LEAP WIRELESS INTERNATIONAL INC
Form 10-Q
May 10, 2006

Table of Contents

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2006

OR

o **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 þ No o

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

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

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 þ No o

The number of shares of registrant s common stock outstanding on May 8, 2006 was 61,224,279.

LEAP WIRELESS INTERNATIONAL, INC.

QUARTERLY REPORT ON FORM 10-Q
For the Quarter Ended March 31, 2006

TABLE OF CONTENTS

Table of Contents

PART I
FINANCIAL INFORMATION

Item 1. Financial Statements.

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

	March 31, 2006 (Unaudited)	December 31, 2005
Assets		
Cash and cash equivalents	$ 299,976	$ 293,073
Short-term investments	65,975	90,981
Restricted cash, cash equivalents and short-term investments	10,687	13,759
Inventories	39,710	37,320
Other current assets	35,160	29,237
Total current assets	451,508	464,370
Property and equipment, net	642,858	621,946
Wireless licenses	821,339	821,288
Assets held for sale (Note 7)	15,135	15,145
Goodwill	431,896	431,896
Other intangible assets, net	105,123	113,554
Other assets	35,651	38,119
Total assets	$ 2,503,510	$ 2,506,318
Liabilities and Stockholders Equity		
Accounts payable and accrued liabilities	$ 136,460	$ 167,770
Current maturities of long-term debt (Note 4)	6,111	6,111
Other current liabilities	53,266	49,627
Total current liabilities	195,837	223,508
Long-term debt (Note 4)	586,806	588,333
Deferred tax liabilities	141,935	141,935
Other long-term liabilities	37,920	36,424
Total liabilities	962,498	990,200
Minority interest	2,463	1,761
Commitments and contingencies (Notes 4 and 8)		

Stockholders equity:		
Preferred stock authorized 10,000,000 shares; $.0001 par value, no shares issued and outstanding		
Common stock authorized 160,000,000 shares; $.0001 par value, 61,214,398 and 61,202,806 shares issued and outstanding at March 31, 2006 and December 31, 2005, respectively	6	6
Additional paid-in capital	1,494,974	1,490,638
Retained earnings	39,299	21,575
Accumulated other comprehensive income	4,270	2,138
Total stockholders equity	1,538,549	1,514,357
Total liabilities and stockholders equity	$ 2,503,510	$ 2,506,318

See accompanying notes to condensed consolidated financial statements.

1

Table of Contents

LEAP WIRELESS INTERNATIONAL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)
(In thousands, except per share data)

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005
Revenues:		
Service revenues	$ 215,840	$ 185,981
Equipment revenues	50,848	42,389
Total revenues	266,688	228,370
Operating expenses:		
Cost of service (exclusive of items shown separately below)	(55,204)	(50,197)
Cost of equipment	(58,886)	(49,178)
Selling and marketing	(29,102)	(22,995)
General and administrative	(49,582)	(36,035)
Depreciation and amortization	(54,036)	(48,104)
Total operating expenses	(246,810)	(206,509)
Operating income	19,878	21,861
Minority interest in loss of consolidated subsidiary	(75)	
Interest income	4,194	1,903
Interest expense	(7,431)	(9,123)
Other income (expense), net	535	(1,286)
Income before income taxes and cumulative effect of change in accounting principle	17,101	13,355
Income taxes		(5,839)
Income before cumulative effect of change in accounting principle	17,101	7,516
Cumulative effect of change in accounting principle (Note 2)	623	
Net income	$ 17,724	$ 7,516
Basic net income per share:		
Income before cumulative effect of change in accounting principle	$ 0.28	$ 0.13
Cumulative effect of change in accounting principle	0.01	
Basic net income per share	$ 0.29	$ 0.13
Diluted net income per share:		
Income before cumulative effect of change in accounting principle	$ 0.28	$ 0.12
Cumulative effect of change in accounting principle	0.01	

Diluted net income per share	$	0.29	$	0.12
Shares used in per share calculations:				
Basic		61,203		60,000
Diluted		61,961		60,236

See accompanying notes to condensed consolidated financial statements.

Table of Contents

LEAP WIRELESS INTERNATIONAL, INC.

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

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005
Operating activities:		
Net cash provided by operating activities	$ 38,290	$ 23,462
Investing activities:		
Purchases of property and equipment	(60,894)	(22,720)
Change in prepayments for purchases of property and equipment	4,573	(1,767)
Purchases of and deposits for wireless licenses	(91)	(212,095)
Purchases of investments	(46,865)	(69,025)
Sales and maturities of investments	72,657	83,568
Restricted cash, cash equivalents and short-term investments, net	(50)	407
Net cash used in investing activities	(30,670)	(221,632)
Financing activities:		
Proceeds from long-term debt		500,000
Repayments of long-term debt	(1,527)	(413,979)
Minority interest	668	
Issuance of stock	233	
Payment of debt issuance costs	(91)	(6,781)
Net cash provided by (used in) financing activities	(717)	79,240
Net increase (decrease) in cash and cash equivalents	6,903	(118,930)
Cash and cash equivalents at beginning of period	293,073	141,141
Cash and cash equivalents at end of period	$ 299,976	$ 22,211
Supplementary disclosure of cash flow information:		
Cash paid for interest	$ 11,098	$ 27,142
Cash paid for income taxes	$ 168	$ 52

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 through Alaska Native Broadband 1 License, LLC (ANB 1 License), a joint venture in which Cricket indirectly owns a 75% non-controlling interest, through a 75% non-controlling interest in Alaska Native Broadband 1, LLC (ANB 1). The Company consolidates its 75% non-controlling interest in ANB 1 (see Note 2).

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 quarter ended March 31, 2006, all of the Company s revenues and long-lived assets related to operations in the United States.

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 and its wholly owned subsidiary ANB 1 License. The Company consolidates its interest in ANB 1 in accordance with Financial Accounting Standards Board (FASB) Interpretation No. 46-R, Consolidation of Variable Interest Entities, because ANB 1 is a variable interest entity and the Company will absorb a majority of ANB 1 s expected losses. All significant intercompany accounts and transactions have been eliminated in the consolidated financial statements.

Revenues and Cost of 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. Amounts received in advance for wireless services from customers who pay in advance are initially recorded as deferred revenues and are recognized as service revenue as services are rendered. Service revenues for customers who pay in arrears are recognized only after the service has been rendered and payment has been received. This is because the Company does not require any of its customers to sign 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. The Company also charges customers for service plan changes, activation fees and other service fees. Revenues from service plan change fees are deferred and recorded to revenue over the estimated customer relationship period, and other service fees are recognized when received. Activation fees are allocated to the other elements of the multiple element arrangement (including service and equipment) on a relative fair value basis. Because the fair values of the Company s handsets are higher than the total consideration received for the handsets and activation fees combined, the Company allocates the activation fees entirely to equipment revenues and recognizes the activation fees when received. Activation fees included in equipment revenues during the three months ended March 31, 2006 and 2005 totaled $6.2 million and $4.6 million, respectively. Direct costs associated with customer activations are expensed as incurred. Cost of service generally includes direct costs and related overhead, excluding depreciation and amortization, of operating the Company s networks.

Equipment revenues arise from the sale of handsets and accessories, and activation fees as described above. Revenues and related costs from the sale of handsets are recognized when service is activated by customers. Revenues and related costs from the sale of accessories are recognized at the point of sale. The costs of handsets and accessories sold are recorded in cost of equipment. 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 for which to establish reliable estimates of returns, it will begin to recognize equipment revenues upon sale to third-party dealers and distributors.

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.

Starting in May 2006, all new and reactivating customers pay for their service in advance, and the Company no longer charges activation fees to new customers.

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 the rent of towers, network facilities, engineering operations, field technicians and related utility and maintenance charges and the salary and overhead charges associated with these functions.

Cost of Equipment. Cost of equipment 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 and promotional costs associated with acquiring new customers and store operating costs such as rent and retail associates salaries and overhead charges.

General and Administrative Expenses. General and administrative expenses primarily include 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, including interest and certain labor costs incurred during the construction period, are capitalized, while expenditures that do not enhance the asset or extend its useful life are charged to operating expenses as incurred. Interest is capitalized on the carrying values of both wireless licenses and equipment during the construction period. 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):

	Depreciable Life
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 and equipment category. As a component of construction-in-progress, the Company capitalizes interest and salaries and related costs of engineering and technical operations employees, to the extent time and expense are contributed to the construction effort, during the construction period. The Company capitalized $4.4 million of interest to property and equipment during the three months ended March 31, 2006. Starting on January 1, 2006, rental costs incurred during the construction period are recognized as rental expense in accordance with FASB Staff Position (FSP) 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 March 31, 2006 and December 31, 2005, property and equipment with a net book value of $5.4 million was classified in 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 required impairment loss would be measured as the amount by which the asset s carrying value exceeds its fair value and would be recorded as a reduction in the carrying value of the related asset and charged to results of operations.

Wireless Licenses

Wireless licenses are initially recorded at cost 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 the wireless licenses may be renewed every ten 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 March 31, 2006 and December 31, 2005, wireless licenses with a carrying value of $8.2 million were classified in 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 March 31, 2006 and December 31, 2005, intangible assets with a net book value of $1.5 million were classified in assets held for sale.

Table of Contents

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 would be measured as the amount by which the asset s carrying value exceeds its fair value. Any required impairment loss would be recorded as a reduction in the carrying value of the related asset and charged to results of operations. The Company conducts its annual tests for impairment during the third quarter of each year. 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.

Basic and Diluted Net Income 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 reflect the potential dilutive effect of additional common shares that are issuable upon exercise of outstanding stock options, restricted stock awards and warrants 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):

	Three Months Ended March 31, 2006	2005
Weighted average shares outstanding basic net income per share	61,203	60,000
Effect of dilutive securities:		
Non-qualified stock options	31	9
Restricted stock awards	381	
Warrants	346	227
Adjusted weighted average shares outstanding diluted net income per share	61,961	60,236

The number of shares not included in the computation of diluted net income per share because their effect would have been antidilutive totaled 1.3 million for the three months ended March 31, 2006. There were no antidilutive shares for the three months ended March 31, 2005.

Comprehensive Income

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

	Three Months Ended March 31,	
	2006	2005
Net income	$ 17,724	$ 7,516
Other comprehensive income:		
Net unrealized holding losses on investments, net of tax	(17)	(46)
Unrealized gains on derivative instruments, net of tax	2,149	
Comprehensive income	$ 19,856	$ 7,470

Table of Contents

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

	March 31, 2006 (Unaudited)	December 31, 2005
Net unrealized holding losses on investments, net of tax	$ (25)	$ (8)
Unrealized gains on derivative instruments, net of tax	4,295	2,146
Accumulated other comprehensive income	$ 4,270	$ 2,138

Share-Based Payments

In December 2004, the Financial Accounting Standards Board (FASB) revised Statement of Financial Accounting Standards No. 123 (SFAS 123R), Share-Based Payment, which establishes the accounting for share-based awards exchanged for employee services. 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 estimated compensation expense for employee share-based awards based on their intrinsic value on the date of grant pursuant to Accounting Principles Board Opinion No. 25 (APB 25), Accounting for Stock Issued to Employees and provided the required pro forma disclosures of FASB Statement No. 123 (SFAS 123), Accounting for Stock-Based Compensation.

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 will be recognized over the remaining service period using the compensation cost calculated in prior periods.

Share-based awards outstanding as of January 1, 2006 consist of 2,080,823 nonqualified stock options and 907,254 restricted stock awards. The Company issued 236,606 nonqualified stock options and 35,499 restricted stock awards during the quarter ended March 31, 2006. The Company issued 839,658 nonqualified stock options, net of forfeitures, during the three months ended March 31, 2005. All nonqualified stock options were granted with an exercise price equal to the fair market value of the common stock on the date of grant, and all restricted stock awards were granted with an exercise price of $0.0001 per share.

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 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 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 award 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 awards of either three or five years.

During the quarter ended March 31, 2006, the Board of Directors approved the modification of the performance conditions related to fiscal 2006 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 will continue to be recognized over the requisite service period.

Share-Based Compensation Information under SFAS 123R

The fair value of the Company s restricted stock awards is based on the grant-date fair market value of the common stock. This was the basis for the intrinsic value method used to measure compensation expense for the

Table of Contents

restricted stock awards prior to fiscal 2006. The weighted-average grant-date fair value of the restricted common stock was $40.53 per share during the three months ended March 31, 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. The weighted-average grant-date fair value of employee stock options granted during the three months ended March 31, 2006 was $26.89 per share, which was estimated using the Black-Scholes model with the following weighted-average assumptions:

	Three Months Ended March 31, 2006
Expected volatility	48%
Expected term (in years)	6.5
Risk-free interest rate	4.53%
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 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 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 change in accounting principle related to the change in accounting for forfeitures under SFAS 123R.

Total share-based compensation expense related to all of the Company s share-based awards for the three months ended March 31, 2006 was comprised as follows (unaudited) (in thousands, except per share data):

	Three Months Ended March 31, 2006	
Cost of service	$	258
Selling and marketing expenses		327
General and administrative expenses		4,141

Share-based compensation expense before tax		4,726
Related income tax benefit		
Share-based compensation expense, net of tax	$	4,726
Net share-based compensation expense per share:		
Basic	$	0.08
Diluted	$	0.08

Table of Contents

Prior to fiscal 2006, the restricted stock awards were granted with an exercise price of $0.0001 per share, and therefore, the Company recognized compensation expense associated with the restricted stock awards based on their intrinsic value. No compensation expense was recorded for stock options prior to adopting SFAS No. 123R, because the Company established the exercise price of the stock options based on the fair market value of the underlying stock at the date of grant. Total share-based compensation expense related to all of the Company s stock options for the three months ended March 31, 2006 was comprised as follows (unaudited) (in thousands, except per share data):

	Three Months Ended March 31, 2006	
Share-based compensation expense before tax	$	2,446
Related income tax benefit		
Share-based compensation expense, net of tax	$	2,446
Share-based compensation expense per share:		
Basic	$	0.04
Diluted	$	0.04

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):

	Three Months Ended March 31, 2005	
As reported net income	$	7,516
Less pro forma compensation expense, net of tax		(1,526)
Pro forma net income	$	5,990
Basic net income per share:		
As reported	$	0.13
Pro forma	$	0.10
Diluted net income per share:		
As reported	$	0.12
Pro forma	$	0.10

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 of generally three or five years.

The weighted-average fair value per share on the grant date for stock options granted during the three months ended March 31, 2005 was $18.85, which was estimated using the Black-Scholes option-pricing model and the following weighted-average assumptions:

	Three Months Ended March 31, 2005
Expected volatility	87%
Expected term (in years)	5.4
Risk-free interest rate	3.48%
Expected dividend yield	

Table of Contents

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

	March 31, 2006 (Unaudited)	December 31, 2005
Property and equipment, net:		
Network equipment	$ 707,974	$ 654,993
Computer equipment and other	47,989	38,778
Construction-in-progress	139,186	134,929
	895,149	828,700
Accumulated depreciation	(252,291)	(206,754)
	$ 642,858	$ 621,946
Accounts payable and accrued liabilities:		
Trade accounts payable	$ 73,675	$ 117,140
Accrued payroll and related benefits	18,225	13,185
Other accrued liabilities	44,560	37,445
	$ 136,460	$ 167,770
Other current liabilities:		
Accrued property taxes	$ 6,634	$ 6,536
Accrued sales, telecommunications and other taxes payable	12,379	15,745
Deferred revenue	28,585	21,391
Other	5,668	5,955
	$ 53,266	$ 49,627

Note 4. Long-Term Debt

Long-term debt as of March 31, 2006 consists of a senior secured credit agreement (the Credit Agreement), which includes $600 million of fully-drawn term loans and an undrawn $110 million revolving credit facility available until January 2010. Under the Credit Agreement, the term loans bear interest at the London Interbank Offered Rate (LIBOR) plus 2.5 percent, with interest periods of one, two, three or six months, or bank base rate plus 1.5 percent, as selected by Cricket. Outstanding borrowings under $500 million of the term loans must be repaid in 20 quarterly payments of $1.25 million each, which commenced on March 31, 2005, followed by four quarterly payments of $118.75 million each, commencing March 31, 2010. Outstanding borrowings under $100 million of the term loans must be repaid in 18 quarterly payments of approximately $278,000 each, which commenced on September 30, 2005, followed by four quarterly payments of $23.75 million each, commencing March 31, 2010.

The maturity date for outstanding borrowings under the revolving credit facility is January 10, 2010. The commitment of the lenders under the revolving credit facility may be reduced in the event mandatory prepayments are required under the Credit Agreement and by one-twelfth of the original aggregate revolving credit commitment on January 1, 2008 and by one-sixth of the original aggregate revolving credit commitment on January 1, 2009 (each such amount to be net of all prior reductions) based on certain leverage ratios and other tests. The commitment fee on the revolving credit facility is payable quarterly at a rate of 1.0 percent per annum when the utilization of the facility (as specified in the Credit Agreement) is less than 50 percent and at 0.75 percent per annum when the utilization exceeds 50 percent. Borrowings under the revolving credit facility would currently accrue interest at LIBOR plus 2.5 percent, with interest periods of one, two, three or six months, or bank base rate plus 1.5 percent, as selected by Cricket, with the rate subject to adjustment based on the Company s leverage ratio.

The facilities under the Credit Agreement are guaranteed by Leap and all of its direct and indirect domestic subsidiaries (other than Cricket, which is the primary obligor, and ANB 1 and ANB 1 License) and are secured by all present and future personal property and owned real property of Leap, Cricket and such direct and indirect domestic subsidiaries. Under the Credit Agreement, the Company is subject to certain limitations, including limitations on its ability to: incur additional debt or sell assets, with restrictions on the use of proceeds; make certain investments and acquisitions; grant liens; and pay dividends and make certain other restricted payments. In addition, the Company will be required to pay down the facilities under certain circumstances if it issues debt or equity, sells assets or property, receives certain extraordinary receipts or generates excess cash flow (as defined in the Credit Agreement). The Company is also subject to financial covenants which include a minimum interest coverage ratio, a maximum total leverage ratio, a maximum senior secured leverage ratio and a minimum fixed charge coverage ratio. The Credit Agreement allows the Company to invest up to $325 million in ANB 1 and ANB 1 License and up to $60 million in other joint ventures and allows the Company to provide limited guarantees for the benefit of ANB 1 License and other joint ventures.

Affiliates of Highland Capital Management, L.P. (a beneficial stockholder of Leap and an affiliate of James D. Dondero, a director of Leap) participated in the syndication of the Credit Agreement in the following amounts: $109 million of the $600 million term loans and $30 million of the $110 million revolving credit facility.

At March 31, 2006, the effective interest rate on the term loans was 6.8%, including the effect of interest rate swaps, and the outstanding indebtedness was $592.9 million. The terms of the Credit Agreement require the Company to enter into interest rate hedging agreements in an amount equal to at least 50% of its outstanding indebtedness. In accordance with this requirement, in April 2005 the Company entered into interest rate swap agreements with respect to $250 million of its debt. These swap agreements effectively fix the interest rate on $250 million of the outstanding indebtedness at 6.7% through June 2007. In July 2005, the Company entered into another interest rate swap agreement with respect to a further $105 million of its outstanding indebtedness. This swap agreement effectively fixes the interest rate on $105 million of the outstanding indebtedness at 6.8% through June 2009. The $5.7 million fair value of the swap agreements at March 31, 2006 was recorded in other assets in the consolidated balance sheet with a corresponding increase in other comprehensive income, net of tax.

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 annual income from continuing operations, excluding unusual or infrequently occurring items. Significant management judgment is required in projecting the Company s annual income 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 that recovery is not likely, it must establish a valuation allowance. The Company considers all available evidence, both positive and negative, to determine the need for a valuation allowance, including the Company s historical operating losses. 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 and tax goodwill 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 (SOP) 90-7, Financial Reporting by Entities in Reorganization under the Bankruptcy Code, future decreases in the valuation allowance established in fresh-start accounting will be accounted for as a reduction in goodwill, rather than as a reduction of tax expense.

The Company s projected deferred tax expense for the full year 2006 consists of the deferred tax effect of the amortization of wireless licenses and tax goodwill for income tax purposes. Since the Company projects a pre-tax loss and income tax expense for the full year, the estimated annual effective tax rate is negative. No income tax

Table of Contents

expense has been recorded in the first quarter of 2006, since the application of the negative tax rate to pre-tax income would result in a tax benefit for the quarter that would be reversed in subsequent quarters.

Note 6. Employee Stock Benefit Plans

Stock Option Plan

The Company s 2004 Stock Option, Restricted Stock and Deferred Stock Unit Plan (the 2004 Plan) allows for the grant of stock options, restricted common 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 1,537,889 shares of common stock are available for issuance under the 2004 Plan as of March 31, 2006. The stock options are exercisable for up to 10 years from the grant date.

A summary of stock option transactions follows:

	Number of Shares (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2005	1,892	$ 28.94		
Options granted	237	40.50		
Options forfeited	(48)	31.58		
Options exercised				
Outstanding at March 31, 2006	2,081	$ 30.20	9.21	$ 27,491
Exercisable at March 31, 2006	76	$ 26.50	8.95	$ 1,291

A summary of nonvested restricted common stock follows:

	Number of Shares (in thousands)	Weighted Average Grant Date Fair Value
Nonvested at December 31, 2005	895	$ 28.56
Shares granted	35	40.53
Shares forfeited	(23)	28.75
Shares vested		
Nonvested at March 31, 2006	907	$ 29.03

No stock options or restricted common stock vested during the three months ended March 31, 2006. At March 31, 2006, total unrecognized estimated compensation cost related to nonvested stock options and restricted stock awards granted prior to that date was $26.7 million and $16.7 million, respectively, which is expected to be recognized over weighted-average periods of 3.1 and 2.4 years, respectively. No share-based compensation cost was capitalized as part of inventory and fixed assets prior to fiscal 2006 or during the three months ended March 31, 2006. No stock options were exercised during the three months ended March 31, 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.

Table of Contents

Additional information about stock options outstanding at March 31, 2006 follows (number of shares in thousands):

	Exercisable		Total	
Exercise Prices	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Less than $35.00	76	$ 26.50	1,827	$ 28.79
Above $35.00			254	40.33
Total outstanding	76	$ 26.50	2,081	$ 30.20

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 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 of common stock 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. A total of 791,970 shares of common stock remain available for issuance under the ESP Plan as of March 31, 2006. The current offering period under the ESP Plan is from January 1, 2006 through June 30, 2006. Compensation expense related to the ESP Plan is insignificant.

Note 7. Significant Acquisitions and Dispositions

In November 2005, the Company signed an agreement to sell its wireless licenses and operating assets in its Toledo and Sandusky, Ohio markets in exchange for $28.5 million and an equity interest in a new joint venture company which owns a wireless license in the Portland, Oregon market. The Company also agreed to contribute to the joint venture approximately $25 million and two wireless licenses and related operating assets in Eugene and Salem, Oregon to increase its non-controlling equity interest in the joint venture to 73.3%. The Company received the final FCC consent required for these transactions on April 26, 2006. Completion of these transactions is subject to customary closing conditions, including third party consents. The aggregate carrying value of the Toledo and Sandusky licenses of $8.2 million, property and equipment with a net book value of $5.4 million and intangible assets with a net book value of $1.5 million have been classified in assets held for sale in the consolidated balance sheets as of March 31, 2006 and December 31, 2005.

On March 1, 2006, a wholly owned subsidiary of Cricket, Cricket Licensee (Reauction), Inc., 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 FCC approval and the receipt of an FCC order agreeing to extend certain build-out requirements with respect to certain of the licenses.

On May 9, 2006, the Company entered into a license swap agreement, whereby it will exchange its wireless license in Grand Rapids, Michigan for a wireless license in Rochester, New York. Completion of this transaction is subject to customary closing conditions, including FCC approval.

Note 8. Commitments and Contingencies

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 May 5, 2006) asserted by the Australian government against Leap remains pending in the U.S. Bankruptcy Court for the Southern District of California in Case Nos. 03-03470-All to 03-035335-All (jointly administered). The Company has objected to this claim and is seeking to resolve it through appropriate court proceedings. The Company does not believe that the resolution of this claim will have a material adverse effect on its consolidated financial statements.

Table of Contents

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 f