their intended credit or business policies, or to fail to comply with legal requirements, such as those under the ECOA, FCRA, or GLBA.

Such errors, particularly if they affect a major client, can harm our business in several ways, including the following:

- we may suffer a loss of revenue if, due to software errors, we are temporarily unable to provide products or services to our clients;

- we may not be paid for the products or services provided to a client that contain errors, or we may be liable for losses or damages sustained by a client or its subscribers as a result of such errors;

we may incur additional unexpected expenses to correct errors in our software, or to fund product development projects that we may undertake to minimize the occurrences of such errors in the future;

we may damage our relationships with clients or suffer a loss of reputation within our industry;

we may become subject to litigation or regulatory scrutiny; and

our clients may terminate or fail to renew their agreements with us or reduce the products and services they purchase from us.

Table of Contents

Our errors and omissions insurance may not adequately compensate us for losses that may occur due to software errors. It is also possible that such insurance might cease to be available to us on commercially reasonable terms or at all.

Our Initiatives to Improve Our Software Design and Development Processes May Not Be Successful.

The development of our products has, in some cases, extended over a period of more than ten years. This incremental development process has resulted in systems which are extremely complex. Systems of the size and complexity of ours are inherently difficult to modify and maintain. We have implemented and are also evaluating changes in our product development, testing and control processes to improve the accuracy and timeliness of modifications that we make to our software, including the frequent modifications that we must make in response to changes in the business policies and technical requirements of our clients. We believe that our initiatives to implement a new product architecture and to improve our product development, test and control processes will be important to our future competitive position and success. If we are not successful in carrying out these initiatives on a timely basis or in a manner that is acceptable to our clients, our business and future prospects could be harmed.

Our Success Is Dependent in Part on PrePay, Which May Not Achieve Market Penetration.

Our future operating results will depend to a significant extent on the demand for and market penetration of PrePay, our prepaid metered billing system. To date, only a small number of wireless carriers, almost all of them outside the U.S., have deployed PrePay, and the rate of adoption of the PrePay system will need to increase significantly in order to achieve our revenue targets. PrePay has been sold predominantly by Ericsson. Ericsson, from time to time, may evaluate and seek to distribute or acquire alternative vendors' prepaid product offerings. Any change in the terms of our distribution arrangements with Ericsson or Ericsson's desire to discontinue our relationship would drastically affect sales of PrePay. Although our own sales force also sells PrePay, it has not yet generated significant PrePay sales. We cannot ensure that sales of the PrePay system will increase or that PrePay will gain market penetration. If PrePay does not gain market penetration our future operating results would be adversely affected.

If We Are Unable to Make Successful Acquisitions, Our Future Growth Will Be Limited.

A key element of our strategy is to acquire businesses, technologies or products that expand and complement our business. We believe acquisitions are necessary for us to grow at a desirable rate, and we will continue to evaluate possible acquisition opportunities in the future. Even if we are able to identify suitable companies or businesses to buy, we may not be able to purchase any of these companies at favorable prices, or at all, for any number of reasons. If we are unable to make acquisitions, we may not be able to grow our business.

We May Not Be Able to Successfully Manage Operational Changes.

Over the last several years, our operations have experienced rapid growth in some areas and significant restructurings and cutbacks in others. These changes have created significant demands on our executive, operational, development and financial personnel and other resources. If we achieve future growth in our business, or if we are forced to make additional restructurings, we may further strain our management, financial and other resources. Our future operating results will depend on the ability of our officers and key employees to manage changing business conditions and to continue to improve our operational and financial controls and reporting systems. We cannot ensure that we will be able to successfully manage the future changes in our business.

Our Quarterly Operating Results May Fluctuate.

Our operating results are difficult to predict and may fluctuate significantly from quarter to quarter. If our operating results fall below the expectations of investors or public market analysts, the price of our common stock could fall dramatically. Our common stock price could also fall dramatically if investors or public market analysts reduce their estimates of our future quarterly operating results, whether as a result of information we disclose, or based on industry, market or economic trends, or other factors.

Our revenues are difficult to forecast for a number of reasons:

Seasonal and retail trends affect our transaction revenues, in both our Payment Processing and TDS businesses, as well as our other products and services. Transaction revenues historically have represented the majority of our total revenues. As a result, our revenues can fluctuate. For example, our revenues generally have been highest in the fourth quarter of each calendar year, particularly in the holiday shopping season between Thanksgiving and Christmas. In addition,

marketing initiatives undertaken by our clients or their competitors may significantly affect the number of transactions we process.

The sales process for our products and services offered to telecommunications clients is lengthy, sometimes exceeding twenty-four months. The length of the sales process makes our revenues difficult to predict. The delay of one or more large orders, particularly orders for software, which typically result in a substantial amount of non-recurring revenue, could cause our quarterly revenues to fall substantially below expectations.

Table of Contents

We ship our software products within a short period after receipt of an order, and we usually do not have a material backlog of unfilled orders of software products. Consequently, our revenues from software licenses in any quarter depend substantially on the orders booked and shipped in that quarter. As a result, a delay in the consummation of a license agreement may cause our revenues to fall below expectations for that quarter.

Our consulting services revenues can fluctuate based on the timing of product sales and projects we perform for our clients. Many of our consulting engagements are of a limited duration, so it can be difficult for us to forecast consulting services revenues or staffing requirements accurately more than a few months in advance.

Most of our expenses, particularly employee compensation, are relatively fixed. As a result, even relatively small variations in the timing of our revenues may cause significant variations in our quarterly operating results and may result in quarterly losses.

Our quarterly results may also vary due to the timing and extent of restructuring and other changes that may occur in a given quarter.

As a result of these factors, we believe that quarter-to-quarter comparisons of our results of operations are not necessarily meaningful. You should not rely on our quarterly results of operations to predict our future performance.

Our Foreign Sales and Operations Subject Us to Risks and Concerns Which Could Negatively Affect Our Business Overall.

We expect our international revenues will continue to represent a significant portion of our total revenues. We also intend to further expand our sales efforts internationally. In addition to the risks generally associated with sales and operations in the U.S., sales to clients outside the U.S. and operations in foreign countries present us with many additional risks, including the following:

- the imposition of financial and operational controls and regulatory restrictions by foreign governments;

- the need to comply with a wide variety of complex U.S. and foreign import and export laws and treaties;

- political and economic instability that may lead to reduced demand for our products and services;

- changes in tariffs, taxes and other barriers that may reduce our ability to sell our solutions or may reduce the profitability of those solutions;

- longer payment cycles and increased difficulties in collecting accounts receivable;

- fluctuations in interest and currency exchange rates, which may reduce our earnings if we denominate arrangements with international clients in the currency of the country in which our products or services are provided, or with respect to arrangements with international clients that are U.S. dollar-denominated, which may make our systems less price-competitive;

- changes in technology standards, such as interfaces between products, that are developed by foreign groups and may require additional development efforts on our part or change the buying behavior of some of our clients;

- reduced protection for intellectual property rights in some countries;

- difficulties in managing a global network of distributors or representatives and in staffing and managing foreign subsidiary operations;

- costs and risks of localizing systems in foreign countries;

- additional complications and expenses related to supporting products internationally; and

the possibility that our purchase agreements may be governed by foreign laws that differ significantly from U.S. laws, which may limit our ability to enforce our rights under these agreements.

Table of Contents

We Face Significant Competition for a Limited Supply of Qualified Software Engineers, Consultants and Sales and Marketing Personnel.

Our business depends on the services of skilled software engineers who can develop, maintain and enhance our products, consultants who can undertake complex client projects and sales and marketing personnel. In general, only highly qualified, highly educated personnel have the training and skills necessary to perform these tasks successfully. In order to maintain the competitiveness of our products and services and to meet client requirements, we need to attract, motivate and retain a significant number of software engineers, consultants and sales and marketing personnel. Qualified personnel such as these are in short supply and we face significant competition for these employees, from not only our competitors but also clients and other enterprises. Other employers may offer software engineers, consultants and sales and marketing personnel significantly greater compensation and benefits or more attractive career paths than we are able to offer. Any failure on our part to hire, train and retain a sufficient number of qualified personnel would seriously damage our business.

Changes in Management Could Affect Our Ability to Operate Our Business.

Our future success will depend to a significant degree on the skills, experience and efforts of our executive officers. We have experienced recent changes in management including the resignation of Pamela D.A. Reeve, our former President and CEO, on August 2, 2004. The loss of any of our executive officers could impair our ability to successfully manage our current business or implement our planned business objectives and our future operations may be adversely affected.

We Face Competition from a Broad and Increasing Range of Vendors.

The market for products and services offered to communications providers and participants in online transactions is highly competitive and subject to rapid change. Each of these markets is fragmented, and a number of companies currently offer one or more products or services competitive with ours. We anticipate continued growth and the formation of new alliances in each of the markets in which we compete, which will result in the entrance of new competitors in the future. We face potential competition from several primary sources:

providers of online payment processing services, including VeriSign, CyberSource Corporation, Plug & Pay Technologies, Inc. and LinkPoint International, Inc.

software vendors that provide one or more customer acquisition, customer relationship management and retention or risk management solutions, including ECtel Ltd., TSI Telecommunications Services Inc. (TSI), Fair Isaac Corporation, Magnum Software Systems, Inc., American Management Systems, Incorporated and SLP Infoware;

telecommunications equipment vendors that market software-based solutions to complement their hardware offerings, such as Hewlett-Packard Company and Ericsson;

service providers that offer customer acquisition, customer relationship management and retention, risk management or authentication services in connection with other services, including Choicepoint Inc., Visa U.S.A., Experian Information Solutions, Inc., Equifax, Inc., Lexis Nexis, Trans Union, L.L.C., Schlumberger Sema plc and Amdocs Ltd;

information technology departments within larger carriers that have the ability to provide products and services that are competitive with those we offer;

information technology vendors that offer wireless and internet software applications such as Oracle Corporation, Microsoft Corporation and International Business Machine Corporation;

consulting firms or systems integrators that may offer competitive services or the ability to develop customized solutions for customer acquisition and qualification, customer relationship management and retention or risk management, such as American Management Systems, Incorporated, Accenture Ltd., BearingPoint, Inc.,

PeopleSoft, Inc., Siebel Systems, Inc. and Cap Gemini Ernst & Young;

software vendors of prepaid wireless billing products, including Boston Communications Group, Inc., Intervoice, Inc., Converse Technology, Inc., Glenayre Technologies, Inc., VeriSign Telecommunications Services, Telemac Cellular Corporation, Fair, Isaac & Co. Inc., ORGA Kartensysteme GmbH, Schlumberger Sema plc, Alcatel USA, Priority Call Management, Lucent Technologies, Inc., Hewlett-Packard Company (Tandem Division), Telcordia Technologies, Inc. and Sixbell;

a number of alternative technologies, including profilers, personal identification numbers and authentication, provided by companies such as Verizon Communications, Inc., Authentix Network Inc. and Fair Isaac Corporation;

Table of Contents

vendors that provide products and services in the wireless data market, such as Bridgewater Systems Corporation, OracleMobile, a division of Oracle Corporation, 4thPass, Inc., TSI, Seven Networks, Inc. and Openwave Systems Inc.; and

vendors that provide or resell products and services in the voice conferencing market such as Spectel, Inc., Polycom Inc., Raindance Communications, Inc., Ptek Holdings, Inc., and the major worldwide telecommunications providers such as AT&T, Sprint, and Global Crossing Limited.

Because competitors can easily penetrate one or more of our markets, we anticipate additional competition from other established and new companies. In addition, competition may intensify as competitors establish cooperative relationships among themselves or alliances with others.

Many of our current and potential competitors have significantly greater financial, marketing, technical and other competitive resources than we do. As a result, these competitors may be able to adapt more quickly to new or emerging technologies and changes in client requirements, or may be able to devote greater resources to the promotion and sale of their products and services. In addition, in order to meet client requirements, we must often work cooperatively with companies that are, in other circumstances, competitors. The need for us to work cooperatively with such companies may limit our ability to compete aggressively with those companies in other circumstances.

A Failure of, Error in or Damage to Our Computer and Telecommunications Systems Would Impair Our Ability to Conduct Transactions, Payment Processing and Support Services and Harm Our Business Operations.

We provide TDS and payment processing transaction services, as well as support services, using complex computer and telecommunications systems. Our business could be significantly harmed if these systems fail or suffer damage from fire, natural disaster, terrorism including cyber terrorism, power loss, telecommunications failure, unauthorized access by hackers, electronic break-ins, intrusions or attempts to deny our ability to deploy our services, computer viruses or similar events. In addition, the growth of our client base, a significant increase in transaction volume or an expansion of our facilities may strain the capacity of our computers and telecommunications systems and lead to degradations in performance or system failure. Many of our agreements with telecommunications carriers contain level of service commitments, which we might be unable to fulfill in the event of a natural disaster, an actual or threatened terrorist attack or a major system failure. Errors in our computer and telecommunications systems may adversely impact our ability to provide the products and services contracted for by our clients. We may need to expend significant capital or other resources to protect against or repair damage to our systems that occur as a result of malicious activities, cyber-terrorism, natural disasters or human error, but these protections and repairs may not be completely effective. Our property and business interruption insurance and errors and omissions insurance might not be adequate to compensate us for any losses that may occur as the result of these types of damage. It is also possible that such insurance might cease to be available to us on commercially reasonable terms, or at all.

Our Success Depends in Part on Our Ability to Obtain Patents for, or Otherwise Protect, Our Proprietary Technologies.

We rely on a combination of copyright, patent, trademark and trade secret laws, license and confidentiality agreements, and software security measures to protect our proprietary rights. Much of our know-how and other proprietary technology is not covered by patent or similar protection, and in many cases cannot be so protected. If we cannot obtain patent or other protection for our proprietary software and other proprietary intellectual property rights, other companies could more easily enter our markets and compete successfully against us.

We have a limited number of patents in the U.S. and abroad, and have pending applications for additional patents, but we cannot be certain that any additional patents will be issued on those applications, that any of our current or future patents will protect our business or technology against competitors that develop similar technology or products or services or provide us with a competitive advantage, or that others will not claim rights in our patents or our proprietary technologies.

Patents issued and patent applications filed relating to products used in the wireless telecommunications and payment processing industry are numerous and it may be the case that current and potential competitors and other

third parties have filed or will file applications for, or have received or will receive, patents or obtain additional proprietary rights relating to products used or proposed to be used by us. We may not be aware of all patents or patent applications that may materially affect our ability to make, use or sell any current or future products or services.

The laws of some countries in which our products are licensed do not protect our products and intellectual property rights to the same extent as U.S. laws. We generally enter into non-disclosure agreements with our employees and clients and restrict access to, and distribution of, our proprietary information. Nevertheless, we may be unable to deter misappropriation of our proprietary information or detect unauthorized use of and take appropriate steps to enforce our intellectual property rights. Our competitors also may independently develop technologies that are substantially equivalent or superior to our technology.

Table of Contents**We May Become a Party to Intellectual Property Infringement Claims, Which Could Harm Our Business.**

We are aware of, and we expect we may become a party to, a pending lawsuit captioned *Net MoneyIN, Inc. v. VeriSign, Inc., et al.*, Case No. CIV 01-441 TUC RCC, which lawsuit was brought by a company that claims to hold patents related to such services. The case was brought in the United States District Court for the District of Arizona, against a variety of defendants, including payment processing gateway providers and banks, which are accused of infringing certain patents involving payment processing over computer networks. The plaintiff alleges that numerous products or services infringe its patents, including the Authorize.Net Payment Gateway Service and eCheck.Net service. Neither Lightbridge nor Authorize.Net is a party to the suit, but Authorize.Net is indemnifying and defending defendants InfoSpace, Inc. and E-Commerce Exchange, Inc. as to services provided by Authorize.Net. Defendant Wells Fargo Bank, N.A. has also requested indemnification, including defense costs, from Authorize.Net based on certain contracts with Authorize.Net. Lightbridge anticipates that plaintiff may attempt to add Authorize.Net and/or Lightbridge as a party defendant. The litigation is currently in the fact discovery phase, and no trial date has been set.

From time to time, we have had and may be forced to respond to or prosecute other intellectual property infringement claims to protect our rights or defend a client's rights. These claims, regardless of merit, may consume valuable management time, result in costly litigation or cause product shipment delays, all of which could seriously harm our business and operating results. Furthermore, parties making such claims may be able to obtain injunctive or other equitable relief that could effectively block our ability to make, use, sell or otherwise practice our intellectual property, whether or not patented or described in pending patent applications, or to further develop or commercialize our products in the U.S. and abroad and could result in the award of substantial damages against us. We may be required to enter into royalty or licensing agreements with third parties claiming infringement by us of their intellectual property in order to settle these claims. These royalty or licensing agreements, if available, may not have terms that are acceptable to us. In addition, if we are forced to enter into a license agreement with terms that are unfavorable to us, our operating results would be materially harmed. We may also be required to indemnify our clients for losses they may incur under indemnification agreements if we are found to have violated the intellectual property rights of others.

Our Business Could Require Additional Financing.

Our future business activities, including our operation of Authorize.Net, the development or acquisition of new or enhanced products and services, the acquisition of additional computer and network equipment, the costs of compliance with government regulations and the international expansion of our business will require us to make significant capital expenditures. If our available cash resources prove to be insufficient, because of unanticipated expenses, revenue shortfalls or otherwise, we may need to seek additional financing or curtail our expansion activities. If we obtain equity financing for any reason, our existing stockholders may experience dilution in their investments. If we obtain debt financing, our business could become subject to restrictions that affect our operations or increase the level of risk in our business. It is also possible that, if we need additional financing, we will not be able to obtain it on acceptable terms, or at all.

Item 8. Financial Statements and Supplementary Data

The financial statements of the Company, as restated, are listed in the index included in Item 15(a)(1) of this Amendment No. 1 to our Annual Report on Form 10-K/A.

Item 9A. Controls and Procedures**(a) Evaluation of disclosure controls and procedures**

In January 2006, we re-evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of December 31, 2004. Our Chief Executive Officer and our Chief Financial Officer supervised and participated in this evaluation. Due to the identification of a material weakness in internal control over financial reporting related to the Company's accounting for income taxes, as described below, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were not effective.

(b) Management's Annual Report on Internal Control Over Financial Reporting (as revised)

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). Our internal control system was designed to provide

reasonable assurance to our management and board of directors regarding the preparation and fair presentation of published financial statements.

Table of Contents

In our 2004 Annual Report on Form 10-K, filed on March 17, 2005, our management included Management's Annual Report on Internal Control Over Financial Reporting therein, which expressed a conclusion by management that as of December 31, 2004, our internal control over financial reporting was effective. As a result of the restatement of our financial statements, as described in Note 2 to the financial statements, we have concluded that a material weakness in internal control over financial reporting existed as of December 31, 2004 and, accordingly, have revised our assessment of the effectiveness of our internal control over financial reporting.

The Public Company Accounting Oversight Board's Auditing Standard No. 2 defines a material weakness as a significant deficiency, or a combination of significant deficiencies, that results in there being a more than remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

In making this revised assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control - Integrated Framework. Based on our revised assessment, we determined that our internal control over financial reporting was not effective.

In January 2005, our Tax Manager voluntarily resigned. We engaged a tax consultant resource to assist us with the tax review for fiscal 2004. We did not have adequate internal technical expertise with respect to income tax accounting to effectively oversee and review our accounting over this area. This lack of adequate internal technical expertise contributed to a material error in our accounting for income taxes, which was identified in January 2006, during the course of the audit of our financial statements for fiscal 2005. This deficiency was determined to be a material weakness. The error related to the deferred income tax liability for the book and income tax basis difference in goodwill and trademarks as a result of the Authorize.Net acquisition in 2004. The deferred income tax liability was incorrectly offset against deferred income tax assets. As a result of the error, we have restated our financial statements for the year ended December 31, 2004.

In March 2004, we acquired Authorize.Net. For purposes of evaluating our internal controls over financial reporting, management determined that the internal control over financial reporting of Authorize.Net would be excluded from the fiscal 2004 internal control assessment, as permitted by the rules and regulations of the Securities and Exchange Commission. The financial statements of Authorize.Net reflect total assets and revenues constituting 8% and 20%, respectively, of the related consolidated financial statement amounts as of and for the year ended December 31, 2004.

Management's January 2006 assessment of the effectiveness of our internal control over financial reporting as of December 31, 2004 has been audited to by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report which is included following Item 9A below.

(c) Changes in internal control over financial reporting

No changes in the Company's internal control over financial reporting occurred during the quarter ended December 31, 2004 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Regarding the material weakness described above, the Company is in the process of taking steps to ensure that the material weakness is remediated by implementing enhanced control procedures over accounting for income taxes which included hiring a new Director of Tax in June 2005 and engaging tax consulting resources to assist with the Company's evaluation of complex issues concerning tax accounting and to assist management in developing its judgments with respect to such issues.

(d) Inherent Limitations of Disclosure Controls and Internal Control Over Financial Reporting

The effectiveness of our disclosure controls and procedures and our internal control over financial reporting is subject to various inherent limitations, including cost limitations, judgments used in decision making, assumptions about the likelihood of future events, the soundness of our systems, the possibility of human error, and the risk of fraud. Moreover, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions and the risk that the degree of compliance with policies or procedures may deteriorate over time. Because of these limitations, there can be no assurance that any system of disclosure controls and procedures or internal control over financial reporting will be successful in preventing all errors or fraud or in making all material information known in a timely manner to the appropriate levels of management.

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
Lightbridge, Inc.

Burlington, Massachusetts

We have audited management's assessment, included in the accompanying Management's Annual Report on Internal Control over Financial Reporting (as revised), that Lightbridge, Inc. & Subsidiaries (the Company) did not maintain effective internal control over financial reporting as of December 31, 2004, because of the effect of the material weakness identified in management's assessment based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. As described in Management's Annual Report on Internal Control Over Financial Reporting, management excluded from their assessment the internal control over financial reporting at Authorize.Net, which was acquired on March 31, 2004 and whose financial statements reflect total assets and revenues constituting 8% and 20%, respectively, of the related consolidated financial statement amounts as of and for the year ended December 31, 2004. Accordingly, our audit did not include the internal control over financial reporting at Authorize.Net. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our report dated March 16, 2005, we expressed an unqualified opinion on management's assessment that the Company maintained effective internal control over financial reporting and an unqualified opinion on the effectiveness of internal control over financial reporting. As described in the following paragraph,

Table of Contents

the Company subsequently identified a material misstatement in its 2004 annual financial statements, which caused such annual financial statements to be restated. Management subsequently revised its assessment due to the identification of a material weakness, described in the following paragraph, in connection with the financial statement restatement. Accordingly, our opinion on the effectiveness of the Company's internal control over financial reporting as of December 31, 2004 expressed herein is different from that expressed in our previous report.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. The following material weakness has been identified and included in management's assessment: The Company's controls over the accounting for income taxes did not operate effectively as of December 30, 2004. Specifically, the Company did not have adequate internal technical expertise in performing the review of the income tax provision and related deferred tax liability and failed to detect a material error. This material weakness resulted in the restatement of the Company's previously issued financial statements as described in Note 2 to the consolidated financial statements.

This material weakness was considered in determining the nature, timing, and extent of audit tests applied in our audit of the consolidated financial statements as of and for the year ended December 31, 2004 (as restated), of the Company and this report does not affect our report on such restated financial statements.

In our opinion, management's revised assessment that the Company did not maintain effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on the criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also in our opinion, because of the effect of the material weakness described above on the achievement of the objectives of the control criteria, the Company has not maintained effective internal control over financial reporting as of December 31, 2004, based on the criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2004 (as restated), of the Company and our report dated March 16, 2005 (February 17, 2006 as to the effects of the restatement discussed in Note 2) expressed an unqualified opinion on those restated financial statements.

/s/ DELOITTE & TOUCHE LLP

Boston, Massachusetts

March 16, 2005 (February 17, 2006 as to the effect of the material weakness)

Table of Contents

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) *Documents filed as part of this report*

(1) Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm – Deloitte & Touche LLP

Consolidated Balance Sheets as of December 31, 2004 (Restated) and 2003

Consolidated Statements of Operations for the years ended December 31, 2004 (Restated), 2003 and 2002

Consolidated Statements of Stockholders' Equity for the years ended December 31, 2004 (Restated), 2003 and 2002

Consolidated Statements of Cash Flows for the years ended December 31, 2004 (Restated), 2003 and 2002

Notes to Consolidated Financial Statements

(2) Consolidated Financial Statement Schedules

All schedules have been omitted because the required information either is not applicable or is shown in the financial statements or notes thereto.

Table of Contents

(3) Exhibits

| Exhibit No. | Description |
|------------------------|---|
| 2.1(1) | Amended and Restated Agreement and Plan of Reorganization dated November 8, 2000 among the Company, Lightning Merger Corporation and Corsair Communications, Inc. |
| 2.2(2) | Stock Sale Agreement by and among InfoSpace, Inc., Go2Net, Inc., Authorize.Net Corporation and Lightbridge, Inc. dated as of February 29, 2004. |
| 3.1(3) | Amended and Restated Certificate of Incorporation of the Company |
| 3.2(3) | Amended and Restated By-Laws of the Company |
| 3.3(4) | Amendment to Amended and Restated By-Laws of the Company, adopted October 29, 1998 |
| 4.1(3) | Specimen Certificate for Common Stock of the Company |
| 4.2(5) | Rights Agreement dated as of November 14, 1997, between Lightbridge, Inc. and American Stock Transfer and Trust Company, as Rights Agent |
| 4.3(5) | Form of Certificate of Designation of Series A Participating Cumulative Preferred Stock of Lightbridge, Inc. |
| 4.4(5) | Form of Right Certificate |
| 10.1(3) | 1991 Registration Rights Agreement dated February 11, 1991, as amended, between the Company and the persons named therein |
| 10.2(3) | Subordinated Note and Warrant Purchase Agreement dated as of August 29, 1994 between the Company and the Purchasers named therein, including form of Subordinated 14% Promissory Notes and form of Common Stock Purchase Warrants |
| 10.3(3) | Form of Common Stock Purchase Warrants issued August 1995 |
| 10.4(3) | Settlement Agreement dated February 2, 1996 between the Company, BEB, Inc., BEB Limited Partnership I, BEB Limited Partnership II, BEB Limited Partnership III, BEB Limited Partnership IV, certain related parties and Brian Boyle |
| 10.5(3) | 1990 Incentive and Nonqualified Stock Option Plan |
| 10.6(3) | 1996 Employee Stock Purchase Plan |
| 10.7(3) | Employment Agreement dated August 16, 1996 between the Company and Pamela D.A. Reeve |
| 10.8(3) | Letter Agreement, dated August 26, 1996, between the Company and Brian E. Boyle, including form of Common Stock Purchase Warrant and Registration Rights Agreement |
| 10.9(3) | |

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Office Lease dated September 30, 1994, as amended, between the Company and Hobbs Brook Office Park

- 10.10(6) Office Lease dated March 5, 1997, between the Company and Sumitomo Life Realty (N.Y.), Inc.
- 10.11(7) First and Second Amendments dated July 22, 1997 and October 6, 1997, respectively, to the Office Lease included as Item 10.10
- 10.12(8) Office Building Lease, dated March 12, 1998, between 8900 Grantline Road Investors and the Company
- 10.13(9) Third and Fourth Amendments dated March 15, 1999 and July 16, 1999, respectively, to the office lease included as Item 10.10

Table of Contents

| Exhibit No. | Description |
|------------------------|---|
| 10.14(9) | Office Lease dated October 4, 1999, between the Company and New Alliance Properties, Inc. |
| 10.15(9) | First Amendment dated September 20, 1999 to the Office Lease included as Item 10.9 |
| 10.16(10) | Fifth and Sixth Amendments dated March 10, 2000 to the office lease included as Item 10.10 |
| 10.17(11) | Employment Agreement dated May 25, 2000 between the Company and Harlan Plumley |
| 10.18(11) | 1996 Incentive and Non-Qualified Stock Option Plan (as amended) |
| 10.19(11) | 1998 Non-Statutory Stock Option Plan (as amended) |
| 10.20(12) | Office lease dated August 15, 2000 between the Company and Arthur Pappathanasi, trustee of 330 Scangas Nominee Trust |
| 10.21(13) | Amendment to 1998 Non-Statutory Stock Option Plan adopted on November 16, 2000 |
| 10.22(14) | Amendment to 1996 Incentive and Non-Qualified Stock Option Plan |
| 10.23(15) | Amendment to 1996 Employee Stock Purchase Plan |
| 10.24(16) | Memorandum Agreement between Harlan Plumley and the Company dated April 23, 2002 |
| 10.25(17) | Separation Agreement and Release between Carla Marcinowski and the Company dated June 28, 2002 |
| 10.26(17) | Letter Agreement between Thomas Reynolds and the Company dated July 19, 2002 |
| 10.27(18) | Amendment to the Company's 1996 Employee Stock Purchase Plan, as amended |
| 10.28(18) | Memorandum Agreement dated August 5, 2002 by and between the Company and Pamela D.A. Reeve |
| 10.29(18) | Memorandum Agreement dated August 5, 2002 by and between the Company and Judith Dumont |
| 10.30(19) | Foreign Exchange Master Agreement dated March 31, 2003 by and among Citizens Bank of Massachusetts, the Company, Corsair Communications, Inc., Coral Systems, Inc., and Lightbridge Security Corporation. |
| 10.31(20) | Separation agreement and release dated July 8, 2003 between Christine Cournoyer and the Company |
| 10.32(21) | Office Building Lease, dated December 23, 2003 between Corporate Drive Corporation, as Trustee of Corporate Drive Nominee Realty Trust, and the Company |
| 10.33(2) | Separation Agreement and Release between Michael Mitsock and the Company dated January 26, 2004 |

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- 10.34(2) Separation Agreement and Release between Stefan Gladyszewski and the Company dated January 26, 2004
 - 10.35(24) Lease between Region of Queens Municipality, LTBG TeleServices ULC and Lightbridge, Inc. dated February 10, 2004
 - 10.36(22) Separation Agreement and Release between Harlan Plumley and the Company dated May 20, 2004
 - 10.37(22) Amendment to the 1996 Stock Purchase Plan
 - 10.38(22) 2004 Stock Incentive Plan
 - 10.39(20) Separation Agreement and Release between Pamela D.A. Reeve and the Company dated August 2, 2004
 - 10.40(20) Employment Agreement between Robert E. Donahue and the Company dated August 2, 2004
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Table of Contents

| Exhibit No. | Description |
|------------------------|---|
| 10.41(20) | Office Lease Agreement between EOP Operating Limited Partnership and the Company dated as of August 10, 2004 |
| 10.42(20) | Terms and Conditions of Stock Options Granted Under the Lightbridge, Inc. 2004 Stock Incentive Plan |
| 10.43(20) | Form of Notice of Grant of Stock Options Under the Lightbridge, Inc. 2004 Stock Incentive Plan |
| 10.44(23) | Separation Agreement and Release between Edward DeArias and the Company dated October 28, 2004 |
| 23.1 | Consent of Independent Registered Public Accounting Firm Deloitte & Touche LLP |
| 31.1 | Certification of Robert E. Donahue dated February 17, 2006 |
| 31.2 | Certification of Timothy C. O'Brien dated February 17, 2006 |
| 32.1 | Certification of Robert E. Donahue and Timothy C. O'Brien dated February 17, 2006 (furnished but not filed with the Securities and Exchange Commission). |
| (1) | Incorporated by reference to the Company's Registration Statement on Form S-4 (Registration Number 333-50196), as filed with the Securities and Exchange Commission on November 17, 2000. |
| (2) | Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2004. |
| (3) | Incorporated by reference to the Company's Registration Statement on Form S-1, as amended (File No. 333-6589). |
| (4) | Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 1998. |
| (5) | Incorporated by reference to the Company's Registration Statement on Form 8-A, as filed with the Securities and Exchange Commission on November 21, 1997. |
| (6) | Incorporated by reference to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 1996. |
| (7) | Incorporated by reference to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 1997. |
| (8) | Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 1998. |
| (9) | |

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Incorporated by reference to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 1999.

- (10) Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2000.
- (11) Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2000.
- (12) Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2000.
- (13) Incorporated by reference to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2000.
- (14) Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2001.
- (15) Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2001.
- (16) Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2002.
- (17) Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2002.
- (18) Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2002.
- (19) Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2003.

Table of Contents

- (20) Incorporated by reference to the Company's Quarterly Report of Form 10-Q for the quarter ended September 30, 2004.
- (21) Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2003.
- (22) Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2004.
- (23) Incorporated by reference to the Company's Current Report on Form 8-K dated November 8, 2004.

Table of Contents**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this amendment to be signed on its behalf by the undersigned, thereunto duly authorized, on the 17th day of February, 2006.

Lightbridge, Inc.

By: /s/ Robert E. Donahue
Robert E. Donahue
President and Chief Executive Officer

Each person whose signature appears below hereby appoints Robert E. Donahue and Timothy C. O'Brien, and each of them severally, acting alone and without the other, his or her true and lawful attorney-in-fact with the authority to execute in the name of each such person, and to file with the Securities and Exchange Commission, together with any exhibits thereto and other documents therewith, any and all amendments to this Annual Report on Form 10-K/A necessary or advisable to enable Lightbridge, Inc., to comply with the rules, regulations, and requirements of the Securities Act of 1934, as amended, in respect thereof, which amendments may make such other changes in the Annual Report on Form 10-K/A as the aforesaid attorney-in-fact executing the same deems appropriate.

Pursuant to the requirements of the Securities Exchange Act of 1934, this amendment has been signed below by the following persons in the capacities and on the dates indicated.

| Name | Title | Date |
|--|--|-------------------|
| /s/ Timothy C. O'Brien Timothy C. O'Brien | Vice President, Finance and Administration, Chief Financial Officer and Treasurer (Principal Financial and Accounting Officer) | February 17, 2006 |
| /s/ Robert E. Donahue Robert E. Donahue | President, Chief Executive Officer and Director (Principal Executive Officer) | February 17, 2006 |
| /s/ Rachelle B. Chong * Rachelle B. Chong | Director | February 17, 2006 |
| /s/ Gary Haroian * Gary Haroian | Director | February 17, 2006 |
| /s/ Kevin C. Melia * Kevin C. Melia | Director | February 17, 2006 |
| /s/ Andrew G. Mills * Andrew G. Mills | Director | February 17, 2006 |
| /s/ David G. Turner * David G. Turner | Director | February 17, 2006 |

* Executed on behalf of the identified individuals by Timothy C. O'Brien, attorney-in-fact.

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
Lightbridge, Inc.

Burlington, Massachusetts

We have audited the accompanying consolidated balance sheets of Lightbridge, Inc. and subsidiaries (the Company) as of December 31, 2004 and 2003, and the related consolidated statements of operations, stockholders equity, and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on the financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Lightbridge, Inc. and subsidiaries as of December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2, the accompanying 2004 consolidated financial statements have been restated.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company s internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated March 16, 2005 (February 17, 2006 as to the material weakness) expressed an unqualified opinion on management s assessment of the effectiveness of the Company s internal control over financial reporting and an adverse opinion on the effectiveness of the Company s internal control over financial reporting.

/s/ Deloitte & Touche LLP

Boston, Massachusetts

March 16, 2005 (February 17, 2006 as to the restatement discussed in Note 2)

F-1

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Amounts in thousands except share and per share amounts)

| | December 31, | |
|--|----------------------------------|-------------|
| | 2004 | 2003 |
| | (As Restated, see Note 2) | |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 39,036 | \$ 69,685 |
| Short-term investments | 12,589 | 63,803 |
| Accounts receivable, net | 18,940 | 20,071 |
| Deferred tax assets | | 3,267 |
| Other current assets | 3,132 | 4,158 |
| | | |
| Total current assets | 73,697 | 160,984 |
| Property and equipment, net | 16,978 | 9,408 |
| Deferred tax assets | | 4,553 |
| Other assets, net | 336 | 362 |
| Restricted cash | 600 | |
| Goodwill | 57,628 | 1,664 |
| Intangible assets, net | 21,247 | 865 |
| | | |
| Total assets | \$ 170,486 | \$ 177,836 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 7,300 | \$ 6,825 |
| Accrued compensation and benefits | 5,073 | 4,493 |
| Other accrued liabilities | 4,113 | 3,887 |
| Deferred rent | 1,592 | |
| Deferred revenues | 3,681 | 5,461 |
| Funds due to merchants | 5,558 | |
| Reserves for restructuring | 3,383 | 2,634 |
| | | |
| Total current liabilities | 30,700 | 23,300 |
| Deferred rent, less current portion | 2,709 | |
| Deferred tax liability | 1,261 | |
| Other long-term liabilities | 149 | 33 |
| | | |
| Total liabilities | 34,819 | 23,333 |

Commitments and contingencies (Note 8)

Stockholders' equity:

Preferred stock; \$0.01 par value, 5,000,000 shares authorized; no shares issued or outstanding at December 31, 2004 and 2003

Common stock; \$0.01 par value, 60,000,000 shares authorized; 29,951,826 and 29,647,795 shares issued; 26,512,783 and 26,843,352 shares outstanding at

December 31, 2004 and 2003, respectively

Additional paid-in capital

Warrants

Foreign currency translation

(Accumulated deficit) retained earnings

Less treasury stock; 3,439,043 and 2,804,443 shares at cost at December 31, 2004 and 2003, respectively

Total stockholders' equity

Total liabilities and stockholders' equity

| | |
|----------|----------|
| 300 | 298 |
| 167,465 | 166,882 |
| 206 | 206 |
| (184) | |
| (11,333) | 4,072 |
| (20,787) | (16,955) |

135,667 154,503

\$ 170,486 \$ 177,836

See notes to consolidated financial statements.

F-2

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(Amounts in thousands except per share amounts)

| | Years Ended December 31, | | |
|---|---------------------------|-----------|-----------|
| | 2004 | 2003 | 2002 |
| | (As Restated, see Note 2) | | |
| Revenues: | | | |
| Transaction services | \$ 103,648 | \$ 80,552 | \$ 88,376 |
| Consulting and maintenance services | 19,898 | 28,666 | 32,491 |
| Software licensing and hardware | 9,509 | 10,760 | 12,571 |
| | | | |
| Total revenues | 133,055 | 119,978 | 133,438 |
| Cost of revenues: | | | |
| Transaction services | 54,831 | 45,667 | 49,194 |
| Consulting and maintenance services | 9,930 | 12,741 | 13,663 |
| Software licensing and hardware | 3,129 | 3,541 | 3,086 |
| | | | |
| Total cost of revenues | 67,890 | 61,949 | 65,943 |
| | | | |
| Gross profit: | | | |
| Transaction services | 48,817 | 34,885 | 39,182 |
| Consulting and maintenance services | 9,968 | 15,925 | 18,828 |
| Software licensing and hardware | 6,380 | 7,219 | 9,485 |
| | | | |
| Total gross profit | 65,165 | 58,029 | 67,495 |
| | | | |
| Operating expenses: | | | |
| Engineering and development | 29,000 | 28,426 | 29,269 |
| Sales and marketing | 22,541 | 14,239 | 13,270 |
| General and administrative | 15,987 | 14,143 | 18,170 |
| Restructuring | 4,346 | 5,079 | 3,616 |
| Impairment of goodwill | 1,664 | | |
| Impairment of other intangible assets | 599 | | |
| Purchased in-process research and development | 679 | | 1,618 |
| Gain on sale of Fraud Centurion assets | (2,673) | | |
| | | | |
| Total operating expenses | 72,143 | 61,887 | 65,943 |

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| | | | |
|---|-------------|------------|----------|
| Income (loss) from operations | (6,978) | (3,858) | 1,552 |
| Other income (expense): | | | |
| Interest income | 1,185 | 1,778 | 2,439 |
| Equity in loss of partnership investment | | (471) | (464) |
| Total other income, net | 1,185 | 1,307 | 1,975 |
| Income (loss) before provision for income taxes | (5,793) | (2,551) | 3,527 |
| Provision for (benefit from) income taxes | 9,612 | (1,102) | (103) |
| Net income (loss) | \$ (15,405) | \$ (1,449) | \$ 3,630 |
| Basic earnings (loss) per share (Note 13) | \$ (0.58) | \$ (0.05) | \$ 0.13 |
| Diluted earnings (loss) per share (Note 13) | \$ (0.58) | \$ (0.05) | \$ 0.13 |

See notes to consolidated financial statements.

F-3

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDER S EQUITY
(Amounts in thousands)

| | Common Stock Shares | Additional Paid-in Capital | Foreign Currency Gain/Loss | Receivable From Stockholders Warrants | Retained Earnings (Accumulated Treasury Stock Deficit) (As Restated, see Note 2) | Treasury Stock Shares | Total Stockholders Equity (As Restated, see Note 2) |
|--|---------------------------|----------------------------------|----------------------------------|--|--|--------------------------|---|
| Balance, January 1, 2002 | 29,093 | 291 | 162,367 | (115) | 206 | 1,891 | 161,522 |
| Issuance of common stock for cash | 72 | 1 | 584 | | | | 585 |
| Exercise of common stock options | 394 | 4 | 2,118 | | | | 2,122 |
| Retirement of treasury stock | (158) | | | | | (158) | |
| Repurchase of common stock | | | | | | 1,186 | (8,505) |
| Tax benefit from disqualifying dispositions of stock options | | | 172 | | | | 172 |
| Shareholder note written off as uncollectible | | | | 115 | | | 115 |
| Net income | | | | | 3,630 | | 3,630 |
| Balance, December 31, 2002 | 29,401 | 296 | 165,241 | | 206 | 5,521 | 159,641 |
| Issuance of common stock for cash | 84 | | 435 | | | | 435 |
| Exercise of common stock options | 163 | 2 | 995 | | | | 997 |
| Repurchase of common stock | | | | | | 685 | (5,332) |
| | | | 211 | | | | 211 |

| | | | | | | | | | | |
|--|--|--|--|--|--|---------|--|--|--|---------|
| Tax benefit from disqualifying dispositions of stock options | | | | | | | | | | |
| Net loss | | | | | | (1,449) | | | | (1,449) |

**Balance,
December 31,
2003**

| | | | | | | | | | |
|--------|--------|------------|----|----|--------|----------|-------|-------------|------------|
| 29,648 | \$ 298 | \$ 166,882 | \$ | \$ | \$ 206 | \$ 4,072 | 2,804 | \$ (16,955) | \$ 154,503 |
|--------|--------|------------|----|----|--------|----------|-------|-------------|------------|

| | | | | | | | | | | |
|--|-----|---|-----|-------|--|----------|-----|---------|--|----------|
| Issuance of common stock for cash | 84 | | 395 | | | | | | | 395 |
| Exercise of common stock options | 220 | 2 | 148 | | | | | | | 150 |
| Repurchase of common stock | | | | | | | 635 | (3,832) | | (3,832) |
| Foreign currency gain/loss | | | | (184) | | | | | | (184) |
| Tax benefit from disqualifying dispositions of stock options | | | 40 | | | | | | | 40 |
| Net loss (As Restated, see Note 2) | | | | | | (15,405) | | | | (15,405) |

**Balance,
December 31,
2004 (As
Restated, see
Note 2)**

| | | | | | | | | | |
|--------|--------|------------|----------|----|--------|-------------|-------|-------------|------------|
| 29,952 | \$ 300 | \$ 167,465 | \$ (184) | \$ | \$ 206 | \$ (11,333) | 3,439 | \$ (20,787) | \$ 135,667 |
|--------|--------|------------|----------|----|--------|-------------|-------|-------------|------------|

See notes to consolidated financial statements.

F-4

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Amounts in thousands)

| | Years Ended December 31, | | |
|--|---------------------------|--------------|--------------|
| | 2004 | 2003 | 2002 |
| | (As Restated, see Note 2) | | |
| Cash flows from operating activities: | | | |
| Net income (loss) | \$ (15,405) | \$ (1,449) | \$ 3,630 |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities: | | | |
| Deferred income taxes | 9,081 | (1,095) | 1,732 |
| Purchased in-process research and development | 679 | | 1,618 |
| Depreciation and amortization | 10,909 | 10,398 | 15,326 |
| Loss on disposal of property and equipment | 63 | 1,511 | 735 |
| Gain on sale of Fraud Centurion assets | (2,673) | | |
| Impairment of goodwill and intangibles | 2,263 | | |
| Tax benefit from disqualifying dispositions of stock options | 40 | 211 | 172 |
| Changes in assets and liabilities: | | | |
| Accounts receivable | 2,967 | (2,392) | 9,964 |
| Inventories | | | 263 |
| Other assets | 1,316 | (699) | 2,298 |
| Accounts payable and accrued liabilities | 528 | 1,359 | (3,361) |
| Funds due to merchants | (839) | | |
| Other long-term liabilities | 116 | (226) | (408) |
| Deferred rent | 4,301 | | |
| Deferred revenues | (1,252) | 1,169 | (1,952) |
| Net cash provided by operating activities | 12,094 | 8,787 | 30,017 |
| Cash flows from investing activities: | | | |
| Purchases of property and equipment | (14,743) | (4,869) | (4,370) |
| Purchase of investments | (33,490) | (179,385) | (119,539) |
| Restricted cash | (600) | | |
| Net cash proceeds from the sale of Fraud Centurion assets | 2,374 | | |
| Proceeds from sales and maturities of short-term investments | 84,705 | 158,388 | 87,804 |
| Acquisition of Authorize.Net, net of cash acquired | (77,510) | | |
| Acquisition of Altawave | | | (4,949) |
| Net cash provided by (used in) investing activities | (39,264) | (25,866) | (41,054) |
| Cash flows from financing activities: | | | |

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| | | | |
|---|-----------|-----------|-----------|
| Repurchases of common stock | (3,832) | (5,332) | (8,505) |
| Proceeds from issuance of common stock | 545 | 1,432 | 2,707 |
| Net cash provided by (used in) financing activities | (3,287) | (3,900) | (5,798) |
| Effects of foreign exchange rate changes on cash and cash equivalents | (192) | | |
| Net increase (decrease) in cash and cash equivalents | (30,649) | (20,979) | (16,835) |
| Cash and cash equivalents, beginning of year | 69,685 | 90,664 | 107,499 |
| Cash and cash equivalents, end of year | \$ 39,036 | \$ 69,685 | \$ 90,664 |

See notes to consolidated financial statements.

F-5

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Business and Acquisition Activity

Business Lightbridge, Inc. (Lightbridge or the Company) was incorporated in June 1989 under the laws of the state of Delaware. The Company develops, markets and supports products and services for businesses that sell products or services online and communications providers, including Internet Protocol (IP)-based payment gateway, customer qualification and acquisition, risk management, prepaid billing, instant conferencing and authentication services. Lightbridge's four areas of business consist of Payment Processing Services (Payment Processing), Telecom Decisioning Services (TDS), Intelligent Network Services (INS), and Instant Conferencing Services (Instant Conferencing).

Asset Purchase On February 22, 2002, a wholly owned subsidiary of Lightbridge acquired all of the assets and certain of the liabilities of Altawave Inc. (Altawave) in exchange for the payment of \$4.0 million in cash, plus up to an additional \$6.0 million payment contingent on the achievement of certain revenue goals. The technology acquired from Altawave includes solutions that offer wireless carriers a service platform for the development and management of data content and applications. The results of Altawave have been included in these consolidated financial statements from the date of acquisition.

The allocation of the Altawave purchase price was based upon an independent appraisal of the estimated fair value of the assets acquired and the liabilities assumed. The initial purchase price of \$4.0 million, plus the capitalized value of acquisition costs and assumed liabilities totaling \$0.9 million, was allocated as follows:

| | Estimated Fair Values (\$ in millions) |
|-------------------------------------|---|
| Acquired technology | \$ 1.3 |
| Fixed assets | 0.3 |
| Goodwill | 1.7 |
| In-process research and development | 1.6 |
| Acquisition costs accrued | (0.6) |
| Operating liabilities assumed | (0.3) |
| | |
| Total cash purchase price | \$ 4.0 |

Any additional contingent consideration that would have been paid in connection with the Altawave acquisition would have been recorded as goodwill when the underlying conditions were met and payment became probable. No contingent payments were required to be made in connection with the Altawave acquisition.

In connection with the Altawave acquisition, the Company recorded a \$1.6 million charge during the first quarter of 2002 for several IPR&D projects. The technology acquired from Altawave includes solutions that offer wireless carriers and enterprises a service platform for the development and management of data content and applications. The complexity of the technology lies in its comprehensive, secure and scalable characteristics. The research projects in process at the date of acquisition related to the development of the Lightbridge Mobile Data Manager (MDM) suite of products consisting of MDM Server, MDM Administration, MDM Altalinks and MDM Provisioner, as well as the Consumer Group Applications (CGA). Development of the technology was started in 2000.

The value of the projects was determined by an independent appraiser using the income approach. The discounted cash flow method was utilized to estimate the present value of the expected income that could be generated through revenues from the projects over their initial estimated useful lives through 2009. The percentage of completion for the projects was determined based on the amount of research and development expenses incurred through the date of acquisition as a percentage of estimated total research and development expenses to bring the projects to technological

feasibility. At the acquisition date, the Company estimated that the MDM suite and CGA were approximately 70% and 32% complete, respectively, with fair values of approximately \$1.0 million and \$0.6 million, respectively. The discount rate used for the fair value calculation was 37% for the MDM suite and 40% for CGA. At the date of acquisition, development of the technology involved risks to the Company including the remaining development effort required to achieve technological feasibility and uncertainty with respect to the market for the technology. Lightbridge completed the development of the MDM suite in the quarter ended September 30, 2002 and the CGA project in the quarter ended September 30, 2003 having spent approximately \$150 and \$300, respectively, on the projects after the acquisition.

F-6

Table of Contents**LIGHTBRIDGE, INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Asset Purchase On March 31, 2004, the Company acquired all of the outstanding stock of Authorize.Net Corp. (Authorize.Net) from InfoSpace, Inc. for \$81.6 million in cash. In addition, the Company incurred approximately \$2.0 million in acquisition related costs. Authorize.Net provides credit card and electronic check payment processing solutions to companies that process orders for goods and services over the Internet, at retail locations and on wireless devices. Authorize.Net connects IP-enabled businesses to large credit card processors and banking organizations, allowing those businesses to accept electronic payments. Through the acquisition of Authorize.Net, the Company expanded its customer transaction business to include online payment processing, while reaching a new customer base of IP-enabled merchants. The results of operations of Authorize.Net have been included in the Company's financial statements since the date of the acquisition.

The aggregate purchase price for the Authorize.Net acquisition has been allocated to the tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values at the date of acquisition as follows (in thousands):

| | |
|---------------------------------------|---------------|
| Tangible assets acquired: | |
| Cash and cash equivalents | \$ 6,097 |
| Accounts receivable | 1,815 |
| Property and equipment | 1,655 |
| Other assets | 265 |
| Liabilities assumed: | |
| Accounts payable and accrued expenses | (1,498) |
| Funds due to merchants | (6,397) |
| Identifiable intangible assets: | |
| In-process research and development | 679 |
| ISO network | 9,300 |
| Merchant customer base | 7,000 |
| Trademarks | 3,600 |
| Existing technology | 3,162 |
| Processor relationships | 300 |
| Goodwill | 57,629 |
| | |
| Total allocated purchase price | \$ 83,607 |

The tangible assets acquired and liabilities assumed were recorded at their estimated fair values. The values of the identifiable intangible assets were determined by an independent appraiser using established valuation techniques accepted in the technology and software industries. The appraisal of the intangible assets involved calculations which were based in part on management's judgments and assumptions. These judgments and assumptions included estimates of growth rates, changes to pricing and margins, estimates of the life of the reseller network and merchant customer base, and an assessment of the value of the existing technology. The reseller network value of \$9.3 million and the processor relationships value of \$300,000 will be amortized over twelve years. The merchant customer base value of \$7.0 million and the existing technology value of \$3.1 million will be amortized over five years. The value of the trademarks of \$3.6 million is not amortized. Excluding trademarks, the weighted average amortization term of the intangible assets is 8.4 years.

In connection with the Authorize.Net acquisition, the Company recorded a \$679,000 charge during the first quarter of 2004 for two in-process research and development (IPR&D) projects. The Authorize.Net technology includes payment gateway solutions that enable merchants to authorize, settle and manage electronic transactions via the Internet, at retail locations and on wireless devices. The research projects in process at the date of acquisition related

to the development of the Card Present Solution (CPS) and the Fraud Tool (FT). Development on the FT project and the CPS project was started at the end of 2003 and the beginning of 2004, respectively. The complexity of the CPS technology lies in its fast, flexible and redundant characteristics. The complexity of the FT technology lies in its responsiveness to changing fraud dynamics and efficiency.

The value of the projects was determined by an independent appraiser using the income method. The discounted cash flow method was utilized to estimate the present value of the expected income that could be generated through revenues from the projects over their estimated useful lives through 2009. The percentage of completion for the projects was determined based on the amount of research and development expenses incurred through the date of acquisition as a percentage of estimated total research and development expenses to bring the projects to technological feasibility. At the acquisition date, the Company estimated that the CPS and the FT projects were approximately 15% and 80% complete, respectively, with fair values of approximately \$638,000 and \$41,000, respectively.

F-7

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The discount rate used for the fair value calculation was 30% for the CPS project and 22% for the FT project. At the date of acquisition, development of the technology involved risks to the Company including the remaining development effort required to achieve technological feasibility and uncertainty with respect to the market for the technology.

Lightbridge completed the development of the FT in May 2004 having spent approximately \$129,000 on the project after the acquisition. Total cost to complete the CPS project after acquisition is estimated to be approximately \$650,000. The CPS project is expected to be completed by September 2005. If the development of the technology is not completed on schedule, the potential consequences to the Company may include increased development costs and increased competition from other companies that have competitive products in the market.

The purchase price in excess of the net assets acquired and the identifiable intangible assets acquired was allocated to goodwill. The entire amount of the goodwill is expected to be deductible for tax purposes.

In accordance with Statement of Financial Accounting Standard No. 142 (SFAS 142), the Company is required to analyze the carrying value of goodwill and other intangible assets against the estimated fair value of those assets for possible impairment on an annual basis. The Company has adopted March 31st as the date of the annual impairment test for Authorize.Net. If impairment has occurred, the Company will record a charge in the amount by which the carrying value of the assets exceeds their estimated fair value. Estimated fair value will generally be determined based on discounted cash flows.

Pro forma financial information

The following table presents the unaudited pro forma financial information of the Company including Authorize.Net for the year ended December 31, 2004 and 2003, as if the acquisition had occurred at the beginning of each period presented, after giving effect to certain purchase accounting adjustments. The pro forma adjustments include elimination of revenue associated with pre-acquisition deferred revenue of Authorize.Net, amortization of intangible assets, elimination of interest income associated with the cash purchase price of the acquisition and related income tax effects.

The pro forma net loss for the year ended December 31, 2004 excludes the expense of IPR&D of \$679,000 related to the Authorize.Net acquisition due to its non-recurring nature. These results are presented for illustrative purposes only and are not necessarily indicative of the actual operating results or financial position that would have occurred if the transaction had been consummated on January 1st of each of the periods presented.

| | December 31, 2004 | December 31, 2003 |
|--|---|----------------------------------|
| | (Amounts in thousands, except per share amounts) | |
| Pro forma net revenues | \$ 141,307 | \$ 147,803 |
| Pro forma net loss | \$ (13,570) | \$ (1,677) |
| Pro forma net loss per basic and diluted share | \$ (0.51) | \$ (0.06) |
| Shares used for basic and diluted computation | 26,643 | 27,015 |

Asset Sale On October 1, 2004, the Company closed the sale of its Fraud Centurion products pursuant to an agreement with India-based Subex Systems, Limited NJ (Subex). The Company received net cash proceeds of

\$2.4 million as a result of the sale. The Company recorded a gain of approximately \$2.7 million in the fourth quarter of 2004 due to this transaction.

As part of this transaction, the Company sold equipment with a net book value of approximately \$200,000 and assigned certain maintenance contracts to Subex. The deferred revenue related to these contracts as of December 31, 2004 totaled approximately \$500,000.

F-8

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2. Restatement of Financial Statements

During the fiscal 2005 year end close process, the Company determined that the deferred income tax liability for the book and income tax basis difference in goodwill and trademarks as a result of the Authorize.Net acquisition in 2004 was incorrectly offset against deferred income tax assets in considering the size of the valuation allowance that was required. In accordance with SFAS 142 the deferred tax liability that arises as the Company's goodwill and trademarks are amortized for tax purposes must be considered as a liability related to an asset with an indefinite life. Accordingly, the deferred tax liability was not available as a source of future taxable income to offset the future deductions or benefits embedded in the deferred tax assets created by other deductible temporary timing differences; and the increase in the tax valuation allowance should have been recorded exclusive of the deferred tax liability for non-amortizing goodwill and trademarks in the year ended December 31, 2004. Therefore, the Company has recorded additional deferred tax expense of approximately \$1.3 million to increase its deferred tax liability as of December 31, 2004.

The Company has restated its December 31, 2004 balance sheet, its fiscal 2004 statements of operations, and deferred tax valuation allowance for the impact of this deferred tax liability as follows:

| | December 31, 2004 | |
|---|--------------------------|--------------------|
| | As | |
| | previously | As restated |
| | reported | |
| BALANCE SHEET DATA: | | |
| Deferred tax liability | \$ | \$ 1,261 |
| Total liabilities | 33,558 | 34,819 |
| (Accumulated deficit) retained earnings | (10,072) | (11,333) |
| Total stockholders' equity | 136,928 | 135,667 |
| STATEMENT OF OPERATIONS DATA: | | |
| Income tax expense | \$ 8,351 | \$ 9,612 |
| Net income (loss) | (14,144) | (15,405) |
| Net income (loss) per common share: | | |
| Basic and Diluted | \$ (0.53) | \$ (0.58) |
| DEFERRED TAX VALUATION ALLOWANCE | (24,703) | (25,964) |

The restatement had no impact on net cash provided by operating, financing, or investing activities on the statements of cash flows. The restatement also impacts certain disclosures in Notes 1, 3, 11 and 16 to the Financial Statements.

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3. Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation These consolidated financial statements include the accounts of the Company and its subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation. Investments in entities over which the Company has significant influence, such as the Company's investment in the limited partnership described below, are accounted for using the equity method. Certain prior period balances have been reclassified to conform to the current period presentation.

Significant Estimates The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at each reporting date and the amount of revenue and expense reported each period. These estimates include provisions for bad debts, certain accrued liabilities, recognition of revenue and expenses, and recoverability of deferred tax assets. Actual results could differ from these estimates.

Financial Instruments Financial instruments consist of cash and cash equivalents, short-term investments and accounts receivable. The estimated fair value of these financial instruments approximates their carrying value.

Cash and Cash Equivalents Cash and cash equivalents include short-term, highly liquid instruments, which consist primarily of money market accounts, purchased with remaining maturities of three months or less. The majority of cash and cash equivalents are maintained with major financial institutions in North America. Deposits with these banks may exceed the amount of insurance provided on such deposits; however, these deposits typically may be redeemed upon demand and, therefore, bear minimal risk.

Short-Term Investments Short-term investments consist of corporate debt securities maturing in one year or less and are classified as available-for-sale. These investments are carried at amortized cost, which approximates fair value.

The carrying value of available-for-sale debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. Realized gains and losses, and declines in value judged to be other than temporary on available-for-sale debt securities, if any, are included in interest income. The cost of securities sold is based on the specific identification method. Interest and dividends on securities are included in interest income.

Restricted Cash The Company's restricted cash balance of \$0.6 million on deposit with a financial institution to cover any deficit account balance that could occur if the amount of transactions returned or charged back exceeds the balance on deposit with the financial institution.

Property and Equipment Property and equipment is recorded at cost. Depreciation is provided using the straight-line method over the estimated useful lives of three to seven years. Leasehold improvements are amortized over the term of the lease or the lives of the assets, whichever is shorter. Acquired property and equipment is recorded at appraised fair value, which is then considered cost, and depreciated over the estimated useful life.

Deferred rent Deferred rent consists of step rent and tenant improvement allowances from landlords related to the Company's operating leases for its facilities. Step rent represents the difference between actual operating lease payments due and straight-line rent expense, which is recorded by the Company over the term of the lease, including the build-out period. The amount of the difference is recorded as a deferred credit in the early periods of the lease, when cash payments are generally lower than straight-line rent expense, and is reduced in the later periods of the lease when payments begin to exceed the straight-line expense. Tenant allowances from landlords for tenant improvements are generally comprised of cash received from the landlord as part of the negotiated terms of the lease. These cash payments are recorded as a deferred credit from landlords that is amortized into income (through lower rent expense) over the term (including the build-out period) of the applicable lease.

Revenue Recognition and Concentration of Credit Risk The Company generates revenue from the processing of qualification and activation transactions; granting of software licenses; services (including maintenance, installation and training); development and consulting contracts; hardware sold in conjunction with certain software licenses; and performing payment processing services. The Company also offers on-demand voice conferencing services through its GroupTalk offering. Revenues from processing of qualification and activation transactions for communications providers are recognized in the period in which services are performed. Revenues from the Company's GroupTalk

offering are recognized as conference services are utilized. To date, the Company has not recognized any transaction revenues from its GroupTalk offering. If substantial doubt exists regarding collection of fees for the Company's products or services at the time of delivery or performance, the Company defers recognition of the associated revenue until the fees are collected.

Revenues from payment processing transaction services are derived from the Company's credit card processing and eCheck processing services (collectively payment processing services), gateway fees and set-up fees. Payment processing services revenue is based on a fee per transaction, and is recognized in the period in which the transaction occurs. Gateway fees are monthly subscription fees charged to merchant customers for the use of the payment gateway.

F-10

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Gateway fees are recognized in the period in which the service is provided. Set-up fees represent one-time charges for initiating the Company's payment processing services. Although these fees are generally paid to the Company at the commencement of the agreement, they are recognized ratably over the estimated average life of the merchant relationship, which is determined through a series of analyses of active and deactivated merchants. Commissions paid to outside sales partners are recorded in sales and marketing expense in the Company's statements of operations.

Revenues from consulting and services contracts are generally recognized as the services are performed. Revenues from software maintenance contracts are recognized ratably over the term of the maintenance agreement and are reported as consulting and services revenues. Revenue from hardware sales is recognized upon shipment, unless testing, integration or implementation services are required, in which case hardware revenue is recognized upon commissioning and acceptance of the product. Revenue from hardware sold in conjunction with software licenses is deferred until the related license revenue is recognized and the aforementioned other criteria for hardware revenue recognition are met.

The Company's software license agreements have typically provided for an initial license fee and annual maintenance fees based on a defined number of subscribers, as well as additional license and maintenance fees for net subscriber additions in certain circumstances. Revenue from software license agreements are recognized when persuasive evidence of an arrangement exists, product has been delivered, fee is fixed and determinable and collectibility is assured. To the extent that obligations exist for other services, the Company allocates revenue between the license and the services based upon their relative fair value or by the residual method.

The Company's TDS customers are providers of wireless telecommunications services and are generally granted credit without collateral. Lightbridge specifically analyzes accounts receivable balances and historical bad debts, customer creditworthiness, current domestic and international economic trends, and changes in its customer payment terms when evaluating the adequacy of the allowance for doubtful accounts. The Company's revenues vary throughout the year, with the period of highest revenue generally occurring during the period October 1 through December 31. The allowance for doubtful accounts at December 31, 2004, 2003, and 2002 was approximately \$1,966,000, \$2,561,000 and \$2,955,000 respectively. The Company recorded bad debt expense of \$0 and \$200,000 for the years ended December 31, 2003 and 2002, respectively. The Company recorded a benefit for bad debt expense of \$1,364,000 for the year ended December 31, 2004. The Company had write-offs, net of recoveries, associated with accounts receivable of \$394,000 and \$210,000 for the years ended December 31, 2003 and 2002, respectively. The Company had recoveries, net of write-offs, associated with accounts receivable of \$769,000 for the year ended December 31, 2004.

Customers exceeding 10% of the Company's revenues during the years ended December 31 are as follows:

| | Years Ended Dec. 31, | | |
|------------------------------|-----------------------------|-------------|-------------|
| | 2004 | 2003 | 2002 |
| Sprint Spectrum L.P. | 21% | 28% | 30% |
| AT&T Wireless Services, Inc. | 16 | 21 | 21 |
| Ericsson AB | * | 14 | 15 |
| Nextel Operations, Inc. | 11 | 12 | 11 |
| | | | |
| Total | 48% | 75% | 77% |

* Represents less than 10% of total revenues in 2004.

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Export Sales The Company had export sales to the following regions for the years ended December 31:

| | 2004 | 2003 | 2002 |
|---------------|-------------|-------------|-------------|
| Latin America | \$ 10,079 | \$ 9,240 | \$ 10,436 |
| Mexico | 4,084 | 6,191 | 9,299 |
| Africa | 465 | 1,476 | 803 |
| Canada | 485 | 604 | 748 |
| Asia | 12 | 79 | 273 |
| Russia | 38 | 947 | 169 |
| Europe | 60 | 120 | 157 |
| | | | |
| Total | \$ 15,223 | \$ 18,657 | \$ 21,885 |

Goodwill and Acquired Intangible Assets During 2002 and 2004, the Company recorded goodwill of \$1.7 million and \$57.6 million in connection with the acquisitions of Altawave and Authorize.Net, respectively. The Company is required to test such goodwill for impairment on at least an annual basis. The Company has adopted January 1st and March 31st as the date of the annual impairment tests for Altawave and Authorize.Net, respectively. The Company will assess the impairment of goodwill on an annual basis or more frequently if other indicators of impairment arise.

Acquired intangible assets related to the acquisition of Altawave in 2002 primarily represent existing technology. These assets were being amortized on a straight-line basis over their five year estimated useful lives. Acquired intangible assets related to the acquisition of Authorize.Net include reseller networks, existing technology merchant customer base, trademarks and processor relationships. The reseller network and the processor relationships will be amortized over twelve years. The merchant customer base and the existing technology will be amortized over five years. Trademarks are not amortized.

On January 1, 2005, the Company performed the annual impairment test for the goodwill balance related to Altawave. The Company used the discounted cash flow methodology to determine the fair value of the reporting unit. The discounted cash flow methodology is based upon converting expected cash flows to present value. The Company's assumptions and methodology in determining the fair value of the reporting unit was reviewed by an independent appraiser. A comparison of the resulting fair value of the reporting unit to its carrying amount, including goodwill, indicated that the goodwill and remaining other intangible assets were fully impaired. As a result, a goodwill impairment charge of approximately \$1.7 million and an other intangible asset impairment charge of approximately \$0.6 million were recorded in the Company's Consolidated Statement of Operations in 2004.

Acquired intangible assets consisted of the following at December 31:

| | 2004 | 2003 |
|--------------------------|-------------|-------------|
| Intangible Assets: | | |
| Existing technology | \$ 3,162 | \$ 1,330 |
| Reseller network | 9,300 | |
| Merchant customer base | 7,000 | |
| Trademarks | 3,600 | |
| Processor relationships | 300 | |
| | 23,362 | 1,330 |
| Accumulated amortization | (2,115) | (465) |

Net \$ 21,247 \$ 865

F-12

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Future amortization expense consisted of the following at December 31, 2004:

| | Amortization |
|-----------------------------------|---------------------|
| 2005 | \$ 2,832 |
| 2006 | 2,832 |
| 2007 | 2,832 |
| 2008 | 2,832 |
| 2009 | 1,319 |
| Thereafter | 5,000 |
| | |
| Total future amortization expense | \$ 16,647 |

Income Taxes The Company records deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the financial reporting and tax bases of existing assets and liabilities. Deferred income tax assets are principally the result of net operating loss carryforwards, income tax credits and differences in depreciation and amortization and accrued expenses and reserves for financial purposes and income tax purposes, and are recognized to the extent realization of such benefits is more likely than not. Lightbridge periodically assesses the recoverability of any tax assets recorded on the balance sheet and provides for any necessary valuation allowances. (See Note 11).

Warranty Reserve As a result of the limited demand for the PhonePrint system, the Company decided to no longer actively sell or market this system and, no significant revenues are expected from this product in the future. The Company no longer has a warranty reserve at December 31, 2004 to cover the costs of PhonePrint replacement units or spare parts. As the number of carriers still operating the PhonePrint system has declined substantially, the Company reduced its PhonePrint warranty reserve by \$526,000 in 2002. The balance in the warranty reserve at December 31, 2004 and 2003 was \$0 and \$250,000 respectively.

Development Costs Development costs, which consist of research and development of new products and services, are expensed as incurred, except for software development costs meeting certain criteria for capitalization. Software development costs are capitalized after establishment of technological feasibility which the Company defines as the point that a working model of the software application has achieved all design specifications and is available for beta testing. No costs have qualified for capitalization to date.

Foreign Currency Translation The financial statements of the Company's foreign subsidiary are translated in accordance with SFAS No. 52, Foreign Currency Translation. The determination of functional currency is based on the subsidiary relative financial and operational independence from the Company. Foreign currency transaction gains or losses are credited or charged to the consolidated statements of operations as incurred. Gains and losses from foreign currency translation related to entities whose functional currency is their local currency are credited or charged to the foreign currency account, included in stockholders' equity in the consolidated balance sheets.

Supplemental Cash Flow Information

| | Years Ended December 31, | | |
|----------------------------|---------------------------------|-------------|-------------|
| | 2004 | 2003 | 2002 |
| | (In thousands) | | |
| Supplemental Item: | | | |
| Cash paid for income taxes | \$ 2,004 | \$ 373 | \$ 3,925 |

Impairment of Long-Lived Assets The Company periodically, or when an impairment event occurs, assesses the recoverability of its long-lived assets by comparing the undiscounted cash flows expected to be generated by those

assets to their carrying value. If the sum of the undiscounted cash flows is less than the carrying value of the assets, an impairment charge is recognized. At January 1, 2005, the annual impairment analysis was performed and, it was determined that the amount of goodwill and intangibles acquired in the Altawave acquisition were fully impaired and should be written-off. Approximately \$0.6 million and \$1.7 million was reflected on the income statement as an impairment of intangible assets and goodwill, respectively.

F-13

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Stock-Based Compensation The Company applies the intrinsic value based method of accounting for stock options granted to employees. The Company accounts for stock options and awards to non-employees using the fair value method.

Under the intrinsic value method, compensation associated with stock awards to employees is determined as the difference, if any, between the current fair value of the underlying common stock on the date compensation is measured and the price an employee must pay to exercise the award. The measurement date for employee awards is generally the date of grant. Under the fair value method, compensation associated with stock awards to non-employees is determined based on the estimated fair value of the award itself, measured using either current market data or an established option pricing model. The measurement date for non-employee awards is generally the date performance of services is complete.

Had the Company used the fair value method to measure compensation expense associated with grants of stock options to employees, reported net income (loss) and basic and diluted earnings (loss) per share would have been as follows:

| | 2004 | 2003 | 2002 |
|--|---|-------------|-------------|
| | (In thousands, except per share amounts) | | |
| Net income (loss) as reported | \$ (15,405) | \$ (1,449) | \$ 3,630 |
| Stock based compensation recorded in net income (loss) | | | |
| Stock based compensation measured using the fair value method (net of tax) | 3,272 | 2,156 | 2,350 |
| Net income (loss) pro forma | \$ (18,677) | \$ (3,605) | \$ 1,280 |
| Basic earnings (loss) per share pro forma | \$ (0.70) | \$ (0.13) | \$ 0.05 |
| Diluted earnings (loss) per share pro forma | \$ (0.70) | \$ (0.13) | \$ 0.05 |

The fair value of options on their grant date was measured using the Black-Scholes Option Pricing Model. Key assumptions used to apply this pricing model are as follows:

| | Years Ended December 31, | | |
|---|---------------------------------|-------------|-------------|
| | 2004 | 2003 | 2002 |
| Risk-free interest rate | 1.9% - 3.4% | 2.9% - 4.7% | 2.9% - 4.7% |
| Expected life of options grants | 1 - 5 years | 1 - 5 years | 1 - 5 years |
| Expected volatility of underlying stock | 82% | 86% | 90% |
| Expected dividend payment rate, as a percentage of the stock price on the date of grant | | | |

Comprehensive Income The amounts that comprise comprehensive income for the years ended December 31, 2004, 2003 and 2002 are as follows (in thousands):

| | 2004 | 2003 | 2002 |
|-------------------------------|-------------|-------------|-------------|
| Net income (loss) as reported | \$ (15,405) | \$ (1,449) | \$ 3,630 |
| Other comprehensive income: | | | |

| | | | |
|-----------------------------|-------------|------------|----------|
| Foreign currency loss | (184) | | |
| Comprehensive income (loss) | \$ (15,589) | \$ (1,449) | \$ 3,630 |

F-14

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Recent Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 123R, Share-Based Payment (SFAS No. 123R). This Statement is a revision of SFAS No. 123, Accounting for Stock-Based Compensation, and supersedes Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and its related implementation guidance. SFAS No. 123R focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions. The Statement requires entities to recognize stock compensation expense for awards of equity instruments to employees based on the grant-date fair value of those awards (with limited exceptions). SFAS No. 123R is effective for the first interim or annual reporting period that begins after June 15, 2005. The Company is evaluating the two methods of adoption allowed by SFAS No. 123R; the modified-prospective transition method and the modified-retrospective transition method.

4. Disclosures About Segments of an Enterprise and Related Information

As a result of the Company's corporate reorganization efforts during 2004, the Company has changed its previously reported operating segments effective in the fourth quarter of 2004. All prior period segment financial information has been restated to conform with the current presentation. Based upon the way financial information is provided to the Company's Chief Executive Officer for use in evaluating allocation of resources and assessing performance of the business, the Company reports its operations in four distinct operating segments: Telecom Decisioning Services (TDS), Payment Processing Services (Payment Processing), Intelligent Network Solutions (INS) and Instant Conferencing Services (Instant Conferencing).

The TDS segment provides wireless subscriber qualification, risk assessment, fraud screening, consulting services and call center services to telecom and other companies. The Payment Processing segment offers a transaction processing system, under the Authorize.Net® brand, that allows businesses to authorize, settle and manage credit card, electronic check and other electronic payment transactions online. The INS segment provides wireless carriers with a real-time rating engine for voice, data and IN services for prepaid subscribers as well as postpaid charging functionality and telecom calling card services. The Instant Conferencing segment provides managed instant conferencing services through its Lightbridge GroupTalk™ product. In 2005, the Company made the decision to no longer actively market or sell its GroupTalk™ product. The Company expects to continue to provide the services for GroupTalk under its agreement with AOL. Within these four segments, performance is measured based on revenue, gross profit and operating income (loss) realized from each segment. There are no transactions between segments.

The Company does not allocate certain corporate or centralized marketing and general and administrative expenses to its business unit segments, because these activities are managed separately from the business units. Also, the Company does not allocate restructuring expenses and other non-recurring gains or charges to its business unit segments because the Company's Chief Executive Officer evaluates the segment results exclusive of these items. Asset information by operating segment is not reported to or reviewed by the Company's Chief Executive Officer and therefore the Company has not disclosed asset information for each operating segment.

Financial information for each reportable segment for the years ended December 31, 2004, 2003 and 2002 were as follows (amounts in thousands):

| December 31, 2004 | TDS | Payment Processing | INS | Instant Conferencing | Sub-total Reportable Segments | Reconciling Items | Consolidated Total |
|-------------------------------|----------|-----------------------|----------|-------------------------|-------------------------------------|----------------------|-----------------------|
| Revenues | \$88,297 | \$ 26,836 | \$17,540 | \$ 382 | \$133,055 | \$ | \$133,055 |
| Gross profit (loss) | 37,020 | 19,580 | 8,790 | (225) | 65,165 | | 65,165 |
| Operating income (loss) | 16,188 | 3,560 | (4,014) | (4,309) | 11,425 | (18,403)(1) | (6,978) |
| Depreciation and amortization | 5,760 | 3,086 | 631 | 555 | 10,032 | 877(2) | 10,909 |

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

| December 31, 2003 | TDS | Payment Processing | INS | Instant Conferencing | Sub-total Reportable Segments | Reconciling Items | Consolidated Total |
|----------------------------------|------------|-------------------------------|------------|---------------------------------|--|------------------------------|-------------------------------|
| Revenues | \$99,023 | \$ | \$20,955 | \$ | \$ 119,978 | \$ | \$ 119,978 |
| Gross profit (loss) | 46,399 | | 11,630 | | 58,029 | | 58,029 |
| Operating income (loss) | 22,025 | | (2,541) | (3,536) | 15,948 | (19,806)(1) | (3,858) |
| Depreciation and amortization | 7,918 | | 1,255 | 536 | 9,709 | 689(2) | 10,398 |

| December 31, 2002 | TDS | Payment Processing | INS | Instant Conferencing | Sub-total Reportable Segments | Reconciling Items | Consolidated Total |
|----------------------------------|------------|-------------------------------|------------|---------------------------------|--|------------------------------|-------------------------------|
| Revenues | \$107,121 | \$ | \$26,045 | \$ 272 | \$ 133,438 | \$ | \$ 133,438 |
| Gross profit (loss) | 51,251 | | 15,972 | 272 | 67,495 | | 67,495 |
| Operating income (loss) | 25,749 | | (1,986) | (4,711) | 19,052 | (17,500)(1) | 1,552 |
| Depreciation and amortization | 11,327 | | 2,761 | 407 | 14,495 | 831(2) | 15,326 |

(1) Reconciling items from segment operating income (loss) to consolidated operating income (loss) include the following:

| | 2004 | 2003 | 2002 |
|--|------------------|------------------|------------------|
| Restructuring costs | \$ 4,346 | \$ 5,079 | \$ 3,616 |
| Gain on sale of Fraud Centurion assets | (2,673) | | |
| Impairment of intangible assets | 2,263 | | |
| Unallocated corporate and centralized marketing, general and administrative expenses | 14,467 | 14,727 | 13,884 |
| Total | \$ 18,403 | \$ 19,806 | \$ 17,500 |

(2) Represent depreciation and amortization included in the unallocated corporate or centralized marketing, general and administrative expenses.

5. Investment

In June 2001, the Company committed to invest up to \$5.0 million in a limited partnership that invested in businesses within the wireless industry. The Company used the equity method of accounting for this limited partnership investment. For the year ended December 31, 2002, the Company's proportionate share of the loss of the limited partnership was \$0.5 million. In July 2003, the partners agreed to dissolve the partnership. Accordingly, future commitments were eliminated, and the remaining \$0.5 million investment was written off in the quarter ended June 30, 2003.

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6. Property and Equipment

Property and equipment consisted of the following at December 31:

| | 2004 | 2003 |
|--|-------------|-------------|
| Furniture and fixtures | \$ 3,593 | \$ 2,430 |
| Leasehold improvements | 10,558 | 8,209 |
| Computer equipment | 19,688 | 23,411 |
| Computer software | 9,464 | 11,262 |
| | 43,303 | 45,312 |
| Less accumulated depreciation and amortization | (26,325) | (35,904) |
| Property and equipment, net | \$ 16,978 | \$ 9,408 |

During the year ended December 31, 2004, the Company performed a review of its property and leasehold improvements and a number of fully depreciated assets were identified as no longer being in service. As a result, the Company removed from the property and leasehold improvement accounts cost and accumulated depreciation of approximately \$12.0 million. Since the assets had been fully depreciated, there was no material impact on the statement of operations.

7. Letters of Credit

At December 31, 2002 the Company had an outstanding letter of credit in the amount of \$1.0 million which expired in May 2003. On January 14, 2003, this letter of credit was replaced with a \$1.0 million letter of credit, which expired in May 2004. On January 7, 2004, the Company entered into another \$1.0 million letter of credit, which was scheduled to expire in January 2005. This letter of credit was renewed in the amount of \$1.6 million and extends through January 2006. In January 2005, the Company restricted \$1.6 million of cash as collateral for the renewed letter of credit.

On January 14, 2003, the Company entered into a foreign exchange agreement, effective April 2003 with a bank for the purchase of one currency in exchange for the sale of another currency. This agreement expired on January 24, 2005. There were no transactions under this agreement.

8. Restructuring Costs

In December 2004, the Company announced a restructuring of its business in order to lower overall expenses to better align them with future revenue expectations. This action followed the Company's announcement of an anticipated revenue reduction as a result of the acquisition of AT&T by Cingular Wireless LLC. This restructuring resulted in the termination of 38 employees, in the Company's corporate offices in Burlington, Massachusetts as follows: 16 in product and service delivery, 11 in engineering and development, 10 in sales and marketing and 1 in general and administrative. The Company recorded a restructuring charge of approximately \$1.4 million relating to employee severance and termination benefits during the three months ended December 31, 2004. Additionally, subsequent to our acquisition of Authorize.net the Company relocated its offices in Bellevue, Washington and the remaining rent paid on the vacated space of \$178 was included in restructuring charges during the fourth quarter of 2004. The Company anticipates that all costs related to this restructuring will be paid by the end of 2005.

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following summarizes the changes to the December 2004 restructuring reserve since it was accrued:

| | Balance at December 31, 2003 | Accrued | Utilized | Balance at December 31, 2004 |
|---|---|-----------------------|-----------------|---|
| | | (In thousands) | | |
| Employee severance and termination benefits | \$ | \$ 1,410 | \$ 46 | \$ 1,364 |
| Facility closing and related costs | | 178 | 178 | |
| Total | \$ | \$ 1,588 | \$ 224 | \$ 1,364 |

In October 2004, the Company announced a restructuring of its business in accordance with the sale of Fraud Centurion product suite to Subex Systems Limited. This action, a continuation of the Company's emphasis on expense management, resulted in the termination of nine employees in the Company's Broomfield, Colorado location as follows: two in product and service delivery, and seven in engineering and development. The Company recorded a restructuring charge of approximately \$172 relating to employee severance and termination benefits during the three months ended December 31, 2004. The Company anticipates that all costs related to this restructuring will be paid by the end of 2005.

The following summarizes the changes to the October 2004 restructuring reserve since it was accrued:

| | Balance at December 31, 2003 | Accrued | Utilized | Balance at December 31, 2004 |
|---|---|-----------------------|-----------------|---|
| | | (In thousands) | | |
| Employee severance and termination benefits | \$ | \$ 172 | \$ 147 | \$ 25 |

In September 2004, the Company announced a restructuring of its business in order to lower overall expenses to better align them with future revenue expectations. This action, a continuation of the Company's emphasis on expense management, resulted in the termination of 64 employees and 2 contractors in the Company's corporate offices in Burlington, Massachusetts and its Broomfield, Colorado location as follows: 12 in product and service delivery, 16 in engineering and development, 25 in sales and marketing and 13 in general and administrative. The Company recorded a restructuring charge of approximately \$2.1 million relating to employee severance and termination benefits during the three months ended September 30, 2004. The Company anticipates that all costs related to this restructuring will be paid by the end of 2005.

The following summarizes the changes to the September 2004 restructuring reserve since it was accrued:

| | Balance at December 31, 2003 | Accrued | Utilized | Balance at December 31, 2004 |
|---|---|-----------------------|-----------------|---|
| | | (In thousands) | | |
| Employee severance and termination benefits | \$ | \$ 2,090 | \$ 1,255 | \$ 835 |

In January 2004, the Company announced a reorganization of its internal business operations. This action, a continuation of the Company's emphasis on expense management, resulted in the termination of ten individuals in the Company's corporate office in Burlington, Massachusetts. The Company recorded a restructuring charge of approximately \$0.5 million relating to employee severance and termination benefits during the three months ended March 31, 2004. The Company anticipates that all costs related to this restructuring will be paid by the end of 2005.

F-18

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following summarizes the changes to the January 2004 restructuring reserves since it was accrued:

| | Balance at December 31, 2003 | | | Accrued Utilized | | Balance at December 31, 2004 | |
|---|---|--|-----------------------|------------------------------|----|---|---|
| | | | (In thousands) | | | | |
| Employee severance and termination benefits | \$ | | \$ 488 | \$ 483 | \$ | | 5 |

In June 2003, the Company announced that it would be closing its Irvine, California facility and transferring certain employment positions to its Broomfield, Colorado facility and reducing its headcount by an estimated 70 employees as follows: 16 in product and service delivery, 30 in development, 13 in sales and marketing and 11 in general and administrative. In the quarter ended June 30, 2003, the Company recorded a restructuring charge of approximately \$0.7 million, consisting mainly of workforce reduction costs. In the quarter ended September 30, 2003, the Company recorded an additional restructuring charge associated with this action of approximately \$3.3 million, consisting of \$1.1 million for workforce reduction, \$1.7 million in future lease obligations for unused facilities and \$0.5 million for capital equipment write-offs. In the quarter ended December 31, 2003, the Company recorded an additional restructuring charge of \$0.1 million related to future lease obligations and employee severance benefits. The capital equipment write-offs and a majority of severance costs related to this restructuring were incurred by the end of 2003, and the Company anticipates that all other costs related to this restructuring, consisting principally of lease obligations on unused space, will be paid by the end of 2006.

The following summarizes the changes to the June 2003 restructuring reserves since it was accrued:

| | Balance at December 31, 2002 | | | Balance at December 31, 2003 | | | Balance at December 31, 2004 | |
|---|---|----------|------------------------------|---|---------|--------|---|--|
| | | | Accrued Utilized | | | | | |
| Employee severance and termination benefits | \$ | \$ 1,795 | \$ 1,542 | \$ 253 | \$ (93) | \$ 160 | \$ | |
| Facility closing and related costs | | 1,743 | 347 | 1,396 | 137 | 665 | 868 | |
| Capital equipment write-offs | | 497 | 497 | | | | | |
| Total | \$ | \$ 4,035 | \$ 2,386 | \$ 1,649 | \$ 44 | \$ 825 | \$ 868 | |

In March 2003, the Company announced that it would be streamlining its existing Broomfield, Colorado call center operations into its Lynn, Massachusetts facility and a smaller facility in Broomfield, Colorado by the end of May 2003. In the quarter ended March 31, 2003, the Company recorded a restructuring charge of approximately \$0.1 million for workforce reductions. In the quarter ended June 30, 2003, the Company recorded an additional restructuring charge associated with this action of approximately \$1.0 million, consisting of approximately \$0.6 million in future lease obligations for unused facilities and approximately \$0.4 million for capital equipment write-offs. The capital equipment write-offs and all of the severance costs related to this restructuring were incurred

by the end of 2003, and the Company anticipates that all other costs relating to this restructuring, consisting principally of lease obligations on unused space, will be paid by the end of the first quarter of 2005.

The following summarizes the changes to the March 2003 restructuring reserves since inception:

| | Balance at December 31, 2002 | Accrued | Utilized | Balance at December 31, 2003 | Accrued | Utilized | Balance at December 31, 2004 |
|---|---|-----------------|-----------------|---|----------------|-----------------|---|
| Employee severance and termination benefits | \$ | \$ 77 | \$ 77 | \$ | \$ | \$ | \$ |
| Facility closing and related costs | | 548 | 185 | 363 | (36) | 324 | 3 |
| Capital equipment write-offs | | 378 | 378 | | | | |
| Total | \$ | \$ 1,003 | \$ 640 | \$ 363 | \$ (36) | \$ 324 | \$ 3 |

F-19

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In June 2002, the Company announced that it was reducing its workforce by seven percent and consolidating its Waltham, Massachusetts call center operations into its Lynn, Massachusetts and Broomfield, Colorado facilities by the end of 2002. The Company recorded a restructuring charge of approximately \$3.6 million, consisting of \$1.6 million for workforce reductions, \$1.3 million for facilities reductions including lease obligations, utilities and security costs on unused space and \$0.7 million for capital equipment write-offs associated with these measures. The restructuring plan resulted in the termination of 65 personnel as follows: 25 in product and service delivery, 22 in development, 11 in sales and marketing and seven in general and administrative. The capital equipment write-offs and a majority of severance costs related to this restructuring were incurred by the end of 2002, and the Company anticipates that all other costs relating to this restructuring, consisting principally of lease obligations on unused space, will be paid by the end of 2005.

The following summarizes the changes to the June 2002 restructuring reserves since inception:

| | Balance at December 31, 2001 | | | Balance at December 31, 2002 | | | Balance at December 31, 2003 | | | Balance at December 31, 2004 | | |
|---|------------------------------|-----------------|-----------------|------------------------------|---------------|---------------|------------------------------|---------------|-----------|------------------------------|---------------|-----------|
| | Accrued | Utilized | | Accrued | Utilized | | Accrued | Utilized | | Accrued | Utilized | |
| Employee severance and termination benefits | \$ 1,580 | \$ 1,237 | \$ 343 | \$ (158) | \$ 185 | \$ | \$ | \$ | \$ | \$ | \$ | \$ |
| Facility closing and related costs | 1,312 | 320 | 992 | 199 | 569 | 622 | | 339 | | | 283 | |
| Capital equipment write-offs | 724 | 724 | | | | | | | | | | |
| Total | \$ 3,616 | \$ 2,281 | \$ 1,335 | \$ 41 | \$ 754 | \$ 622 | \$ | \$ 339 | \$ | \$ | \$ 283 | \$ |

9. Commitments and Contingencies

At December 31, 2004, the Company was holding funds in the amount of \$4.4 million on behalf of merchants utilizing Authorize.Net's eCheck services. The funds are included in cash and cash equivalents and funds due to merchants on the Company's consolidated balance sheet. Authorize.Net typically holds eCheck funds for approximately seven business days; the actual number of days depends on the contractual terms with each merchant. In addition, at December 31, 2004, the Company held funds in the amount of \$1.2 million for and on behalf of merchants processing credit card and ACH transactions using the Integrated Payment Solution (IPS) product. The funds are included in cash and cash equivalents and funds due to merchants on the Company's consolidated balance sheet. Credit card funds are typically held for approximately two business days; ACH funds are held for approximately four business days, according to the specifications of the IPS product and the contract between Authorize.Net and the financial institution through which the transactions are processed.

In addition, the Company currently has \$600,000 on deposit with a financial institution to cover any deficit account balance that could occur if the amount of transactions returned or charged back exceeds the balance on deposit with the financial institution. To date, the deposit has not been applied to offset any deficit balance, and management believes that the likelihood of incurring a deficit balance with the financial institution due to the amount of transactions returned or charged back is remote. The deposit will be held continuously for as long as Authorize.Net utilizes the ACH processing services of the financial institution, and the amount of the deposit may increase as

processing volume increases.

The Company's primary contractual obligations and commercial commitments are under its operating leases and a letter of credit. The Company maintained a letter of credit in the amount of \$1.0 million which was scheduled to expire in January 2005, as required for security under the lease for its headquarters. This letter of credit was renewed in the amount of \$1.6 million and extends through January 2006. In January 2005, the Company provided \$1.6 million of cash as collateral for the renewed letter of credit.

F-20

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Leases The Company has noncancelable operating lease agreements for office space and certain equipment. These lease agreements expire at various dates through 2011 and certain of them contain provisions for extension on substantially the same terms as are currently in effect.

Future minimum payments under operating leases, including facilities affected by restructurings and the Company's new headquarters lease, consisted of the following at December 31, 2004 (amounts in thousands):

| | Operating Leases |
|------------------------------|-----------------------------|
| 2005 | \$ 4,840 |
| 2006 | 3,820 |
| 2007 | 3,013 |
| 2008 | 2,758 |
| 2009 | 2,108 |
| Thereafter | 3,526 |
| | |
| Total minimum lease payments | \$ 20,065 |

Rent expense for operating leases was approximately \$5,401,000, \$4,017,000 and \$6,052,000 for the years ended December 31, 2004, 2003 and 2002, respectively.

The Company leases its corporate headquarters and its principal sales, consulting, marketing, operations and product development facility. This lease was executed and delivered in January, 2004, had a rent commencement date in June 2004 and expires in 2011. The Company was not required to pay rent during the construction period from January 2004 through May 2004 and the amount of the landlord's tenant improvement allowance was approximately \$3.3 million. In addition, the Company's Bellevue, Washington lease was executed in August 2004, and had a rent commencement date in September 2004. The Company was not obligated to pay rent during the construction period prior to the rent commencement date and the amount of the landlord's tenant improvement allowance was approximately \$177,000. The Company also received abated rent for the first three months of the lease term. The Company's Nova Scotia lease was entered into in February 2004, and had a rent commencement date in May 2004. The Company was allowed access to the premises in Nova Scotia for a period of 90 days prior to May 2004 in order to make tenant improvements.

Warranties and Indemnities The Company provides certain warranties and related indemnities in its client contracts. These warranties may include warranties that the transactions processed on a client's behalf have been processed in accordance with the contract, that products delivered or services rendered meet designated specifications or service levels, and that certain applicable laws and regulations are complied with in the performance of services for or provision of products to a client. The Company maintains errors and omissions insurance that may provide coverage for certain warranty and indemnity claims. However, such insurance might cease to be available to the Company on commercially reasonable terms or at all.

The Company generally undertakes to defend and indemnify the indemnified party for damages and expenses or settlement amounts arising from certain patent, copyright or other intellectual property infringement claims by any third party with respect to the Company's products. Some agreements provide for indemnification for claims relating to property damage or personal injury resulting from the performance of services or provision of products by the Company, breaches of contract by the Company or the failure by the Company to comply with applicable laws in the performance of services or provision of products by the Company to its clients. Historically, the Company's costs to defend lawsuits, or settle or pay claims relating to such indemnification provisions, have not been material. Accordingly, the estimated fair value of these indemnification provisions is not material.

Litigation In a case pending in the United States District Court for the District of Arizona, a variety of defendants, including payment processing gateway providers and banks, are accused of infringing certain patents involving payment processing over computer networks. The case is captioned *Net MoneyIN, Inc. v. VeriSign, Inc., et al.*, Case No. CIV 01-441 TUC RCC. The plaintiff alleges that numerous products or services infringe its patents, including the Authorize.Net Payment Gateway Service and eCheck.Net service. Neither Lightbridge nor Authorize.Net is a party to the lawsuit, but Authorize.Net is indemnifying and defending defendants InfoSpace, Inc. and E-Commerce Exchange, Inc. as to services provided by Authorize.Net. Defendant Wells Fargo Bank, N.A. has also requested indemnification, including defense costs, from Authorize.Net based on certain contracts with Authorize.Net. Lightbridge anticipates that plaintiff may attempt to add Authorize.Net and/or Lightbridge as a party defendant. The litigation is currently in the fact discovery phase, and no trial date has been set.

F-21

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company intends to defend any claims brought against it, Authorize.Net or third parties that it is contractually obligated to defend in connection with the lawsuit. While there can be no assurances as to the outcome of the lawsuit, an adverse outcome in the lawsuit could have a material effect on the Company's financial condition, results of operations or cash flow.

10. Common Stock Option Plans, Warrants, Stockholder Rights Plan***Stock Option Plans***

1990 Incentive and Nonqualified Stock Option Plan Under the Company's 1990 Incentive and Nonqualified Stock Option Plan, the Company could grant either incentive or nonqualified stock options to officers, directors, employees or consultants for the purchase of up to 2,400,000 shares of common stock. Options were granted with an exercise price equal to the common stock's market value at the date of grant, as determined by the Board of Directors of the Company (the Board), and expired ten years later. No further grants can be made under the 1990 Incentive and Nonqualified Stock Option Plan.

1996 Employee Stock Plans On June 14, 1996, the Board authorized and the stockholders approved the adoption of the 1996 Incentive and Nonqualified Stock Option Plan and the 1996 Employee Stock Purchase Plan for the issuance of options or sale of shares to employees. The Company cannot make any further grants under the 1996 Incentive and Nonqualified Stock Plan. Both plans became effective immediately after the closing of the Company's initial public offering:

1996 Incentive and Nonqualified Stock Option Plan The 1996 Incentive and Nonqualified Stock Option Plan (the 1996 Plan) provided for the issuance of options to purchase up to 4,350,000 shares of the Company's common stock. Options could be either qualified incentive stock options or nonqualified stock options at the discretion of the Board. Exercise prices must be greater than or equal to the fair market value on the date of grant, in the case of incentive stock options and nonqualified options.

1996 Employee Stock Purchase Plan The 1996 Employee Stock Purchase Plan provides for the sale of up to 600,000 shares of the Company's common stock to employees. Employees are allowed to purchase shares at a discount from the lower of fair value at the beginning or end of the purchase periods through payroll deductions. At December 31, 2004, 194,624 shares were available for purchase and reserved for issuance under the 1996 Employee Stock Purchase Plan.

1997 Stock Incentive Plan and Restricted Stock Purchase Plan The 1997 Stock Incentive Plan and Restricted Stock Purchase Plan provided for the issuance of up to 8,516,667 options to acquire shares of common stock. The Company does not plan to make any further grants under the 1997 Stock Incentive Plan and Restricted Stock Purchase Plan.

1998 Non-Statutory Stock Option Plan The 1998 Non-Statutory Stock Option Plan (the 1998 Plan) provided for the issuance of options to purchase up to 1,000,000 shares of the Company's common stock. Options are granted with an exercise price no less than the common stock's market value at the date of the grant, as authorized by the Board. No further grants can be made under the 1998 Non-Statutory Stock Option Plan.

2004 Stock Incentive Plan In April and June 2004, respectively, the Board authorized and the stockholders approved the adoption of the 2004 Stock Incentive Plan which provides for the issuance of options and other stock-based awards to purchase up to 2,500,000 shares of the Company's common stock, plus the number of shares then remaining available for future grants under the Company's 1996 Plan and the 1998 Plan, plus the number of shares subject to any stock option granted pursuant to the 1996 Plan or the 1998 Plan that expires, is cancelled or otherwise terminates (other than by exercise) after the effective date of the 2004 Plan. Options are granted with an exercise price of no less than the common stock's market value at the date of grant. At December 31, 2004, 2,305,233 shares were available for grant under the 2004 Stock Incentive Plan.

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents activity under all stock option plans:

| | Number of Options (In thousands) | Weighted- Average Exercise Price | Weighted- Average Fair Value of Options Granted |
|----------------------------------|---|---|--|
| Outstanding at January 1, 2002 | 4,645 | \$ 13.17 | |
| Granted | 1,260 | 9.44 | \$ 5.56 |
| Exercised | (394) | 5.39 | |
| Forfeited | (1,605) | 16.34 | |
| Outstanding at December 31, 2002 | 3,906 | 11.41 | |
| Granted | 393 | 7.27 | \$ 3.86 |
| Exercised | (163) | 6.11 | |
| Forfeited | (807) | 16.46 | |
| Outstanding at December 31, 2003 | 3,329 | 10.12 | |
| Granted | 2,905 | 5.71 | \$ 3.12 |
| Exercised | (220) | 0.68 | |
| Forfeited | (1,331) | 9.15 | |
| Outstanding at December 31, 2004 | 4,683 | \$ 8.00 | |

The number of options exercisable at the dates presented below and their weighted average exercise price were as follows:

| | Options Exercisable (In thousands) | Weighted- Average Exercise Price |
|-------------------|---|---|
| December 31, 2002 | 2,278 | \$11.76 |
| December 31, 2003 | 2,335 | \$10.12 |
| December 31, 2004 | 2,502 | \$10.05 |

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table sets forth information regarding options outstanding at December 31, 2004:

| Number of Options (In thousands) | Range of Exercise Prices | | Number Currently Exercisable (In thousands) | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life (Years) | Weighted Average Exercise Price for Currently Exercisable |
|--|-----------------------------|---------|---|--|--|--|
| 369 | \$ 0.46 | \$ 4.44 | 52 | \$ 3.85 | 8.5 | \$ 3.52 |
| 889 | | 4.67 | 137 | 4.67 | 9.7 | 4.67 |
| 659 | 4.69 | 5.90 | 120 | 5.56 | 9.2 | 5.45 |
| 482 | 6.02 | 7.63 | 258 | 6.63 | 8.1 | 6.67 |
| 541 | 7.69 | 7.94 | 375 | 7.76 | 8.7 | 7.79 |
| 421 | 8.04 | 9.92 | 302 | 9.03 | 6.1 | 8.99 |
| 279 | 10.06 | 10.91 | 228 | 10.77 | 6.6 | 10.78 |
| 558 | 11.25 | 12.13 | 553 | 11.93 | 5.1 | 11.93 |
| 226 | 12.49 | 12.88 | 226 | 12.57 | 6.1 | 12.57 |
| 180 | 12.90 | 18.31 | 174 | 15.30 | 5.7 | 15.34 |
| 80 | 19.00 | 42.97 | 77 | 23.98 | 5.3 | 23.56 |
| 4,683 | | | 2,502 | \$ 8.00 | | \$ 10.05 |

Stock Repurchases On October 4, 2001, Lightbridge announced that its board of directors authorized the repurchase of up to 2 million shares of the Company's common stock at an aggregate price of up to \$20 million. The shares may be purchased from time to time on or after October 8, 2001, depending on market conditions. On April 23, 2003, the board approved an expansion of the plan to authorize Lightbridge to purchase up to 4 million shares of the Company's common stock at an aggregate price of up to \$40 million through September 26, 2005. As of December 31, 2004, the Company had purchased approximately 2.5 million shares at a total cost of approximately \$17.9 million since the inception of its repurchase program. There were no repurchases during the third or fourth quarters of 2004. The maximum number of shares that could yet be purchased under the plan was 1,452,862 at December 31, 2004.

The following summarizes the purchases during 2004:

| Period | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plan | Maximum Number of Shares that May yet be Purchased under the Plan |
|---------------------------------------|---|--|---|---|
| January 1, 2004 to January 31, 2004 | | | | 2,087,462 |
| February 1, 2004 to February 29, 2004 | | | | 2,087,462 |

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| | | | | |
|-----------------------------------|---------|---------|---------|-----------|
| March 1, 2004 to March 31, 2004 | 114,600 | \$ 6.69 | 114,600 | 1,972,862 |
| April 1, 2004 to April 30, 2004 | | | | 1,972,862 |
| May 1, 2004 to May 31, 2004 | 520,000 | \$ 5.83 | 520,000 | 1,452,862 |
| June 1, 2004 to December 31, 2004 | | | | 1,452,862 |
| | | | | |
| Total | 634,600 | \$ 5.99 | 634,600 | |

F-24

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Common Stock Warrants At December 31, 2004, pursuant to the Company's acquisition of Coral Systems, Inc. in November 1997, there were warrants outstanding to purchase 9,682 shares of Lightbridge common stock at exercise prices ranging from \$3.44 to \$34.35. These warrants expired in February 2005.

Stockholder Rights Plan In November 1997, the Board of Directors of Lightbridge declared a dividend of one right (each a Right and collectively the Rights) for each outstanding share of common stock. The Rights were issued to the holders of record of common stock outstanding on November 14, 1997, and will be issued with respect to common stock issued thereafter until the Distribution Date (as defined below) and, in certain circumstances, with respect to shares of common stock issued after the Distribution Date. Each Right, when it becomes exercisable, will entitle the registered holder to purchase from Lightbridge one one-hundredth (1/100th) of a share of Series A participating cumulative preferred stock, par value \$0.01 per share, of Lightbridge at a price of \$75.00. The Rights will be issued upon the earlier of the date which Lightbridge learns that a person or group acquired, or obtained the right to acquire, beneficial ownership of fifteen percent or more of the outstanding shares of common stock or such date designated by the Board following the commencement of, or first public disclosure of an intent to commence, a tender or exchange offer for outstanding shares of the Company's common stock that could result in the offer or becoming the beneficial owner of fifteen percent or more of the outstanding shares of the Company's common stock (the earlier of such dates being called the Distribution Date).

11. Income Taxes

The income tax provision (benefit) for the years ended December 31 consisted of the following (in thousands):

| | 2004 | 2003 | 2002 |
|------------------------------------|--------------|----------------|--------------|
| Current: | | | |
| Federal | \$ (777) | \$ (83) | \$ (1,933) |
| Foreign | 1,562 | | |
| State | (254) | 76 | 98 |
| Deferred: | | | |
| Federal | 7,909 | (1,053) | 1,697 |
| State | 1,172 | (42) | 35 |
| Income tax provision (benefit) | \$ 9,612 | \$ (1,102) | \$ (103) |

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tax effects of temporary differences that give rise to deferred tax assets/(liabilities) at December 31 were as follows (in thousands):

| | 2004 | 2003 | 2002 |
|---|------------|----------|----------|
| Current Items: | | | |
| Assets: | | | |
| Allowance for doubtful accounts | \$ 786 | \$ 1,024 | \$ 1,182 |
| Capital loss carryforwards | 192 | | |
| Accrued expenses | 1,482 | 1,178 | 1,327 |
| Restructuring reserve | 1,353 | 1,065 | 503 |
| Less valuation allowance | (3,813) | | |
| Net current deferred tax assets | \$ | \$ 3,267 | \$ 3,012 |
| Long-Term Items: | | | |
| Assets: | | | |
| Depreciation and amortization | \$ 4,014 | \$ 1,894 | \$ 1,218 |
| Acquisition costs | 357 | 649 | 942 |
| Intangible assets | 325 | 625 | 1,461 |
| Loss carryforwards | 9,934 | 11,676 | 10,383 |
| Foreign tax credit carry-forward | 1,822 | | |
| R&D tax credit carry-forward | 5,699 | 1,840 | |
| Valuation allowance | (22,151) | (12,131) | (10,291) |
| Long-term deferred tax assets | | 4,553 | 3,713 |
| Liabilities: | | | |
| Tax amortization of non-lived intangibles | (1,261) | | |
| Long-term deferred tax liabilities | (1,261) | | |
| Total net long-term deferred tax assets/(liabilities) | \$ (1,261) | \$ 4,553 | \$ 3,713 |

The net change in the valuation allowance for the years ended December 31, 2004, 2003 and 2002 was an increase (decrease) of approximately \$13,833,000, \$1,840,000 and \$(612,000), respectively. At December 31, 2004, the Company had \$43,967,000 of federal and state net operating loss carryforwards which expire, if unused, in years 2011 through 2018. At December 31, 2004, the Company had federal research and development credit carryforwards of \$3,399,000 which expire, if unused, in years 2015 through 2022. At December 31, 2004, the Company had state research and development credit carryforwards of \$2,300,000 which the Company can use for an indefinite period. In addition at December 31, 2004, the Company had foreign tax credit carryforwards for federal purposes of \$1,822,000 which expire, if unused, in 2013. As a result of a liquidation of a subsidiary by the Company, certain tax attributes,

including operating loss and research and development tax credit carryforwards of approximately \$4.0 million, which were available to the Company at December 31, 2003 were no longer available at December 31, 2004.

In evaluating its ability to recover its deferred tax assets, the Company considers all available positive and negative evidence including its past operating results, the existence of cumulative losses in the most recent fiscal years and its forecast of future taxable income. In determining future taxable income, the Company is responsible for assumptions utilized including the amount of state, federal and international pre-tax operating income, the reversal of temporary differences and the implementation of feasible and prudent tax planning strategies. These assumptions require significant judgment about the forecasts of future taxable income and are consistent with the plans and estimates the Company is using to manage the underlying businesses.

After considering all available evidence, both positive and negative, regarding the ability to realize its deferred tax assets, the Company concluded that an increase to the valuation allowance for its deferred tax assets was required. In November 2004, the Company announced that it expects its future revenue from AT&T to decline significantly. This announcement had a considerable impact on the Company's conclusion regarding the realizability of its deferred tax assets. Accordingly, based on the Company's best estimate, the Company recorded a non-cash charge of \$9.1 million in the fourth quarter of 2004. If circumstances change such that the realization of the deferred tax assets is concluded to be more likely than not, the Company will record future income tax benefits at the time that such determination is made.

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following is a reconciliation of income taxes at the federal statutory rate to the Company's effective tax rate for the years ended December 31:

| | 2004 | 2003 | 2002 |
|---|-------------|-------------|-------------|
| Statutory federal income tax rate | 34% | 34% | 34% |
| State taxes, net of federal benefit | (1) | (1) | 2 |
| Foreign taxes | (27) | | |
| Foreign tax credits | 31 | | |
| Change in valuation allowance | (239) | 72 | (14) |
| Research & development credits | (52) | (62) | (23) |
| Change in tax contingency reserves | 16 | | |
| Effect of liquidation of a subsidiary on tax attributes | 69 | | |
| Other, net | 3 | (1) | (2) |
| Effective tax rate | (166)% | 42% | (3)% |

The Company is routinely under audit by federal, state or local authorities in the areas of income taxes and the remittance of sales and use taxes. These audits include questioning the timing and amount of deductions, the nexus of income among various tax jurisdictions and compliance with federal, state and local tax laws. In evaluating the exposure associated with various tax filing positions, the Company often accrues charges for probable exposures. During the annual evaluation of tax positions for 2004, the Company decreased amounts previously accrued for probable exposures by approximately \$792,000. At December 31, 2004, the Company believes it has appropriately accrued for probable exposures.

12. Retirement Plan

The Company has a 401(k) Retirement Plan. All employees of the Company are eligible to participate, subject to employment eligibility requirements. The Company pays a matching contribution of 50% up to the first 6% contributed by the employee. The Company's 401(k) matching expense was approximately \$990,000, \$1,037,000 and \$1,246,000 for the years ended December 31, 2004, 2003 and 2002, respectively.

13. Earnings Per Share (EPS)

Basic EPS is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock.

A reconciliation of the shares used to compute basic income per share to those used for diluted income per share is as follows for the years ended December 31 (in thousands):

| | 2004 | 2003 | 2002 |
|--|-------------|-------------|-------------|
| Shares for basic computation | 26,643 | 27,015 | 28,030 |
| Options and warrants (treasury stock method) | | | 403 |
| Shares for diluted computation | 26,643 | 27,015 | 28,433 |

Stock options for which the exercise price exceeds the average market price over the period have an anti-dilutive effect on EPS and, accordingly, are excluded from the diluted computation. Had such shares been included, shares for the diluted computation would have increased by approximately 3,009,000, 2,164,000 and 2,620,000 for the years

ended December 31, 2004, 2003 and 2002, respectively.

In addition, all other stock options and warrants convertible into common stock have been excluded from the diluted EPS computation in the years ended December 31, 2004 and 2003, as they are anti-dilutive due to the net losses recorded by the Company in those periods. Had such shares been included, the number of shares for the diluted computation for the year ended December 31, 2004 and 2003 would have increased by approximately 155,000 and 401,000, respectively.

F-27

Table of Contents

LIGHTBRIDGE, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

14. Worldcom, Inc. Settlement

During the quarter ended September 30, 2004, the Company received a settlement payment of approximately \$538,000 as a result of the WorldCom, Inc. bankruptcy proceedings for services provided to WorldCom in 2002. As part of the bankruptcy settlement, the Company also realized a one-time benefit of approximately \$1.2 million related to the release from liability of amounts owed to WorldCom, Inc. and amounts that had been reserved for potential claims against the Company as part of the WorldCom, Inc. bankruptcy proceedings. Approximately \$1.0 million of the benefit was recorded in general and administrative expenses and \$0.2 million was included in transaction cost of revenues for 2004.

15. Subsequent Events

On January 28, 2005, the Company closed its call center facility in Broomfield, Colorado. The Broomfield, Colorado call center facility had been supporting the Company's TDS operating segment. The work being performed at the facility has been transitioned to other Lightbridge call center facilities. In conjunction with the closure, the Company expects to record a restructuring charge of approximately \$0.9 million in the first quarter of 2005, primarily relating to facility closing costs and employee severance and termination benefits.

The Company plans to close its Fremont, California facility, where its Instant Conferencing business is located, effective March 31, 2005. In connection with the closure, the Company expects to record a restructuring charge in the first quarter of 2005 of approximately \$0.3 million, primarily relating to employee severance and termination benefits. Lightbridge expects to continue to provide the services for GroupTalk, its Instant Conferencing product, under its agreement with America Online, Inc.

16. Quarterly Financial Data (Unaudited)

| | Q1 | Q2 | Q3 | Q4 |
|--|---|-----------|------------|---------------|
| | (In thousands, except per share amounts) | | | |
| 2004 | | | | |
| Revenues | \$29,625 | \$36,685 | \$34,273 | \$ 32,472 |
| Gross profit | \$13,559 | \$19,201 | \$16,814 | \$ 15,591 |
| Income (loss) from operations | \$ (1,863) | \$ 827 | \$ (3,975) | \$ (1,967) |
| Net income (loss) (Q4 restated) | \$ (741) | \$ 573 | \$ (4,300) | \$(10,937)(a) |
| Basic and diluted earnings (loss) per share (Q4 restated) | \$ (0.03) | \$ 0.02 | \$ (0.16) | \$ (0.41)(a) |
| 2003 | | | | |
| Revenues | \$28,423 | \$31,299 | \$29,566 | \$ 30,690 |
| Gross profit | \$13,591 | \$15,953 | \$14,152 | \$ 14,333 |
| Income (loss) from operations | \$ (916) | \$ (493) | \$ (2,743) | \$ 294 |
| Net income (loss) | \$ (357) | \$ (83) | \$ (1,893) | \$ 884 |
| Basic and diluted earnings (loss) per share | \$ (0.01) | \$ (0.00) | \$ (0.07) | \$ 0.03 |

In light of views expressed by the Securities and Exchange Commission on February 7, 2005 with respect to accounting for operating leases, the Company recorded a fourth quarter 2004 adjustment related to tenant improvement allowances and rent holidays provided by landlords. The adjustment resulted in a cumulative \$0.6 million increase in net loss attributable to prior interim periods in 2004. The Company believes the effect of the adjustment is not material to the year ended December 31, 2004 financial statements.

(a) The Company previously reported a net loss and basic and diluted loss per share of \$9,676 and \$0.41 in Q4 2004 respectively. See Note 2 for discussion of restatement of financial statements.