

LEAP WIRELESS INTERNATIONAL INC

Form 10-Q/A

December 05, 2006

**Table of Contents**

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

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

(Mark One)

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

**For the quarterly period ended September 30, 2006  
OR**

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

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

**Commission File Number 0-29752**

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

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

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

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

**92121  
(Zip Code)**

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

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

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

The number of shares of registrant's common stock outstanding on November 1, 2006 was 67,763,650.

---

**Table of Contents**

**EXPLANATORY NOTE**

Leap Wireless International, Inc. has prepared this Amendment No. 1 to its Quarterly Report on Form 10-Q for the quarter ended September 30, 2006, or the Form 10-Q, for the sole purpose of furnishing to the Securities and Exchange Commission corrected certifications of our Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Exhibit 32 to the Form 10-Q). The original Exhibit 32 to the Form 10-Q was inadvertently furnished with typographical errors.

We have also supplemented Item 6 of Part II to include current certifications of our Chief Executive Officer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, filed as Exhibits 31.1 and 31.2 to this Amendment No. 1.

**Except for the filing and furnishing of Exhibits 31.1, 31.2 and 32 hereto, nothing in the Form 10-Q has been changed in this Amendment No. 1, which is otherwise identical to the Form 10-Q filed on November 9, 2006.**

---

**LEAP WIRELESS INTERNATIONAL, INC.**

**QUARTERLY REPORT ON FORM 10-Q  
For the Quarter Ended September 30, 2006**

**TABLE OF CONTENTS**

	<b>Page</b>	
<b><u>PART I FINANCIAL INFORMATION</u></b>		
<u>Item 1.</u>	<u>Financial Statements</u>	1
<u>Item 2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	21
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	36
<u>Item 4.</u>	<u>Controls and Procedures</u>	37
<b><u>PART II OTHER INFORMATION</u></b>		
<u>Item 1.</u>	<u>Legal Proceedings</u>	40
<u>Item 1A.</u>	<u>Risk Factors</u>	41
<u>Item 2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	56
<u>Item 3.</u>	<u>Defaults Upon Senior Securities</u>	57
<u>Item 4.</u>	<u>Submission of Matters to a Vote of Security Holders</u>	57
<u>Item 5.</u>	<u>Other Information</u>	57
<u>Item 6.</u>	<u>Exhibits</u>	57
<u>EXHIBIT 31.1</u>		
<u>EXHIBIT 31.2</u>		
<u>EXHIBIT 32</u>		

---

**Table of Contents**

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

**Item 1. Financial Statements.**

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

	<b>September 30, 2006 (Unaudited)</b>	<b>December 31, 2005</b>
<b>Assets</b>		
Cash and cash equivalents	\$ 233,594	\$ 293,073
Short-term investments	47,096	90,981
Restricted cash, cash equivalents and short-term investments	10,009	13,759
Inventories	50,937	37,320
Other current assets	41,657	29,237
Total current assets	383,293	464,370
Property and equipment, net	870,779	621,946
Wireless licenses	821,338	821,288
Assets held for sale (Note 8)	20,354	15,145
Goodwill	431,896	431,896
Other intangible assets, net	88,260	113,554
Deposits for wireless licenses (Note 8)	305,000	
Other assets	43,631	38,119
Total assets	\$ 2,964,551	\$ 2,506,318
<b>Liabilities and Stockholders Equity</b>		
Accounts payable and accrued liabilities	\$ 238,369	\$ 167,770
Current maturities of long-term debt (Note 4)	9,000	6,111
Other current liabilities	55,782	49,627
Total current liabilities	303,151	223,508
Long-term debt (Note 4)	888,750	588,333
Deferred tax liabilities	138,755	141,935
Other long-term liabilities	44,582	36,424
Total liabilities	1,375,238	990,200
Minority interests	25,099	1,761

Commitments and contingencies (Notes 4 and 9)

Stockholders' equity:

Preferred stock authorized 10,000,000 shares; \$.0001 par value, no shares issued and outstanding

Common stock authorized 160,000,000 shares; \$.0001 par value, 61,298,539 and 61,202,806 shares issued and outstanding at September 30, 2006 and

December 31, 2005, respectively

Additional paid-in capital

Retained earnings

Accumulated other comprehensive income

Total stockholders' equity

Total liabilities and stockholders' equity

6	6
1,505,217	1,490,638
56,788	21,575
2,203	2,138
1,564,214	1,514,357
\$ 2,964,551	\$ 2,506,318

See accompanying notes to condensed consolidated financial statements.

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

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Revenues:				
Service revenues	\$ 249,081	\$ 193,675	\$ 695,706	\$ 569,360
Equipment revenues	38,445	36,852	126,361	116,366
Total revenues	287,526	230,527	822,067	685,726
Operating expenses:				
Cost of service (exclusive of items shown separately below)	(70,722)	(50,304)	(186,181)	(150,109)
Cost of equipment	(68,624)	(49,576)	(179,591)	(141,553)
Selling and marketing	(42,948)	(25,535)	(107,992)	(73,340)
General and administrative	(49,110)	(41,306)	(145,268)	(119,764)
Depreciation and amortization	(56,409)	(49,076)	(163,781)	(144,461)
Impairment of indefinite-lived intangible assets	(4,701)	(689)	(7,912)	(12,043)
Total operating expenses	(292,514)	(216,486)	(790,725)	(641,270)
Gains on sales of wireless licenses and operating assets (Note 8)	21,990	14,593	21,990	14,593
Operating income	17,002	28,634	53,332	59,049
Minority interests in income of consolidated subsidiaries	(138)		(347)	
Interest income	5,491	2,991	15,218	6,070
Interest expense	(15,753)	(6,679)	(31,606)	(23,368)
Other income (expense), net	272	2,352	(5,112)	1,027
Income before income taxes	6,874	27,298	31,485	42,778
Income tax benefit (expense)	3,105	(10,901)	3,105	(17,762)
Income before cumulative effect of change in accounting principle	9,979	16,397	34,590	25,016
Cumulative effect of change in accounting principle			623	
Net income	\$ 9,979	\$ 16,397	\$ 35,213	\$ 25,016
Basic net income per share:				
Income before cumulative effect of change in accounting principle	\$ 0.17	\$ 0.27	\$ 0.57	\$ 0.42



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

Cumulative effect of change in accounting principle				0.01	
Basic net income per share	\$	0.17	\$	0.27	\$ 0.58 \$ 0.42
Diluted net income per share:					
Income before cumulative effect of change in accounting principle	\$	0.16	\$	0.27	\$ 0.56 \$ 0.41
Cumulative effect of change in accounting principle				0.01	
Diluted net income per share	\$	0.16	\$	0.27	\$ 0.57 \$ 0.41
Shares used in per share calculations:					
Basic		60,295		60,246	60,286 60,093
Diluted		62,290		61,395	61,866 60,727

See accompanying notes to condensed consolidated financial statements.

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

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

	<b>Nine Months Ended</b>	
	<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>
Operating activities:		
Net cash provided by operating activities	\$ 223,007	\$ 191,191
Investing activities:		
Cash purchases of property and equipment	(348,911)	(82,259)
Change in prepayments for purchases of property and equipment	2,770	(1,137)
Purchases of and deposits for wireless licenses	(307,128)	(243,987)
Proceeds from sales of wireless licenses and operating assets	27,968	99,050
Purchases of investments	(120,398)	(270,587)
Sales and maturities of investments	165,982	158,501
Change in restricted cash, cash equivalents and short-term investments, net	(3,443)	83
Net cash used in investing activities	(583,160)	(340,336)
Financing activities:		
Proceeds from long-term debt	900,000	600,000
Repayment of long-term debt	(596,694)	(416,757)
Debt issuance costs	(8,058)	(6,951)
Minority interest contributions	5,767	
Proceeds from issuance of common stock, net	725	
Costs related to forward equity sale	(1,066)	
Net cash provided by financing activities	300,674	176,292
Net increase (decrease) in cash and cash equivalents	(59,479)	27,147
Cash and cash equivalents at beginning of period	293,073	141,141
Cash and cash equivalents at end of period	\$ 233,594	\$ 168,288
Supplementary disclosure of cash flow information:		
Cash paid for interest	\$ 41,942	\$ 44,951
Cash paid for income taxes	\$ 327	\$ 280

See accompanying notes to condensed consolidated financial statements.

**Table of Contents**

**LEAP WIRELESS INTERNATIONAL, INC.**

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

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

Leap Wireless International, Inc. ( Leap ), a Delaware corporation, together with its wholly owned subsidiaries, is a wireless communications carrier that offers digital wireless service in the United States of America under the Cricket® and Jump Mobile brands. Leap conducts operations through its subsidiaries and has no independent operations or sources of operating revenue other than through dividends, if any, from its operating subsidiaries. Cricket and Jump Mobile services are offered by Leap's wholly owned subsidiary, Cricket Communications, Inc. ( Cricket ). Leap, Cricket and their subsidiaries are collectively referred to herein as the Company. Cricket and Jump Mobile services are also offered in certain markets by Alaska Native Broadband 1 License, LLC ( ANB 1 License ) and by LCW Wireless Operations, LLC ( LCW Operations ), both of which are designated entities under Federal Communications Commission ( FCC ) regulations. Cricket owns an indirect 75% non-controlling interest in ANB 1 License through a 75% non-controlling interest in Alaska Native Broadband 1, LLC ( ANB 1 ), and an indirect 72% non-controlling interest in LCW Operations through a 72% non-controlling interest in LCW Wireless, LLC ( LCW Wireless ) (see Note 8). In May 2006, Cricket acquired a non-controlling interest in Denali Spectrum, LLC ( Denali ), which participated in Auction #66 as a designated entity through its wholly owned subsidiary, Denali Spectrum License, LLC ( Denali License ). Cricket currently holds an 82.5% non-controlling interest in Denali.

The Company operates in a single operating segment as a wireless communications carrier that offers digital wireless service in the United States of America. As of and for the nine months ended September 30, 2006, all of the Company's revenues and long-lived assets related to operations in the United States of America.

**Note 2. Basis of Presentation and Significant Accounting Policies**

***Basis of Presentation***

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

The condensed consolidated financial statements include the accounts of Leap and its wholly owned subsidiaries as well as the accounts of ANB 1, LCW Wireless and Denali and their wholly owned subsidiaries. The Company consolidates its interests in ANB 1, LCW Wireless and Denali in accordance with Financial Accounting Standards Board ( FASB ) Interpretation No. ( FIN ) 46-R, Consolidation of Variable Interest Entities, because these entities are variable interest entities and the Company will absorb a majority of their expected losses. All significant intercompany accounts and transactions have been eliminated in the consolidated financial statements.

***Revenues***

Cricket's business revenues principally arise from the sale of wireless services, handsets and accessories. Wireless services are generally provided on a month-to-month basis. The Company's Cricket service offers customers unlimited wireless service in their Cricket service area for a flat monthly rate, and the Jump Mobile service offers customers a per-minute prepaid service. The Company does not require any of its customers to sign fixed-term service commitments or submit to a credit check, and therefore some of its customers may be more likely to terminate service for inability to pay than the customers of other wireless providers. Amounts received in advance

## **Table of Contents**

for wireless services from customers who pay in advance of their billing cycle are initially recorded as deferred revenues and are recognized as service revenues as services are rendered. Service revenues for customers who pay in arrears are recognized only after the service has been rendered and payment has been received. Starting in May 2006, all new and reactivating customers pay for their service in advance.

Equipment revenues arise from the sale of handsets and accessories. Revenues and related costs from the sale of handsets are recognized when service is activated by customers. Revenues and related costs from the sale of accessories are recognized at the point of sale. The costs of handsets and accessories sold are recorded in cost of equipment. Sales of handsets to third-party dealers and distributors are recognized as equipment revenues when service is activated by customers, as the Company does not yet have sufficient relevant historical experience to establish reliable estimates of returns by such dealers and distributors. Handsets sold by third-party dealers and distributors are recorded as inventory until they are sold to and activated by customers. Once the Company believes it has sufficient relevant historical experience on which to establish reliable estimates of returns, it will begin to recognize equipment revenues upon sale to third-party dealers and distributors. The Company is currently reviewing its experience and may be able to establish reliable estimates of returns in the foreseeable future.

Sales incentives offered without charge to customers and volume-based incentives paid to the Company's third-party dealers and distributors are recognized as a reduction of revenue and as a liability when the related service or equipment revenue is recognized. Customers have limited rights to return handsets and accessories based on time and/or usage. Customer returns of handsets and accessories have historically been insignificant.

## ***Costs and Expenses***

The Company's costs and expenses include:

*Cost of Service.* The major components of cost of service are: charges from other communications companies for long distance, roaming and content download services provided to the Company's customers; charges from other communications companies for their transport and termination of calls originated by the Company's customers and destined for customers of other networks; and expenses for tower and network facility rent, engineering operations, field technicians and related utility and maintenance charges, and salary and overhead charges associated with these functions.

*Cost of Equipment.* Cost of equipment primarily includes the cost of handsets and accessories purchased from third-party vendors and resold to the Company's customers in connection with its services, as well as lower-of-cost-or-market write-downs associated with excess and damaged handsets and accessories.

*Selling and Marketing.* Selling and marketing expenses primarily include advertising, promotional and public relations costs associated with acquiring new customers, store operating costs such as retail associates' salaries and rent, and overhead charges associated with selling and marketing functions.

*General and Administrative.* General and administrative expenses primarily include call center and other customer care program costs and salary and overhead costs associated with the Company's customer care, billing, information technology, finance, human resources, accounting, legal and executive functions.

## ***Property and Equipment***

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

service.

**Table of Contents**

The following table summarizes the depreciable lives for property and equipment (in years):

	<b>Depreciable Life</b>
Network equipment:	
Switches	10
Switch power equipment	15
Cell site equipment and site acquisitions and improvements	7
Towers	15
Antennae	3
Computer hardware and software	3-5
Furniture, fixtures, retail and office equipment	3-7

The Company's network construction expenditures are recorded as construction-in-progress until the network or assets are placed in service, at which time the assets are transferred to the appropriate property or equipment category. As a component of construction-in-progress, the Company capitalizes interest and salaries and related costs of engineering and technical operations employees, to the extent time and expense are contributed to the construction effort, during the construction period. Interest is capitalized on the carrying values of both wireless licenses and equipment during the construction period and is amortized over an estimated useful life of 10 years. During the three and nine months ended September 30, 2006, the Company capitalized \$3.4 million and \$12.3 million, respectively, of interest to property and equipment. During the three and nine months ended September 30, 2005, the Company capitalized \$3.6 million and \$4.3 million, respectively, of interest to property and equipment. Starting on January 1, 2006, site rental costs incurred during the construction period are recognized as rental expense in accordance with FASB Staff Position No. FAS 13-1, Accounting for Rental Costs Incurred During a Construction Period. Prior to fiscal 2006, such rental costs were capitalized as construction-in-progress.

Property and equipment to be disposed of by sale is not depreciated and is carried at the lower of carrying value or fair value less costs to sell. At September 30, 2006, there was no property and equipment classified as assets held for sale. At December 31, 2005, property and equipment with a net book value of \$5.4 million was classified as assets held for sale.

***Wireless Licenses***

Wireless licenses are initially recorded at cost and are not amortized. Wireless licenses are considered to be indefinite-lived intangible assets because the Company expects to continue to provide wireless service using the relevant licenses for the foreseeable future, and wireless licenses may be renewed every ten to fifteen years for a nominal fee. Wireless licenses to be disposed of by sale are carried at the lower of carrying value or fair value less costs to sell. At September 30, 2006 and December 31, 2005, wireless licenses with a carrying value of \$20.4 million and \$8.2 million, respectively, were classified as assets held for sale.

***Goodwill and Other Intangible Assets***

Goodwill represents the excess of reorganization value over the fair value of identified tangible and intangible assets recorded in connection with fresh-start reporting as of July 31, 2004. Other intangible assets were recorded upon adoption of fresh-start reporting and consist of customer relationships and trademarks which are being amortized on a straight-line basis over their estimated useful lives of four and fourteen years, respectively. At September 30, 2006, there were no intangible assets classified as assets held for sale. At December 31, 2005, intangible assets with a net

book value of \$1.5 million were classified as assets held for sale.

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

The Company assesses potential impairments to its long-lived assets, including property and equipment and certain intangible assets, when there is evidence that events or changes in circumstances indicate that the carrying value may not be recoverable. An impairment loss may be required to be recognized when the undiscounted cash flows expected to be generated by a long-lived asset (or group of such assets) is less than its carrying value. Any



**Table of Contents**

required impairment loss would be measured as the amount by which the asset's carrying value exceeds its fair value and would be recorded as a reduction in the carrying value of the related asset and charged to results of operations.

***Impairment of Indefinite-Lived Intangible Assets***

The Company assesses potential impairments to its indefinite-lived intangible assets, including goodwill and wireless licenses, annually and when there is evidence that events or changes in circumstances indicate that an impairment condition may exist. The Company's wireless licenses in its operating markets are combined into a single unit of accounting for purposes of testing impairment because management believes that these wireless licenses as a group represent the highest and best use of the assets, and the value of the wireless licenses would not be significantly impacted by a sale of one or a portion of the wireless licenses, among other factors. An impairment loss is recognized when the fair value of the asset is less than its carrying value and is measured as the amount by which the asset's carrying value exceeds its fair value. Any required impairment losses are recorded as a reduction in the carrying value of the related asset and charged to results of operations. The Company conducts its annual tests for impairment during the third quarter of each year. As a result of the annual impairment tests of wireless licenses, the Company recorded impairment charges of \$4.7 million and \$0.7 million during the quarters ended September 30, 2006 and 2005, respectively, to reduce the carrying values of certain non-operating wireless licenses to their estimated fair values. Estimates of the fair value of the Company's wireless licenses are based primarily on available market prices, including successful bid prices in FCC auctions and selling prices observed in wireless license transactions.

During the second quarter of 2006, the Company recorded impairment charges of \$3.2 million to reduce the carrying values of certain non-operating wireless licenses to their estimated fair values as a result of a sale transaction (see Note 8). During the second quarter of 2005, the Company recorded impairment charges of \$11.4 million to reduce the carrying values of certain non-operating wireless licenses to their estimated fair values as a result of a sale transaction.

***Basic and Diluted Earnings Per Share***

Basic earnings per share is calculated by dividing net income by the weighted-average number of common shares outstanding during the reporting period. Diluted earnings per share reflects the potential dilutive effect of additional common shares that are issuable upon exercise of outstanding stock options and warrants, restricted stock awards and forward equity agreements calculated using the treasury stock method.

A reconciliation of weighted-average shares outstanding used in calculating basic and diluted net income per share is as follows (unaudited) (in thousands):

	<b>Three Months</b>		<b>Nine Months</b>	
	<b>Ended September 30,</b>		<b>Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Weighted-average shares outstanding				
share	60,295	60,246	60,286	60,093
Effect of dilutive securities:				
Non-qualified stock options	247		147	62
Restricted stock awards	974	861	933	327
Warrants	379	288	367	245
Common shares issuable upon physical settlement of forward sale agreements	395		133	

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

Adjusted weighted-average shares outstanding	diluted net				
income per share		62,290	61,395	61,866	60,727

The number of shares not included in the computation of diluted net income per share because their effect would have been anti-dilutive totaled 1.2 million and 1.4 million for the three and nine months ended September 30,

**Table of Contents**

2006, respectively, and 1.8 million and 0.4 million for the three and nine months ended September 30, 2005, respectively.

**Comprehensive Income**

Comprehensive income consists of the following (unaudited) (in thousands):

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Net income	\$ 9,979	\$ 16,397	\$ 35,213	\$ 25,016
Other comprehensive income:				
Net unrealized holding gains (losses) on investments, net of tax	(128)	120	(170)	82
Unrealized gains (losses) on interest rate swaps, net of tax	(3,033)	2,007	235	1,213
Comprehensive income	\$ 6,818	\$ 18,524	\$ 35,278	\$ 26,311

Components of accumulated other comprehensive income consist of the following (in thousands):

	<b>September 30, 2006 (Unaudited)</b>	<b>December 31, 2005</b>
Net unrealized holding losses on investments, net of tax	\$ (178)	\$ (8)
Unrealized gains on interest rate swaps, net of tax	2,381	2,146
Accumulated other comprehensive income	\$ 2,203	\$ 2,138

**Share-Based Payments**

The Company accounts for share-based awards exchanged for employee services in accordance with Statement of Financial Accounting Standards ( SFAS ) No. 123R, Share-Based Payment ( SFAS 123R ). Under SFAS 123R, share-based compensation cost is measured at the grant date, based on the estimated fair value of the award, and is recognized as expense over the employee's requisite service period. The Company adopted SFAS 123R, as required, on January 1, 2006. Prior to fiscal 2006, the Company recognized compensation expense for employee share-based awards based on their intrinsic value on the grant date pursuant to Accounting Principles Board Opinion No. 25 ( APB 25 ), Accounting for Stock Issued to Employees, and provided the required pro forma disclosures of SFAS No. 123, Accounting for Stock-Based Compensation ( SFAS 123 ).

The Company adopted SFAS 123R using a modified prospective approach. Under the modified prospective approach, prior periods are not revised for comparative purposes. The valuation provisions of SFAS 123R apply to new awards and to awards that are outstanding on the effective date and subsequently modified or cancelled. Compensation expense, net of estimated forfeitures, for awards outstanding at the effective date is recognized over the remaining service period using the compensation cost calculated in prior periods.

The Company has granted nonqualified stock options, restricted stock awards and deferred stock units under its 2004 Stock Option, Restricted Stock and Deferred Stock Unit Plan (the 2004 Plan ). Most of the Company's stock options and restricted stock awards include both a service condition and a performance condition that relates only to vesting. The stock options and restricted stock awards generally vest in full three or five years from the grant date with no interim time-based vesting. In addition, the stock options and restricted stock awards generally provide for the possibility of annual accelerated performance-based vesting of a portion of the awards if the Company achieves specified performance conditions. Certain stock options and restricted stock awards include only a service condition and vest over periods of up to approximately three years from the grant date. All share-based awards provide for accelerated vesting if there is a change in control (as defined in the 2004 Plan). Compensation expense is amortized on a straight-line basis over the requisite service period for the entire award, which is generally the maximum vesting period of the award.

**Table of Contents**

During the quarter ended March 31, 2006, the Board of Directors approved a modification of the accelerated vesting performance conditions for all outstanding share-based awards with such performance conditions to take into account changes in business conditions that were not considered when the performance conditions were originally established, including the planned build-out of new markets. The performance conditions were originally established and subsequently modified such that they are neither probable nor improbable of achievement. As a result, the modifications of the performance conditions did not result in changes in the expected lives of the awards and, therefore, did not result in changes in the fair value of the awards. The original compensation cost related to the modified awards continues to be recognized over the requisite service period.

*Share-Based Compensation Information under SFAS 123R*

Under SFAS 123R, the fair value of the Company's restricted stock awards is based on the grant date fair value of the common stock. This was the basis for the intrinsic value method used to measure compensation expense for the restricted stock awards prior to fiscal 2006. All restricted stock awards were granted with an exercise price of \$0.0001 per share. The weighted-average grant date fair value of the restricted common stock was \$45.59 and \$44.26 per share, respectively, during the three and nine months ended September 30, 2006.

The Company uses the Black-Scholes option pricing model to estimate the fair value of its stock options under SFAS 123R. This valuation model was previously used for the Company's pro forma disclosures under SFAS 123. All stock options were granted with an exercise price equal to the fair value of the common stock on the grant date. The weighted-average grant date fair value of employee stock options granted during the three and nine months ended September 30, 2006 was \$24.53 and \$23.68 per share, respectively, which was estimated using the following weighted-average assumptions:

	<b>Three Months Ended September 30, 2006</b>	<b>Nine Months Ended September 30, 2006</b>
Expected volatility	47%	47%
Expected term (in years)	6.5	6.5
Risk-free interest rate	4.87%	4.80%
Expected dividend yield		

The determination of the fair value of stock options using an option pricing model is affected by the Company's stock price, as well as assumptions regarding a number of complex and subjective variables. The methods used to determine these variables are generally similar to the methods used prior to fiscal 2006 for purposes of the Company's pro forma information under SFAS 123. The volatility assumption is based on a combination of the historical volatility of the Company's common stock and the volatilities of similar companies over a period of time equal to the expected term of the stock options. The volatilities of similar companies are used in conjunction with the Company's historical volatility because of the lack of sufficient relevant history for the Company's common stock equal to the expected term. The expected term of employee stock options represents the weighted-average period the stock options are expected to remain outstanding. The expected term assumption is estimated based primarily on the options' vesting terms and remaining contractual life and employees' expected exercise and post-vesting employment termination behavior. The risk-free interest rate assumption is based upon observed interest rates on the grant date appropriate for the term of the employee stock options. The dividend yield assumption is based on the expectation of no future dividend payouts by the Company.

As share-based compensation expense under SFAS 123R is based on awards ultimately expected to vest, it is reduced for estimated forfeitures. SFAS 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Forfeitures were accounted for as they occurred in the Company's pro forma disclosures under SFAS 123. The Company recorded a gain of \$0.6 million as a cumulative effect of a change in accounting principle related to the change in accounting for forfeitures under SFAS 123R.

**Table of Contents**

Total share-based compensation expense related to all of the Company's share-based awards for the three and nine months ended September 30, 2006 was allocated as follows (unaudited) (in thousands, except per share data):

	<b>Three Months Ended September 30, 2006</b>	<b>Nine Months Ended September 30, 2006</b>
Cost of service	\$ 311	\$ 830
Selling and marketing expenses	637	1,437
General and administrative expenses	4,115	12,210
Share-based compensation expense before tax	5,063	14,477
Related income tax benefit		
Share-based compensation expense, net of tax	\$ 5,063	\$ 14,477
Net share-based compensation expense per share:		
Basic	\$ 0.08	\$ 0.24
Diluted	\$ 0.08	\$ 0.23

Prior to fiscal 2006, the restricted stock awards and deferred stock units were granted with an exercise price of \$0.0001 per share and, therefore, the Company recognized compensation expense associated with these awards based on their intrinsic value. No compensation expense was recorded for stock options prior to adopting SFAS 123R, because the Company established the exercise price of the stock options based on the fair value of the underlying stock at the date of grant. During the three months ended September 30, 2005, the Company granted a total of 390,975 non-qualified stock options and 125,781 shares of restricted common stock to directors, executive officers and other employees of the Company. During the nine months ended September 30, 2005, the Company granted a total of 2,073,692 non-qualified stock options, 932,204 shares of restricted common stock and 246,484 deferred stock units to directors, executive officers and other employees of the Company. The Company recorded \$2.7 million and \$9.9 million of share-based compensation expense for the three and nine months ended September 30, 2005, respectively, resulting from the grant of the restricted common stock and immediately vested deferred stock units. The total intrinsic value of the deferred stock units of \$6.9 million was recorded as share-based compensation expense during the nine months ended September 30, 2005. The total intrinsic value of the restricted stock awards is being amortized on a straight-line basis over the maximum vesting period of the awards of either three or five years.

Total share-based compensation expense for the three and nine months ended September 30, 2005 was allocated as follows (unaudited) (in thousands):

	<b>Three Months Ended September 30, 2005</b>	<b>Nine Months Ended September 30, 2005</b>
Cost of service	\$ 217	\$ 1,014

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

Selling and marketing expenses	203	896
General and administrative expenses	2,301	7,941
Share-based compensation expense	\$ 2,721	\$ 9,851



**Table of Contents***Pro Forma Information under SFAS 123 for Periods Prior to Fiscal 2006*

The pro forma effects on net income and earnings per share of recognizing share-based compensation expense under the fair value method required by SFAS 123 was as follows (unaudited) (in thousands, except per share data):

	<b>Three Months Ended September 30, 2005</b>	<b>Nine Months Ended September 30, 2005</b>
As reported net income	\$ 16,397	\$ 25,016
Add back share-based compensation expense included in net income	2,721	9,851
Less pro forma compensation expense, net of tax	(4,962)	(15,002)
Pro forma net income	\$ 14,156	\$ 19,865
Basic net income per share:		
As reported	\$ 0.27	\$ 0.42
Pro forma	\$ 0.24	\$ 0.33
Diluted net income per share:		
As reported	\$ 0.27	\$ 0.41
Pro forma	\$ 0.23	\$ 0.33

For purposes of pro forma disclosures under SFAS 123, the estimated fair value of the stock options was amortized on a straight-line basis over the maximum vesting period of the awards.

The weighted-average fair value per share on the grant date for stock options granted during the three and nine months ended September 30, 2005 was \$26.31 and \$20.58, respectively, which was estimated using the Black-Scholes option pricing model and the following weighted-average assumptions:

	<b>Three Months Ended September 30, 2005</b>	<b>Nine Months Ended September 30, 2005</b>
Expected volatility	87%	87%
Expected term (in years)	6.5	5.7
Risk-free interest rate	3.93%	3.61%
Expected dividend yield		

**Recent Accounting Pronouncements**

In September 2006, the Securities and Exchange Commission ( SEC ) issued Staff Accounting Bulletin No. 108 ( SAB 108 ), which addresses how the effects of prior year uncorrected misstatements should be considered when quantifying misstatements in current year financial statements. SAB 108 requires companies to quantify misstatements using a balance sheet and income statement approach and to evaluate whether either approach results in quantifying an error that is material in light of relevant quantitative and qualitative factors. When the effect of initial adoption is material, companies may record the effect as a cumulative effect adjustment to beginning of year retained earnings. SAB 108 is effective for annual financial statements covering the first fiscal year ending after November 15, 2006. The Company is required to adopt this interpretation by December 31, 2006. The Company does not believe the initial adoption will have a material impact on its consolidated financial statements.

In September 2006, the FASB issued Statement No. 157, Fair Value Measurements ( SFAS 157 ), which defines fair value, establishes a framework for measuring fair value in accounting principles generally accepted in the United States of America and expands disclosure about fair value measurements. SFAS 157 is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company will be

**Table of Contents**

required to adopt SFAS 157 in the first quarter of fiscal year 2008. The Company is currently evaluating what impact, if any, SFAS 157 will have on its consolidated financial statements.

In June 2006, the FASB issued FIN 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109. This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. This Interpretation is effective for fiscal years beginning after December 15, 2006. The Company is currently assessing what impact, if any, the Interpretation will have on its consolidated financial statements.

**Note 3. Supplementary Balance Sheet Information (in thousands):**

	<b>September 30, 2006 (Unaudited)</b>	<b>December 31, 2005</b>
Other current assets:		
Accounts receivable, net	\$ 23,208	\$ 17,397
Prepaid expenses	15,495	9,884
Other	2,954	1,956
	\$ 41,657	\$ 29,237
Property and equipment, net:		
Network equipment	\$ 908,559	\$ 654,993
Computer equipment and other	63,593	38,778
Construction-in-progress	239,785	134,929
	1,211,937	828,700
Accumulated depreciation	(341,158)	(206,754)
	\$ 870,779	\$ 621,946
Accounts payable and accrued liabilities:		
Trade accounts payable	\$ 164,772	\$ 117,140
Accrued payroll and related benefits	25,263	13,185
Other accrued liabilities	48,334	37,445
	\$ 238,369	\$ 167,770
Other current liabilities:		
Deferred revenues	\$ 24,167	\$ 21,391
Accrued property taxes	9,796	6,536
Sales, telecommunications and other tax liabilities	9,552	15,745
Other	12,267	5,955
	\$ 55,782	\$ 49,627

**Note 4. Long-Term Debt**

*Senior Secured Credit Facility*

Long-term debt as of September 30, 2006 consisted of an amended and restated senior secured credit agreement (the Credit Agreement ), which included a \$900 million term loan and an undrawn \$200 million revolving credit facility available until June 2011. Under the Credit Agreement, the term loan bears interest at the London Interbank Offered Rate (LIBOR) plus 2.75 percent, with interest periods of one, two, three or six months, or bank base rate plus 1.75 percent, as selected by Cricket, with the rate subject to adjustment based on Leap s corporate family debt rating. Outstanding borrowings under the term loan must be repaid in 24 quarterly payments

**Table of Contents**

of \$2.25 million each, commencing September 30, 2006, followed by four quarterly payments of \$211.5 million each, commencing September 30, 2012.

The maturity date for outstanding borrowings under the revolving credit facility is June 16, 2011. The commitment of the lenders under the revolving credit facility may be reduced in the event mandatory prepayments are required under the Credit Agreement. The commitment fee on the revolving credit facility is payable quarterly at a rate of between 0.25 and 0.50 percent per annum, depending on the Company's consolidated senior secured leverage ratio. Borrowings under the revolving credit facility would currently accrue interest at LIBOR plus 2.75 percent or the bank base rate plus 1.75 percent, as selected by Cricket, with the rate subject to adjustment based on the Company's consolidated senior secured leverage ratio.

The facilities under the Credit Agreement are guaranteed by Leap and all of its direct and indirect domestic subsidiaries (excluding Cricket, which is the primary obligor, and ANB 1, LCW Wireless and Denali and their respective subsidiaries) and are secured by substantially all of the present and future personal property and owned real property of Leap, Cricket and such direct and indirect domestic subsidiaries. Under the Credit Agreement, the Company is subject to certain limitations, including limitations on its ability to: incur additional debt or sell assets, with restrictions on the use of proceeds; make certain investments and acquisitions; grant liens; pay dividends; and make certain other restricted payments. In addition, the Company will be required to pay down the facilities under certain circumstances if it issues debt, sells assets or property, receives certain extraordinary receipts or generates excess cash flow (as defined in the Credit Agreement). The Company is also subject to a financial covenant with respect to a maximum consolidated senior secured leverage ratio and, if a revolving credit loan or uncollateralized letter of credit is outstanding, with respect to a minimum consolidated interest coverage ratio, a maximum consolidated leverage ratio and a minimum consolidated fixed charge ratio. In addition to investments in joint ventures relating to the FCC's recent Auction #66, the Credit Agreement allows the Company to invest up to \$325 million in ANB 1 and ANB 1 License, up to \$85 million in LCW Wireless and its subsidiaries, and up to \$150 million plus an amount equal to an available cash flow basket in other joint ventures, and allows the Company to provide limited guarantees for the benefit of ANB 1, LCW Wireless and other joint ventures.

Affiliates of Highland Capital Management, L.P. (a beneficial stockholder of Leap and an affiliate of James D. Dondero, a director of Leap) participated in the syndication of the Credit Agreement in initial amounts equal to \$225 million of the term loan and \$40 million of the revolving credit facility, and Highland Capital Management received a syndication fee of \$300,000 in connection with their participation.

At September 30, 2006, the effective interest rate on the term loan was 7.8%, including the effect of interest rate swaps, and the outstanding indebtedness was \$897.8 million. The terms of the Credit Agreement require the Company to enter into interest rate swap agreements in a sufficient amount so that at least 50% of the Company's outstanding indebtedness for borrowed money bears interest at a fixed rate by December 31, 2006. The Company has entered into interest rate swap agreements with respect to \$355 million of its debt. These swap agreements effectively fix the interest rate on \$250 million of indebtedness at 6.7% and \$105 million of indebtedness at 6.8% through June 2007 and 2009, respectively. The fair value of the swap agreements at September 30, 2006 and 2005 was \$3.8 million and \$2.0 million, respectively, and was recorded in other assets in the consolidated balance sheet.

Long-term debt at December 31, 2005 consisted of a senior secured credit agreement which included term loans with an aggregate outstanding balance of \$594.4 million and an undrawn \$110 million revolving credit facility. A portion of the proceeds from the new term loan under the Credit Agreement was used to repay these existing term loans in June 2006. Upon repayment of the existing term loans and execution of the new revolving credit facility, the Company wrote off unamortized deferred debt issuance costs related to the existing credit agreement of \$5.6 million to other expense for the second quarter of 2006.

***Bridge Loan Facility***

On August 8, 2006, the Company entered into a bridge credit agreement consisting of an unsecured \$850 million bridge loan facility, available until the earlier of March 31, 2007 and 15 days after the date payment was required in full to the FCC for wireless licenses acquired in Auction #66. In October 2006, the Company borrowed \$570 million under the bridge loan facility to pay a portion of the final balance it owed to the FCC for its Auction #66 licenses and to loan Denali License \$182.6 million to permit it to pay the final balance it owed to the

**Table of Contents**

FCC for its Auction #66 license. The Company used a portion of the cash proceeds from the sale of unsecured senior notes issued in October 2006 (see Note 10) to repay the outstanding obligations, including accrued interest, under the bridge loan facility. Upon repayment of the outstanding indebtedness, the bridge loan facility was terminated.

**Note 5. Income Taxes**

The provision for income taxes during interim quarterly reporting periods is based on the Company's estimate of the annual effective tax rate for the full fiscal year. The Company determines the annual effective tax rate based upon its estimated ordinary income (loss), which is its annual income (loss) from continuing operations before tax, excluding unusual or infrequently occurring items. Significant management judgment is required in projecting the Company's annual income (loss) and determining its annual effective tax rate. The Company provides for income taxes in each of the jurisdictions in which it operates. This process involves estimating the actual current tax expense and any deferred income tax expense resulting from temporary differences arising from differing treatments of items for tax and accounting purposes. These temporary differences result in deferred tax assets and liabilities. Deferred tax assets are also established for the expected future tax benefits to be derived from net operating loss and capital loss carryforwards.

The Company must then assess the likelihood that its deferred tax assets will be recovered from future taxable income. To the extent that the Company believes it is more likely than not that its deferred tax assets will not be recovered, it must establish a valuation allowance. The Company considers all available evidence, both positive and negative, including the Company's historical operating losses, to determine the need for a valuation allowance. The Company has recorded a full valuation allowance on its net deferred tax asset balances for all periods presented because of uncertainties related to utilization of the deferred tax assets. Deferred tax liabilities associated with wireless licenses, tax goodwill and investments in joint ventures cannot be considered a source of taxable income to support the realization of deferred tax assets, because these deferred tax liabilities will not reverse until some indefinite future period.

At such time as the Company determines that it is more likely than not that the deferred tax assets are realizable, the valuation allowance will be reduced. Pursuant to American Institute of Certified Public Accountants' Statement of Position 90-7, Financial Reporting by Entities in Reorganization under the Bankruptcy Code, future decreases in the valuation allowance established in fresh-start reporting will be accounted for as a reduction in goodwill rather than as a reduction of tax expense.

**Note 6. Employee Stock Benefit Plans**

***Stock Option Plan***

The Company's 2004 Plan allows for the grant of stock options, restricted stock and deferred stock units to employees, independent directors and consultants. A total of 4,800,000 shares of common stock were initially reserved for issuance under the 2004 Plan. A total of 970,108 shares of common stock were available for issuance under the 2004 Plan as of September 30, 2006. The stock options are exercisable for up to 10 years from the grant date.

**Table of Contents**

A summary of stock option transactions follows:

	<b>Number of Shares (In thousands)</b>	<b>Weighted- Average Exercise Price Per Share</b>	<b>Weighted- Average Remaining Contractual Term (In years)</b>	<b>Aggregate Intrinsic Value (In thousands)</b>
Outstanding at December 31, 2005	1,892	\$ 28.94		
Options granted	745	44.08		
Options forfeited	(85)	31.01		
Options exercised				
Outstanding at September 30, 2006	2,552	\$ 33.30	8.91	\$ 37,939
Exercisable at September 30, 2006	76	\$ 26.50	8.44	\$ 1,654

A summary of unvested restricted stock follows:

	<b>Number of Shares (In thousands)</b>	<b>Weighted- Average Grant Date Fair Value Per Share</b>
Unvested at December 31, 2005	895	\$ 28.56
Shares granted	139	44.26
Shares forfeited	(33)	28.85
Shares vested		
Unvested at September 30, 2006	1,001	\$ 30.74

No stock options or restricted stock vested during the three and nine months ended September 30, 2006. At September 30, 2006, total unrecognized compensation cost related to unvested stock options and restricted stock awards was \$29.5 million and \$16.1 million, respectively, which is expected to be recognized over weighted-average periods of 3.0 and 2.1 years, respectively. No share-based compensation cost was capitalized as part of inventory and fixed assets prior to fiscal 2006 or during the three and nine months ended September 30, 2006. No stock options were exercised during the three and nine months ended September 30, 2006.

Upon option exercise, the Company issues new shares of stock. The terms of the restricted stock grant agreements allow the Company to repurchase unvested shares at the option, but not the obligation, of the Company for a period of



sixty days, commencing ninety days after the employee has a termination event. If the Company elects to repurchase all or any portion of the unvested shares, it may do so at the original purchase price per share.

Additional information about stock options outstanding at September 30, 2006 follows:

Exercise Prices	Exercisable		Total	
	Number of Shares (In thousands)	Weighted-Average Exercise Price Per Share	Number of Shares (In thousands)	Weighted-Average Exercise Price Per Share
Less than \$35.00	76	\$ 26.50	1,789	\$ 28.76
Above \$35.00			763	43.94
Total outstanding	76	\$ 26.50	2,552	\$ 33.30

***Employee Stock Purchase Plan***

The Company's Employee Stock Purchase Plan (the "ESP Plan") allows eligible employees to purchase shares of common stock during a specified offering period. The purchase price is 85% of the lower of the fair market value

**Table of Contents**

of such stock on the first or last day of the offering period. Employees may authorize the Company to withhold up to 15% of their compensation during any offering period for the purchase of shares under the ESP Plan, subject to certain limitations. A total of 800,000 shares of common stock were initially reserved for issuance under the ESP Plan, and a total of 778,989 shares remained available for issuance under the ESP Plan as of September 30, 2006. The current offering period under the ESP Plan is from July 1, 2006 through December 31, 2006. Compensation expense related to the ESP Plan has been insignificant.

**Note 7. Stockholders Equity**

***Forward Sale Agreements***

In August 2006, in connection with a public offering of Leap common stock, Leap entered into forward sale agreements for the sale of an aggregate of 6,440,000 shares of its common stock, including an amount equal to the underwriters over-allotment option in the public offering (which was fully exercised). The initial forward sale price was \$40.11 per share, which was equivalent to the public offering price less the underwriting discount, and was subject to daily adjustment based on a floating interest factor equal to the federal funds rate, less a spread of 1.0%. The forward sale agreements allowed the Company to elect to physically settle the transactions, or to issue shares of its common stock in satisfaction of its obligations under the forward sale agreements, in all circumstances (unless the Company had previously elected otherwise). As a result, these forward sale agreements were initially measured at fair value and reported in permanent equity. Subsequent changes in fair value have not been recognized as the forward sale agreements continued to be classified as permanent equity. In October 2006, Leap issued 6,440,000 shares of its common stock to physically settle its forward sale agreements and received aggregate cash proceeds of \$260.0 million (before expenses) from such physical settlements. Upon such full settlement, the forward sale agreements were fully performed.

**Note 8. Significant Acquisitions and Dispositions**

In September 2006, a wholly owned subsidiary of Cricket was named the winning bidder in Auction #66 for 99 wireless licenses with an aggregate purchase price of \$710.2 million and covering 121.2 million potential customers (adjusted to eliminate duplication among certain overlapping licenses won by it in Auction #66), and Denali License was named the winning bidder for one wireless license with a net purchase price of \$274.1 million and covering 59.3 million potential customers (which includes markets covering 5.7 million potential customers which overlap with certain licenses won by Cricket's wholly owned subsidiary in Auction #66). In July 2006, Cricket and Denali License paid to the FCC \$255 million and \$50 million, respectively, as bidding deposits for Auction #66. The balance of the purchase price for these licenses was paid to the FCC in October 2006.

In July 2006, the Company completed the sale of its wireless licenses and operating assets in its Toledo and Sandusky, Ohio markets in exchange for \$28.0 million in cash and an equity interest in LCW Wireless. The Company also contributed to LCW Wireless \$21.0 million in cash and two wireless licenses and related operating assets, resulting in Cricket owning a 72% non-controlling membership interest in LCW Wireless. The Company recognized a net gain of \$21.5 million in the third quarter of 2006 associated with these transactions.

From June 2006 through October 2006, the Company entered into four agreements to sell wireless licenses that the Company was not using to offer commercial service for an aggregate sales price of \$22.4 million. In October 2006, three of these transactions were completed. Completion of the remaining transaction is subject to customary closing conditions, including FCC approval. During the second quarter of 2006, the Company recorded impairment charges of \$3.2 million to adjust the carrying values of four of the licenses to their estimated fair values, which were based on the agreed upon sales prices.

In March 2006, the Company entered into an agreement with a debtor-in-possession for the purchase of 13 wireless licenses in North Carolina and South Carolina for an aggregate purchase price of \$31.8 million. Completion of this transaction is subject to customary closing conditions, including the receipt of certain FCC approvals and orders which have already been issued but which have not yet become final.

**Table of Contents****Note 9. Commitments and Contingencies*****Outstanding Bankruptcy Claims***

Although the Company's plan of reorganization became effective and the Company emerged from bankruptcy in August 2004, a tax claim of approximately \$4.9 million Australian dollars (approximately \$3.8 million U.S. dollars as of November 2, 2006) asserted by the Australian government against Leap in the U.S. Bankruptcy Court for the Southern District of California has not yet been resolved. The Bankruptcy Court sustained the Company's objection to the claim and dismissed the claim in June 2006. However, the Australian government has appealed the Bankruptcy Court order to the United States District Court for the Southern District of California. The Company, the Australian government and the trust established in bankruptcy for the benefit of the Leap general unsecured creditors have agreed in principle to settle this claim. The Company does not believe that the resolution of this claim will have a material adverse effect on its consolidated financial statements.

***Patent Litigation***

On June 14, 2006, the Company sued MetroPCS Communications, Inc. ( MetroPCS ) in the United States District Court for the Eastern District of Texas for infringement of U.S. Patent No. 6,813,497 *Method for Providing Wireless Communication Services and Network and System for Delivering Same*, issued to the Company. The Company's complaint seeks damages and an injunction against continued infringement. On August 3, 2006, MetroPCS (i) answered the complaint, (ii) raised a number of affirmative defenses, and (iii) together with two related entities (referred to, collectively with MetroPCS, as the MetroPCS entities ), counterclaimed against Leap, Cricket, numerous Cricket subsidiaries, ANB 1 License, Denali License, and current and former employees of Leap and Cricket, including Leap CEO Doug Hutcheson. The countersuit alleges claims for breach of contract, misappropriation, conversion and disclosure of trade secrets, misappropriation of confidential information and breach of confidential relationship, relating to information provided by MetroPCS to such employees, including prior to their employment by Leap, and asks the court to award damages, including punitive damages, impose an injunction enjoining the Company from participating in Auction #66, impose a constructive trust on the Company's business and assets for the benefit of MetroPCS, and declare that the MetroPCS entities have not infringed U.S. Patent No. 6,813,497 and that such patent is invalid. MetroPCS's claims allege that the Company and the other counterclaim defendants improperly obtained, used and disclosed trade secrets and confidential information of the MetroPCS entities and breached confidentiality agreements with the MetroPCS entities. On October 13, 2006, ANB 1 License, Denali License, and two of the individual counterclaim defendants filed motions to dismiss the claims against them, and the remaining counterclaim defendants answered the counterclaims. Based upon the Company's preliminary review of the counterclaims, the Company believes that it has meritorious defenses and intends to vigorously defend against the counterclaims. If the MetroPCS entities were to prevail in their counterclaims, it could have a material adverse effect on the Company's business, financial condition and results of operations. On September 22, 2006, Royal Street Communications, LLC ( Royal Street ), an entity affiliated with MetroPCS, filed an action in the United States District Court for the Middle District of Florida seeking a declaratory judgment that the Company's U.S. Patent No. 6,813,497 is invalid and is not being infringed by Royal Street or its PCS systems. On October 17, 2006, the Company filed a motion to dismiss the case or, in the alternative, to transfer the case to the Eastern District of Texas. The Company intends to vigorously defend against these actions.

On August 3, 2006, MetroPCS filed a separate action in the United States District Court for the Northern District of Texas seeking a declaratory judgment that the Company's U.S. Patent No. 6,959,183 *Operations Method for Providing Wireless Communication Services and Network and System for Delivering Same* is invalid and is not being infringed by MetroPCS and its affiliates. On October 13, 2006, Leap and Cricket filed a motion to dismiss this action or, in the alternative, to transfer the action to the United States District Court for the Eastern District of Texas where another suit is pending between the Company, MetroPCS and other parties as described in the preceding

paragraph. The Company intends to vigorously defend against the action.

On August 17, 2006, the Company was served with a complaint filed by the MetroPCS entities in the Superior Court of the State of California, which names Leap, Cricket, certain of its subsidiaries, and certain current and former employees of Leap and Cricket, including Leap CEO Doug Hutcheson, as defendants. In the complaint, the MetroPCS entities allege unfair competition, misappropriation of trade secrets, (with respect to the individuals

**Table of Contents**

sued) intentional and negligent interference with contract, breach of contract, intentional interference with prospective economic advantage and trespass, and ask the court to award damages, including punitive damages, and restitution. On October 13, 2006, all defendants joined in a motion to stay the case until resolution of the case in the Eastern District of Texas because of the substantial overlap of the cases. If and when the case proceeds, based on the initial complaint, it is unclear whether, if the MetroPCS entities were to prevail, it could have a material adverse effect on the Company's business, financial condition and results of operations. The Company intends to vigorously defend against the actions.

***Tortious Interference and Unfair Competition Litigation***

On July 10, 2006, the Company sued T-Mobile USA, Inc. ( T-Mobile ) in the District Court of Harris County, Texas for tortious interference with existing contract, tortious interference with prospective relations, business disparagement, and antitrust violations arising out of anticompetitive activities of T-Mobile in the Houston, Texas marketplace. In response, on August 8, 2006, T-Mobile filed a counterclaim against Cricket, alleging tortious interference with T-Mobile's contracts with employees, ex-employees, authorized dealers and customers and unfair competition, and asking the court to award damages, including punitive damages, in an unspecified amount. If T-Mobile was to prevail in its counterclaim, it could have a material adverse effect on the Company's business, financial condition and results of operations. The Company intends to vigorously defend against the counterclaim.

***Other***

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

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

have appealed the ruling to the state supreme court.

Although Leap is not a defendant in either the Whittington or AWG Lawsuits, several of the defendants have indemnification agreements with the Company. Leap's D&O insurers have not filed a reservation of rights letter and have been paying defense costs. Management believes that the liability, if any, from the AWG and Whittington

**Table of Contents**

Lawsuits and the related indemnity claims of the defendants against Leap is not probable or estimable; therefore, no accrual has been made in Leap's consolidated financial statements as of September 30, 2006 and December 31, 2005 related to these contingencies.

In addition to the matters described above, the Company is often involved in certain other claims arising in the course of business, seeking monetary damages and other relief. The amount of the liability, if any, from such claims cannot currently be reasonably estimated; therefore, no accruals have been made in the Company's consolidated financial statements as of September 30, 2006 and December 31, 2005 for such claims.

***Commitments***

The Company has entered into non-cancelable operating lease agreements to lease its administrative and retail facilities, and sites for towers, equipment and antennae required for the operation of its wireless networks. These leases typically include renewal options and escalation clauses. In general, site leases have five year initial terms with four five year renewal options. The following table summarizes the approximate future minimum rentals under non-cancelable operating leases, including renewals that are reasonably assured, in effect at September 30, 2006 (unaudited) (in thousands):

**Year Ended December 31:**

Remainder of 2006	\$ 20,461
2007	77,608
2008	75,570
2009	74,257
2010	73,940
Thereafter	389,472
<b>Total</b>	<b>\$ 711,308</b>

**Note 10. Subsequent Events*****Senior Notes***

In October 2006, Cricket issued \$750 million of unsecured senior notes due in 2014. The notes bear interest at the rate of 9.375% per year, payable semi-annually in cash in arrears beginning in May 2007. The notes are guaranteed on an unsecured senior basis by Leap and each of its existing and future domestic subsidiaries (excluding Cricket, which is the issuer of the notes, and ANB 1, LCW Wireless and Denali and their respective subsidiaries) that guarantee indebtedness for money borrowed of Leap, Cricket or any subsidiary guarantor. Currently, such guarantors include Leap and each of its direct or indirect wholly owned domestic subsidiaries, excluding Cricket. The notes and the guarantees are Leap's, Cricket's and the guarantors' general senior unsecured obligations and rank equally in right of payment with all of Leap's, Cricket's and the guarantors' existing and future unsubordinated unsecured indebtedness. The notes and the guarantees are effectively junior to Leap's, Cricket's and the guarantors' existing and future secured obligations, including those under the senior secured credit facility, to the extent of the value of the assets securing such obligations, as well as to future liabilities of Leap's and Cricket's subsidiaries that are not guarantors and of ANB 1, LCW Wireless and Denali and their respective subsidiaries. In addition, the notes and the guarantees are senior in right of payment to any of Leap's, Cricket's and the guarantors' future subordinated indebtedness.



Prior to November 1, 2009, Cricket may redeem up to 35% of the aggregate principal amount of the notes at a redemption price of 109.375% of the principal amount thereof, plus accrued and unpaid interest and additional interest, if any, thereon to the redemption date, from the net cash proceeds of specified equity offerings. Prior to November 1, 2010, Cricket may redeem the notes, in whole or in part, at a redemption price equal to 100% of the principal amount thereof plus the applicable premium and any accrued and unpaid interest. The applicable premium is calculated as the greater of (i) 1.0% of the principal amount of such notes and (ii) the excess of (a) the present value at such date of redemption of (1) the redemption price of such notes at November 1, 2010 plus (2) all remaining required interest payments due on such notes through November 1, 2010 (excluding accrued but unpaid

**Table of Contents**

interest to the date of redemption), computed using a discount rate equal to the Treasury Rate plus 50 basis points, over (b) the principal amount of such notes. The notes may be redeemed, in whole or in part, at any time on or after November 1, 2010, at a redemption price of 104.688% and 102.344% of the principal amount thereof if redeemed during the twelve months ending October 31, 2011 and 2012, respectively, or at 100% of the principal amount if redeemed during the twelve months ending October 31, 2013 or thereafter, plus accrued and unpaid interest. If a change of control (as defined in the indenture governing the notes) occurs, each holder of the notes may require Cricket to repurchase all of such holder's notes at a purchase price equal to 101% of the principal amount of the notes, plus accrued and unpaid interest.

The indenture governing the notes limits, among other things, Leap's, Cricket's and the guarantors' ability to: incur additional debt; create liens or other encumbrances; place limitations on distributions from restricted subsidiaries; pay dividends; make investments; prepay subordinated indebtedness or make other restricted payments; issue or sell capital stock of restricted subsidiaries; issue guarantees; sell assets; enter into transactions with its affiliates; and make acquisitions or merge or consolidate with another entity.

Affiliates of Highland Capital Management, L.P. (a beneficial stockholder of Leap and an affiliate of James D. Dondero, a director of Leap) purchased an aggregate of \$25.0 million principal amount of senior notes in the Company's offering.

***LCW Operations Senior Secured Credit Agreement***

In October 2006, LCW Operations entered into a senior secured credit agreement consisting of two term loans for \$40 million in the aggregate. The loans bear interest at LIBOR plus the applicable margin ranging from 2.70% to 6.33%. The obligations under the loans are guaranteed by LCW Wireless and LCW Wireless License, LLC, a wholly owned subsidiary of LCW Operations (and are non-recourse to Leap, Cricket and their other subsidiaries). Outstanding borrowings under the term loans must be repaid in varying quarterly installments starting in June 2008, with an aggregate final payment of \$24.5 million due in June 2011. Under the senior secured credit agreement, LCW Operations and the guarantors are subject to certain limitations, including limitations on their ability to: incur additional debt or sell assets; make certain investments; grant liens; pay dividends; and make certain other restricted payments. In addition, LCW Operations will be required to pay down the facilities under certain circumstances if it or the guarantors issue debt, sell assets or generate excess cash flow. The senior secured credit agreement requires that LCW Operations and the guarantors comply with financial covenants related to earnings before interest, taxes, depreciation and amortization, gross additions of subscribers, minimum cash and cash equivalents and maximum capital expenditures, among other things.

**Table of Contents**

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

*As used in this report, the terms we, our, ours, and us refer to Leap Wireless International, Inc., a Delaware corporation, and its wholly owned subsidiaries, unless the context suggests otherwise. Leap refers to Leap Wireless International, Inc., and Cricket refers to Cricket Communications, Inc. Unless otherwise specified, information relating to population and potential customers, or POPs, is based on 2006 population estimates provided by Claritas Inc.*

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

Except for the historical information contained herein, this report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements reflect management's current forecast of certain aspects of our future. You can identify most forward-looking statements by forward-looking words such as believe, think, may, could, will, estimate, continue, anticipate, intend, seek, plan, expect, or similar expressions in this report. Such statements are based on currently available operating, financial and competitive information and are subject to various risks, uncertainties and assumptions that could cause actual results to differ materially from those anticipated or implied in our forward-looking statements. Such risks, uncertainties and assumptions include, among other things:

our ability to attract and retain customers in an extremely competitive marketplace;

changes in economic conditions that could adversely affect the market for wireless services;

the impact of competitors' initiatives;

our ability to successfully implement product offerings and execute market expansion plans;

failure of the FCC to approve the transfers to our wholly owned subsidiary, Cricket Licensee (Reaction), Inc., or to Denali Spectrum License, LLC of the wireless licenses for which they were named winning bidders in Auction #66;

our ability to attract, motivate and retain an experienced workforce;

our ability to comply with the covenants in our senior secured credit agreement, indenture and any future credit agreement, indenture or similar instrument;

failure of our network or information technology systems to perform according to expectations; and

other factors detailed in Part II Item 1A. Risk Factors below.

All forward-looking statements in this report should be considered in the context of these risk factors. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. In light of these risks and uncertainties, the forward-looking events and circumstances discussed

in this report may not occur and actual results could differ materially from those anticipated or implied in the forward-looking statements. Accordingly, users of this report are cautioned not to place undue reliance on the forward-looking statements.

## Overview

*Our Business.* We are a communications carrier that offers digital wireless service in the United States of America under the Cricket® and Jump Mobile brands. Our Cricket service offers customers unlimited wireless service in their Cricket service area for a flat monthly rate without requiring a fixed-term contract or credit check, and our new Jump Mobile service offers customers a per-minute prepaid service. Cricket and Jump Mobile services are also offered in certain markets by Alaska Native Broadband 1 License, LLC, or ANB 1 License, and by LCW Wireless Operations, LLC, or LCW Operations, both of which are designated entities. Cricket owns an indirect 75% non-controlling interest in ANB 1 License through a 75% non-controlling interest in Alaska Native

**Table of Contents**

Broadband 1 LLC, or ANB 1, and an indirect 72% non-controlling interest in LCW Operations through a 72% non-controlling interest in LCW Wireless, LLC, or LCW Wireless. In May 2006, Cricket acquired a non-controlling interest in Denali Spectrum, LLC, or Denali, which participated in Auction #66 as a designated entity through its wholly owned subsidiary, Denali Spectrum License, LLC, or Denali License. Cricket currently holds an 82.5% non-controlling interest in Denali.

At September 30, 2006, Cricket and Jump Mobile services were offered in 21 states in the U.S.A. and had approximately 1,967,000 customers. As of September 30, 2006, we, ANB 1 License and LCW Wireless owned wireless licenses covering a total of 70.4 million potential customers, or POPs, in the aggregate, and our networks in our operating markets covered approximately 39.7 million POPs. In October 2006, LCW Wireless transferred its wireless licenses to LCW Wireless License, LLC, or LCW License, a wholly owned subsidiary of LCW Operations. We are currently building out and launching the new markets that we, ANB 1 License and LCW License have acquired or expect to acquire, and we anticipate that our combined network footprint will cover approximately 50 million POPs by mid 2007.

In addition, we participated as a bidder in Auction #66, both directly through a wholly owned subsidiary and as an investor in Denali License. In Auction #66, our wholly owned subsidiary was the winning bidder for 99 wireless licenses with an aggregate purchase price of \$710.2 million and covering 121.2 million POPs (adjusted to eliminate duplication among certain overlapping licenses won by it in Auction #66), and Denali License was the winning bidder for one wireless license with a net purchase price of \$274.1 million and covering 59.3 million POPs (which includes markets covering 5.7 million POPs which overlap with certain licenses won by our wholly owned subsidiary in Auction #66). We anticipate that these licenses will provide the opportunity to substantially enhance our coverage area and allow us and Denali License to launch Cricket service in numerous new markets in multiple construction phases over time. Moreover, the licenses for which we were the winning bidder, together with licenses we currently own, provide 20MHz coverage and the opportunity to offer enhanced data services in almost all markets that we currently operate or are building out. If Denali License were to make available to us certain spectrum for which it was the winning bidder in Auction #66, we would have 20MHz coverage in all markets in which we currently operate or are building out. The post-Auction grants of these licenses remain subject to FCC approval, and we cannot assure you that the FCC will award these licenses to us or Denali License. Assuming the FCC approves the post-Auction grants of these licenses, our spectrum portfolio, together with that of ANB 1 License, LCW License and Denali License (all of which entities or their affiliates currently offer or are expected to offer Cricket service), will consist of approximately 181.7 million POPs (adjusted to eliminate duplication of overlapping licenses among these entities).

Our premium Cricket service plan, which is our most popular service plan, offers customers unlimited local and domestic long distance service from their Cricket service area combined with unlimited use of multiple calling features and messaging services, generally for a flat rate of \$45 per month. We also offer a basic service plan which allows customers to make unlimited calls within their Cricket service area and receive unlimited calls from any area, generally for \$35 per month, and an intermediate service plan which also includes unlimited long distance service, generally for \$40 per month. In 2005, we launched our first per-minute prepaid service, Jump Mobile, to bring Cricket's attractive value proposition to customers who prefer active control over their wireless usage and to better target the urban youth market. During the last two years, we have added instant messaging, multimedia (picture) messaging, games and our Travel Time<sup>®</sup> roaming option to our product portfolio. In 2006, we broadened and expect to continue to broaden our data product and service offerings to better meet the needs of our customers.

We believe that our business model can be expanded successfully into adjacent and new markets because we offer a differentiated service and attractive value proposition to our customers at costs significantly lower than most of our competitors. For example:

In 2005, we acquired four wireless licenses in the FCC's Auction #58 covering 11.3 million POPs and ANB 1 License acquired nine licenses covering 10.2 million POPs.

In August 2005, we launched service in our newly acquired Fresno, California market to form a cluster with our existing Modesto and Visalia, California markets, which doubled our Central Valley network footprint to 2.4 million POPs.

**Table of Contents**

In March 2006, we entered into an agreement with a debtor-in-possession for the purchase of 13 wireless licenses in North Carolina and South Carolina for an aggregate purchase price of \$31.8 million. Completion of this transaction is subject to customary closing conditions, including the receipt of certain FCC approvals and orders which have already been issued but which have not yet become final.

In July 2006, we acquired a 72% non-controlling membership interest in LCW Wireless, which held a license for the Portland, Oregon market and to which we contributed, among other things, our existing Eugene and Salem, Oregon markets to create a new Oregon cluster of licenses covering 3.2 million POPs.

In August 2006, we exchanged our wireless license in Grand Rapids, Michigan for a wireless license in Rochester, New York to form a new market cluster with our existing Buffalo and Syracuse markets in upstate New York. These three licenses cover 3.1 million POPs.

In September 2006, our wholly owned subsidiary was the winning bidder for 99 wireless licenses covering 121.2 million POPs (adjusted to eliminate duplication among certain overlapping licenses won by it in Auction #66), and Denali License was the winning bidder for one wireless license covering 59.3 million POPs (which includes markets covering 5.7 million POPs which overlap with certain licenses won by our wholly owned subsidiary in Auction #66). The post Auction grants of these licenses remain subject to FCC approval, and we cannot assure you that the FCC will award these licenses to us or Denali License. The use of any licenses that we or Denali License acquire in Auction #66 may be affected by the requirements to clear the spectrum of existing U.S. government and other private sector wireless operations, some of which are permitted to continue for several years.

We, ANB 1 License and LCW Operations have launched 12 markets in 2006, and we currently expect to launch two additional markets by the end of 2006.

We continue to seek additional opportunities to enhance our current market clusters and expand into new geographic markets by participating in FCC spectrum auctions (including the recently concluded Auction #66), by acquiring spectrum and related assets from third parties, or by participating in new partnerships or joint ventures.

Any large scale construction projects for the build-out of our new markets will require significant capital expenditures and may suffer cost overruns. In addition, we will experience higher operating expenses as we build out and after we launch our service in new markets. Any significant capital expenditures or increased operating expenses, including in connection with the build-out and launch of markets for any licenses that we and Denali License acquire in Auction #66, would negatively impact our earnings, operating income before depreciation and amortization, or OIBDA, and free cash flow for the periods in which we incur such capital expenditures and increased operating expenses.

Of the wireless licenses for which we and Denali License were named the winning bidders in Auction #66, licenses covering approximately 64.3 million POPs constitute additional overlay spectrum where we, ANB 1 License or LCW License already have existing licenses. Of the Auction #66 licenses for which we and Denali License were named the winning bidders that are located in new markets, we expect that we and Denali License (which we expect will offer Cricket service) will build-out markets located within these licenses for Cricket service in multiple construction phases over time. We currently expect that the first phase of construction for Auction #66 licenses that we and Denali License intend to build out will include networks covering approximately 24 million POPs. We currently expect that the aggregate capital expenditures for this first phase of construction will be less than \$28.00 per covered POP. We also currently expect that the build-outs for this first phase of construction will commence in 2007 and will be substantially completed by the end of 2009. We generally build-out our Cricket networks in local population centers

of metropolitan communities serving the areas where our customers live, work and play. Some of the Auction #66 licenses for which we and Denali License were named the winning bidders include large regional areas covering both rural and metropolitan communities. Based on our preliminary analysis of the Auction #66 licenses for which we and Denali License were named the winning bidders that are located in new markets, we believe that a significant portion of the POPs included within such new licenses may not be well-suited for Cricket service. Therefore, among other things, we may seek to partner with others, sell spectrum or pursue alternative products or services to utilize or benefit from the spectrum not otherwise used for Cricket service.



**Table of Contents**

Our principal sources of liquidity are our existing unrestricted cash, cash equivalents and short-term investments, cash generated from operations, and cash available from borrowings under our \$200 million revolving credit facility (which was undrawn at September 30, 2006). From time to time, we may also generate additional liquidity through the sale of assets that are not material to or are not required for the ongoing operation of our business. See Liquidity and Capital Resources below.

**Results of Operations****Operating Items**

The following tables summarize operating data for the Company's consolidated operations (in thousands, except percentages):

	Three Months Ended September 30,					
	2006	% of 2006 Service Revenues	2005	% of 2005 Service Revenues	Change from Prior Year	
					Dollars	Percent
Revenues:						
Service revenues	\$ 249,081		\$ 193,675		\$ 55,406	28.6%
Equipment revenues	38,445		36,852		1,593	4.3%
Total revenues	287,526		230,527		56,999	24.7%
Operating expenses:						
Cost of service (exclusive of items shown separately below)	70,722	28.4%	50,304	26.0%	20,418	40.6%
Cost of equipment	68,624	27.6%	49,576	25.6%	19,048	38.4%
Selling and marketing	42,948	17.2%	25,535	13.2%	17,413	68.2%
General and administrative	49,110	19.7%	41,306	21.3%	7,804	18.9%
Depreciation and amortization	56,409	22.6%	49,076	25.3%	7,333	14.9%
Impairment of indefinite-lived intangible assets	4,701	1.9%	689	0.4%	4,012	582.3%
Total operating expenses	292,514	117.4%	216,486	111.8%	76,028	35.1%
Gain on sale of wireless licenses and operating assets	21,990	8.8%	14,593	7.5%	7,397	50.7%
Operating income	\$ 17,002	6.8%	\$ 28,634	14.8%	\$ (11,632)	(40.6)%

**Table of Contents**

	<b>Nine Months Ended September 30,</b>					
	<b>2006</b>	<b>% of 2006 Service Revenues</b>	<b>2005</b>	<b>% of 2005 Service Revenues</b>	<b>Change from Prior Year</b>	
					<b>Dollars</b>	<b>Percent</b>
<b>Revenues:</b>						
Service revenues	\$ 695,706		\$ 569,360		\$ 126,346	22.2%
Equipment revenues	126,361		116,366		9,995	8.6%
<b>Total revenues</b>	<b>822,067</b>		<b>685,726</b>		<b>136,341</b>	<b>19.9%</b>
<b>Operating expenses:</b>						
Cost of service (exclusive of items shown separately below)	186,181	26.8%	150,109	26.4%	36,072	24.0%
Cost of equipment	179,591	25.8%	141,553	24.9%	38,038	26.9%
Selling and marketing	107,992	15.5%	73,340	12.9%	34,652	47.2%
General and administrative	145,268	20.9%	119,764	21.0%	25,504	21.3%
Depreciation and amortization	163,781	23.5%	144,461	25.4%	19,320	13.4%
Impairment of indefinite-lived intangible assets	7,912	1.1%	12,043	2.1%	(4,131)	(34.3)%
<b>Total operating expenses</b>	<b>790,725</b>	<b>113.7%</b>	<b>641,270</b>	<b>112.6%</b>	<b>149,155</b>	<b>23.3%</b>
Gain on sale of wireless licenses and operating assets	21,990	3.2%	14,593	2.6%	7,397	50.7%
<b>Operating income</b>	<b>\$ 53,332</b>	<b>7.7%</b>	<b>\$ 59,049</b>	<b>10.4%</b>	<b>\$ (5,717)</b>	<b>(9.7)%</b>

The following tables summarize customer activity:

	<b>2006</b>	<b>2005</b>	<b>Change</b>	
			<b>Amount</b>	<b>Percent</b>
<b><u>For the Three Months Ended September 30:</u></b>				
Gross customer additions	405,178	233,699	171,479	73.4%
Net customer additions	161,688	23,298	138,390	594.0%
Weighted average number of customers	1,870,204	1,605,222	264,982	16.5%
<b><u>As of September 30:</u></b>				
Total customers	1,967,369	1,622,526	344,843	21.3%
	<b>2006</b>	<b>2005</b>	<b>Change</b>	
			<b>Amount</b>	<b>Percent</b>
<b><u>For the Nine Months Ended September 30:</u></b>				
Gross customer additions	936,581	626,454	310,127	49.5%

Net customer additions	329,780	71,609	258,171	360.5%
Weighted average number of customers	1,792,928	1,601,706	191,222	11.9%

***Three and Nine Months Ended September 30, 2006 Compared to Three and Nine Months Ended September 30, 2005***

Service revenues increased \$55.4 million, or 28.6%, for the three months ended September 30, 2006 compared to the corresponding period of the prior year. This increase resulted from the 16.5% increase in average total customers and a 10.4% increase in average monthly revenues per customer. The increase in average revenues per customer was due primarily to the continued increase in customer adoption of our higher-end service plans.

Service revenues increased \$126.3 million, or 22.2%, for the nine months ended September 30, 2006 compared to the corresponding period of the prior year. This increase resulted from the 11.9% increase in average total customers and a 9.1% increase in average monthly revenues per customer. The increase in average revenues per customer was due primarily to the continued increase in customer adoption of our higher-end service plans.

Equipment revenues increased \$1.6 million, or 4.3%, for the three months ended September 30, 2006 compared to the corresponding period of the prior year. An increase of 63.6% in handset sales volume was largely

**Table of Contents**

offset by lower net revenue per handset sold as a result of bundling the first month of service with the initial handset price and eliminating activation fees for new customers purchasing equipment.

Equipment revenues increased \$10.0 million, or 8.6%, for the nine months ended September 30, 2006 compared to the corresponding period of the prior year. An increase of 44.5% in handset sales volume was largely offset by lower net revenue per handset sold as a result of bundling the first month of service with the initial handset price and eliminating activation fees for new customers purchasing equipment.

Cost of service increased \$20.4 million, or 40.6%, for the three months ended September 30, 2006 compared to the corresponding period of the prior year. As a percentage of service revenues, cost of service increased to 28.4% from 26.0% in the prior year period. Network infrastructure costs increased by 2.1% of service revenues due primarily to lease costs and network transport costs associated with our new markets. Variable product costs increased by 0.4% of service revenues due to increased customer usage of our value-added services.

Cost of service increased \$36.1 million, or 24.0%, for the nine months ended September 30, 2006 compared to the corresponding period of the prior year. As a percentage of service revenues, cost of service increased to 26.8% from 26.4% in the prior year period. Variable product costs increased by 0.5% of service revenues due to increased customer usage of our value-added services.

Cost of equipment increased \$19.0 million, or 38.4%, for the three months ended September 30, 2006 compared to the corresponding period of the prior year. This increase was primarily attributable to the 63.6% increase in handset sales volumes, partially offset by reductions in costs to support our handset replacement programs for existing customers.

Cost of equipment increased \$38.0 million, or 26.9%, for the nine months ended September 30, 2006 compared to the corresponding period of the prior year. This increase was primarily attributable to the 44.5% increase in handset sales volumes, partially offset by reductions in costs to support our handset replacement programs for existing customers.

Selling and marketing expenses increased \$17.4 million, or 68.2%, for the three months ended September 30, 2006 compared to the corresponding period of the prior year. As a percentage of service revenues, such expenses increased to 17.2% from 13.2% in the prior year period. This increase was primarily due to increases in media and advertising costs and labor and related costs of 2.6% and 0.7% of service revenues, respectively, both of which were attributable to our new market launches. In addition, facility and other costs increased by 0.7% of service revenues due to the increase in infrastructure to support our new market launches.

Selling and marketing expenses increased \$34.7 million, or 47.2%, for the nine months ended September 30, 2006 compared to the corresponding period of the prior year. As a percentage of service revenues, such expenses increased to 15.5% from 12.9% in the prior year period. This increase was primarily due to increases in media and advertising costs and labor and related costs of 1.8% and 0.5% of service revenues, respectively, both of which were attributable to our new market launches.

General and administrative expenses increased \$7.8 million, or 18.9%, for the three months ended September 30, 2006 compared to the corresponding period of the prior year. As a percentage of service revenues, such expenses decreased to 19.7% from 21.3% in the prior year period. Customer care expenses decreased by 2.1% of service revenues due to decreases in call center and other customer care-related program costs. Professional services fees decreased by 1.1% of service revenues due largely to incremental costs incurred in the prior year period related to Sarbanes-Oxley Section 404 compliance, and other expenses decreased by 0.8% of service revenues due to the increase in service revenues and consequent benefits in scale. Partially offsetting these decreases was an increase in labor and related costs of 2.6% of service revenues due primarily to new employee additions necessary to support our growth and the adoption of SFAS 123R in 2006.

General and administrative expenses increased \$25.5 million, or 21.3%, for the nine months ended September 30, 2006 compared to the corresponding period of the prior year. As a percentage of service revenues, such expenses decreased to 20.9% from 21.0% in the prior year period. Customer care expenses decreased by 1.7% of service revenues due to reductions in call center and other customer care-related program costs, and professional services fees and other expenses decreased by 0.6% of service revenues in the aggregate due to the increase in

**Table of Contents**

service revenues and consequent benefits in scale. Offsetting these decreases was an increase in labor and related costs of 2.2% of service revenues due primarily to new employee additions necessary to support our growth and the adoption of SFAS 123R in 2006.

Depreciation and amortization expense increased \$7.3 million, or 14.9%, and \$19.3 million, or 13.4%, for the three and nine months ended September 30, 2006, respectively, compared to the corresponding periods of the prior year. The increases in the dollar amounts of depreciation and amortization expense were due primarily to the build-out of our new markets and the upgrade of network assets in our other markets. As a percentage of service revenues, such expenses decreased slightly as compared to prior year periods.

As a result of our annual impairment tests of wireless licenses, we recorded impairment charges of \$4.7 million and \$0.7 million during the three months ended September 30, 2006 and 2005, respectively, to reduce the carrying values of certain non-operating wireless licenses to their estimated fair market values. In addition, during the second quarters of 2006 and 2005, we recorded impairment charges of \$3.2 million and \$11.4 million, respectively, in connection with agreements to sell certain non-operating wireless licenses. We adjusted the carrying values of those licenses to their estimated fair values, which were based on the agreed upon sales prices.

During the three months ended September 30, 2006, we completed the sale of our wireless licenses and operating assets in the Toledo and Sandusky, Ohio markets in exchange for \$28.0 million and an equity interest in LCW Wireless, resulting in a gain of \$21.5 million. In addition, we completed the exchange of our wireless license in Grand Rapids, Michigan for a wireless license in Rochester, New York, resulting in a gain of \$0.4 million during the same period. During the three months ended September 30, 2005, we completed the sale of 23 wireless licenses and substantially all of our operating assets in our Michigan markets for \$102.5 million, resulting in a gain of \$14.6 million.

**Non-Operating Items**

The following tables summarize non-operating data for the Company's consolidated operations (in thousands).

	<b>Three Months Ended September 30,</b>		
	<b>2006</b>	<b>2005</b>	<b>Change</b>
Interest income	\$ 5,491	\$ 2,991	\$ 2,500
Interest expense	(15,753)	(6,679)	(9,074)
Minority interests in income of consolidated subsidiaries	(138)		(138)
Other income (expense), net	272	2,352	(2,080)
Income tax benefit (expense)	3,105	(10,901)	14,006

	<b>Nine Months Ended September 30,</b>		
	<b>2006</b>	<b>2005</b>	<b>Change</b>
Interest income	\$ 15,218	\$ 6,070	\$ 9,148
Interest expense	(31,606)	(23,368)	(8,238)
Minority interests in income of consolidated subsidiaries	(347)		(347)
Other income (expense), net	(5,112)	1,027	(6,139)
Income tax benefit (expense)	3,105	(17,762)	20,867

***Three and Nine Months Ended September 30, 2006 Compared to Three and Nine Months Ended September 30, 2005***

Interest income increased \$2.5 million and \$9.1 million for the three and nine months ended September 30, 2006, respectively, compared to the corresponding periods of the prior year. These increases were primarily due to increases in the average cash and cash equivalents and investment balances resulting primarily from increased cash flows from operations and financing activities.

Interest expense increased \$9.1 million and \$8.2 million for the three and nine months ended September 30, 2006, respectively, compared to the corresponding periods of the prior year. The increases in interest expense

**Table of Contents**

resulted primarily from the increase in the amount of the term loan under our amended and restated senior secured credit agreement (see Liquidity and Capital Resources below), partially offset by the capitalization of \$3.4 million and \$12.3 million of interest during the three and nine months ended September 30, 2006, respectively. We capitalize interest costs associated with our wireless licenses and property and equipment during the build-out of new markets. The amount of such capitalized interest depends on the carrying values of the licenses and property and equipment involved in those markets and the duration of the build-out. We expect capitalized interest to continue to be significant during the build-out of our planned new markets in the fourth quarter of 2006. At September 30, 2006, the effective interest rate on our \$900 million term loan was 7.8%, including the effect of interest rate swaps described below. We expect that interest expense will continue to increase due to our new unsecured senior notes. See Liquidity and Capital Resources below.

Other income, net of other expenses, decreased by \$2.1 million and \$6.1 million for the three and nine months ended September 30, 2006, respectively, compared to the corresponding periods of the prior year. During the second quarter of 2006, we wrote off \$5.6 million of unamortized deferred debt issuance costs related to our previous credit agreement as a result of the repayment of the term loans and replacement of the revolving credit facility under the previous credit agreement.

During the three and nine months ended September 30, 2006, we recorded an income tax benefit of \$3.1 million compared to income tax expense of \$10.9 million and \$17.8 million for the three and nine months ended September 30, 2005, respectively. Ordinary income tax expense for the full year 2006, which excludes the effect of unusual or infrequently occurring (or discrete) items, is projected to consist primarily of the deferred tax effect of the amortization of wireless licenses and tax goodwill for income tax purposes. We do not expect to release fresh-start related valuation allowances in fiscal 2006. Our estimated annual effective tax rate for 2006 is negative. Therefore, no income tax expense or benefit has been recorded relative to ordinary income or loss during the first three quarters of 2006, since the application of the negative annual tax rate to year-to-date pre-tax ordinary income would result in a tax benefit in these periods that would be reversed in a subsequent quarter. However, several discrete items resulted in an income tax benefit in the third quarter of 2006. In conjunction with the July 2006 contribution of the assets associated with our Eugene and Salem, Oregon markets to LCW Wireless, we transferred wireless licenses with a \$3.3 million deferred tax liability and other assets with a \$1.8 million deferred tax asset. As a result of the transfer, the net \$1.5 million deferred tax liability has been reported as a book-tax basis difference in our investment in LCW Wireless. Because this deferred tax liability will not reverse until some indefinite future period and cannot be considered a source of taxable income to support the realization of our deferred tax assets, it has been recorded as a discrete income tax expense in the third quarter. The \$3.3 million reduction in the deferred tax liability on our wireless licenses contributed to LCW Wireless has been recorded as a discrete income tax benefit in the third quarter of 2006. In addition, the impairment charge on certain of our wireless licenses resulted in a \$1.4 million reduction in our wireless license deferred tax liability that has been recorded as a discrete income tax benefit in the third quarter. We expect to pay only minimal cash taxes for fiscal 2006.

During the three and nine months ended September 30, 2005, we recorded income tax expense at an effective tax rate of 39.9% and 41.5%, respectively. Despite the fact that we recorded a full valuation allowance on our deferred tax assets, we recognized income tax expense for the three and nine months ended September 30, 2005 because the release of the valuation allowance associated with the reversal of deferred tax assets recorded in fresh-start reporting is recorded as a reduction of goodwill rather than as a reduction of income tax expense. The effective tax rates for the three and nine months ended September 30, 2005 were higher than the statutory tax rate due primarily to permanent items not deductible for tax purposes.

Net income for the three months ended September 30, 2006 was \$10.0 million, or \$0.16 per diluted share, compared to net income of \$16.4 million, or \$0.27 per diluted share, for the three months ended September 30, 2005. Absent the \$21.5 million net gain we recognized as a result of the sale of wireless licenses and operating assets in Toledo and



Sandusky, Ohio in July 2006, we would have recorded a net loss of approximately \$11.6 million for the three months ended September 30, 2006. Net income for the nine months ended September 30, 2006 was \$35.2 million, or \$0.57 per diluted share, compared to net income of \$25.0 million, or \$0.41 per diluted share, for the nine months ended September 30, 2005. We expect net income to decrease in the fourth quarter of fiscal 2006, and we expect to realize a net loss for the full year 2006, due mainly to our new market launches and expenses associated with our new debt.

**Table of Contents*****Performance Measures***

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

ARPU is service revenue divided by the weighted-average number of customers, divided by the number of months during the period being measured. Management uses ARPU to identify average revenue per customer, to track changes in average customer revenues over time, to help evaluate how changes in our business, including changes in our service offerings and fees, affect average revenue per customer, and to forecast future service revenue. In addition, ARPU provides management with a useful measure to compare our subscriber revenue to that of other wireless communications providers. We believe investors use ARPU primarily as a tool to track changes in our average revenue per customer and to compare our per customer service revenues to those of other wireless communications providers. Other companies may calculate this measure differently.

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

CCU is cost of service and general and administrative costs (excluding applicable share-based compensation expense included in cost of service and general and administrative expense) plus net loss on equipment transactions unrelated to initial customer acquisition (which includes the gain or loss on sale of handsets to existing customers and costs associated with handset replacements and repairs (other than warranty costs which are the responsibility of the handset manufacturers)), divided by the weighted-average number of customers, divided by the number of months during the period being measured. CCU does not include any depreciation and amortization expense. Management uses CCU as a tool to evaluate the non-selling cash expenses associated with ongoing business operations on a per customer basis,

to track changes in these non-selling cash costs over time, and to help evaluate how changes in our business operations affect non-selling cash costs per customer. In addition, CCU provides management with a useful measure to compare our non-selling cash costs per customer with those of other wireless communications providers. We believe investors use CCU primarily as a tool to track changes in our non-selling

**Table of Contents**

cash costs over time and to compare our non-selling cash costs to those of other wireless communications providers. Other companies may calculate this measure differently.

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

The following table shows metric information for the three months ended September 30, 2006 and 2005:

	<b>Three Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
ARPU	\$ 44.39	\$ 40.22
CPGA	\$ 176	\$ 142
CCU	\$ 20.74	\$ 19.52
Churn	4.3%	4.4%

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

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

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

	<b>Three Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
Selling and marketing expense	\$ 42,948	\$ 25,535
Less share-based compensation expense included in selling and marketing expense	(637)	(203)
Plus cost of equipment	68,624	49,576
Less equipment revenue	(38,445)	(36,852)
Less net loss on equipment transactions unrelated to initial customer acquisition	(983)	(4,917)
Total costs used in the calculation of CPGA	\$ 71,507	\$ 33,139
Gross customer additions	405,178	233,699

CPGA

\$ 176 \$ 142

**Table of Contents**

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

	<b>Three Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
Cost of service	\$ 70,722	\$ 50,304
Plus general and administrative expense	49,110	41,306
Less share-based compensation expense included in cost of service and general and administrative expense	(4,426)	(2,518)
Plus net loss on equipment transactions unrelated to initial customer acquisition	983	4,917
Total costs used in the calculation of CCU	\$ 116,389	\$ 94,009
Weighted-average number of customers	1,870,204	1,605,222
CCU	\$ 20.74	\$ 19.52

**Liquidity and Capital Resources***Overview*

Our principal sources of liquidity are our existing unrestricted cash, cash equivalents and short-term investments, cash generated from operations and cash available from borrowings under our \$200 million revolving credit facility (which was undrawn at September 30, 2006). From time to time, we may also generate additional liquidity through the sale of assets that are not material to or are not required for the ongoing operation of our business.

At September 30, 2006, we had a total of \$290.7 million in unrestricted cash, cash equivalents and short-term investments. This amount included the effects of the consummation of the following transactions:

In June 2006, we replaced our previous \$710 million senior secured credit facility with a new amended and restated senior secured credit facility consisting of a \$900 million term loan and a \$200 million revolving credit facility. The replacement term loan generated proceeds of approximately \$307 million, after repayment of the principal balances of the old term loans and prior to the payment of fees and expenses. See Senior Secured Credit Facilities below.

In July 2006, we and Denali License paid to the FCC \$255 million and \$50 million, respectively, as bidding deposits for Auction #66.

At October 31, 2006, we had in excess of \$550 million in unrestricted cash, cash equivalents and short-term investments. This amount included the effects of the consummation of the following transactions:

In October 2006, we physically settled 6,440,000 shares of Leap common stock pursuant to our forward sale agreements and received aggregate cash proceeds of \$260 million (before expenses) from such physical settlements. See Forward Sale Agreements below.

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

In October 2006, we borrowed \$570 million under our \$850 million unsecured bridge loan facility to finance a portion of the remaining amounts owed by us and Denali License to the FCC for Auction #66 licenses.

In October 2006, we and Denali License paid to the FCC \$455.2 million and \$224.1 million, respectively, in satisfaction of the remaining amounts owed by us and Denali License to the FCC for Auction #66 licenses.

In October 2006, we issued \$750 million of 9.375% senior notes due 2014, and we used a portion of the approximately \$739 million of cash proceeds (after commission and before expenses) from the sale to repay our outstanding obligations, including accrued interest, under our bridge loan facility. Upon repayment of our outstanding indebtedness, the bridge loan facility was terminated. See Senior Notes below.

## **Table of Contents**

We believe that our existing unrestricted cash, cash equivalents and short-term investments at October 31, 2006, the liquidity under our revolving credit facility and our anticipated cash flows from operations will be sufficient to meet the projected operating and capital requirements for our existing and currently expected business, including (1) the build-out and launch of the wireless licenses that we acquired prior to Auction #66 and the acquisition, build-out and launch of the wireless licenses that we have agreed to acquire in North and South Carolina, (2) the investments we have agreed to make in ANB 1 License and LCW Wireless to support the build-out and launch of the licenses each of them acquired prior to Auction #66, and (3) the projected operating and capital requirements for the first phase of construction for Auction #66 licenses that we and Denali License intend to build out, with such first phase expected to include the construction of networks covering approximately 24 million POPs. If we expand the scope of the initial phase of our planned Auction #66 build-out, we may need to raise additional capital.

In addition, depending on the timing and scope of further Auction #66 license build-outs, we may need to raise significant additional capital in the future to finance the build-out and initial operating costs associated with Leap's and Denali License's Auction #66 licenses that are not included in the first phase of construction. However, other than network design and other build-out planning and preparation activities, we generally do not intend to commence the build-out of any individual license until we have sufficient funds available to us to pay for all of the related build-out and initial operating costs associated with such license.

### ***Cash Flows***

Net cash provided by operating activities was \$223.0 million during the nine months ended September 30, 2006 compared to \$191.2 million during the nine months ended September 30, 2005. This increase was primarily attributable to an increase in accounts payable related to the build-out of our new markets.

Net cash used in investing activities was \$583.2 million during the nine months ended September 30, 2006 compared to \$340.3 million during the nine months ended September 30, 2005. This increase was due primarily to an increase in purchases of property and equipment for the build-out of our new markets.

Net cash provided by financing activities was \$300.7 million during the nine months ended September 30, 2006 compared to \$176.3 million during the nine months ended September 30, 2005. This increase was due primarily to the net proceeds from the \$900 million term loan under our amended and restated senior secured credit agreement, or the Credit Agreement.

### ***Senior Secured Credit Facilities***

Long-term debt as of September 30, 2006 consisted of our Credit Agreement, which included a \$900 million term loan and an undrawn \$200 million revolving credit facility available until June 2011. Under our Credit Agreement, the term loan bears interest at the London Interbank Offered Rate (LIBOR) plus 2.75 percent, with interest periods of one, two, three or six months, or at the bank base rate plus 1.75 percent, as selected by Cricket, with the rate subject to adjustment based on Leap's corporate family debt rating. Outstanding borrowings under the term loan must be repaid in 24 quarterly payments of \$2.25 million each, commencing September 30, 2006, followed by four quarterly payments of \$211.5 million each, commencing September 30, 2012.

The maturity date for outstanding borrowings under the revolving credit facility is June 16, 2011. The commitment of the lenders under the revolving credit facility may be reduced in the event mandatory prepayments are required under the Credit Agreement. The commitment fee on the revolving credit facility is payable quarterly at a rate of between 0.25 and 0.50 percent per annum, depending on our consolidated senior secured leverage ratio. Borrowings under the revolving credit facility would currently accrue interest at LIBOR plus 2.75 percent or the bank base rate plus



1.75 percent, as selected by Cricket, with the rate subject to adjustment based on our consolidated senior secured leverage ratio.

The facilities under the Credit Agreement are guaranteed by Leap and all of its direct and indirect domestic subsidiaries (excluding Cricket, which is the primary obligor, and ANB 1, LCW Wireless and Denali and their respective subsidiaries) and are secured by substantially all of the present and future personal property and owned real property of Leap, Cricket and such direct and indirect domestic subsidiaries. Under the Credit Agreement, we

**Table of Contents**

are subject to certain limitations, including limitations on our ability to: incur additional debt or sell assets, with restrictions on the use of proceeds; make certain investments and acquisitions; grant liens; and pay dividends and make certain other restricted payments. In addition, we will be required to pay down the facilities under certain circumstances if we issue debt, sell assets or property, receive certain extraordinary receipts or generate excess cash flow (as defined in the Credit Agreement). We are also subject to a financial covenant with respect to a maximum consolidated senior secured leverage ratio and, if a revolving credit loan or uncollateralized letter of credit is outstanding, with respect to a minimum consolidated interest coverage ratio, a maximum consolidated leverage ratio and a minimum consolidated fixed charge ratio. In addition to investments in joint ventures relating to Auction #66, the Credit Agreement allows us to invest up to \$325 million in ANB 1 and ANB 1 License, up to \$85 million in LCW Wireless and its subsidiaries, and up to \$150 million plus an amount equal to an available cash flow basket in other joint ventures, and allows us to provide limited guarantees for the benefit of ANB 1, LCW Wireless and other joint ventures.

Affiliates of Highland Capital Management, L.P. (a beneficial stockholder of Leap and an affiliate of James D. Dondero, a director of Leap) participated in the syndication of the Credit Agreement in initial amounts equal to \$225 million of the term loan and \$40 million of the revolving credit facility, and Highland Capital Management received a syndication fee of \$300,000 in connection with their participation.

At September 30, 2006, the effective interest rate on our term loan under the Credit Agreement was 7.8%, including the effect of interest rate swaps, and the outstanding indebtedness was \$897.8 million. The terms of the Credit Agreement require us to enter into interest rate swap agreements in a sufficient amount so that at least 50% of our outstanding indebtedness for borrowed money bears interest at a fixed rate by December 31, 2006. We have entered into interest rate swap agreements with respect to \$355 million of our debt. These swap agreements effectively fix the interest rate on \$250 million of our indebtedness at 6.7% and \$105 million of our indebtedness at 6.8% through June 2007 and 2009, respectively. The fair value of the swap agreements at September 30, 2006 and 2005 was \$3.8 million and \$2.0 million, respectively, and was recorded in other assets in the consolidated balance sheet.

In October 2006, LCW Operations entered into a senior secured credit agreement consisting of two term loans for \$40 million in the aggregate. The loans bear interest at LIBOR plus the applicable margin ranging from 2.70% to 6.33%. The obligations under the loans are guaranteed by LCW Wireless and LCW License (and are non-recourse to Leap, Cricket and their other subsidiaries). Outstanding borrowings under the term loans must be repaid in varying quarterly installments starting in June 2008, with an aggregate final payment of \$24.5 million due in June 2011. Under the senior secured credit agreement, LCW Operations and the guarantors are subject to certain limitations, including limitations on their ability to: incur additional debt or sell assets; make certain investments; grant liens; pay dividends; and make certain other restricted payments. In addition, LCW Operations will be required to pay down the facilities under certain circumstances if it or the guarantors issue debt, sell assets or generate excess cash flow. The senior secured credit agreement requires that LCW Operations and the guarantors comply with financial covenants related to earnings before interest, taxes, depreciation and amortization, gross additions of subscribers, minimum cash and cash equivalents and maximum capital expenditures, among other things.

***Forward Sale Agreements***

In August 2006, in connection with a public offering of Leap common stock, Leap entered into forward sale agreements for the sale of an aggregate of 6,440,000 shares of its common stock, including an amount equal to the underwriters' over-allotment option in the public offering (which was fully exercised). The initial forward sale price was \$40.11 per share, which was equivalent to the public offering price less the underwriting discount, and was subject to daily adjustment based on a floating interest factor equal to the federal funds rate, less a spread of 1.0%. In October 2006, Leap issued 6,440,000 shares of its common stock to physically settle its forward sale agreements and received aggregate cash proceeds of \$260.0 million (before expenses) from such physical settlements. Upon such full

settlement, the forward sale agreements were fully performed.

**Table of Contents*****Senior Notes***

In October 2006, Cricket issued \$750 million of unsecured senior notes due in 2014. The notes bear interest at the rate of 9.375% per year, payable semi-annually in cash in arrears beginning in May 2007. The notes are guaranteed on an unsecured senior basis by Leap and each of its existing and future domestic subsidiaries (excluding Cricket, which is the issuer of the notes, and ANB 1, LCW Wireless and Denali and their respective subsidiaries) that guarantees indebtedness for money borrowed of Leap, Cricket or any subsidiary guarantor. Currently, such guarantors include Leap and each of its direct or indirect wholly owned domestic subsidiaries, excluding Cricket. The notes and the guarantees are Leap's, Cricket's and the guarantors' general senior unsecured obligations and rank equally in right of payment with all of Leap's, Cricket's and the guarantors' existing and future unsubordinated unsecured indebtedness. The notes and the guarantees are effectively junior to Leap's, Cricket's and the guarantors' existing and future secured obligations, including those under the Credit Agreement, to the extent of the value of the assets securing such obligations, as well as to future liabilities of Leap's and Cricket's subsidiaries that are not guarantors and of ANB 1, LCW Wireless and Denali and their respective subsidiaries. In addition, the notes and the guarantees are senior in right of payment to any of Leap's, Cricket's and the guarantors' future subordinated indebtedness.

Prior to November 1, 2009, Cricket may redeem up to 35% of the aggregate principal amount of the notes at a redemption price of 109.375% of the principal amount thereof, plus accrued and unpaid interest and additional interest, if any, thereon to the redemption date, from the net cash proceeds of specified equity offerings. Prior to November 1, 2010, Cricket may redeem the notes, in whole or in part, at a redemption price equal to 100% of the principal amount thereof plus the applicable premium and any accrued and unpaid interest. The applicable premium is calculated as the greater of (i) 1.0% of the principal amount of such notes and (ii) the excess of (a) the present value at such date of redemption of (1) the redemption price of such notes at November 1, 2010 plus (2) all remaining required interest payments due on such notes through November 1, 2010 (excluding accrued but unpaid interest to the date of redemption), computed using a discount rate equal to the Treasury Rate plus 50 basis points, over (b) the principal amount of such notes. The notes may be redeemed, in whole or in part, at any time on or after November 1, 2010, at a redemption price of 104.688% and 102.344% of the principal amount thereof if redeemed during the twelve months ending October 31, 2011 and 2012, respectively, or at 100% of the principal amount thereof if redeemed during the twelve months ending October 31, 2013 or thereafter, plus accrued and unpaid interest. If a change of control (as defined in the indenture governing the notes, or the Indenture) occurs, each holder of the notes may require Cricket to repurchase all of such holder's notes at a purchase price equal to 101% of the principal amount of the notes, plus accrued and unpaid interest.

The Indenture limits, among other things, our ability to: incur additional debt; create liens or other encumbrances; place limitations on distributions from restricted subsidiaries; pay dividends; make investments; prepay subordinated indebtedness or make other restricted payments; issue or sell capital stock of restricted subsidiaries; issue guarantees; sell assets; enter into transactions with its affiliates; and make acquisitions or merge or consolidate with another entity.

Affiliates of Highland Capital Management, L.P. (a beneficial stockholder of Leap and an affiliate of James D. Dondero, a director of Leap) purchased an aggregate of \$25.0 million principal amount of senior notes in our offering.

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

We, ANB 1 License and LCW Operations currently expect to incur between \$525 million and \$585 million in capital expenditures, including capitalized interest, for the year ending December 31, 2006.

During the nine months ended September 30, 2006, we, ANB 1 License and LCW Wireless incurred \$348.9 million in capital expenditures. These capital expenditures were primarily for: (i) expansion and improvement of our existing wireless networks, (ii) costs associated with the build-out of our new markets, (iii) costs incurred by ANB 1 License and LCW Wireless in connection with the build-out of their new markets, and (iv) expenditures for EV-DO technology.

## **Table of Contents**

During the year ended December 31, 2005, we and ANB 1 License incurred \$208.8 million in capital expenditures. These capital expenditures were primarily for: (i) expansion and improvement of our existing wireless networks, (ii) the build-out and launch of the Fresno, California market and the related expansion and network change-out of our existing Visalia and Modesto/Merced markets, (iii) costs associated with the build-out of our new markets, (iv) costs incurred by ANB 1 License in connection with the build-out of its new markets, and (v) initial expenditures for EV-DO technology.

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

In May 2005, we purchased four wireless licenses covering approximately 11.3 million POPs in the FCC's Auction #58 for \$166.9 million. In September 2005, ANB 1 License purchased nine wireless licenses covering approximately 10.2 million POPs in Auction #58 for \$68.2 million. We have launched three of the four markets we purchased in Auction #58, and ANB 1 License has launched all of its Auction #58 markets.

### *Auction #66 Properties and Build-Outs*

In September 2006, our wholly owned subsidiary was named the winning bidder in Auction #66 for 99 wireless licenses with an aggregate purchase price of \$710.2 million and covering 121.2 million POPs (adjusted to eliminate duplication among certain overlapping licenses won by it in Auction #66), and Denali License was named the winning bidder for one wireless license with a net purchase price of \$274.1 million and covering 59.3 million POPs (which includes markets covering 5.7 million POPs which overlap with certain licenses won by our wholly owned subsidiary in Auction #66). We expect that we and Denali License (which we expect will offer Cricket service) will build out wireless networks in markets covered by these licenses in multiple construction phases over time. We currently expect that the first phase of construction for Auction #66 licenses that we and Denali License intend to build out will include networks covering approximately 24 million POPs. We currently expect that the aggregate capital expenditures for this first phase of construction will be less than \$28.00 per covered POP. We also currently expect that the build-outs for this first phase of construction will commence in 2007 and will be substantially completed by the end of 2009. Moreover, the licenses for which we were the winning bidder, together with the licenses we currently own, provide 20MHz coverage and the opportunity to offer enhanced data services in almost all markets that we currently operate or are building out. If Denali License were to make available to us certain spectrum for which it was the winning bidder in Auction #66, we would have 20MHz coverage in all markets in which we currently operate or are building out.

### *Arrangements with Denali*

In May 2006, Cricket and Denali Spectrum Manager, LLC, or DSM, formed Denali as a joint venture to participate (through its wholly owned subsidiary Denali License) in Auction #66 as a very small business designated entity under FCC regulations. In July 2006, Cricket and DSM entered into an amended and restated limited liability company agreement, or the Denali LLC Agreement, under which Cricket and DSM made equity investments in Denali of approximately \$7.6 million and \$1.6 million, respectively. On October 2, 2006, Cricket and DSM made further equity investments in Denali of \$34.2 million and \$7.3 million, respectively. Cricket and Denali have agreed to make further equity investments on the first anniversary of the conclusion of Auction #66 in an amount equal to approximately 15.3% and 3.2%, respectively, of the aggregate net purchase price of the wireless license Denali acquired in Auction #66, up to a specified maximum amount. Cricket owns an 82.5% non-controlling membership interest and DSM owns a 17.5% controlling membership interest in Denali. DSM, as the sole manager of Denali, has the exclusive right and power to manage, operate and control Denali and its business and affairs, subject to certain protective provisions for the benefit of Cricket.

Also in July 2006, Cricket entered into a senior secured credit agreement with Denali License and Denali. Pursuant to this agreement, as amended, Cricket has agreed to loan to Denali License up to approximately \$223.4 million to fund

the payment of its net winning bid in Auction #66, under which borrowings of \$40.8 million principal amount were outstanding at September 30, 2006. In October 2006, we loaned Denali License an additional \$182.6 million to permit it to pay the final balance it owed to the FCC for its Auction #66 license. Cricket also agreed to loan to Denali License an amount equal to \$0.75 times the aggregate number of POPs covered by the license for which it was the winning bidder to fund a portion of the costs of the construction and operation of wireless networks using such license, which build-out loan sub-facility may be increased from time to time with

## **Table of Contents**

Cricket's approval. Loans under the credit agreement accrue interest at the rate of 14% per annum and such interest is added to principal quarterly. All outstanding principal and accrued interest is due on the tenth anniversary of the grant date of the wireless licenses awarded to Denali License in Auction #66. However, if DSM makes an offer to sell its membership interests in Denali to Cricket under the Denali LLC Agreement and Cricket accepts such offer, then all outstanding principal and accrued interest under the credit agreement will become due upon the first business day following the date on which Cricket has paid DSM the offer price for its membership interests in Denali. Denali License may prepay loans under the credit agreement at any time without premium or penalty. The obligations of Denali License and Denali under the credit agreement are secured by all of the personal property, fixtures and owned real property of Denali License and Denali, subject to certain permitted liens.

### *Other Acquisitions and Dispositions*

From June 2006 through October 2006, we entered into four agreements to sell wireless licenses that we were not using to offer commercial service for an aggregate sales price of \$22.4 million. In October 2006, three of these transactions were completed. Completion of the remaining transaction is subject to customary closing conditions, including FCC approval. Although we expect the FCC to grant such approval and we expect to satisfy the other conditions, we cannot assure you that such approval will be granted or that the other conditions will be satisfied. During the second quarter of 2006, we recorded impairment charges of \$3.2 million to adjust the carrying values of four of the licenses to their estimated fair values, which were based on the agreed upon sales prices.

In August 2006, we completed the exchange of our wireless license in Grand Rapids, Michigan for a wireless license in Rochester, New York to form a new market cluster with our existing Buffalo and Syracuse markets in upstate New York. These three licenses cover 3.1 million POPs.

In July 2006, we completed the sale of our wireless licenses and operating assets in our Toledo and Sandusky, Ohio markets in exchange for \$28.0 million in cash and an equity interest in LCW Wireless. We also contributed to LCW Wireless \$21.0 million in cash and wireless licenses in Eugene and Salem, Oregon and related operating assets, resulting in Cricket owning a 72% non-controlling membership interest in LCW Wireless. We expect to receive additional membership interests in LCW Wireless once we have completed replacing certain network equipment, although we cannot assure you that this will be completed. Upon receipt of such interests, we will own a 73.3% non-controlling membership interest in LCW Wireless. We recognized a net gain of \$21.5 million in the third quarter of 2006 associated with these transactions.

In March 2006, we entered into an agreement with a debtor-in-possession for the purchase of 13 wireless licenses in North Carolina and South Carolina for an aggregate purchase price of \$31.8 million. Completion of this transaction is subject to customary closing conditions, including the receipt of certain FCC approvals and orders which have already been issued but which have not yet become final.

### *Off-Balance Sheet Arrangements*

We had no material off-balance sheet arrangements at September 30, 2006.

## **Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

*Interest Rate Risk.* As of September 30, 2006, we had \$898 million in outstanding floating rate debt under our Credit Agreement. Changes in interest rates would not significantly affect the fair value of our outstanding indebtedness. The terms of our Credit Agreement require us to enter into interest rate swap agreements in a sufficient amount so that at least 50% of our outstanding indebtedness for borrowed money bears interest at a fixed rate by December 31, 2006. We have entered into interest rate swap agreements with respect to \$355 million of our debt. These swap agreements



effectively fix the interest rate on \$250 million of our indebtedness at 6.7% and \$105 million of our indebtedness at 6.8% through June 2007 and 2009, respectively. As of September 30, 2006, net of the effect of the interest rate swap agreements described above, our outstanding floating rate indebtedness totaled \$543 million. The primary base interest rate is three month LIBOR. Assuming the outstanding balance on our floating rate indebtedness remains constant over a year, a 100 basis point increase in the interest rate would decrease pre-tax income and cash flow, net of the effect of the swap agreements, by approximately \$5.4 million.

*Hedging Policy.* Our policy is to maintain interest rate hedges when required by credit agreements. We do not currently engage in any hedging activities against foreign currency exchange rates or for speculative purposes.

**Table of Contents**

**Item 4. Controls and Procedures.**

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

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified by the SEC and that such information is accumulated and communicated to management, including its chief executive officer (or CEO) and chief financial officer (or CFO), as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Management, with participation by the Company's CEO and CFO, has designed the Company's disclosure controls and procedures to provide reasonable assurance of achieving the desired objectives. As required by SEC Rule 13a-15(b), in connection with filing this Quarterly Report on Form 10-Q, management conducted an evaluation, with the participation of the Company's CEO and CFO, of the effectiveness of the design and operation of the Company's disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as of September 30, 2006, the end of the period covered by this report. Based upon that evaluation, the Company's CEO and CFO concluded that two control deficiencies, each of which constituted a material weakness, as discussed below, existed in the Company's internal control over financial reporting as of September 30, 2006. As a result of these material weaknesses, the Company's CEO and CFO concluded that the Company's disclosure controls and procedures were not effective at the reasonable assurance level as of September 30, 2006.

In light of these material weaknesses, the Company performed additional analyses and procedures in order to conclude that its condensed consolidated financial statements for the quarter ended September 30, 2006 were fairly stated in accordance with accounting principles generally accepted in the United States of America for such financial statements. Accordingly, management believes that despite the Company's material weaknesses, the Company's condensed consolidated financial statements for the quarter ended September 30, 2006 are fairly stated, in all material respects, in accordance with generally accepted accounting principles.

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

*Insufficient Staffing in the Accounting, Financial Reporting and Tax Functions.* The Company did not maintain a sufficient complement of personnel with the appropriate skills, training and Company-specific experience to identify and address the application of generally accepted accounting principles in complex or non-routine transactions. The Company has also experienced staff turnover and an associated loss of Company-specific experience within its accounting, financial reporting and tax functions. This control deficiency could result in a misstatement of accounts and disclosures that would result in a material misstatement to the Company's interim or annual consolidated financial statements that would not be prevented or detected. Accordingly, management has determined that this control deficiency constitutes a material weakness. The Company has taken the following actions to remediate this material weakness:

The Company hired a new executive vice president, chief financial officer in August 2006. This individual has over 20 years of experience as a financial executive, including over seven years as a chief financial officer of public companies.

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

The Company hired a new assistant controller in October 2006. This individual is a certified public accountant with over 15 years of experience as an accounting executive with a large public company. She also possesses a strong background in technical accounting and the application of generally accepted accounting principles in complex or non-routine transactions.

**Table of Contents**

In June 2006, the Company hired a new director of tax to lead its tax function. This individual is a certified public accountant with over 19 years of experience as a tax professional, including over nine years with the tax practices of large public accounting firms. He possesses a strong background in interpreting and applying income tax accounting literature and preparing income tax provisions for public companies.

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

The Company has used experienced qualified consultants to assist management in addressing the application of generally accepted accounting principles in complex or non-routine transactions for the quarters ended September 30, 2006, June 30, 2006 and March 31, 2006 and the year ended December 31, 2005, and will continue to use such consultants in the future, as needed, to supplement its existing staff.

Based on the new leadership and management in the accounting and tax functions, the Company's identification of certain of the historical errors in its accounting for income taxes and the timely completion of the Quarterly Reports on Form 10-Q for the first, second and third quarters of fiscal 2006, the Company believes that it has made substantial progress in addressing this material weakness as of September 30, 2006. The Company expects that this material weakness will be fully remediated once it has fully remediated the material weakness related to the accounting for income taxes, and it demonstrates continued timely completion of its SEC reports, particularly the Annual Report on Form 10-K for the year ending December 31, 2006.

This material weakness contributed to the following control deficiency, which is considered to be a material weakness.

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

The Company has taken the following actions to remediate this material weakness:

In June 2006, the Company hired a new director of tax to lead its tax function. This individual is a certified public accountant with over 19 years of experience as a tax professional, including over nine years with the tax practices of large public accounting firms. He possesses a strong background in interpreting and applying income tax accounting literature and preparing income tax provisions for public companies.

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

The Company used experienced qualified consultants to assist management in interpreting and applying income tax accounting literature and preparing the Company's income tax provision for the quarters ended

September 30, 2006, June 30, 2006 and March 31, 2006 and the year ended December 31, 2005, and may continue to use such consultants in the future to obtain access to as much income tax accounting expertise as it needs.

**Table of Contents**

As a result of the remediation initiatives described above, the Company identified certain of the errors that gave rise to the restatements of the consolidated financial statements for deferred income taxes. In addition, the Company prepared accurate and timely income tax provisions for the year ended December 31, 2005 and the first three quarters of fiscal 2006. Based on these remediation initiatives, the Company believes that it has made substantial progress in addressing this material weakness as of September 30, 2006. The Company expects that this material weakness will be fully remediated once it demonstrates continued accurate and timely preparation of its income tax provisions, particularly the 2006 annual tax provision.

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

There were no changes in the Company's internal control over financial reporting during the quarter ended September 30, 2006 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**Table of Contents**

**PART II  
OTHER INFORMATION**

**Item 1. Legal Proceedings.**

We are involved in certain legal proceedings that are described in our Annual Report on Form 10-K for the year ended December 31, 2005 filed with the Securities and Exchange Commission, or the SEC, on March 27, 2006. There have been no material developments in the status of those legal proceedings during the nine months ended September 30, 2006, except as noted in the following paragraph with respect to outstanding bankruptcy claims.

***Outstanding Bankruptcy Claims***

Although our plan of reorganization became effective and we emerged from bankruptcy in August 2004, a tax claim of approximately \$4.9 million Australian dollars (approximately \$3.8 million U.S. dollars as of November 2, 2006) asserted by the Australian government against Leap in the U.S. Bankruptcy Court for the Southern District of California in Case Nos. 03-03470-All to 03-035335-All (jointly administered) has not yet been resolved. The Bankruptcy Court sustained our objection to the claim and dismissed the claim in June 2006. However, the Australian government has appealed the Bankruptcy Court order to the United States District Court for the Southern District of California in Case No. 06-CCV-1282. We, the Australian government and the trust established in bankruptcy for the benefit of the Leap general unsecured creditors have agreed in principle to settle this claim. We do not believe that the resolution of this claim will have a material adverse effect on our consolidated financial statements.

***Patent Litigation***

On June 14, 2006, we sued MetroPCS Communications, Inc., or MetroPCS, in the United States District Court for the Eastern District of Texas, Marshall Division, Civil Action No. 2-06H-CV-00240-TJW, for infringement of U.S. Patent No. 6,813,497 *Method for Providing Wireless Communication Services and Network and System for Delivering Same*, issued to us. Our complaint seeks damages and an injunction against continued infringement. On August 3, 2006, MetroPCS (i) answered the complaint, (ii) raised a number of affirmative defenses, and (iii) together with two related entities, counterclaimed against Leap, Cricket, numerous Cricket subsidiaries, ANB 1 License, Denali License, and current and former employees of Leap and Cricket, including Leap CEO Doug Hutcheson. The countersuit alleges claims for breach of contract, misappropriation, conversion and disclosure of trade secrets, misappropriation of confidential information and breach of confidential relationship, relating to information provided by MetroPCS to such employees, including prior to their employment by Leap, and asks the court to award damages, including punitive damages, impose an injunction enjoining us from participating in Auction #66, impose a constructive trust on our business and assets for the benefit of MetroPCS, and declare that the MetroPCS entities have not infringed U.S. Patent No. 6,813,497 and that such patent is invalid. MetroPCS's claims allege that we and the other counterclaim defendants improperly obtained, used and disclosed trade secrets and confidential information of the MetroPCS entities and breached confidentiality agreements with the MetroPCS entities. On October 13, 2006, ANB 1 License, Denali License, and two of the individual counterclaim defendants filed motions to dismiss the claims against them, and the remaining counterclaim defendants answered the counterclaims. Based upon our preliminary review of the counterclaims, we believe that we have meritorious defenses and intend to vigorously defend against the counterclaims. If the MetroPCS entities were to prevail in their counterclaims, it could have a material adverse effect on our business, financial condition and results of operations. On September 22, 2006, Royal Street Communications, LLC, or Royal Street, an entity affiliated with MetroPCS, filed an action in the United States District Court for the Middle District of Florida, Tampa Division, Civil Action No. 8:06-CV-01754-T-23TBM, seeking a declaratory judgment that Cricket's U.S. Patent No. 6,813,497 *Method for Providing Wireless Communication Services and*

*Network and System for Delivering Same* (the same patent that is the subject of our infringement action against MetroPCS) is invalid and is not being infringed by Royal Street or its PCS systems. On October 17, 2006, we filed a motion to dismiss the case or, in the alternative, to transfer the case to the Eastern District of Texas. We intend to vigorously defend against these actions.

On August 3, 2006, MetroPCS filed a separate action in the United States District Court for the Northern District of Texas, Dallas Division, Civil Action No. 3-06CV1399-D, seeking a declaratory judgment that our



## **Table of Contents**

U.S. Patent No. 6,959,183 *Operations Method for Providing Wireless Communication Services and Network and System for Delivering Same* (a different patent from the one that is the subject of our infringement action against MetroPCS) is invalid and is not being infringed by MetroPCS and its affiliates. On October 13, 2006, Leap and Cricket filed a motion to dismiss this action or, in the alternative, to transfer the action to the United States District Court for the Eastern District of Texas where another suit is pending between the Company, MetroPCS and other parties as described in the preceding paragraph. We intend to vigorously defend against the action.

On August 17, 2006, we were served with a complaint filed by MetroPCS and certain of its affiliates (together with MetroPCS, the MetroPCS entities ) in the Superior Court of the State of California, County of Stanislaus, Case No. 382780, which names Leap, Cricket, certain of our subsidiaries, and certain current and former employees of Leap and Cricket, including Leap CEO Doug Hutcheson, as defendants. In the complaint, the MetroPCS entities allege (i) unfair competition, (ii) misappropriation of trade secrets, (iii) (with respect to the individuals sued) intentional and negligent interference with contract, (iv) breach of contract, (v) intentional interference with prospective economic advantage and (vi) trespass, and ask the court to award damages, including punitive damages, and restitution. On October 13, 2006, all defendants joined in a motion to stay the case until resolution of the case in the Eastern District of Texas because of the substantial overlap of the cases. If and when the case proceeds, based on the initial complaint, it is unclear whether, if the MetroPCS entities were to prevail, it could have a material adverse effect on our business, financial condition and results of operations. We intend to vigorously defend against the actions.

### ***Tortious Interference and Unfair Competition Litigation***

On July 10, 2006, we sued T-Mobile USA, Inc., or T-Mobile, in the District Court of Harris County, Texas, Cause No. 2006-42215, for tortious interference with existing contract, tortious interference with prospective relations, business disparagement, and antitrust violations arising out of anticompetitive activities of T-Mobile in the Houston, Texas marketplace. In response, on August 8, 2006, T-Mobile filed a counterclaim against Cricket, alleging tortious interference with T-Mobile's contracts with employees, ex-employees, authorized dealers and customers and unfair competition, and asking the court to award damages, including punitive damages, in an unspecified amount. If T-Mobile was to prevail in its counterclaim, it could have a material adverse effect on our business, financial condition and results of operations. We intend to vigorously defend against the counterclaim.

In addition to the matters described above, we are often involved in claims arising in the course of business, seeking monetary damages and other relief. The amount of the liability, if any, from such claims cannot currently be reasonably estimated; therefore, no accruals have been made as of September 30, 2006 for such claims. We believe that the ultimate liability for such claims will not have a material adverse effect on our consolidated financial statements.

### **Item 1A. Risk Factors.**

There have been no material changes to the Risk Factors described under Item 1A. Risk Factors in our Quarterly Report on Form 10-Q for the three months ended June 30, 2006 previously filed with the SEC other than changes to:

the Risk Factor below entitled We Expect to Incur Substantial Costs in Connection with the Build-Out of Our New Markets, and any Delays or Cost Increases in the Build Out of Our New Markets Could Adversely Affect Our Business, which has been updated to reflect risks associated with the manufacture and supply of network equipment and handsets for AWS spectrum;

the Risk Factor below entitled If We Are Unable to Manage Our Planned Growth, Our Operations Could Be Adversely Impacted, which has been updated to reflect additional risks associated with continued growth;

the Risk Factors below entitled Our Indebtedness Could Adversely Affect Our Financial Health, Despite Current Indebtedness Levels, We May Incur Substantially More Indebtedness. This Could Further Increase the Risks Associated with Our Leverage and Covenants in Our Indenture and Credit Agreement and Other Credit Agreements or Indentures That We May Enter Into in the Future May Limit Our Ability to Operate Our Business, and the addition of a new Risk Factor below entitled We May Be Unable to Refinance Our

**Table of Contents**

Indebtedness, which have been updated or added to reflect our borrowings under and repayment of our bridge loan facility, and the issuance by Cricket in October 2006 of \$750 million of unsecured senior notes due in 2014 (see Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Senior Notes in Part I above); and

the Risk Factors below entitled We May Not Be Successful in Protecting and Enforcing Our Intellectual Property Rights, We May Be Subject to Claims of Infringement Regarding Telecommunications Technologies That Are Protected by Patents and Other Intellectual Property Rights, and We Rely Heavily on Third Parties to Provide Specialized Services; a Failure by Such Parties to Provide the Agreed Services Could Materially Adversely Affect Our Business, Results of Operations and Financial Condition, which have been updated to reflect developments.

***Risks Related to Our Business and Industry***

**We Have Experienced Net Losses, and We May Not Be Profitable in the Future.**

We experienced net losses of \$8.4 million and \$49.3 million (excluding reorganization items, net) for the five months ended December 31, 2004 and the seven months ended July 31, 2004, respectively. In addition, we experienced net losses of \$597.4 million for the year ended December 31, 2003, \$664.8 million for the year ended December 31, 2002 and \$483.3 million for the year ended December 31, 2001. Although we had net income of \$30.0 million and \$35.2 million for the year ended December 31, 2005 and the nine months ended September 30, 2006, respectively, we may not generate profits in the future on a consistent basis, or at all. Absent the \$21.5 million net gain we recognized as a result of the sale of wireless licenses and operating assets in Toledo and Sandusky, Ohio in July 2006, we would have recorded a net loss of approximately \$11.6 million for the three months ended September 30, 2006. We expect net income to decrease in the fourth quarter of 2006, and we may realize a net loss for fiscal 2006. If we fail to achieve consistent profitability, that failure could have a negative effect on our financial condition.

**We May Not Be Successful in Increasing Our Customer Base Which Would Negatively Affect Our Business Plans and Financial Outlook.**

Our growth on a quarter-by-quarter basis has varied substantially in the past. We believe that this uneven growth generally reflects seasonal trends in customer activity, promotional activity, the competition in the wireless telecommunications market, and varying national economic conditions. Our current business plans assume that we will increase our customer base over time, providing us with increased economies of scale. If we are unable to attract and retain a growing customer base, our current business plans and financial outlook may be harmed.

**If We Experience High Rates of Customer Turnover, Our Ability to Remain Profitable Will Decrease.**

Because we do not require customers to sign fixed-term contracts or pass a credit check, our service is available to a broader customer base than many other wireless providers and, as a result, some of our customers may be more likely to terminate service due to an inability to pay than the average industry customer, particularly during economic downturns or during periods of high gasoline prices. In addition, our rate of customer turnover may be affected by other factors, including the size of our calling areas, our handset or service offerings, customer care concerns, phone number portability and other competitive factors. Our strategies to address customer turnover may not be successful. A high rate of customer turnover would reduce revenues and increase the total marketing expenditures required to attract the minimum number of replacement customers required to sustain our business plan, which, in turn, could have a material adverse effect on our business, financial condition and results of operations.

**We Have Made Significant Investment, and Will Continue to Invest, in Joint Ventures That We Do Not Control.**

In November 2004, we acquired a 75% non-controlling interest in ANB 1, whose wholly owned subsidiary, ANB 1 License, was awarded certain licenses in Auction #58. In July 2006, we acquired a 72% non-controlling interest in LCW Wireless, which was awarded a wireless license for the Portland, Oregon market in Auction #58

## **Table of Contents**

and to which we contributed, among other things, two wireless licenses in Eugene and Salem, Oregon and related operating assets. Both ANB 1 License and LCW Wireless acquired their Auction #58 wireless licenses as very small business designated entities under FCC regulations. In July 2006, we acquired an 82.5% non-controlling interest in Denali, an entity which (through a wholly owned subsidiary) participated in Auction #66 as a very small business designated entity under FCC regulations. Our participation in these joint ventures is structured as a non-controlling interest in order to comply with FCC rules and regulations. We have agreements with our joint venture partners in ANB 1, LCW Wireless and Denali, and we plan to have similar agreements in connection with any future joint venture arrangements we may enter into, which are intended to allow us to actively participate to a limited extent in the development of the business through the joint venture. However, these agreements do not provide us with control over the business strategy, financial goals, build-out plans or other operational aspects of any such joint venture. The FCC's rules restrict our ability to acquire controlling interests in such entities during the period that such entities must maintain their eligibility as a designated entity, as defined by the FCC. The entities or persons that control the joint ventures may have interests and goals that are inconsistent or different from ours which could result in the joint venture taking actions that negatively impact our business or financial condition. In addition, if any of the other members of a joint venture files for bankruptcy or otherwise fails to perform its obligations or does not manage the joint venture effectively, we may lose our equity investment in, and any present or future opportunity to acquire the assets (including wireless licenses) of, such entity.

The FCC recently implemented rule changes aimed at addressing alleged abuses of its designated entity program, affirmed these changes on reconsideration and has sought comment on further rule changes. In that proceeding, the FCC has re-affirmed its goals of ensuring that only legitimate small businesses reap the benefits of the program, and that such small businesses are not controlled or manipulated by larger wireless carriers or other investors that do not meet the small business qualification tests. While we do not believe that the FCC's recent rule changes materially affect our current joint ventures with ANB 1, LCW Wireless and Denali, the scope and applicability of these rule changes to such current designated entity structures remains in flux, and parties have already sought further reconsideration or judicial review of these rule changes. In addition, we cannot predict how further rule changes or increased regulatory scrutiny by the FCC flowing from this proceeding will affect our current or future business ventures with designated entities or our participation with such entities in future FCC spectrum auctions.

### **We Face Increasing Competition Which Could Have a Material Adverse Effect on Demand for the Cricket Service.**

In general, the telecommunications industry is very competitive. Some competitors have announced rate plans substantially similar to Cricket's service plans (and have also introduced products that consumers perceive to be similar to Cricket's service plans) in markets in which we offer wireless service. In addition, the competitive pressures of the wireless telecommunications market have caused other carriers to offer service plans with large bundles of minutes of use at low prices which are competing with the predictable and unlimited Cricket calling plans. Some competitors also offer prepaid wireless plans that are being advertised heavily to demographic segments that are strongly represented in Cricket's customer base. These competitive offerings could adversely affect our ability to maintain our pricing and increase or maintain our market penetration. Our competitors may attract more customers because of their stronger market presence and geographic reach. Potential customers may perceive the Cricket service to be less appealing than other wireless plans, which offer more features and options. In addition, existing carriers and potential non-traditional carriers are exploring or have announced the launch of service using new technologies and/or alternative delivery plans.

In addition, some of our competitors are able to offer their customers roaming services on a nationwide basis and at lower rates. We currently offer roaming services on a prepaid basis. Many competitors have substantially greater financial and other resources than we have, and we may not be able to compete successfully. Because of their size and bargaining power, our larger competitors may be able to purchase equipment, supplies and services at lower prices

and attract a larger number of dealers than we can. Prior to the launch of a large market in 2006, disruptions by a competitor interfered with our indirect dealer relationships, reducing the number of dealers offering Cricket service during the initial weeks of launch. As consolidation in the industry creates even larger competitors, any purchasing advantages our competitors have may increase, as well as their bargaining power as wholesale providers

## **Table of Contents**

of roaming services. For example, in connection with the offering of our Travel Time roaming service, we have encountered problems with certain large wireless carriers in negotiating terms for roaming arrangements that we believe are reasonable, and believe that consolidation has contributed significantly to such carriers' control over the terms and conditions of wholesale roaming services.

We also compete as a wireless alternative to landline service providers in the telecommunications industry. Wireline carriers are also offering unlimited national calling plans and bundled offerings that include wireless and data services. We may not be successful in the long term, or continue to be successful, in our efforts to persuade potential customers to adopt our wireless service in addition to, or in replacement of, their current landline service.

The FCC is currently pursuing policies designed to increase the number of wireless licenses available in each of our markets. For example, the FCC has adopted rules that allow the partitioning, disaggregation and leasing of PCS and other wireless licenses, and continues to allocate and auction additional spectrum that can be used for wireless services, which may increase the number of our competitors.

### **We Have Identified Material Weaknesses in Our Internal Control Over Financial Reporting, and Our Business and Stock Price May Be Adversely Affected If We Do Not Remediate All of These Material Weaknesses, or If We Have Other Material Weaknesses in Our Internal Control Over Financial Reporting.**

In connection with their evaluations of our disclosure controls and procedures, our CEO and CFO have concluded that certain material weaknesses in our internal control over financial reporting existed as of September 30, 2004, December 31, 2004, March 31, 2005, June 30, 2005, September 30, 2005, December 31, 2005, March 31, 2006, June 30, 2006 and September 30, 2006 with respect to turnover and staffing levels in our accounting, financial reporting and tax departments and the preparation of our income tax provision, and as of as of December 31, 2004 and March 31, 2005 with respect to the application of lease-related accounting principles, fresh-start reporting oversight, and account reconciliation procedures. We believe we have adequately remediated the material weaknesses associated with lease accounting, fresh-start reporting oversight and account reconciliation procedures.

Although we are engaged in remediation efforts with respect to the material weaknesses related to turnover and staffing and income tax provision preparation, the existence of one or more material weaknesses could result in errors in our financial statements, and substantial costs and resources may be required to rectify these or other internal control deficiencies. If we cannot produce reliable financial reports, investors could lose confidence in our reported financial information, the market price of Leap's common stock could decline significantly, we may be unable to obtain additional financing to operate and expand our business, and our business and financial condition could be harmed. For a description of these material weaknesses and the steps we are undertaking to remediate them, see Item 4. Controls and Procedures contained in Part I of this report. We cannot assure you that we will be able to remediate these material weaknesses in a timely manner.

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

Section 404 of the Sarbanes-Oxley Act of 2002 requires companies to do a comprehensive evaluation of their internal control over financial reporting. To comply with this statute, we are required to document and test our internal control over financial reporting; our management is required to assess and issue a report concerning our internal control over financial reporting; and our independent registered public accounting firm is required to attest to and report on management's assessment and the effectiveness of internal control over financial reporting. We were required to comply with Section 404 of the Sarbanes-Oxley Act in connection with the filing of our Annual Report on Form 10-K for the year ended December 31, 2005. We conducted a rigorous review of our internal control over financial reporting in order to become compliant with the requirements of Section 404. The standards that must be met for

management to assess our internal control over financial reporting are new and require significant documentation and testing. Our assessment identified the need for remediation of some aspects of our internal control over financial reporting. Our internal control over financial reporting has been subject to certain material



## **Table of Contents**

weaknesses in the past and is currently subject to material weaknesses related to turnover and staffing and preparation of our income tax provision as described in Item 4. Controls and Procedures contained in Part I of this report. Our management concluded and our independent registered public accounting firm has attested and reported that our internal control over financial reporting was not effective as of December 31, 2005. If we are unable to implement effective control over financial reporting, investors could lose confidence in our reported financial information and the market price of Leap's common stock could decline significantly, we may be unable to obtain additional financing to operate and expand our business and our business and financial condition could be harmed.

### **Our Primary Business Strategy May Not Succeed in the Long Term.**

A major element of our business strategy is to offer consumers service plans that allow unlimited calls for a flat monthly rate without entering into a fixed-term contract or passing a credit check. However, unlike national wireless carriers, we do not seek to provide ubiquitous coverage across the U.S. or all major metropolitan centers, and instead have a smaller network footprint covering only the principal population centers of our various markets. This strategy may not prove to be successful in the long term. From time to time, we also evaluate our service offerings and the demands of our target customers and may modify, change or adjust our service offerings or offer new services. We cannot assure you that these service offerings will be successful or prove to be profitable.

### **We Expect to Incur Substantial Costs in Connection with the Build-Out of Our New Markets, and any Delays or Cost Increases in the Build-Out of Our New Markets Could Adversely Affect Our Business.**

Our ability to achieve our strategic objectives will depend in part on the successful, timely and cost-effective build-out of the networks associated with newly acquired FCC licenses, including the license acquired by LCW Wireless in Auction #58 and the licenses that we and Denali License expect to be awarded as a result of Auction #66 or licenses we may acquire from third parties. Large scale construction projects such as the build-out of our new markets will require significant capital expenditures and may suffer cost-overruns. In addition, we will experience higher operating expenses as we build out and after we launch our service in new markets. Any significant capital expenditures or increased operating expenses, including in connection with the build-out and launch of markets for the licenses that we and Denali License expect to be awarded as a result of Auction #66, would negatively impact our earnings and free cash flow for those periods in which we incur such capital expenditures or increased operating expenses. In addition, the build-out of the networks may be delayed or adversely affected by a variety of factors, uncertainties and contingencies, such as natural disasters, difficulties in obtaining zoning permits or other regulatory approvals, our relationships with our joint venture partners, and the timely performance by third parties of their contractual obligations to construct portions of the networks.

The spectrum that was auctioned in Auction #66 currently is used by U.S. federal government and/or incumbent commercial licensees. FCC rules require winning bidders to avoid interfering with these existing users or to clear the incumbent users from the spectrum through specified relocation procedures. We have considered the estimated cost and time frame required to clear the spectrum for which we and Denali License were declared the winning bidders in the auction. However, the actual cost of clearing the spectrum may exceed our estimated costs. Furthermore, delays in the provision of federal funds to relocate government users, or difficulties in negotiating with incumbent commercial licensees, may extend the date by which the auctioned spectrum can be cleared of existing operations, and thus may also delay the date on which we can launch commercial services using such licensed spectrum. In addition, certain existing government operations are using the spectrum that is being auctioned at classified geographic locations that have not yet been identified to bidders, which creates additional uncertainty about the time at which such spectrum will be available for commercial use.

Although our vendors have announced their intention to manufacture and supply network equipment and handsets that operate in the Advanced Wireless Services, or AWS, spectrum bands, network equipment and handsets that support

AWS are not presently available. If network equipment and handsets for the AWS spectrum are not made available on a timely basis in the future by our suppliers, our proposed build-outs and launches of new Auction #66 markets could be delayed, which would negatively impact our earnings and cash flows. In addition, if due to delays in the availability of AWS network equipment and handsets we ultimately must choose a technology platform for our networks other than CDMA, the adoption of such alternative technology solution could have a material adverse effect on our capital expenditures and capital spending plans. Any significant increase in our

## **Table of Contents**

expected capital expenditures in connection with the build-out and launch of Auction #66 licenses could negatively impact our earnings and free cash flow for those periods in which we incur such capital expenditures.

Any failure to complete the build-out of our new markets on budget or on time could delay the implementation of our clustering and strategic expansion strategies, and could have a material adverse effect on our results of operations and financial condition.

### **If We Are Unable to Manage Our Planned Growth, Our Operations Could Be Adversely Impacted.**

We have experienced growth in a relatively short period of time and expect to continue to experience growth in the future in our existing and new markets. The management of such growth will require, among other things, continued development of our financial and management controls and management information systems, stringent control of costs, diligent management of our network infrastructure and its growth, increased spending associated with marketing activities and acquisition of new customers, the ability to attract and retain qualified management personnel and the training of new personnel. In addition, continued growth will eventually require the expansion of our billing, customer care and sales systems and platforms, which will require additional capital expenditures and may divert the time and attention of management personnel who oversee any such expansion. Furthermore, the implementation of any such systems or platforms, including the transition to such systems or platforms from our existing infrastructure, could result in unpredictable technological or other difficulties. Failure to successfully manage our expected growth and development or timely and adequately resolve any such difficulties could have a material adverse effect on our business, financial condition and results of operations.

### **Our Indebtedness Could Adversely Affect Our Financial Health.**

We have now and will continue to have a significant amount of indebtedness. As of September 30, 2006, our total outstanding indebtedness under the Credit Agreement was \$898 million and we also had a \$200 million undrawn revolving credit facility (which forms part of our senior secured credit facility). In August 2006, we entered into a bridge credit agreement providing for an \$850 million bridge loan facility. In October 2006, we borrowed \$570 million under the bridge loan facility to pay a portion of the final balance we owed to the FCC for our Auction #66 licenses and to loan Denali License \$182.6 million to permit it to pay the final balance it owed to the FCC for its Auction #66 license. We used a portion of the net proceeds from our sale of \$750 million in unsecured senior notes issued in October 2006 to repay the outstanding obligations, including accrued interest, under the bridge loan facility. Upon repayment of the outstanding indebtedness under the bridge loan facility, the bridge loan facility was terminated. In addition, we may seek to raise additional funds in the future. Indebtedness under our senior secured credit facility bears interest at a variable rate, but we have entered into interest rate swap agreements with respect to \$355 million of our indebtedness. Our substantial indebtedness could have important consequences. For example, it could:

make it more difficult for us to satisfy our debt obligations;

increase our vulnerability to general adverse economic and industry conditions;

impair our ability to obtain additional financing in the future for working capital needs, capital expenditures, building out our network, acquisitions and general corporate purposes;

require us to dedicate a substantial portion of our cash flows from operations to the payment of principal and interest on our indebtedness, thereby reducing the availability of our cash flows to fund working capital needs, capital expenditures, acquisitions and other general corporate purposes;

limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate; place us at a disadvantage compared to our competitors that have less indebtedness; and expose us to higher interest expense in the event of increases in interest rates because indebtedness under our senior secured credit facility bears interest at a variable rate. For a description of our senior secured credit facility, see Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Senior Secured Credit Facilities in Part I of this report.

## **Table of Contents**

As of September 30, 2006, 55.5% of our assets consisted of goodwill and other intangibles, including wireless licenses and deposits for wireless licenses. This percentage will increase significantly following the expected acquisition of the wireless licenses for which we and Denali License were named the winning bidders in Auction #66, which have a collective purchase price of approximately \$984.3 million. The value of our assets, and in particular, our intangible assets, will depend on market conditions, the availability of buyers and similar factors. By their nature, our intangible assets may not have a readily ascertainable market value or may not be saleable or, if saleable, there may be substantial delays in their liquidation. For example, prior FCC approval is required in order for any remedies to be exercised with respect to our wireless licenses and obtaining such approval could result in significant delays and reduce the proceeds obtained from the sale or other disposition of our wireless licenses.

### **Despite Current Indebtedness Levels, We May Incur Substantially More Indebtedness. This Could Further Increase the Risks Associated with Our Leverage.**

We may incur substantial additional indebtedness in the future. The terms of the Indenture permit us, subject to specified limitations, to incur additional indebtedness, including secured indebtedness. In addition, our Credit Agreement permits us to incur additional indebtedness under various financial ratio tests.

In October 2006, we borrowed an aggregate of \$570 million under our bridge loan facility to pay a portion of the final balance we owed to the FCC for our Auction #66 licenses and to loan Denali License \$182.6 million to permit it to pay the final balance it owed to the FCC for its Auction #66 license. A portion of the net proceeds from our sale of \$750 million of unsecured senior notes in October 2006 was used to repay our outstanding obligations under the bridge loan facility, after which our bridge loan facility was terminated. In addition, we may require significant additional capital in the future to finance the build-out and initial operating costs associated with licenses that we and Denali License expect to be awarded as a result of Auction #66.

If new indebtedness is added to our current levels of indebtedness, the related risks that we now face could intensify. See Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources in Part I of this report. Furthermore, any licenses that we acquire in Auction #66 and the subsequent build-out of the networks covered by those licenses may significantly reduce our free cash flow, increasing the risk that we may not be able to service our indebtedness.

### **To Service Our Indebtedness and Fund Our Working Capital and Capital Expenditures, We Will Require a Significant Amount of Cash. Our Ability to Generate Cash Depends on Many Factors Beyond Our Control.**

Our ability to make payments on our indebtedness will depend upon our future operating performance and on our ability to generate cash flow in the future, which is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control. We cannot assure you that our business will generate sufficient cash flow from operations, or that future borrowings, including borrowings under our revolving credit facility, will be available to us or available in an amount sufficient to enable us to pay our indebtedness or to fund our other liquidity needs. If the cash flow from our operating activities is insufficient, we may take certain actions, such as delaying or reducing capital expenditures (including expenditures to build out our newly acquired wireless licenses), attempting to restructure or refinance our indebtedness prior to maturity, selling assets or operations or seeking additional equity capital. Any or all of these actions may be insufficient to allow us to service our debt obligations. Further, we may be unable to take any of these actions on commercially reasonable terms, or at all.

### **We May Be Unable to Refinance Our Indebtedness.**

We may need to refinance all or a portion of our indebtedness, before maturity. We cannot assure you that we will be able to refinance any of our indebtedness, including under our Indenture or our Credit Agreement, on commercially reasonable terms or at all. There can be no assurance that we will be able to obtain sufficient funds to enable us to repay or refinance our debt obligations on commercially reasonable terms or at all.

**Table of Contents**

**Covenants in Our Indenture and Credit Agreement and Other Credit Agreements or Indentures That We May Enter Into in the Future May Limit Our Ability to Operate Our Business.**

Our Indenture and Credit Agreement contain covenants that restrict the ability of Leap, Cricket and the subsidiary guarantors to make distributions or other payments to our investors or creditors until we satisfy certain financial tests or other criteria. In addition, the Indenture and the Credit Agreement include covenants restricting, among other things, the ability of Leap, Cricket and their restricted subsidiaries to:

- incur additional indebtedness;
- create liens or other encumbrances;
- place limitations on distributions from restricted subsidiaries;
- pay dividends, make investments, prepay subordinated indebtedness or make other restricted payments;
- issue or sell capital stock of restricted subsidiaries;
- issue guarantees;
- sell or otherwise dispose of all or substantially all of our assets;
- enter into transactions with affiliates; and
- make acquisitions or merge or consolidate with another entity.

Under the Credit Agreement, we must also comply with, among other things, financial covenants with respect to a maximum consolidated senior secured leverage ratio and, if a revolving credit loan or uncollateralized letter of credit is outstanding, with respect to a minimum consolidated interest coverage ratio, a maximum consolidated leverage ratio and a minimum consolidated fixed charge ratio. The restrictions in our Credit Agreement could limit our ability to make borrowings, obtain debt financing, repurchase stock, refinance or pay principal or interest on our outstanding indebtedness, complete acquisitions for cash or debt or react to changes in our operating environment. Any credit agreement or indenture that we may enter into in the future may have similar restrictions.

If we default under our Indenture or our Credit Agreement because of a covenant breach or otherwise, all outstanding amounts thereunder could become immediately due and payable. Our failure to timely file our Annual Report on Form 10-K for fiscal year ended December 31, 2004 and our Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2005 constituted defaults under our previous senior secured credit agreement, and the restatement of certain of the historical consolidated financial information contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2005 may have constituted a default under our previous senior secured credit agreement. Although we were able to obtain limited waivers under our previous senior secured credit agreement with respect to these events, we cannot assure you that we will be able to obtain a waiver in the future should a default occur.

We cannot assure you that we would have sufficient funds to repay all of the outstanding amounts under our Indenture or our Credit Agreement, and any acceleration of amounts due would have a material adverse effect on our liquidity and financial condition.

**Rises in Interest Rates Could Adversely Affect our Financial Condition.**

An increase in prevailing interest rates would have an immediate effect on the interest rates charged on our variable rate debt, which rise and fall upon changes in prevailing interest rates. As of September 30, 2006, we estimate that approximately 60% of our debt was variable rate debt after considering the effect of our interest rate swap agreements. If prevailing interest rates or other factors result in higher interest rates on our variable rate debt, the increased interest expense would adversely affect our cash flow and our ability to service our debt.



**Table of Contents**

**The Wireless Industry is Experiencing Rapid Technological Change, and We May Lose Customers if We Fail to Keep Up with These Changes.**

The wireless communications industry is experiencing significant technological change, as evidenced by the ongoing improvements in the capacity and quality of digital technology, the development and commercial acceptance of wireless data services, shorter development cycles for new products and enhancements and changes in end-user requirements and preferences. In the future, competitors may seek to provide competing wireless telecommunications service through the use of developing technologies such as Wi-Fi, Wi-Max, and Voice over Internet Protocol, or VoIP. The cost of implementing or competing against future technological innovations may be prohibitive to us, and we may lose customers if we fail to keep up with these changes.

For example, we have committed a substantial amount of capital to upgrade our network with 1xEV-DO technology to offer advanced data services. However, if such upgrades, technologies or services do not become commercially accepted, our revenues and competitive position could be materially and adversely affected. We cannot assure you that there will be widespread demand for advanced data services or that this demand will develop at a level that will allow us to earn a reasonable return on our investment.

**The Loss of Key Personnel and Difficulty Attracting and Retaining Qualified Personnel Could Harm Our Business.**

We believe our success depends heavily on the contributions of our employees and on attracting, motivating and retaining our officers and other management and technical personnel. We do not, however, generally provide employment contracts to our employees. If we are unable to attract and retain the qualified employees that we need, our business may be harmed.

We have experienced higher than normal employee turnover in the past, in part because of our bankruptcy, including turnover of individuals at the most senior management levels. We may have difficulty attracting and retaining key personnel in future periods, particularly if we were to experience poor operating or financial performance. The loss of key individuals in the future may have a material adverse impact on our ability to effectively manage and operate our business.

**Risks Associated with Wireless Handsets Could Pose Product Liability, Health and Safety Risks That Could Adversely Affect Our Business.**

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

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

Malfunctions have caused at least one major handset manufacturer to recall certain batteries used in its handsets, including batteries in a handset sold by Cricket and other wireless providers.

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

## **Table of Contents**

ability to add and maintain customers for Cricket service could be materially adversely affected by negative public reactions.

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

### **We Rely Heavily on Third Parties to Provide Specialized Services; a Failure by Such Parties to Provide the Agreed Services Could Materially Adversely Affect Our Business, Results of Operations and Financial Condition.**

We depend heavily on suppliers and contractors with specialized expertise in order for us to efficiently operate our business. In the past, our suppliers, contractors and third-party retailers have not always performed at the levels we expect or at the levels required by their contracts. If key suppliers, contractors or third-party retailers fail to comply with their contracts, fail to meet our performance expectations or refuse or are unable to supply us in the future, our business could be severely disrupted. Generally, there are multiple sources for the types of products we purchase. However, some suppliers, including software suppliers, are the exclusive sources of their specific products. In addition, we currently purchase a substantial majority of the handsets we sell from one supplier. Because of the costs and time lags that can be associated with transitioning from one supplier to another, our business could be substantially disrupted if we were required to replace the products or services of one or more major suppliers with products or services from another source, especially if the replacement became necessary on short notice. Any such disruption could have a material adverse affect on our business, results of operations and financial condition.

A key software supplier recently informed us that it expects to cease operations. We are taking steps to license the supplier's software source code and documentation and to engage selected supplier personnel for software maintenance support to avoid a material impact to our business. However, we cannot provide assurances to our investors about the effect of this supplier's expected closure, or the possible future effect on us of disruptions in the business of other suppliers whose products or services cannot be immediately replaced with the products or services of another supplier.

### **System Failures Could Result in Higher Churn, Reduced Revenue and Increased Costs, and Could Harm Our Reputation.**

Our technical infrastructure (including our network infrastructure and ancillary functions supporting our networks such as billing and customer care) is vulnerable to damage or interruption from technology failures, power loss, floods, windstorms, fires, human error, terrorism, intentional wrongdoing, or similar events. Unanticipated problems at our facilities, system failures, hardware or software failures, computer viruses or hacker attacks could affect the quality of our services and cause service interruptions. In addition, we are in the process of upgrading some of our systems, including our billing system, and we cannot assure you that we will not experience delays or interruptions while we transition our data and existing systems onto our new systems. If any of the above events were to occur, we could experience higher churn, reduced revenues and increased costs, any of which could harm our reputation and have a material adverse effect on our business.

### **We May Not be Successful in Protecting and Enforcing Our Intellectual Property Rights.**

We rely on a combination of patent, service mark, trademark, and trade secret laws and contractual restrictions to establish and protect our proprietary rights, all of which only offer limited protection. We endeavor to enter into agreements with our employees and contractors and agreements with parties with whom we do business in order to limit access to and disclosure of our proprietary information. Despite our efforts, the steps we have taken to protect our intellectual property may not prevent the misappropriation of our proprietary rights. Moreover, others may

independently develop processes and technologies that are competitive to ours. The enforcement of our intellectual property rights may depend on any legal actions that we undertake against such infringers being successful, but we cannot be sure that any such actions will be successful, even when our rights have been infringed.

## **Table of Contents**

We cannot assure you that our pending, or any future, patent applications will be granted, that any existing or future patents will not be challenged, invalidated or circumvented, that any existing or future patents will be enforceable, or that the rights granted under any patent that may issue will provide competitive advantages to us. For example, on June 14, 2006, we sued MetroPCS Communications, Inc., or MetroPCS, in the United States District Court for the Eastern District of Texas, Marshall Division, Civil Action No. 2-06-CV-00240-TJW, for infringement of U.S. Patent No. 6,813,497 *Method for Providing Wireless Communication Services and Network and System for Delivering Same*, issued to us. Our complaint seeks damages and an injunction against continued infringement. On August 3, 2006, MetroPCS (i) answered the complaint, (ii) raised a number of affirmative defenses, and (iii) together with two related entities (referred to, collectively with MetroPCS, as the MetroPCS entities), counterclaimed against Leap, Cricket, numerous Cricket subsidiaries, ANB 1 License, Denali License, and current and former employees of Leap and Cricket, including Leap CEO Doug Hutcheson. The countersuit alleges claims for breach of contract, misappropriation, conversion and disclosure of trade secrets, misappropriation of confidential information and breach of confidential relationship, relating to information provided by MetroPCS to such employees, including prior to their employment by Leap, and asks the court to award damages, including punitive damages, impose an injunction enjoining us from participating in Auction #66, impose a constructive trust on our business and assets for the benefit of MetroPCS, and declare that the MetroPCS entities have not infringed U.S. Patent No. 6,813,497 and that such patent is invalid. MetroPCS's claims allege that we and the other counterclaim defendants improperly obtained, used and disclosed trade secrets and confidential information of the MetroPCS entities and breached confidentiality agreements with the MetroPCS entities. Based upon our preliminary review of the counterclaims, we believe that we have meritorious defenses and intend to vigorously defend against the counterclaims. If the MetroPCS entities were to prevail in their counterclaims, it could have a material adverse effect on our business, financial condition and results of operations. Also, on September 22, 2006, Royal Street Communications, LLC, or Royal Street, an entity affiliated with MetroPCS, filed an action in the United States District Court for the Middle District of Florida, Tampa Division, Civil Action No. 8:06-CV-01754-T-23TBM, seeking a declaratory judgment that Cricket's U.S. Patent No. 6,813,497 *Method for Providing Wireless Communication Services and Network and System for Delivering Same* (the same patent that is the subject of our infringement action against MetroPCS) is invalid and is not being infringed by Royal Street or its PCS systems. We intend to vigorously defend against these actions.

On August 3, 2006, MetroPCS filed a separate action in the United States District Court for the Northern District of Texas, Dallas Division, Civil Action No. 3-06CV1399-D, seeking a declaratory judgment that our U.S. Patent No. 6,959,183 *Operations Method for Providing Wireless Communication Services and Network and System for Delivering Same* (a different patent from the one that is the subject of our infringement action against MetroPCS) is invalid and is not being infringed by MetroPCS and its affiliates. We intend to vigorously defend against the action.

Similarly, we cannot assure you that any trademark or service mark registrations will be issued with respect to pending or future applications or that any registered trademarks or service marks will be enforceable or provide adequate protection of our brands.

### **We May Be Subject to Claims of Infringement Regarding Telecommunications Technologies That Are Protected by Patents and Other Intellectual Property Rights.**

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

requiring us to redesign our business operations or systems to avoid claims of infringement.

## **Table of Contents**

A third party with a large patent portfolio has contacted us and suggested that we need to obtain a license under a number of its patents in connection with our current business operations. We understand that the third party has raised similar issues with other telecommunications companies, and has obtained license agreements from one or more of such companies. If we cannot reach a mutually agreeable resolution with the third party, we may be forced to enter into a licensing or royalty agreement with the third party. In addition, a wireless provider has contacted us and asserted that Cricket's practice of providing service to customers with phones that were originally purchased for use on that provider's network violates copyright laws and interferes with that provider's contracts with its customers. Based on our preliminary review, we do not believe that Cricket's actions violate copyright laws or otherwise violate the other provider's rights. We do not currently expect that the eventual resolution of these matters will materially adversely affect our business, but we cannot provide assurance to our investors about the effect of any such future resolution.

### **Regulation by Government Agencies May Increase Our Costs of Providing Service or Require Us to Change Our Services.**

The FCC regulates the licensing, construction, modification, operation, ownership, sale and interconnection of wireless communications systems, as do some state and local regulatory agencies. We cannot assure you that the FCC or any state or local agencies having jurisdiction over our business will not adopt regulations or take other enforcement or other actions that would adversely affect our business, impose new costs or require changes in current or planned operations. In particular, state regulatory agencies are increasingly focused on the quality of service and support that wireless carriers provide to their customers and several agencies have proposed or enacted new and potentially burdensome regulations in this area.

In addition, we cannot assure you that the Communications Act of 1934, as amended, or the Communications Act, from which the FCC obtains its authority, will not be further amended in a manner that could be adverse to us. The FCC recently implemented rule changes and sought comment on further rule changes focused on addressing alleged abuses of its designated entity program, which gives certain categories of small businesses preferential treatment in FCC spectrum auctions based on size. In that proceeding, the FCC has re-affirmed its goals of ensuring that only legitimate small businesses benefit from the program, and that such small businesses are not controlled or manipulated by larger wireless carriers or other investors that do not meet the small business qualification tests. We cannot predict the degree to which rule changes or increased regulatory scrutiny that may follow from this proceeding will affect our current or future business ventures or our participation in future FCC spectrum auctions.

Our operations are subject to various other regulations, including those regulations promulgated by the Federal Trade Commission, the Federal Aviation Administration, the Environmental Protection Agency, the Occupational Safety and Health Administration and state and local regulatory agencies and legislative bodies. Adverse decisions or regulations of these regulatory bodies could negatively impact our operations and costs of doing business. Because of our smaller size, governmental regulations and orders can significantly increase our costs and affect our competitive position compared to other larger telecommunications providers. We are unable to predict the scope, pace or financial impact of regulations and other policy changes that could be adopted by the various governmental entities that oversee portions of our business.

### **If Call Volume under Our Cricket and Jump Mobile Services Exceeds Our Expectations, Our Costs of Providing Service Could Increase, Which Could Have a Material Adverse Effect on Our Competitive Position.**

During the year ended December 31, 2005, Cricket customers used their handsets approximately 1,450 minutes per month, and some markets were experiencing substantially higher call volumes. Our Cricket service plans bundle certain features, long distance and unlimited local service for a fixed monthly fee to more effectively compete with other telecommunications providers. In addition, call volumes under our Jump Mobile services have been significantly

higher than expected. If customers exceed expected usage, we could face capacity problems and our costs of providing the services could increase. Although we own less spectrum in many of our markets than our competitors, we seek to design our network to accommodate our expected high call volume, and we consistently assess and try to implement technological improvements to increase the efficiency of our wireless spectrum. However, if future wireless use by Cricket and Jump Mobile customers exceeds the capacity of our network, service



## **Table of Contents**

quality may suffer. We may be forced to raise the price of Cricket and Jump Mobile service to reduce volume or otherwise limit the number of new customers, or incur substantial capital expenditures to improve network capacity.

### **We May Be Unable to Acquire Additional Spectrum in the Future at a Reasonable Cost or on a Timely Basis.**

Because we offer unlimited calling services for a fixed fee, our customers' average minutes of use per month is substantially above the U.S. wireless customer average. We intend to meet this demand by utilizing spectrum efficient technologies. There may come a point where we need to acquire additional spectrum in order to maintain an acceptable grade of service or provide new services to meet increasing customer demands. We also intend to acquire additional spectrum in order to enter new strategic markets. However, we cannot assure you that we will be able to acquire additional spectrum at auction or in the after-market at a reasonable cost, that we will be awarded the licenses for which we and Denali License were winning bidders at Auction #66, or that additional spectrum would be made available by the FCC on a timely basis. If such additional spectrum is not available to us at that time or at a reasonable cost, our results of operations could be adversely affected.

### **Our Wireless Licenses are Subject to Renewal and Potential Revocation in the Event that We Violate Applicable Laws.**

Our existing PCS wireless licenses are subject to renewal upon the expiration of the 10-year period for which they are granted, commencing for some of our PCS wireless licenses in 2006. The FCC will award a renewal expectancy to a wireless licensee that has provided substantial service during its past license term and has substantially complied with applicable FCC rules and policies and the Communications Act. The FCC has routinely renewed wireless licenses in the past. However, the Communications Act provides that licenses may be revoked for cause and license renewal applications denied if the FCC determines that a renewal would not serve the public interest. FCC rules provide that applications competing with a license renewal application may be considered in comparative hearings, and establish the qualifications for competing applications and the standards to be applied in hearings. We cannot assure you that the FCC will renew our wireless licenses upon their expiration.

### **Future Declines in the Fair Value of Our Wireless Licenses Could Result in Future Impairment Charges.**

During the three months ended June 30, 2003, we recorded an impairment charge of \$171.1 million to reduce the carrying value of our wireless licenses to their estimated fair value. However, as a result of our adoption of fresh-start reporting under American Institute of Certified Public Accountants' Statement of Position 90-7, Financial Reporting by Entities in Reorganization under the Bankruptcy Code, or SOP 90-7, we increased the carrying value of our wireless licenses to \$652.6 million at July 31, 2004, the fair value estimated by management based in part on information provided by an independent valuation consultant. During the nine months ended September 30, 2006 and the year ended December 31, 2005, we recorded impairment charges of \$7.9 million and \$12.0 million, respectively.

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

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

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

market prices decline as a result of the sales prices in recent and upcoming FCC auctions, including Auction #66.

In addition, the price of wireless licenses could decline as a result of the FCC's pursuit of policies designed to increase the number of wireless licenses available in each of our markets. For example, the FCC has recently auctioned an additional 90 MHz of spectrum in the 1700 MHz to 2100 MHz band in Auction #66 and has announced that it intends to auction additional spectrum in the 700 MHz and 2.5 GHz bands in subsequent auctions. If the

## **Table of Contents**

market value of wireless licenses were to decline significantly, the value of our wireless licenses could be subject to non-cash impairment charges.

We assess potential impairments to our indefinite-lived intangible assets, including wireless licenses, annually and when there is evidence that events or changes in circumstances indicate that an impairment condition may exist. We conduct our annual tests for impairment of our wireless licenses during the third quarter of each year. Estimates of the fair value of our wireless licenses are based primarily on available market prices, including successful bid prices in FCC auctions and selling prices observed in wireless license transactions. A significant impairment loss could have a material adverse effect on our operating income and on the carrying value of our wireless licenses on our balance sheet.

### **Declines in Our Operating Performance Could Ultimately Result in an Impairment of Our Indefinite-Lived Assets, Including Goodwill, or Our Long-Lived Assets, Including Property and Equipment.**

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

### **We May Incur Higher Than Anticipated Inter-carrier Compensation Costs.**

When our customers use our service to call customers of other carriers, we are required under the current inter-carrier compensation scheme to pay the carrier that serves the called party. Similarly, when a customer of another carrier calls one of our customers, that carrier is required to pay us. While in most cases we have been successful in negotiating agreements with other carriers that impose reasonable reciprocal compensation arrangements, some carriers have claimed a right to unilaterally impose what we believe to be unreasonably high charges on us. The FCC is actively considering possible regulatory approaches to address this situation but we cannot assure you that the FCC rulings will be beneficial to us. An adverse ruling or FCC inaction could result in carriers successfully collecting higher inter-carrier fees from us, which could adversely affect our business.

The FCC also is considering making various significant changes to the inter-carrier compensation scheme to which we are subject. We cannot predict with any certainty the likely outcome of this FCC proceeding. Some of the alternatives that are under active consideration by the FCC could severely increase the interconnection costs we pay. If we are unable to cost-effectively provide our products and services to customers, our competitive position and business prospects could be materially adversely affected.

### **Because Our Consolidated Financial Statements Reflect Fresh-Start Reporting Adjustments Made upon Our Emergence from Bankruptcy, Financial Information in Our Current and Future Financial Statements Will Not Be Comparable to Our Financial Information for Periods Prior to Our Emergence from Bankruptcy.**

As a result of adopting fresh-start reporting on July 31, 2004, the carrying values of our wireless licenses and our property and equipment, and the related depreciation and amortization expense, among other things, changed considerably from that reflected in our historical consolidated financial statements. Thus, our current and future balance sheets and results of operations will not be comparable in many respects to our balance sheets and consolidated statements of operations data for periods prior to our adoption of fresh-start reporting. You are not able

to compare information reflecting our post-emergence balance sheet data, results of operations and changes in financial condition to information for periods prior to our emergence from bankruptcy without making adjustments for fresh-start reporting.

**Table of Contents**

**If We Experience High Rates of Credit Card, Subscription or Dealer Fraud, Our Ability to Become Profitable Will Decrease.**

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

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

**Our Stock Price May Be Volatile, and You May Lose All or Some of Your Investment.**

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

variations in our operating results;

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

recruitment or departure of key personnel;

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

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

**The 16,460,077 Shares of Leap Common Stock Registered for Resale By Our Shelf Registration Statement May Adversely Affect The Market Price of Leap's Common Stock.**

As of November 1, 2006, 67,763,650 shares of Leap common stock were issued and outstanding. Our resale shelf Registration Statement, as amended, registers for resale 16,460,077 shares, or approximately 24.3%, of Leap's outstanding common stock. We are unable to predict the potential effect that sales into the market of any material portion of such shares may have on the then prevailing market price of Leap's common stock. If any of Leap's stockholders cause a large number of securities to be sold in the public market, these sales could reduce the trading price of Leap's common stock. These sales also could impede our ability to raise future capital.

**Your Ownership Interest in Leap Will Be Diluted Upon Issuance of Shares We Have Reserved for Future Issuances, and Future Issuances or Sales of Such Shares May Adversely Affect The Market Price of Leap's Common Stock.**

As of November 1, 2006, 67,763,650 shares of Leap common stock were issued and outstanding, and 4,876,350 additional shares of Leap common stock were reserved for issuance, including 3,497,361 shares reserved for issuance upon exercise of awards granted or available for grant under Leap's 2004 Stock Option, Restricted Stock and Deferred Stock Unit Plan, 778,989 shares reserved for issuance under Leap's Employee Stock Purchase Plan, and 600,000 shares reserved for issuance upon exercise of outstanding warrants.

In addition, Leap has reserved five percent of its outstanding shares, which was 3,388,183 shares as of November 1, 2006, for potential issuance to CSM upon the exercise of CSM's option to put its entire equity interest in LCW Wireless to Cricket. Under the amended and restated limited liability company agreement with CSM and WLPCS Management, LLC, or WLPCS, the purchase price for CSM's equity interest is calculated on a pro rata basis using either the appraised value of LCW Wireless or a multiple of Leap's enterprise value divided by its adjusted EBITDA and applied to LCW Wireless' adjusted EBITDA to impute an enterprise value and equity value for LCW Wireless. Cricket may satisfy the put price either in cash or in Leap common stock, or a combination thereof, as determined by Cricket in its discretion. However, the covenants in the Credit Agreement do not permit Cricket to satisfy any substantial portion of its put obligations to CSM in cash. If Cricket elects to satisfy its put

## **Table of Contents**

obligations to CSM with Leap common stock, the obligations of the parties are conditioned upon the block of Leap common stock issuable to CSM not constituting more than five percent of Leap's outstanding common stock at the time of issuance. Dilution of the outstanding number of shares of Leap's common stock could adversely affect prevailing market prices for Leap's common stock.

We have agreed to prepare and file a resale shelf registration statement for any shares of Leap common stock issued to CSM in connection with the put, and to use our reasonable efforts to cause such registration statement to be declared effective by the SEC. See Item 1. Business Arrangements with LCW Wireless in our Annual Report on Form 10-K for the year ended December 31, 2005 for further discussion of our arrangements with LCW Wireless. In addition, we have registered all shares of common stock that we may issue under our stock option, restricted stock and deferred stock unit plan and under our employee stock purchase plan. When we issue shares under these stock plans, they can be freely sold in the public market. If any of Leap's stockholders cause a large number of securities to be sold in the public market, these sales could reduce the trading price of Leap's common stock. These sales also could impede our ability to raise future capital.

### **Our Directors and Affiliated Entities Have Substantial Influence over Our Affairs.**

Our directors and entities affiliated with them beneficially owned in the aggregate approximately 24.6% of Leap common stock as of November 1, 2006. These stockholders have the ability to exert substantial influence over all matters requiring approval by our stockholders. These stockholders will be able to influence the election and removal of directors and any merger, consolidation or sale of all or substantially all of Leap's assets and other matters. This concentration of ownership could have the effect of delaying, deferring or preventing a change in control or impeding a merger or consolidation, takeover or other business combination.

### **Provisions in Our Amended and Restated Certificate of Incorporation and Bylaws or Delaware Law Might Discourage, Delay or Prevent a Change in Control of Our Company or Changes in Our Management and, Therefore, Depress The Trading Price of Our Common Stock.**

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

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

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

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

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

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

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

may discourage, delay or prevent a change in control of our company.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

None.



**Table of Contents**

**Item 3. Defaults Upon Senior Securities.**

None.

**Item 4. Submission of Matters to a Vote of Security Holders.**

None.

**Item 5. Other Information.**

None.

**Item 6. Exhibits.**

*Index to Exhibits:*

<b>Exhibit Number</b>	<b>Description of Exhibit</b>
4.1(1)	Confirmation of Forward Sale Transaction, dated August 15, 2006, by and between Leap Wireless International, Inc. and Goldman Sachs Financial Markets, L.P.
4.2(1)	Confirmation of Forward Sale Transaction, dated August 15, 2006, by and between Leap Wireless International, Inc. and Citibank, N.A.
4.3(2)	Indenture, dated as of October 23, 2006, by and among Cricket Communications, Inc., the Initial Guarantors (as defined therein) and Wells Fargo Bank, N.A., as trustee.
4.4(2)	Registration Rights Agreement, dated as of October 23, 2006, by and among Cricket Communications, Inc., the Guarantors (as defined therein), Citigroup Global Markets Inc. and Goldman, Sachs & Co., as representatives of the Initial Purchasers named therein.
10.1*	Amendment No. 6 to Amended and Restated System Equipment Purchase Agreement, effective as of August 31, 2006, by and between Cricket Communications, Inc. and Nortel Networks Inc.
10.2*	Amendment No. 7 to Amended and Restated System Equipment Purchase Agreement, effective as of October 18, 2006, by and between Cricket Communications, Inc. and Nortel Networks Inc.
10.3*	Letter Amendment to the Amended and Restated Security Agreement dated as of June 16, 2006 by and among Cricket Communications, Inc., Leap Wireless International, Inc. and Bank of America, N.A., as administrative agent, dated October 16, 2006
10.4(3)	Credit Agreement, dated as of July 13, 2006, by and among Cricket Communications, Inc., Denali Spectrum License, LLC and Denali Spectrum, LLC.
10.4.1*	Amendment No. 1 to Credit Agreement by and among Cricket Communications, Inc., Denali Spectrum License, LLC and Denali Spectrum, LLC, dated as of September 28, 2006, between Cricket Communications, Inc., Denali Spectrum License, LLC and Denali Spectrum, LLC.
10.5(4)	Bridge Credit Agreement, dated August 8, 2006, by and among Cricket Communications, Inc., Leap Wireless International, Inc., the lenders party thereto and Citicorp North America, Inc., as administrative agent.
10.5.1(4)	Parent Guaranty, dated August 8, 2006, made by Leap Wireless International, Inc. in favor of the lenders under the Bridge Credit Agreement.
10.5.2(4)	Subsidiary Guaranty, dated August 8, 2006, made by the Subsidiary Guarantors in favor of the lenders under the Bridge Credit Agreement.

- 10.5.3\* Letter Amendment to the Bridge Credit Agreement dated as of August 8, 2006 by and among Cricket Communications, Inc., Leap Wireless International, Inc., Citicorp North America, Inc., as administrative agent, and the lenders party thereto, dated October 12, 2006.
- 31.1\*\* Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2\*\* Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32\*\*\* Certifications of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

\* Filed previously.

\*\* Filed herewith.

**Table of Contents**

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

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

- (1) Filed as an exhibit to Leap's Current Report on Form 8-K, dated August 15, 2006, filed with the SEC on October 30, 2006, and incorporated herein by reference.
- (2) Filed as an exhibit to Leap's Current Report on Form 8-K, dated October 23, 2006, filed with the SEC on October 24, 2006, and incorporated herein by reference.
- (3) Filed as an exhibit to Leap's Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2006, as filed with the SEC on August 8, 2006, and incorporated herein by reference.
- (4) Filed as an exhibit to Leap's Current Report on Form 8-K, dated August 8, 2006, filed with the SEC on August 10, 2006, and incorporated herein by reference.

**Table of Contents**

**SIGNATURES**

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

LEAP WIRELESS INTERNATIONAL, INC.

By:  
/s/ Amin I. Khalifa

AMIN I. KHALIFA  
Executive Vice President and  
Chief Financial Officer  
(Principal Financial Officer)

Date: December 4, 2006