

Neonode, Inc
Form S-3/A
August 26, 2008

AS FILED WITH THE SECURITIES AND EXCHANGE COMMISSION ON AUGUST 26, 2008

REGISTRATION NO. 333-152163

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

**AMENDMENT NO. 1
TO
FORM S-3**

**REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933**

NEONODE INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

94-1517641

(I.R.S. Employer Identification Number)

**Warfvingsväg 45
SE-112 51 Stockholm
Sweden**

+468 678 18 50

(Address, including zip code, and telephone number, including area code,
of registrant's principal executive offices)

**David Brunton
Chief Financial Officer
Neonode Inc.**

**4000 Executive Parkway, Suite 200
San Ramon, CA 94583
(925) 355-7700**

(Address, including zip code, and telephone number, including area code, of agent for service)

Copies to:

Don Reinke, Esq.
Reed Smith LLP
Two Embarcadero Center, Suite 2000
San Francisco, California 94111
(415) 543-8700

Approximate date of commencement of proposed sale to the public: From time to time after the effective date of this registration statement, as determined by the selling stockholders.

If the only securities being registered on this Form are being offered pursuant to dividend or interest reinvestment plans, please check the following box:

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, as amended, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box. x

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this Form is a registration statement pursuant to General Instruction I.D. or a post-effective amendment thereto that shall become effective upon filing with the Commission pursuant to Rule 462(e) under the Securities Act, check the following box. o

If this Form is a post-effective amendment to a registration statement filed pursuant to General Instruction I.D. filed to register additional securities or additional classes of securities pursuant to Rule 413(b) under the Securities Act, check the following box. o

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

Large accelerated filer <input type="checkbox"/> o	Accelerated filer <input type="checkbox"/> o
Non-accelerated filer <input type="checkbox"/> o	Smaller reporting company <input checked="" type="checkbox"/> x

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to Section 8(a), may determine.

The information in this preliminary prospectus is not complete and may be changed. The selling stockholders may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities, and the selling stockholders are not soliciting offers to buy these securities, in any jurisdiction where the offer or sale of these securities is not permitted.

SUBJECT TO COMPLETION, DATED AUGUST 26, 2008

PROSPECTUS

6,408,480 SHARES

COMMON STOCK

This prospectus relates to the resale of (i) 1,662,467 shares of common stock, \$0.001 par value per share ("Common Stock"), of Neonode Inc., a Delaware corporation, and (ii) 4,746,013 shares of Common Stock issuable upon the exercise of warrants, that the selling stockholders named in this prospectus or any prospectus supplement may offer from time to time. The selling stockholders are those holders named in the table under the section entitled "Selling Stockholders" beginning on page 15 of this prospectus or named in a supplement to this prospectus.

We will not receive any of the proceeds from the sale of the shares of our common stock by the selling stockholders, although we may receive proceeds from the exercise of warrants for shares of our common stock. We will bear the cost of the registration of these shares.

Subject to the restrictions described in this prospectus, the selling stockholders (directly, or through agents or dealers designated from time to time) may sell the shares of our common stock being offered by this prospectus from time to time, on terms to be determined at the time of sale. The prices at which these selling stockholders may sell the shares will be determined by the prevailing market price for the shares or in negotiated transactions.

Our common stock is listed on the NASDAQ Capital Market under the symbol "NEON." On August 25, 2008, the last reported sales price of our common stock, as reported on the NASDAQ Capital Market, was \$0.24 per share.

INVESTING IN OUR COMMON STOCK INVOLVES SUBSTANTIAL RISKS. SEE THE SECTION ENTITLED "RISK FACTORS" BEGINNING ON PAGE 4 OF THIS PROSPECTUS TO READ ABOUT FACTORS YOU SHOULD CONSIDER BEFORE BUYING SHARES OF OUR COMMON STOCK.

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED OF THESE SECURITIES OR PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The date of this prospectus is _____, 2008.

Table of Contents

	Page
About This Prospectus	1
Prospectus Summary	2
Risk Factors	4
Cautionary Statement Concerning Forward-Looking Information	14
Use of Proceeds	14
Selling Stockholders	15
Relationship of Selling Stockholders to the Company	21
Plan of Distribution	22
Legal Matters	23
Experts	23
Where You Can Find More Information	24
Incorporation of Certain Documents by Reference	24

You should rely only on the information contained or incorporated by reference in this prospectus and in any prospectus supplement hereto. We have not authorized, and the selling stockholders may not authorize, any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not, and the selling stockholders are not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in this prospectus is accurate only as of the date on the front cover of this prospectus. Our business, financial condition, results of operations and prospectus may have changed since that date.

ABOUT THIS PROSPECTUS

This prospectus is part of a registration statement on Form S-3 that we filed with the Securities and Exchange Commission, or SEC, on behalf of the selling stockholders, who are named in the table under the section entitled “Selling Stockholders” beginning on page 15 of this prospectus, using a “shelf” registration or continuous offering process. Under this shelf registration process, the selling stockholders may from time to time until the registration statement is withdrawn from registration by us, sell the shares of our common stock being offered pursuant to this prospectus in one or more offerings.

This prospectus provides you with a general description of the securities that the selling stockholders may offer. To the extent required, the number of shares of our common stock to be sold, the purchase price, the public offering price, the names of any agent or dealer and any applicable commission or discount with respect to a particular offering by any selling stockholder may be set forth in an accompanying prospectus supplement. The prospectus supplement may also add, update or change information contained in this prospectus. You should read both this prospectus and any prospectus supplement together with the additional information described in the section entitled “Where You Can Find More Information.”

To the extent permitted by applicable law, rules or regulations, we may add, update or change the information contained in this prospectus by means of a prospectus supplement or post-effective amendments to the registration statement of which this prospectus forms a part, through filings we make with the SEC that are incorporated by reference into this prospectus or by another method as may then be permitted under applicable law, rules or regulations.

You should rely only on the information contained in this prospectus or any related prospectus supplement, including the content of all documents now or in the future incorporated by reference into the registration statement of which this prospectus forms a part. The selling stockholders may not authorize anyone to provide you with different information. We are not, and the selling stockholders are not, making an offer of the shares of our common stock to be sold under this prospectus in any jurisdiction where the offer or sale is not permitted. You should not assume that the information contained in this prospectus or any related prospectus supplement is accurate as of any date other than the date on the front cover of this prospectus or the related prospectus supplement, or that the information contained in any document incorporated by reference is accurate as of any date other than the date of the document incorporated by reference. Other than as required under the federal securities laws, we undertake no obligation to publicly update or revise such information, whether as a result of new information, future events or any other reason.

PRIOR TO MAKING A DECISION ABOUT INVESTING IN OUR COMMON STOCK, YOU SHOULD CAREFULLY CONSIDER THE SPECIFIC RISKS CONTAINED IN THE SECTION ENTITLED “RISK FACTORS” IN THIS PROSPECTUS, AND ANY APPLICABLE PROSPECTUS SUPPLEMENT, TOGETHER WITH ALL OF THE OTHER INFORMATION CONTAINED IN THIS PROSPECTUS AND ANY PROSPECTUS SUPPLEMENT OR APPEARING IN THE REGISTRATION STATEMENT OF WHICH THIS PROSPECTUS FORMS A PART.

In this prospectus, we refer to Neonode Inc. as “we,” “us,” “our,” the “company” or “Neonode.” References to “selling stockholders” refers to those holders of our common stock listed herein under “Selling Stockholders,” who may sell shares from time to time as described in this prospectus. All trade names used in this prospectus are either our registered trademarks or trademarks of their respective holders.

PROSPECTUS SUMMARY

The following is only a summary and therefore does not contain all of the information you should consider before investing in our securities. We urge you to read this entire prospectus, including the more detailed consolidated financial statements, notes to the consolidated financial statements and other information incorporated by reference herein, carefully. See “Where You Can Find More Information” on page 24 for information regarding the documents incorporated by reference herein. In addition, investing in our common stock involves risks. You should carefully consider the information provided under the heading “Risk Factors” beginning on page 4.

Overview

Historically, we designed, manufactured and sold embedded communications hardware and storage software products. Our hardware business generated the overwhelming majority of our sales and cash flow. Our business was characterized by a concentration of sales to a small number of OEMs and distributors who provide products and services to the communications and data storage markets. On March 30, 2007, we sold our hardware business to One Stop Systems, Inc. for \$2.2 million in cash. We received \$1.7 million of the cash on the date of the sale and an additional \$500,000 in cash on June 5, 2007. In addition, One Stop assumed the lease for the building housing our San Ramon offices and certain equipment leases. As part of the sale, we transferred our entire inventory and the engineering and test equipment used to support the hardware business to One Stop. As of March 30, 2007, we no longer participate in the embedded communications hardware business.

On August 10, 2007, we completed a merger with Old Neonode, a Delaware corporation, pursuant to the terms of the Agreement and Plan of Merger and Reorganization, dated January 19, 2007 and amended on May 16, 2007, referred to in this prospectus as the Merger Agreement. The merger was treated as a recapitalization and issuance of shares by Old Neonode for the net cash of SBE for accounting purposes and as such, the historical financial statements of Old Neonode became the historical financial statements of New Neonode. As a result of the merger, we changed our name from “SBE, Inc.” to “Neonode Inc.” Effective as of the merger, the business and operations of Old Neonode prior to the merger became our primary business and operations. Unless the context otherwise requires, all references herein to “Neonode” refer to Private Neonode prior to the Merger, and Neonode Inc. (formally known as SBE, Inc.) and its wholly-owned subsidiaries after the Merger.

Our business is now focused on a combination of licensing our touchscreen technology to other companies and developing and selling our own products using our technology in mobile device markets. The cornerstone of our business is our innovative patent pending touchscreen solutions. We believe that in the future keyboards and keypads with moving parts will become obsolete and that our touchscreen solutions and technologies will be at the forefront of a new wave of input technologies that will be able to run everything from small mobile devices to large industrial applications.

We believe our current product, the Neonode N2, is the world’s smallest touchscreen mobile phone handset. The N2 fits in the palm of your hand and is designed to allow the user to navigate the menus and functions with simple finger-based taps and sweeps. The N2 incorporates our patent pending touchscreen and other proprietary technologies to deliver a mobile phone with a completely unique user experience that doesn’t require keypads, buttons or other moving parts.

The first model of our touchscreen multimedia mobile phone, the N1, was released in November 2004. The N1 was primarily a concept phone that was sold in limited quantities from late 2004 to early 2006. The N2 is our first production-quality product. We began shipping the N2 to customers in mid-July 2007 and resumed shipments of the N2 in the second quarter of 2008 following our voluntary recall and stopping shipments in the first quarter of 2008.

Corporate Headquarters

As a result of the merger with Old Neonode, our corporate headquarters moved to Stockholm, Sweden, although we continue to maintain a U.S. office in San Ramon, California. Our headquarters are located at Warfvingesväg 45, SE-112 51 Stockholm, Sweden and our telephone number at this address is 468 678 18 50. Our office in the U.S. is located at 4000 Executive Parkway, Suite 200, San Ramon, California 94583 and our telephone number at this address is (925) 355-7700. Our website address is www.neonode.com. Information contained on our website, or that can be accessed through our website, is not a part of this prospectus.

- 2 -

See the section entitled “Where You Can Find More Information” on page 24.

The Offering

This prospectus relates to the resale by certain selling stockholders of up to 6,408,480 shares of our common stock, including 4,746,013 shares issuable upon the exercise of certain warrants to purchase shares of our common stock. The number of shares (and shares issuable upon exercise of warrants) being registered represents 18.4% of our shares issued and outstanding and 49.5% of our shares issued and outstanding held by persons other than the selling stockholders, affiliates of our Company or affiliates of the selling stockholders, in each case based on 29,979,493 shares of common stock issued and outstanding as of August 12, 2008 (and assuming the exercise of the warrants for the shares being registered hereby). We will not receive any proceeds from the sale of securities by the selling stockholders listed herein.

The selling stockholders may sell the shares of common stock subject to this prospectus from time to time and may also decide not to sell all the shares they are allowed to sell under this prospectus. The selling stockholders will act independently of us in making decisions with respect to the timing, manner and size of each sale. Furthermore, the selling stockholders may effectuate such transactions by selling the securities to or through broker-dealers, and such broker-dealers may receive compensation in the form of discounts, concessions or commissions from the selling stockholders and/or the purchasers of the securities for whom such broker-dealers may act as agent or to whom they sell as principal, or both. The selling stockholders may be deemed to be “underwriters,” as defined in the Securities Act. If any broker-dealers are used by the selling stockholders, any commissions paid to broker-dealers and, if broker-dealers purchase any selling stockholders’ securities as principals, any profits received by such broker-dealers on the resale of the selling stockholders’ securities may be deemed to be underwriting discounts or commissions under the Securities Act. In addition, any profits realized by the selling stockholders may be deemed to be underwriting commissions. All costs, expenses and fees in connection with the registration of the selling stockholders’ securities offered by selling stockholders will be borne by us. Brokerage commission, if any, attributable to the sale of the selling stockholders’ securities will be borne by the selling stockholders. Based on information provided to us by the selling stockholders, to our knowledge, none of the selling stockholders have an existing short position in our common stock as of the date of this prospectus.

See the section entitled “Plan of Distribution” beginning on page 22.

Our common stock is traded on the NASDAQ Capital Market under the symbol “NEON.” Our common stock is currently at risk for delisting from the NASDAQ Capital Market. See “Risk Factors – Risks Related to Our Business” for more information regarding this risk.

RISK FACTORS

An investment in our common stock involves a high degree of risk. Before investing in our common stock, you should consider carefully the specific risks detailed in this “Risk Factors” section and any applicable prospectus supplement, together with all of the other information contained in this prospectus and any prospectus supplement or incorporated by reference herein or therein. If any of these risks occur, our business, results of operations and financial condition could be harmed, the price of our common stock could decline, and you may lose all or part of your investment.

RISKS RELATED TO OUR BUSINESS

We will require additional capital in the future to fund our operations, which capital may not be available on commercially attractive terms or at all.

We will require sources of capital in addition to cash on hand to continue operations and to implement our strategy. In March 2008, we closed an aggregate of \$4.0 million, net of offering expenses, of private equity financing and in May 2008, we closed an aggregate of \$4.2 million, net of offering expenses, of private equity financing. We project that we have sufficient liquid assets to continue operating into the end of the third quarter of 2008. We estimate that we will need a minimum of approximately \$7 million to \$10 million of additional cash from a combination of revenue growth and additional financings to fund operating expenses and capital expenditures for the twelve-months ending June 30, 2009. We are currently evaluating different financing alternatives including, but not limited to, selling shares of our common stock or issuing notes that may be converted in shares of our common stock, which could result in the issuance of additional shares. If our operations do not become cash flow positive as projected, we will be forced to seek credit line facilities from financial institutions, additional private equity investment or debt arrangements. No assurances can be given that we will be successful in obtaining such additional financing on reasonable terms, or at all. If adequate funds are not available on acceptable terms, or at all, we may be unable to adequately fund our business plans and it could have a negative effect on our business, results of operations and financial condition. We may even be required to cease operations. In such event, you may lose a portion or all of your investment. In addition, if funds are available, the issuance of equity securities or securities convertible into equity could dilute the value of shares of our common stock and cause the market price to fall, and the issuance of debt securities could impose restrictive covenants that could impair our ability to engage in certain business transactions.

Our common stock is at risk for delisting from the NASDAQ Capital Market. If it is delisted, our stock price and your liquidity may be impacted.

Our common stock is listed on the NASDAQ Capital Market under the symbol NEON. In order for our common stock to continue to be listed on the NASDAQ Capital Market, we must satisfy various listing maintenance standards established by NASDAQ. Among other things, as such requirements pertain to us, we are required to have stockholders' equity of at least \$2.5 million or a market capitalization of \$35 million and our common stock must have a minimum closing bid price of \$1.00 per share. On May 29, 2008, we received a NASDAQ Staff deficiency letter indicating that the market value of our listed securities had been below the minimum \$35 million requirement for continued inclusion under its listing standards (the “Market Capitalization Rule”), and provided us until June 30, 2008 to demonstrate compliance. On July 1, 2008, we received a NASDAQ Staff Determination letter stating that we had not regained compliance with the Market Capitalization Rule and, unless we request an appeal of this determination, trading of our common stock will be suspended at the opening of business on July 10, 2008 and NASDAQ will remove our securities from listing and registration on the NASDAQ Capital Market. We have requested an appeal of the determination with the NASDAQ Listing Qualifications Panel (the “Panel”), which stays the suspension of our securities pending the Panel's decision and are scheduled to appear before the Panel on August 28, 2008. In addition, on July 3, 2008, we received a NASDAQ Staff deficiency letter indicating that for the last 30 consecutive days, the bid price for our common stock had closed below the \$1.00 minimum requirement for continued inclusion under its listing standards (the “Minimum Bid Price Rule”), and provided us 180 days (or until December 30, 2008) to regain

compliance. In light of the recent closing bid prices for shares of our common stock and our results of operations, there is no guarantee that we will be able to meet the continued listing standards of the NASDAQ Capital Market during this period of time and there can be no assurance that the Panel will grant our appeal. If our appeal is not successful, our common stock will be delisted from the NASDAQ Capital Market and our stock price and your liquidity may be impacted.

Our vendors may deny our requests to delay or reduce the payment of amounts owed to them or to cancel shipments of materials and products purchased from and to allow us to return unused materials and products already received from them.

We are indebted to vendors in excess of \$8 million and have cash resources totaling \$2.1 million at June 30, 2008. We are not generating cash from operations and have been incurring significant losses. We have been funding our operations primarily with cash proceeds raised through the sale of notes that are convertible into our common stock, shares of our common stock and warrants. Unless we are able to increase our revenues and decrease expenses substantially and secure an external funding source, we may not be able to pay our vendors the amount due them and we will not have sufficient cash to support our operations for the next six months.

Our vendors may not allow us to return unused materials or renegotiate amounts owed them, or they may resort to legal action to try to enforce payment in full pursuant to the terms or the original payment commitment.

- 4 -

Our independent registered public accounting firm issued a going concern opinion on our financial statements, questioning our ability to continue as a going concern.

Due to our need to raise additional financing to fund our operations and satisfy obligations as they become due, our independent registered public accounting firm has included an explanatory paragraph in its report on our December 31, 2007 consolidated financial statements regarding its substantial doubt as to our ability to continue as a going concern. This may have a negative impact on the trading price of our common stock and adversely impact our ability to obtain necessary financing.

We have never been profitable and we anticipate significant additional losses in the future.

Neonode was formed in 2006 as a holding company owning and operating Neonode AB, which was formed in 2004 and has been primarily engaged in the business of developing and selling mobile phones. We have a limited operating history on which to base an evaluation of our business and prospects. Our prospects must be considered in light of the risks and uncertainties encountered by companies in the early stages of development, particularly companies in new and rapidly evolving markets. Our success will depend on many factors, including, but not limited to:

- the growth of mobile telephone usage;
- the efforts of our marketing partners;
- the level of competition faced by us; and
- our ability to meet customer demand for products and ongoing service.

In addition, we have experienced substantial net losses in each fiscal period since our inception. These net losses resulted from a lack of substantial revenues and the significant costs incurred in the development of our products and infrastructure. Our ability to continue as a going concern is dependent on our ability to raise additional funds and implement our business plan. In addition, in accordance with Swedish law, our subsidiary, Neonode AB, is required to maintain positive shareholder equity, and in certain circumstances, its board members may incur personal liability if such requirement is not met, or it may face forced liquidation. We are currently addressing this issue, and are considering raising additional equity sufficient to restore shareholder equity to a positive balance.

Our limited operating history and the emerging nature of our market, together with the other risk factors set forth in this report, make prediction of our future operating results difficult. There can also be no assurance that we will ever achieve significant revenues or profitability or, if significant revenues and profitability are achieved, that they could be sustained.

If we fail to develop and introduce new products and services successfully and in a cost effective and timely manner, we will not be able to compete effectively and our ability to generate revenues will suffer.

We operate in a highly competitive, rapidly evolving environment, and our success depends on our ability to develop and introduce new products and services that our customers and end users choose to buy. If we are unsuccessful at developing and introducing new products and services that are appealing to our customers and end users with acceptable quality, prices and terms, we will not be able to compete effectively and our ability to generate revenues will suffer.

The development of new products and services is very difficult and requires high levels of innovation. The development process is also lengthy and costly. If we fail to anticipate our end users' needs or technological trends accurately, or we are unable to complete the development of products and services in a cost effective and timely fashion, we will be unable to introduce new products and services into the market or successfully compete with other providers. In addition, there may be unexpected problems with our new products. For example, we stopped shipments of our N2 phones in the first quarter of 2008 and undertook a voluntary recall after we discovered a technical issue that affected the quality of reception of our phones in the 900 Megahertz bandwidth and lower. Although we corrected

the problem and resumed shipments in the second quarter of 2008, we nevertheless have since had to reevaluate our selling efforts, and had to record a \$7.7 million write-down of our inventory in the second quarter of 2008 (reducing the value of our inventory to \$6.0 million as at June 30, 2008).

As we introduce new or enhanced products or integrate new technology into new or existing products, we face risks including, among other things, disruption in customers' ordering patterns, excessive levels of older product inventories, inability to deliver sufficient supplies of new products to meet customers' demand, possible product and technology defects, and a potentially different sales and support environment. Premature announcements or leaks of new products, features or technologies may exacerbate some of these risks. Our failure to manage the transition to newer products or the integration of newer technology into new or existing products could adversely affect our business, results of operations and financial condition.

We are dependent on third parties to manufacture and supply our products and components of our products.

Our products are built by a production partner. Although we provide our production partner with key performance specifications for the phones, our production partner could:

- manufacture phones with defects that fail to perform to our specifications;
- fail to meet delivery schedules; or
- fail to properly service phones or honor warranties.

Any of the foregoing could adversely affect our ability to sell our products and services, which, in turn, could adversely affect our revenues, profitability and liquidity, as well as our brand image.

We may become highly dependent on wireless carriers for the success of our products.

Our business strategy includes significant efforts to establish relationships with international wireless carriers. We cannot assure you that we will be successful in establishing new relationships, or maintaining such relationships, with wireless carriers or that these wireless carriers will act in a manner that will promote the success of our multimedia phone products. Factors that are largely within the control of wireless carriers, but which are important to the success of our multimedia phone products, include:

- testing of our products on wireless carriers' networks;
- quality and coverage area of wireless voice and data services offered by the wireless carriers;
- the degree to which wireless carriers facilitate the introduction of and actively market, advertise, promote, distribute and resell our multimedia phone products;
- the extent to which wireless carriers require specific hardware and software features on our multimedia phone to be used on their networks;
- timely build out of advanced wireless carrier networks that enhance the user experience for data centric services through higher speed and other functionality;
- contractual terms and conditions imposed on them by wireless carriers that, in some circumstances, could limit our ability to make similar products available through competitive carriers in some market segments;
- wireless carriers' pricing requirements and subsidy programs; and
- pricing and other terms and conditions of voice and data rate plans that the wireless carriers offer for use with our multimedia phone products.

For example, flat data rate pricing plans offered by some wireless carriers may represent some risk to our relationship with such carriers. While flat data pricing helps customer adoption of the data services offered by carriers and therefore highlights the advantages of the data applications of its products, such plans may not allow its multimedia phones to contribute as much average revenue per user to wireless carriers as when they are priced by usage, and therefore reduces our differentiation from other, non-data devices in the view of the carriers. In addition, if wireless carriers charge higher rates than consumers are willing to pay, the acceptance of our wireless solutions could be less than anticipated and our revenues and results of operations could be adversely affected.

Wireless carriers have substantial bargaining power as we enter into agreements with them. They may require contract terms that are difficult for us to satisfy, which could result in higher costs to complete certification requirements and negatively impact our results of operations and financial condition. Moreover, we may not have agreements with some of the wireless carriers with whom they will do business and, in some cases, the agreements may be with third-party distributors and may not pass through rights to us or provide us with recourse or contact with the carrier. The absence of agreements means that, with little or no notice, these wireless carriers could refuse to continue to purchase all or some of our products or change the terms under which they purchase our products. If these wireless carriers were to stop purchasing our products, we may be unable to replace the lost sales channel on a timely basis and our results of operations could be harmed.

Wireless carriers could also significantly affect our ability to develop and launch products for use on their wireless networks. If we fail to address the needs of wireless carriers, identify new product and service opportunities, or modify or improve our multimedia phone products in response to changes in technology, industry standards or wireless carrier requirements, our products could rapidly become less competitive or obsolete. If we fail to timely develop products that meet carrier product planning cycles or fail to deliver sufficient quantities of products in a timely manner to wireless carriers, those carriers may choose to emphasize similar products from our competitors and thereby reduce their focus on its products which would have a negative impact on our business, results of operations

and financial condition.

Carriers, who control most of the distribution and sale of, and virtually all of the access for, multimedia phone products could commoditize multimedia phones, thereby reducing the average selling prices and margins for our products which would have a negative impact on our business, results of operations and financial condition. In addition, if carriers move away from subsidizing the purchase of mobile phone products, this could significantly reduce the sales or growth rate of sales of mobile phone products. This could have an adverse impact on our business, revenues and results of operations.

- 6 -

As we build strategic relationships with wireless carriers, we may be exposed to significant fluctuations in revenue for our multimedia phone products.

Because of their large sales channels, wireless carriers may purchase large quantities of our products prior to launch so that the products are widely available. Reorders of products may fluctuate quarter to quarter, depending on end-customer demand and inventory levels required by the carriers. As we develop new strategic relationships and launch new products with wireless carriers, our revenue could be subject to significant fluctuation based on the timing of carrier product launches, carrier inventory requirements, marketing efforts and our ability to forecast and satisfy carrier and end-customer demand. We do not have a history of selling to wireless carriers and as a result do not have a basis for estimating what the potential fluctuations in our revenue will be from the sale of our multimedia phones.

The mobile communications industry is highly competitive and many of our competitors have significantly greater resources to engage in product development, manufacturing, distribution and marketing.

The mobile communications industry, in which we are engaged, is a highly competitive business with companies of all sizes engaged in business in all areas of the world, including companies with far greater resources than we have. There can be no assurance that other competitors, with greater resources and business connections, will not compete successfully against us in the future. Our competitors may adopt new technologies that reduce the demand for our products or render our technologies obsolete, which may have a material adverse effect on the cost structure and competitiveness of our products, possibly resulting in a negative effect on our revenues, profitability or liquidity.

Our future results could be harmed by economic, political, regulatory and other risks associated with international sales and operations.

Because we sell our products worldwide and most of the facilities where our devices are manufactured, distributed and supported are located outside the United States, our business is subject to risks associated with doing business internationally, such as:

- changes in foreign currency exchange rates;
- the impact of recessions in the global economy or in specific sub economies;
- changes in a specific country's or region's political or economic conditions, particularly in emerging markets;
- changes in international relations;
- trade protection measures and import or export licensing requirements;
- changes in tax laws;
- compliance with a wide variety of laws and regulations which may have civil and/or criminal consequences for them and our officers and directors who they indemnify;
- difficulty in managing widespread sales operations; and
- difficulty in managing a geographically dispersed workforce in compliance with diverse local laws and customs.

In addition, we are subject to changes in demand for our products resulting from exchange rate fluctuations that make our products relatively more or less expensive in international markets. If exchange rate fluctuations occur, our business and results of operations could be harmed by decreases in demand for our products or reductions in margins.

While we sell our products worldwide, one component of our strategy is to expand our sales efforts in countries with large populations and propensities for adopting new technologies. We have limited experience with sales and marketing in some of these countries. There can be no assurance that we will be able to market and sell our products in all of our targeted international markets. If our international efforts are not successful, our business growth and results of operations could be harmed.

We must significantly enhance our sales and product development organizations.

We will need to improve the effectiveness and breadth of our sales operations in order to increase market awareness and sales of our products, especially as we expand into new markets. Competition for qualified sales personnel is intense, and we may not be able to hire the kind and number of sales personnel we are targeting. Likewise, our efforts to improve and refine our products require skilled engineers and programmers. Competition for professionals capable of expanding our research and development organization is intense due to the limited number of people available with the necessary technical skills. If we are unable to identify, hire or retain qualified sales, marketing and technical personnel, our ability to achieve future revenue may be adversely affected.

We are dependent on the services of our key personnel.